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Attached is the CBA comment letter on the OTS Advance Notice of Proposed Rulemaking, "Responsible Alternative Mortgage Lending," Docket No. 2000-34. Please contact us if you have any difficulty with the attachment.

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Thank you for the opportunity to present our views.
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Manager
Dissemination Branch
Information Management and Services Division
Office of Thrift Supervision
1700 G Street, NW,
Washington, DC 20552

July 5, 2000

Attention: Docket No. 2000-34

Dear Sir or Madam:

The Consumer Bankers Association (CBA)* is pleased to comment on the Advance Notice of Proposed Rulemaking (ANPR) of the Office of Thrift Supervision (OTS) regarding the Alternative Mortgage Transaction Parity Act (the Parity Act). The OTS is seeking input on the questions it will consider as it reviews its mortgage lending regulations to determine their effect on savings associations and on state-regulated housing creditors who may be making alternative mortgage transactions under the Parity Act.

The Parity Act was enacted in 1982 during a time of high interest rates in order to give state-chartered housing creditors parity with federally chartered institutions by authorizing those creditors to make, purchase and enforce alternative mortgage loans, notwithstanding more restrictive state laws. It applies to loans with any "alternative" payment features, such as variable rates, balloon payments, or call features. In recent years, certain alternative payment features have been cited among those that are employed by so-called predatory lenders to complement aggressive marketing and a range of fraudulent and deceptive practices. Thus, the OTS has sought public input as to whether the application of the Parity Act creates an environment that aids or abets "predatory lending."

When the House Banking Committee held hearings on the subject of "predatory lending," CBA testified, and we are attaching a copy of that testimony as our comment to the ANPR. In our testimony, we present our views on many of the questions raised in the ANPR: The nature of the problems being addressed; suggestions for tackling them; and

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* CBA is the recognized voice on retail banking issues in the nation's capital. Member institutions are the leaders in consumer finance (auto, home equity and education), electronic retail delivery systems, bank sales of investment products, small business services, and community development. CBA was founded in 1919 and provides leadership and representation on retail banking issues such as privacy, fair lending, and consumer protection legislation/regulation. CBA members include 85% of the nation's largest 50 bank holding companies and hold two-thirds of the industry's total assets.

the appropriate role of the states and the federal government in that process. In addition, we wish to stress that a uniform, national approach is preferable to piecemeal state-by-state or city-by-city solutions, which may only serve to confuse consumers, add to the cost for lenders, and in many cases drive legitimate lenders out of the business of lending to low- and moderate-income consumers.

As you note in the ANPR, "The flow of responsibly delivered credit to underserved markets is critical to their survival." We trust that whatever approach is adopted will recognize the importance of that flow of credit and the need for uniformity of treatment to enhance it.

Thank you for the opportunity to share our comments. If we can be of any assistance, please do not hesitate to ask.

Very truly yours,

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Attachment

Attachment

TESTIMONY OF

RALPH ROHNER

ON BEHALF OF

THE CONSUMER BANKERS ASSOCIATION

ON

PREDATORY LENDING PRACTICES

BEFORE

THE COMMITTEE ON BANKING AND FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

MAY 24, 2000

Good morning. I am Ralph Rohner, Special Counsel to the Consumer Bankers Association. CBA represents most of the major banks engaged in consumer lending. CBA members include most of the top bank holding companies and hold two-thirds of the industry's total assets, including billions of dollars of expanding lending activity in subprime markets.

We are pleased to participate, with the Committee and with our colleagues on the panel, in this effort to address the problem of unfair and deceptive mortgage lending.

On this subject, CBA is an agreeable group — to a point.

We quite agree with the observations from regulators, legislators and others that the growth of subprime, or maybe better called risk-based, mortgage products has been healthy for our economy, and of enormous value to consumers with imperfect credit profiles. That growth has permitted more consumers than ever before to purchase, improve or retain their homes, at affordable prices, in mainstream mortgage markets. The data on mortgage volumes, including the encouraging figures on loans to minorities and in previously under-served communities, are a source of great pride to the banking industry.

The past decade has witnessed a virtually unprecedented economic boom. In particular, credit to low and moderate income borrows and to minorities has exploded in recent years, and this expansion has been shared by all sectors of the economy. It has been called by some the democratization of credit.

As Federal Reserve Board Governor Gramlich recently observed, conventional home-mortgage lending to low-income borrowers between 1993 and 1998 increased nearly 75%, compared with a 52% increase for upper-income borrowers. Conventional mortgages to African-Americans increased 95%, and to Hispanics 78%, over the same time period, compared to a 40% increase overall.

That expansion has been due in part to a good economic run, innovative alternative credit products, and other factors. Certainly, much of the credit goes to banks for their outreach efforts in lower-income communities. But all the evidence suggests that much of the increase is also the result of the dramatic growth in risk based lending.

