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Manager, Dissemination Branch
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Office of Thrift Supervision
1700 G Street, NW
Washington, D.C. 20552

RE: Docket No. 2000-34; Responsible Alternative Mortgage Lending;
12 CFR Part 560; 65 Fed. Reg. 17811; April 5, 2000

Dear Sir or Madam:

The American Bankers Association ("ABA") appreciates the opportunity to comment on the Advance Notice of Proposed Rulemaking ("ANPR") on the Alternative Mortgage Transaction Parity Act ("AMTPA") and predatory lending issued by the Office of Thrift Supervision ("OTS") on April 5, 2000. The American Bankers Association brings together all categories of banking institutions to best represent the interests of the rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country.

The Advance Notice of Proposed Rulemaking

The Alternative Mortgage Transaction Parity Act (AMTPA), originally enacted in 1982, enables state-licensed housing creditors and state savings associations and savings banks to enter into alternative mortgage transactions, such as variable rate loans, without regard to state law, so long as they comply with the regulations governing such transactions that apply to OTS-regulated institutions. OTS's role under the AMTPA is limited to designating which OTS lending regulations affecting alternative mortgage transactions are appropriate and applicable to housing creditors that make such loans under the AMTPA.

Because of concerns over predatory lending practices and the efforts by states to address such activities, the OTS published the ANPR to determine whether it should change its lending regulations in order to help curb egregious lending practices and, if so, in what manner. OTS acknowledged the need to proceed cautiously in this area so that it did not handicap long-standing safe and sound lending practices or legitimate programs reaching out to under-served populations and communities.

As part of its discussion on predatory lending practices, the OTS noted that other approaches than regulatory amendments may be more effective. ABA supports OTS's exploration of alternatives to regulatory changes and encourages the OTS to focus its efforts on enforcement of existing laws and regulations and consumer education efforts.

This comment letter focuses on the AMTPA and its place in the OTS preemption arsenal and on predatory lending practices. Each of these broad categories will be addressed in turn.

The Alternative Mortgage Transaction Parity Act

The AMTPA was enacted at a vastly different economic time. High inflation, disintermediation, and economic hardship forced lenders of all types to be creative in their financing products. Many loan products were born out of this crucible of economic difficulty – the adjustable rate mortgage, wraparound mortgages, brokered deposits, and the rollover mortgage in which the loan is due in five years, but the payments amortized over 20 or 30 years. Each product was designed to anticipate and reflect the high inflation of the period. Housing lenders struggled to maintain liquidity and preserve eroding capital as underwater portfolios were sold to Wall Street at deep discounts. Use of mortgage-backed securities expanded exponentially.

The year 1982 was also notable for a landmark Supreme Court decision, Fidelity Federal Savings & Loan Ass'n v. de la Cuesta, 458 U.S. 141, 152-54 (1982) ("de la Cuesta"). Federal preemption of state law was recognized both on an express and inferred basis based on the federal government's occupation of the field, or where a state law contradicted or conflicted with a federal requirement. In the case of the Federal Home Loan Bank Board, which administered the Home Owners Loan Act provisions in question in *de la Cuesta*, the courts recognized that the federal regulatory scheme governing the operation of savings institutions was so pervasive that it was, and still is, characterized as "cradle to grave" corporate regulation.[1]

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[1] People v. Coast Fed. Savings & Loan Ass'n, 98F. Supp. 311, 316 (S.D. Cal. 1951) ("The FHLBB has adopted comprehensive rules and regulations governing the powers and operations of every Federal savings and loan association from its cradle to its corporate grave."). See, also, Conference of Fe. Savings & Loan Ass'ns v. Stein, 604 F. 2d 1256, 1260 (9^{th} Cir. 1979) ("[T]he regulatory control of the [FHLBB] over federal savings and loan associations is so pervasive as to leave no room for state regulatory control. . . . The broad regulatory authority over the federal associations conferred upon the [FHLBB] by HOLA does wholly preempt the field of regulatory control over these associations."), aff'd mem., 445 U.S. 921 (1980); FHLBB v. Empie, 628 F. Supp. 223, 225 (W.D. Okla. 1983) ("Congress intended the HOLA to preempt all state regulation over federally-chartered savings and loan institutions.")

