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Jennifer J. Johnson, Secretary
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To: regs.comments@ots.treas.gov
Regulation Comments /
Chief Counsel's Office
Office of Thrift Supervision

RE: **EGRPRA REVIEW OF CONSUMER PROTECTION LENDING RULES**

Dear Sir or Madam:

The Independent Bankers Association of Texas ("IBAT") makes these comments on behalf of its over 600 independent community bank members domiciled in Texas and Oklahoma. Before addressing specific comments about lending regulations we would first observe that IBAT has one staff attorney devoted 100% to responding to bank compliance questions. In addition, the general counsel spends approximately 1/3 of her time addressing compliance issues. The association publishes a monthly newsletter on regulatory changes and maintains a compliance list serve. At the same time, the Texas Bankers Association, which also represents banks in Texas, has a staff attorney devoted to responding to bank compliance questions. In short, a great deal of resources is devoted to this issue by just the trade associations. Several years ago, IBAT sent a regulatory burden survey to the members of its regulatory liaison council. At that time, we discovered, in an admittedly unscientific survey, that the cost of compliance for our smaller members was as much as 70 times more expensive when considered as a ratio of costs to deposits than compliance costs were for our largest member banks. In short, regulatory burden falls most heavily on the small independent institutions of our State.

Next, we would note that the comments in this letter are based at least in part on the hundreds of telephone calls that IBAT receives every month from confused and harried bankers who are doing their best to comply with the myriad of federal laws and regulations.

Also, as a general observation, we would note that there seems to be a complete disconnect between the requirements in consumer lending regulation and the information that consumers find desirable and useful. Many of the burdensome disclosure requirements are mandated by the statue itself. In other words, there is little regulatory flexibility for change. We would suggest that a true overhaul and reduction of regulatory burden would begin with focus groups meeting with representative consumers and finding out from them what information would be useful, the format for those disclosures, and the delivery that would be most effective. As a case in point, one of the hallmarks of Truth in Lending is disclosure of the APR. Based on feedback from bankers and several FTC studies, it is apparent that APR is not information that customers are particularly interested in. Rather, they are most concerned with monthly payments and how that fits within their budget.

**Flood Hazard.** On the positive side, we would note that the flood hazard handbook published by the OCC is an extremely helpful tool in understanding the requirements and intricacies of the flood hazard rules.

The major problems with the flood insurance requirements are primarily connected with customer relations. Frequently, customers are upset with the rigid flood requirements, particularly when property is obviously above a flood line but no correction to the flood map has been formally obtained. The process for the LOMR is expensive and cumbersome and causes customer unhappiness. Other problems that have been experienced with regard to flood requirements relate to condominium situations. In some scenarios, the home owners association has refused to obtain the insurance. A loan to an individual homeowner with mandatory insurance placement is difficult to explain to the consumer and enforce.

Compliance with the flood insurance requirements has been significantly simplified in recent years by the development of an industry that provides determination information and monitors the loans during their life. These services essentially manage this compliance function to some extent for most lenders. The price typically is also modest and therefore not a problem for consumers. Perhaps one of the most difficult problems of late for lenders has been the failure of Congress to timely continue the flood insurance program itself and appropriately fund it.

**Equal Credit Opportunity Act.** Perhaps the most volatile issue with regard to Regulation B of late is the change in commentary clarifying requirements for intent to make a joint application. Although the Federal Reserve has manifested an intent to provide significant flexibility to the creditor, there still are many scenarios that cause problems for creditor and borrow alike. One spouse will actually make an application for credit or take the application form home for the other spouse to complete. The ability to effectively prove that both intended for the application to be a joint one may be difficult in these situations. One additional comment with regard to joint applicants could clarify this problem. That is, if both parties actually sign the note, that that should suffice as intent of proof to jointly apply for credit. If there is concern that the customer would be confused and may not understand the significance of the act of signing the note, then a notice comparable to the cosigner notice found in Regulation AA could be implemented.

An ongoing dilemma in Texas is that of spousal signatures. As a community property state, our property provisions with regard to married couples are somewhat complex. The possible types of property that can be owned in Texas include husband's sole and separate property, wife's sole and separate property, community property jointly managed, community property managed by the husband and community property managed by the wife. Our prior Family Code provided at least that the community property was subject to contractual debt incurred during marriage. However, that section has been revised with rules indicating that if the property is subject to sole management and control, then it may not be subject to a debt incurred solely by the other spouse. Extremely complex legal and factual conclusions are required in order to determine whether or not a particular piece of property might be available to support the debt of one or other of the spouses. A simple rule that spousal signatures on any instrument for collateral may be obtained – without the qualifying requirement of deeming it necessary to reach the collateral-would be a preferable clarification from our prospective.

