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Comments on Proposed Sunshine Act Regulations

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The Neighborhood Assistance Corporation of America (NACA) is a non-profit neighborhood stabilization organization that is the largest housing services organization in the country with tens of thousands of members nationwide. NACA is known for its "Best in America" mortgage program and its aggressive advocacy against predatory and discriminatory lending practices. NACA offers low and moderate-income Americans home mortgages with low interest rates, no down payment, and no closing costs. Perfect credit is not required. Through the NACA program, thousands of Americans have realized the dream of home ownership. The current interest rate for NACA mortgages is 7.5% fixed for 30 years with no down payment, no closing costs, and no fees. In addition, NACA provides comprehensive housing services at no cost to the borrower. NACA provides prime loans for "sub-prime borrowers." It sounds too good to be true but NACA is setting the standard nationwide for affordable home ownership by providing prime loans for sub-prime borrowers.

NACA has twenty-one offices across the country with $4.3 Billion committed to the best mortgage program in America. This $4.3 billion commitment is the result of agreements between lending institutions around the country. These agreements are beneficial business arrangements for the lenders and are not the result of the Community Reinvestment Act (CRA). NACA is sufficiently established to address the issues proposed in the so-called "Sunshine Act." Because of this and the fact that none of the lending agreements fall under the act, our comments are directed to the chilling impact the draft regulations will have in the provision of affordable home ownership for working people. In fact the "Sunshine Act" regulations encourage predatory lending.

NACA believes the draft regulations submitted by the OCC, the Board of Governors of the Federal Reserve System, the FDIC, and OTS with regard to the Disclosure and Reporting of CRA-Related Agreements are unconstitutional. They are unconstitutional in that they have the effect of promoting the following:

- Discriminatory and Predatory lending practices that adversely affect disadvantaged, primarily minority borrowers and communities,
- Over reaching regulatory authority that is arbitrary and capricious,
- The violation of the free expression of individuals and community groups and their members.

A set of regulations that promotes predatory lending, grants invasive powers to regulatory agencies over particular entities that are similarly situated, and stifles free speech, is clearly unconstitutional. Even if there is a statutory basis for the distinctions between nongovernmental entities that make CRA contacts and ones that don't and entities that make below market rate loans and ones that don't, the Congress does not have the authority the force agencies to act in an unconstitutional manner. The agencies should simply not issue regulations or issue regulations that eliminate any unconstitutional distinctions.

Promotes Discriminatory And Predatory Lending Practices:

The regulations promote sub-prime and predatory lending practices. If a depository institution has an agreement to purchase loans from a mortgage broker on predatory terms that agreement is not covered since the funds are not at a below market rate. Section 35.2(b)(1) of the OCC draft of the regulations states that agreements are not covered agreements if they involve (ii) "Any specific contract or commitment for a loan or extension of credit to individuals, businesses, farms, or other entities if (A) The funds are loaned at rates not substantially below market rates; and (B) The purpose of the loan or extension of credit does not include any re-lending of the borrowed funds to third parties." See also δ 207.1(b)(1)(ii) of the Federal Reserve draft regulations, δ 346.2(b)(2)(ii) of the FDIC draft regulations, δ 533.2(b)(1)(ii) of the OTS draft regulations.

The irony is incredible. While virtually every regulatory institution, politicians across party lines, and even Alan Greenspan are condemning predatory lending and the regulators are looking at actions and regulations to limit it, the "Sunshine Act" encourages predatory lending practices. The following examples depict the contrast. The following agreement would not be covered:

A specific agreement between a depository lending institution and a mortgage broker to purchase loans with the following characteristics typical in the massive sub-prime and predatory lending:

- Interest rate from 12% to over 16%,
- Points and fees exceeding five percent,
- Yield Spread premium (the lender pays the mortgage broker additional fees for a higher interest rate),
- Borrower's payment to the mortgage broker often exceeding five percent,
- Pre-payment penalty,
- Unreasonable credit life policies, and
- Numerous additional predatory terms and practices.

The following agreement, however, appears likely to be covered:

- Interest rate at 7.5% fixed for thirty years,
- No fees,
- No down payment,

- No Yield spread premium,
- No pre-payment penalty,
- No borrower's brokerage payment,
- No credit life requirement,

The effect is to arbitrarily promote sub prime and predatory lenders who lend to working people and in low and moderate income neighborhoods while discouraging conventional lenders from offering and marketing competitive products to those individuals and communities. This adds governmental discrimination on top of the years and years of private redlining that has devastated low and moderate and minority communities.