CBA also agrees that there are continuing problems in segments of the mortgage market, instigated by unscrupulous lenders or brokers who through deception, distortion or fraud impose on mortgage borrowers obligations that are simply unconscionable. This recognition, however, ought not surprise anyone. Deceptive and heavy-handed lending practices are not new; there have always been rogues or out-riders willing to skirt the boundaries of the law to take advantage of consumers who are vulnerable, out of lack of sophistication or out of sheer desperation. The right to "cool off" and rescind certain mortgage transactions was included in the original Truth in Lending Act more than 30 years ago for just that reason. And Congress acted again, in the Home Ownership and Equity Protection Act (HOEPA) of 1994, to curb abuses in these riskier mortgage markets. It is regrettable that the problem of over-reaching persists, and perhaps has increased with the growth of subprime lending, but its persistence is altogether predictable.

The question before us today is what can be done <u>effectively</u> to curtail unconscionable mortgage lending.

1. Step one, CBA believes, is to recognize that virtually every instance of bad practices reported in the court cases and in the press is riddled with deceptive and hard-sell practices, distortion and ignoring of existing rules on disclosure and documentation,

and outright fraud. These patterns do not need new law. They need effective enforcement of existing law, by the Federal Trade Commission and the banking agencies at the federal level, and by the attorneys general and similar officials at the state level. There is nothing like a visible, active "cop on the beat" to discourage and apprehend law breakers.

Numerous laws, state and federal, already exist in this area. On the federal level, the Truth in Lending Act (TILA) creates a regime of disclosure that includes the APR, a figure that represents the cost of credit and is intended to permit comparison shopping. TILA includes numerous additional disclosures and consumer protections, designed, for the most part, to inform the consumer of the terms of the loan transaction. The HOEPA amended TILA in 1994 in order to deal with many of the issues that we are discussing today. HOEPA defines a class of "high cost" home loans, which have closing costs of 8 points or more, or have an annual percentage rate (APR) 10 points above Treasury rates with comparable maturities. HOEPA loans have additional disclosures beyond those normally required by TILA, and HOEPA prohibits a number of practices. Balloon payments are prohibited within the first 5 years of the loan; certain prepayment penalties are also prohibited; as is negative amortization and some advance payments. It is a violation of HOEPA to engage in a pattern or practice of making loans without regard to the consumers' ability to repay, or to make direct payments to home improvement contractors.

Other federal laws also address many consumer protections relevant to the issue of predatory lending. The Real Estate Settlement Procedures Act (RESPA) requires that consumers be provided with timely information about the nature and costs of the real estate settlement process, including the costs of obtaining a mortgage loan. RESPA also protects consumers from unnecessarily high settlement charges caused by kickbacks and unearned fees involved in real estate settlement services.

The Fair Housing Act prohibits discrimination on the basis of race, color, religion, sex, familial status, national origin, or handicap in residential real-estate related transactions, which are defined to include the making or purchasing of mortgage loans. The Equal Credit Opportunity Act has overlapping coverage for discriminatory practices in lending.

Section 5 of the FTC Act declares unfair or deceptive acts or practices in or affecting commerce to be unlawful and gives the FTC the authority to enforce that prohibition.

As Federal Reserve Board Governor Gramlich recently stated: "A significant component of predatory lending involves outright fraud and deception, practices that are clearly illegal. The policy response should simply be better enforcement."

It is worth pointing out, as Governor Gramlich also noted, that over 70% of the lenders on the HUD list of subprime lenders are only regulated by the FTC, so the FTC's enforcement authority, if exercised with vigilance, would go a long way. Recently, the FTC exercised that authority to target seven lenders for violations of existing law (HOEPA), and has worked jointly with the Department of Justice and HUD to obtain a high-profile settlement with another lender.

Suggestions have been floated to establish a national system of licensing for loan originators and brokers in the mortgage process, and a tracking mechanism to monitor licensee behavior. CBA has reservations about creating a new, expensive bureaucracy, but would consider supporting an efficient system created by federal law or industry-wide collaboration. The threat of license revocation, and notoriety for bad practices, could be important disincentives for such practices.

2. Secondly, and ironically, part of the opportunity for over-reaching comes from the intricate structures of disclosure and documentation under existing law. It is easy for a manipulative lender or broker to dissuade borrowers from paying attention to or reacting to disclosures that, even if accurate, are voluminous, complicated, and at times at odds with one another. Congress several years ago instructed the Federal Reserve Board and HUD to consider improvements to TILA and RESPA to streamline and rationalize the mortgage disclosure rules. Despite the difficulty of reaching consensus among the

interested parties, the agencies issued thoughtful reports in 1998 — to which there has been no regulatory or legislative follow-up.