The adverse action notices requirements of the Equal Credit Opportunity Act creates traps for the unwary. If a lender discloses too many reasons for a turndown, then it will be criticized. However, if it does not disclose enough reasons then it is facing a dilemma with the borrower arguing that the reason is not appropriate when a decision may not be entirely back and white. Most community banks do not use scoring systems but rather subjective ones. Therefore, it can be difficult to pinpoint with laser accuracy the reason for a turndown when it may be a mixture of reason.

A Texas compliance officer once performed an experiment and utilized the short form adverse action notice merely advising consumers that they had a right to know the reason for the turn down. This compliance department, in one of the largest Texas domiciled banks, discovered that virtually no consumer ever asked for an explanation for the exact reason. Typically, the customer already has a fairly strong understanding of the defects in their credit history that led to the turndown. Thus, the adverse action disclosure is irrelevant for most customers. However, a failure to comply carries severe adverse consequences.

Recently one of the most troubling dilemmas faced by banks is balancing compliance with the customer identification program requirements of the USA Patriot Act against the limitations in information gathering of the Equal Credit Opportunity Act. These present quandaries for officers who want to obtain enough information to verify identity without collecting information that might subsequently be held inappropriate under a Reg B analysis.

**Home Mortgage Disclosure Act ("HMDA").** This law and its implementing regulation is terribly burdensome, particularly for smaller community banks. One improvement could be a significantly higher threshold for exclusion, such as $250 million. Furthermore, I do not believe that it serves the purpose for which it was designed. Perhaps Mark Twin said it best: "*There are three types of lies: lies, damn lies, and statistics*". HMDA represents the sort of lies that occur when statistics are used inappropriately. Consider the following real life examples.

- Suppose a bank is in an area with very few minorities. Six African Americans apply for credit. If one of them is turned down, then the turn down rate for African Americans is greater than that for whites. If two African Americans are turned down, then the statistics are horrific.

Another example from a Texas institution is also particularly distributing:

- A "Border Bank" decided to do an aggressive outreach to Spanish speaking potential customers. It engaged in an aggressive advertising campaign for mortgage loans in Spanish. As a result of those efforts, there was a flood of applications. The bank weeded out those customers who did not have valid immigration papers and thus could not guarantee that they would be in the United States long enough to make payments on their home loan. This was quite a few applications in this border town. None-the-less, the bank actually booked a tremendous volume of new mortgage loans to Hispanic customers. They were recognized for their effort under the Community Reinvestment Act but criticized severely and punished for their turn down rate as reflected in HMDA.

Consumer advocates have expressed a need for consumers to shop well for credit. However, if consumers actually shop for credit, then every bank with whom they apply is going to have an application on the HMDA log. Only one of the institutions will have a completed loan. Therefore, to the extent we are successful in encouraging consumers to shop for the best credit terms, we are also significantly adversely affecting HMDA statistics.

The recent revisions to HMDA present horrible data collection and reporting nightmares for community banks. Among burdensome requirements include the requirement to assess loans against the Home Ownership and Equity Protection Act ("HOEPA") and reporting rate spread; determining the date the interest rate was set; determining physical property address or census tract information in some rural areas; and analyzing credit life insurance sales to determine whether HOEPA standards are met.

Racial determinations are also increasingly complex. Personally, I have grandchildren who are ¼ Japanese, ¼ Hispanic (Puerto Rican) and ½ Anglo. Should they select multiple categories or only one? They could be Asian American or Hispanic or Anglo. Asking some of these questions are actually more offensive to borrowers than they are helpful.

Texas banks have only been able to offer home equity loans for brief period of time. Therefore, the application of HMDA to Home Equity is a fairly new issue to us. We find it very confusing. If a loan is secured by the home, then it seems like it should be reportable under HMDA. Looking to the underlying purpose is simply too confusing and doesn't appear to serve any rational purpose.

**Truth in Lending Act.** As noted above, in our experience customers are not interested in APR. Rather, they are interested in monthly payments and how those fit into a budget. None-the-less, creditors are severely punished for missing the APR outside of the tolerances. Clearly Truth in Lending is significantly better following the Truth in Lending Simplification Act in 1981. However, it too still contains problem areas.