Many lenders and entities, including Fannie Mae, consider the "market rate" for low and moderate income borrowers or borrowers who may have had some credit problems in the past to be substantially above rates it gives to "A" borrowers. The regulations would perpetuate these rates even if another lender determines that it would be profitable to enter that market with rates it offers its better customers because those rates may be considered "substantially below market". This will leave the market open to mortgage brokers and lenders that target low and moderate-income individuals and neighborhoods for the purpose of exploitation and predation.

In addition, the regulations encourage predatory mortgage brokers to testify before regulators in support of lenders they have agreements with. Non-governmental entities that provide a "below market" alternative may be penalized for such testimony. The effect of regulation promulgated by the OCC under Section 35 and the equivalent section of the regulation promulgated by other regulators is that the opinions of non-governmental entities that may wish to stop discrimination and offer competitive rate loans are stifled while the opinions of other entities that continue the discriminatory practices of the past are given greater weight in making regulatory decisions.

<u>Overreaching Government Authority:</u>

The "Sunshine Act" regulations effectively give regulatory power over non-government entities to regulators who have no jurisdiction over these entities. Agreements between non-governmental entities and depository institutions are private agreements. The agreements make legally binding a business relationship. These relationships have competitive and other aspects that should not be disclosed to other institutions.

It is arbitrary and capricious to regulate non-governmental entities based on the interest rates provided in the agreement and their involvement with CRA issues. While it is permissible for the government to create laws and regulations that distinguish between similarly situated persons and legal entities in order to serve a public purpose, it is a violation of the equal protection rights of the employees,

members, and officers of such an entity to do so for reasons that are arbitrary and capricious. Since it is not required that loans be substantially below market in order for depositories to report them as CRA loans, the distinction between the two types of loans does not have any relationship to any CRA purpose. In addition, discussions and presentations of a non-governmental entity cannot be a basis for subjecting that entity to new regulatory authority. Since there is no clear policy reason why there should be a different law for the two types of entities in question, the regulation then is arbitrary.

Stifles Free Speech:

The proposed regulations violate the first amendment in that they have a chilling affect on free speech, the right of free association and participation in the political process. Under these regulations normal activities, such as conversations between private individuals, attendance at events and testimony before government agencies, trigger regulatory oversite and requirements. The ambiguous definitions contained in the regulations mean depository institutions and non-government entities cannot freely discuss matters or meet to resolve issues without the fear of coming under the scrutiny of the regulators. Non-government entities cannot testify at hearings regarding the needs of their communities without risking future agreements with Depository institutions that are risk averse to additional regulatory scrutiny.

Section 35.2 of the OCC draft regulations contain a number of sections that illustrate these concerns. Section 35.2(b)(2) entitled "Agreements where there has not been a CRA contact" provides in δ 35.2(b)(2)(i) that a covered agreement "does not include any agreement entered into by an insured depository institution or affiliate of an insured depository institution with a person who has not commented on, testified about, or discussed with the institution, or otherwise contacted the institution, concerning the CRA." Contacts under δ 35.2(b)(2)(ii) include under (A)(1) and (2), CRA contact with a federal banking agency in which the CRA performance of an insured depository institution is mentioned and providing oral testimony or comments to a federal banking agency concerning the record or performance or future performance under the CRA of an insured depository institution." See also δ 207.2 of the Federal Reserve draft regulations, δ 346.2 of the FDIC draft, δ 533.2 of the OTS draft for equivalent regulations and examples.

The regulation contains further examples of CRA contacts. Under δ 35.2(b)(2)(ii)(B), these include "CRA contact with an insured depository institution or affiliate when an entity, (3) "has a discussion with, or otherwise contacts, an insured depository institution or any affiliate of the institution concerning the CRA rating of the institution, or the CRA record of performance of the institution." They also include, (4) having a discussion with or otherwise contacting an insured depository institution or any affiliate of the institution concerning any actions that should be taken to improve the CRA performance of

the institution or any CRA affiliate of the institution., or (5) where a discussion or contact occurs "concerning an obligation or responsibility" that an institution has to "meet the banking need of its community," and that discussion occurs "while the institution or any affiliate has an application for a deposit facility pending at a federal banking agency or is undergoing a publicly announced CRA performance examination." See also δ 207.2 of the Federal Reserve draft regulations, δ 346.2 of the FDIC draft, δ 533.2 of the OTS draft for equivalent regulations and examples.

