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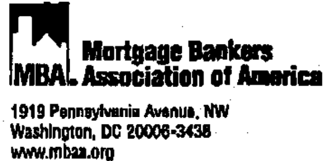
The Premier Association of Real Estate Finance



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December 2, 2002

Carolyn J. Buck, Esq.
Chief Counsel
Office of Thrift Supervision
Department of the Treasury
1700 G Street, NW
Washington, DC 20552

Re: Request for Delayed Effective Date for OTS Amendments to Alternative Mortgage Transaction Parity Act Regulations--12 C.F.R. Section 560.220

Dear Ms. Buck:

Through this letter, we confirm our meeting on Monday, November 25, 2002, at which the Mortgage Bankers Association of America ("MBA") requested that the Office of Thrift Supervision ("OTS") delay the effective date for the recent amendments to Section 560.220 of its regulations, implementing the preemptive authority granted to state housing creditors pursuant to the Alternative Mortgage Transactions Parity Act of 1982 (the "Amendments").[1] We thank OTS for its consideration in this important matter, and submit this letter to summarize our reasons for requesting the delay and to address the staff's desire for additional information concerning our request.

As the OTS is aware, MBA is a trade association representing approximately 2,600 members involved in all aspects of real estate finance. Our members include small and large institutions, national and regional lenders, mortgage brokers, mortgage conduits, and service providers. MBA encompasses residential mortgage lenders, both single-family and multifamily, and commercial mortgage lenders. Among others, MBA's membership includes state and federally chartered mortgage lenders, including FDIC-insured institutions such as federal and state savings associations, as well as numerous mortgage banking companies affiliated with both bank and savings and loan companies.

Following the promulgation of the Amendments, and after full analysis of its implications, numerous members subject to the requirements of Section 560.220 have recognized that the effective date for the Amendments--January 1, 2003-- will not permit

[1] *67 Fed. Reg.* 60542 (September 26, 2002)

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sufficient time to adequately implement all necessary changes to comply with the array of requirements triggered by this change. The changes required by the Amendments are technical and extremely burdensome. More importantly, the changes create great risk for exorbitant legal liability if undertaken improperly or in haste. Accordingly, MBA requests that the OTS stay the effective date for the Amendments until at least July 1, 2003.

As requested by OTS at our meeting, MBA engaged its members in an expeditious survey of the compliance activities relating to the implementation of the Amendments. Generally, the tasks that our members will face as a result of this rule break down into the following broad categories: identifying state law requirements, systems modifications, marketing and advertising, training, and verification and testing. Each category is discussed in turn.

Identifying State Law Requirements:

> The initial step in ensuring compliance with the Amendments is to determine the panoply of legal requirements that become applicable in the event federal preemption is not applicable. It is crucial to understand that financial institutions that have heretofore relied on the Parity Act had generally linked their compliance activities, as allowed by law, to federal requirements *without regard* for state restrictions. The lifting of the preemption privileges does not therefore represent a "minor" rule change. Rather, the Amendments alter the legal environment and impose brand new regulatory regimes that had heretofore been inapplicable to covered housing creditors.
>
> State lenders must now survey each state in which they conduct business in order to ascertain the applicability of late charge and repayment requirements that will now become applicable. Such a survey necessitates full-blown legal analysis of the relevant provisions because state mortgage regulations are not only complex and archaic, but are customarily accompanied by layers of judicial interpretations that require tailored attention. Often, applicable state restrictions vary among the various jurisdictions of the same state. Often, the requirements and restrictions vary on the basis of distinctions in lender product lines. For example, depending upon the particular license a lender might hold in a state, small loan limitations regarding late charges may apply, often imposing specialized formatting and disclosure requirements relating to that product. Moreover, due to the recent proliferation of state and municipal predatory lending statutes, lenders now face multiple levels of late charge and prepayment restrictions and disclosures. There are additional complications regarding the application of these novel "predatory lending" laws, as they have differing "trigger" mechanisms that involve very complex mathematical calculations. All these multiple restrictions may apply simultaneously to the same loan program, and as mentioned, may indeed vary among product lines.

Systems Modifications:

Once creditors complete the technically intense task of determining the scope, nature and applicability of state rules and restrictions, the changes have to be implemented into the systems and disclosures pertaining to the loan products. In regards to systems modifications, we urge that the OTS note that the Amendments will impact every significant area of mortgage banking operations, from application processing to loan origination and servicing.

In terms of application and loan origination, a most obvious point is that forms and disclosures--including Truth-in-Lending disclosures--will require modification. The task of fixing loan disclosures extends to the state-mandated disclosures, as many state jurisdictions require lenders and brokers to provide loan-specific forms that include explanations of late payment and prepayment terms and conditions. As most disclosures are now generated electronically, the Amendments will require implementing changes to document drawing systems for every loan product offered by the lender. The fixes will have to include changes to promissory notes and loan agreements. To illustrate, in the instance in which a mortgage lender operates in 50 jurisdictions and offers in each jurisdiction 25 different loan products, the current changes will mandate that the lender create up to 1,250 variations to their state compliant loan notes and security agreements.[2]

In terms of loan servicing, standard loan servicing computer programs must be modified to now calculate state-specific late charge and prepayment formulas, all of which must be integrated into monthly servicing notifications and default calculation and disclosures. This is no small task, as such programs are generally "embedded" in integrated servicing software that renders it very difficult to tinker and fix only specific pieces of the whole. MBA members indicate that in some instances, they may be required to altogether replace their servicing software.