The revisions to the Home Ownership and Equity Protection Act ("HOEPA") requirements are difficult and confusing. Obviously, there is a public policy attempt to push creditors into offering monthly premium product. However, I performed an open records request in the State of Texas to determine what monthly premium insurance products were available. I found no level premium products until very recently. Furthermore, the Texas Department of Insurance took approximately 18 months to approve the insurance carrier filing for monthly level premium credit life. All of the other insurance programs are based on a monthly outstanding balance. Data processing systems offered by the major vendors in Texas support level premium but not monthly outstanding balance for closed end loans. Therefore, the regulation is pushing lenders to offer a product that is not generally available or to deny consumers the right to have credit life, accident and health insurance. Although credit life products are despised by consumer advocates, there are many consumers in Texas for whom the credit life product is the only one that they have to protect their family and in fact may be the only product for which they can qualify since it is a guaranteed issue group program.

The Right of Recission rules are difficult to understand in certain situations and are much despised by customers. Revisions to Regulation Z have made it virtually impossible to waive the waiting period. This infuriates customers who want to get started on a home improvement project. Furthermore, the waiver is permissible only for a financial emergency. Often times, the emergency is not financial in nature. Yet, bankers are afraid to conclude that an emergency based upon a natural disaster is the equivalent of a financial emergency outside of a formal pronouncement from the Fed. Texas has many natural disasters including floods, hurricanes, tornadoes, strong winds, and other problems that Mother Nature throws at us. All too often, these result in damages to homes. Must the homeowner prove up a financial component to their problem or simply wait three days to begin repair their home? The answer is not clear enough. Furthermore, the application of Right of Recission in bridge loan situations is also not as clear as it should be to the front line loan officer trying to comply.

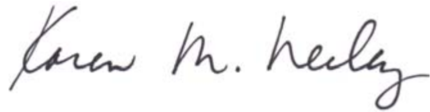
Determining what does and does not go into finance charge and does and does not go into APR continues to boggle the imagination of lenders. Again, the rules are complex and riddled with exceptions. Recently, the Federal Reserve and the FDIC disagreed (to the detriment of a state bank) as to how to handle a debt cancellation product. Regulation Z states that debt cancellation agreements are excluded from finance charge if they are voluntary and certain disclosures are made. However, the FDIC examiner concluded that if the bank had charged more than the contractual liability policy used to manage the risks, then the amount of the difference constituted a finance charge. This flies in the face of the plain language of the regulation but presents a terrible reimbursement dilemma to financial institutions attempting to offer a gap product (a type of debt cancellation agreement).

Prepaid finance charges continue to confuse consumers and compliance officers alike. They cause distorted APRs much to the dismay of the lender. Texas recently authorized a $25.00 administrative fee on consumer loans ($20.00 for loans of $1,000 or less). The last Fed functional cost analysis on loans indicates that it cost more than $100 to make a consumer loan. Texas law does not permit a bank to recoup the cost of documentation, credit reports, or any other of the items that go into making the loan. Only the administrative fee can be used to help with some of the costs. That administrative fee is a prepaid finance charge and significantly increases the APR on a small consumer loan. This confuses the consumer and distresses the bank that is trying to offer a reasonably priced product to its customers.

Another area that is especially troubling and confusing and one that is treated differently by different regulators is the distinction between the modification of a loan and refinancing. FDIC examiners do not recognize modifications. Federal Reserve examiners and OCC examiners do. It is not uncommon for small banks to use balloon notes in their real estate portfolio with a five year term and a balloon. It is simply too expensive for these banks to comply with the Truth in Lending variable rate disclosures and too easy for them to make mistakes. Therefore, they use five year notes with a balloon. The note is usually modified and extended at the end of the term. Under one logical analysis this is just a modification and should not trigger new disclosures. However, FDIC examiners conclude that it is a refinancing and always trigger new disclosures. This inconsistency is troubling. Also, the inability to read the rule and actually know what is meant by "refinancing" without consulting a lawyer is equally troubling.

Thank you for the opportunity to comment. We realize that many of the changes that would make these regulations less burdensome will necessitate statutory revisions. However, we hope that his process will continue and that only those disclosures that are meaningful to consumers will be retained while overrules will be overhauled or eliminated.

Sincerely,



Karen M. Neeley
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