Based on these regulations, a non-governmental entity that protests outside a Depository Institution and claims the Depository Institution has not met its community obligations would be subject to the "Sunshine Act." If the entity proposes a solution to community lending problems, the Institution has a strong disincentive to sign an agreement with the non-governmental entity because of the reporting requirements that the agreement will require. Even if the Institution determines that it is in its best interest financially to work to address the issues raised by the non-governmental entity, it may not want to do so with the entity that raised the issue. The same agreement that would trigger government scrutiny if signed with the entity that asserted its free speech rights will not require reporting if signed with another entity. Since the penalty lasts indefinitely, many non-governmental entities will be reluctant to speak out on important issues for fear that they will trigger the "Sunshine Act" and put themselves at a serious disadvantage when trying to work with Depository Institutions to address the needs of their communities.

While a protest where the word "CRA" is shouted may be a clear trigger of the "Sunshine Act", non-governmental entities may also be barred from all contact with Depository Institutions or speaking about the CRA or community development if they want to remain free of additional government regulation. For example there is no distinction between a private and a public conversation and there is little assistance in determining what is "CRA performance". A private conversation between the president of a bank and the chief legal officer for a non-profit entity regarding how to do more lending to minorities could be considered a discussion of CRA performance and trigger the Sunshine Act.[1] If three years later, the depository institution in question made an agreement with the non-profit in question, the entire content of the conversation would come into question when deciding whether the agreement fell under these regulations. If the bank was undergoing a merger or CRA examination at the time the conversation took place, the very fact that a conversation related to a CRA purpose occurred would make any subsequent agreement between the two organizations automatically CRA agreements as would any discussion involving

[1] It is important to note that it is not at all clear who speaks for a particular entity. The regulations do not answer or discuss this issue. In fact, the regulations use the term "persons" to describe non-governmental entities making it impossible to make distinctions between the actions of individuals and entities.

"meeting the banking needs of the community." The officer of the non-governmental agency would not even need to be aware that the bank in question was undergoing a merger or CRA examination at the time the discussion took place so long as there was public notice of this fact.
Non-governmental entities will also be discouraged from participating in Federal Regulatory hearings where their expertise is crucial. The examples given in δ 35.2(b) show that in order to uphold these regulations the agencies must restrict the speech of non-governmental entities and their members in a way that will have a chilling effect on these entities. Under δ 35.2(b)(2)(iii)(A), testimony that is specifically requested by a regulatory agency is exempted from δ 35.2(b)(2)(ii), but testimony in response to a general request by an agency is considered CRA testimony. This means that where someone, who could be considered a spokesperson for a non-governmental entity, has information regarding a party to a merger that might be useful to a regulatory agency, he/she is given an incentive to withhold this information for fear that the entity that he is affiliated with may years later (as of now there are no time limits included in the regulation) not be able to sign a contract with a successor to one of the merging entities without being subject to additional regulations.

In order to enforce the above regulations, the OCC and the other agencies in question would have to be given the power to scrutinize all conversations public or private between spokespeople for depository institutions and non-governmental entities. Since the leaders of banks and non-governmental entities often attend the same fundraisers and seminars, regulatory agencies may need to conduct investigations of what interactions occurred at these events where they suspect there was a CRA contact. Witnesses might need to be interviewed and transcripts checked. This would be highly intrusive particularly with respect to the non-governmental entities which unlike the banks are not part of a specific governmental regulatory scheme and therefore become subject to this scrutiny simply as a result of having a relationship with the bank.

The "Sunshine Act" regulations may even discourage individuals and non-governmenal entities from joining umbrella organizations where they may come into contact with non-governmental entities for fear that something they say privately to an organization may later be deemed to trigger the Sunshine Act. This will mean that the organizations that have the knowledge and desire to resolve issues in their community will be discouraged from meeting with each other or be locked out of participating in the agreements unless they bear additional costs and burdens that other entities that have not spoken out will not have to bear.

Summary:

The intent of the "Sunshine Act" is primarily an effort by Senator Phil Gramm to prevent affordable home ownership for working people. His attempt to destroy the CRA failed. He held up the Financial Modernization Bill until he was able to

pressure the administration to accept his back door effort through the "Sunshine Act" to limit the impact of the CRA. NACA is aware that certain regulators have understood that certain provisions of the Sunshine Act were unconstitutional and that therefore the writing and enforcement of regulations designed to implement these provision amounts to an illegal use of regulatory powers. However, these regulators apparently have felt intense pressure from Senator Gramm to implement these provisions even though they know them to be unsound. The regulators should not be intimidated and pressured by Senator Gramm to enforce t this unconstitutional legislation. Clearly the tens of thousands of NACA members and the many working people who have fought the battles against discriminatory and predatory lending are not afraid. The regulators and the administration needs to have the backbone to stand together with working people throughout the country against this attack on affordable home ownership.