Marketing and Advertising:

In regard to marketing and advertising, state lenders will be required to review their existing materials and revise them to the extent that current documentation incorrectly describes the late charge or prepayment terms and conditions. Among other things, this process will include identifying the channels through which marketing and advertising materials are disseminated by the particular

[2] Due to the tight time frames presented by the implementation of the Amendments, we have found it difficult to survey MBA associate members that supply our membership with compliance software products. From the limited contacts that we have had, we can ascertain however, that a number of these vendors insist that they will require more than the allotted three months to fully test their systems and ensure full and accurate compliance for their clients.

lender, retrieving obsolete materials and supplying the distribution channel with newly printed and accurate documentation.

We note that mistakes in advertising pose inordinate legal risk in terms of class action suits and enforcement action. States are vigilant, and properly so, with regards to deceptive advertising and unfair and deceptive trades and practices. More importantly, inaccuracies in marketing materials are destructive to the "reputational capital" of financial institutions. Such reputational risks are crucial to lenders, as mortgage companies depend on trust and impeccable community standing to generate business and survive in their communities.

Training:

All regulatory changes, regardless of size, impose heavy retraining burdens on responsible lending institutions. In light of the Amendments, state housing creditors must now consider various distinct components relating to training.

As a first item, state chartered lenders must identify affected loan products and produce training materials for internal and external training purposes. Second, we note that lenders that are most affected by the Amendments are multi-state lenders that operate with "diversified," as opposed to "centralized," loan origination systems. These affected lenders would, therefore, be required to schedule and undertake training sessions in one or several geographic areas in order to familiarize company personnel with all policies and procedures affected by the Amendments. Third, institutions will have to undertake systems training for computer and underwriting personnel with regard to the electronic processing of applicants, loans and servicing. Lastly, lenders that operate a wholesale lending system must assure, from a training perspective, the dissemination of accurate information by the mortgage brokerage community. In this regard, we note that the changes occasioned by the amendments deal with important loan terms that have real effects on the type of products that consumers receive. Responsible lenders will want to ensure that brokers are fully conscious of such changes and are fully able to explain their effect to consumers.

System Verification and Testing:

Finally, once all changes and processes are implemented and instituted, the systems will have to undergo verifications and testing in order to identify data processing and programming errors. We urge that the OTS fully consider the heavy implication of this challenge, as many mortgage lenders employ a mixture of legacy systems and vendor programs--all of which potentially require modifications and systems verification. In addition, the OTS must consider that, in light of all the above-mentioned changes, originators and servicers will have to re-tool their audit systems to make sure that they detect any inaccuracies with regard to the new requirements covering prepayment and late charge fees.

As a general point, it is important to note that the Amendments are *atypical* in that they do not set forth a cohesive and finite set of changes or standards. To the contrary, by lifting the preemption privileges of the Parity Act, these Amendments, in a single stroke, impose 51 potential sets of differing new standards. For this reason, a rule change as the one involved here merits special consideration with regards to implementation deadlines.

After a full analysis of the changes required to implement the Amendments, we reiterate that MBA lender members indicate that they will require a delay in the effective date until July 1, 2003. While it may certainly be the case that some mortgage lenders will achieve compliance earlier or later than that date, the consensus is such that a July 1, 2003 effective date is achievable. Our members have expressed their urgent concern that failure to stay the effective date as requested will force them to altogether suspend certain product lines indefinitely, as they are unwilling to risk the uncertainties imposed by state law.

As a final point, MBA believes that existing precedent supports the view that a delay in the effective date of the Amendments is appropriate in these circumstances. As the OTS is aware, the Federal Reserve Board recently granted the mortgage industry approximately a 6 months delay in the implementation of its amendments to Regulation C for similar compliance reasons. In all, the Board has granted a full 18-month period to allow for adequate time frames so that covered lenders could ensure full compliance with the HMDA rule changes. Moreover, it should be noted that the implementation of changes required by Regulation C (*e.g.*, modifying the LARs computer and paper-based systems) does not involve the same degree of complexity as the compliance burden associated with the Amendments.

In conclusion, we again thank the OTS for considering this important request. In that regard, the MBA wishes to confirm its willingness to provide the OTS with experts in the areas described in this letter in order to verify the accuracy of the factual matters set forth herein that support the request for a delayed effective date. Should the OTS find that such a dialogue might be helpful, the MBA would be pleased to arrange either a conference call or a meeting at OTS headquarters office to further explore these issues.

Thank you for your consideration.

Sincerely,

Kurt Pfotenhauer
Senior Vice President
Government Affairs