Although the two agencies were not able to agree on everything in the report, they did recommend a number of changes to TILA in general that would have a profound impact on the mortgage lending process, by among other things, clarifying the disclosures and changing the timing of disclosures to improve shopping. The two agencies also agreed on additional reforms to address substantive abuses in lending. For loans subject to HOEPA, they recommended further restrictions against balloon payments and a prohibition on the advance collection of lump sum premiums for credit insurance. For all loans, they also recommend that, prior to any foreclosure sale, creditors first provide a written explanation of any right to cure or redeem, the steps to exercise that right, a description of the foreclosure process, and information about the availability of third party counseling.

Although CBA did not endorse the overall package of reforms (we believed, for example, that disclosures needed to be still simpler than was being proposed), we encouraged a continued review of the possible reforms to improve TILA and RESPA. Regarding the predatory practices, we supported additional state licensing and examination of marginal lenders, including maintaining national data bases on those who engage in fraudulent and illegal loan practices, and increased education for consumers.

At the same time, CBA was a participant in the broad-based "Mortgage Reform Working Group," a loose-knit coalition of industry and consumer representatives, which worked to refine various reform options that, we believe, ought to get further attention. CBA suggests that a critical part of addressing <u>unfair</u> mortgage practices is to improve the "transparency" of the mortgage process as a whole, so that from the borrower's perspective "what you see is what you get," without surprises or unexpected or hidden terms and costs.

3. A third essential step is to increase significantly our public education about mortgage finance. This cannot remain a theoretical or illusory goal. Recent studies have pointed out the abysmal levels of "financial literacy" among our youth and young adults. All of us involved in these hearings — lawmakers, regulators, industry, consumer representatives –share responsibility for the inculcation of a basic understanding of consumer finance in our citizenry. CBA absolutely pledges its support to efforts in this direction, which should include ready public access by shoppers to reliable data on mortgage products through institutional bulletin boards, on site, in the press, and over the Internet.

As OTS Chairman Ellen Seidman recently said: "An informed consumer, and one with options, is less likely to fall victim to loan scams. Community organizations and others (such as faith-based organizations and schools) can and do play an essential role in this education process."

Banks, of course, are actively engaged in this process. A survey that CBA did of its members showed that almost 90% of banks had mortgage counseling programs in place in 1995, and the percentage had been rising annually. Banks routinely engage in other financial education programs, including first-time home buyer and foreclosure prevention programs, often in partnership with local non-profit organizations serving low-and moderate income consumers. Continued bank involvement in the community and in partnerships with community based organizations can be a positive force for change.

In addition, federal, state, and local governments could do a lot more to target these practices through public awareness campaigns. If the issue is indeed a priority, then resources should be devoted to teaching the public how to recognize and avoid bad mortgages. CBA recently joined forces with the Department of the Treasury in a coordinated national campaign to enhance financial education and awareness. The National Partners for Financial Empowerment (NPFE) is a public-private partnership to promote personal financial skills development to improve financial literacy, personal savings and financial empowerment. As the Treasury Department has stated: "We firmly believe that NPFE can help raise public focus on the challenges of less-skilled Americans who confront daily a complicated and fast-moving market." This Partnership, and others like it, adequately funded, can be a part of the overall campaign.

Ultimately, this will require a coordinated effort by all of us, public and private, for profit and not for profit, lenders and consumers, to bring consumers to the level of awareness that will make it harder for unscrupulous lenders or brokers to operate with impunity.

4. An additional issue concerns the process and range of any new law reform effort. CBA questions whether new federal *legislation* is necessary at this time, or whether reform options might not better be developed at the agency level rather than by statute. Every federal agency with jurisdiction over mortgage lending has begun an examination of unconscionable practices. The Federal Trade Commission has broad authority to regulate unfair or deceptive acts or practices, and the bank agencies are required to emulate FTC initiatives. Under HOEPA [TILA § 129(*l*)(2)], the Federal Reserve has a mandate to regulate practices that are "unfair, deceptive, or designed to evade the provisions of [HOEPA], or that are "abusive . . . or . . . otherwise not in the interest of the borrower." These are adequate authorizations to permit the agencies to develop regulatory restraints that draw on the agencies' technical expertise and continuing access to information through their investigative and examination powers. This approach — law reform by regulation rather than statutory dictate — is preferable for two reasons: (1) it permits more flexible and nuanced rules that are more easily adjusted as circumstances dictate; and (2) it allows the agencies to assess, on a continuing basis, how much preemptive effect the federal rules should have on state lawmaking on the same topic.

You may have noticed that my comments have not yet included the "P" word. "Predatory" is a pejorative description, but that is the extent of its usefulness. It does not begin to define itself, nor to identify those characteristics of a mortgage loan that ought to