Indeed, the amount of authority recognizing the federal preemption of state requirements is one of the strengths of the federal savings association charter.[2] This feature has been recognized throughout recent congressional debate over the repeal of Glass Steagall and the consideration of functional regulation leading to the enactment of the Gramm-Leach-Bliley Financial Modernization Act. The federal savings association charter is an effective and proven vehicle for a national and regional financial services provider. For those focused on a state or more local business, the federal preemption feature provides comfort and protection against rapid and arbitrary changes in state requirements. Federal preemption has positively influenced state regulation both in innovations and advances in supervision, and also by providing stability in the face of changing public opinion (e.g., recent ATM surcharge legislation in Santa Monica and San Francisco). [3]

The reason for reciting the status and importance of federal preemption is simple. It works. The ANPR raises an unfortunate cloud over the status and extent of federal preemption. For decades, the OTS and its predecessor, the FHLBB, pursued a careful, but thorough application of the preemption doctrine. While ABA understands and sympathizes with the goal of the OTS to address the fraudulent and illegal acts of predatory lenders, OTS's zeal must be carefully tempered to not place savings associations at a disadvantage. OTS continued and clarified its long-standing approach to preemption when it adopted 12 CFR 560.2(b) in 1996 outlining 13 examples of types of state laws preempted by its regulations. In addition, the regulation sets forth the criteria for OTS to use in its preemption determinations, including whether a law or regulation furthers a vital state interest and has only an incidental effect on lending operations or is

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[2] In contrast to the body of case law, statutes and regulations delineating OTS's clear preemption authority, the OCC, for example, depends on interpretations of "incidental" powers and conflicting requirements. See, Barnett Bank of Marion County, N.A. v. Nelson, 116 S. Ct. 1103, 1108 (1996) (National banks are generally subject to state law unless a particular statute stands in "irreconcilable conflict" with a federal law such that the state law would "forbid or . . . impair significantly, the exercise of the power that Congress explicitly granted."); Smiley v. Citibank (South Dakota), N.A., 116 S. Ct. 1730 (1996); Atherton v. FDIC, 117 S. Ct. 666, 671-673 (1997) quoting National Bank v. Commonwealth, 9 Wall 353, 361, 19 L.Ed. 701 (1869) that national banks "are subject to the laws of the State, and are governed in their daily course of business far more by the laws of the State than of the nation. All their contracts are governed and construed by State laws. Their acquisition and transfer of property, their right to collect debts, and their liability to be sued for debts, are all based on State law. It is only when the state law incapacitates the banks from discharging their duties to the government that it becomes unconstitutional." The total impact of Gramm-Leach-Bliley Financial Modernization Act preemption provisions remains to be determined.

[3] OTS Op. Chief Counsel (Nov. 22, 1999) citing OTS Op. Chief Counsel (July 1, 1998) preempting Iowa and Wyoming laws governing ATMs. OTS Chief Counsel Mem. (Dec. 22, 1998) preempting a Massachusetts regulation restricting placement of ATMs.

not other otherwise contrary to the purposes of Federal preemption.[4] This clarity promotes competitiveness and encourages innovation as savings associations have confidence in the settled nature of the law in this area.

To change this approach, even under the most sympathetic of circumstances, risks standing decades of legal precedence on its head. It is important to remember that federal preemption played a key role in resolving troubled institutions (Section 13(k) of the Federal Deposit Insurance Act (12 U.S.C.A. 1823(k)) and section 5(p) of the HOLA (12 U.S.C.A. 1464(p)). OTS's primary mission is the safe and sound operation of federal savings associations. To weaken or damage any of the tools available for OTS's use in fulfilling its mission would be shortsighted and unfortunate. To do it in order to address issues with entities that are not FDIC-insured depository institutions would be incomprehensible. For these reasons, ABA opposes efforts by OTS to "turn back the clock" and retreat from the 1996 regulatory amendments noted above and cited in the ANPR. Indeed, the reasons compelling those changes, as contained in the Chief Counsel's opinion issued on April 13, 1996, preempting application of a Wisconsin prepayment penalty restriction on variable rate mortgages for state-chartered savings associations, still remain today. The reach of the AMTPA to state-chartered savings associations and banks is an important reason to focus the result of the ANPR on the true culprits of predatory lending, rather than burden the broad industry with additional requirements that the unscrupulous will ignore.

Predatory Lending Practices

Rather than amend its wide-reaching lending regulations to address the predatory practices of a few, ABA respectively suggests that a more effective approach would be to focus agency efforts at both the state and federal level on the enforcement of existing laws. Most, if not all, of the anecdotal examples of predatory lending are violative of existing laws, including fraudulent inducement to contract and failure to comply with the Truth-in-Lending Act. For the worst perpetrators, nothing short of court action will reform their business practices. The banking agencies, with their expertise in lending, could partner with the Federal Trade Commission, state and local prosecutors, and state attorneys general in a joint effort to enforce laws against unfair and deceptive practices. This type of targeted action sends a message to the unregulated that unscrupulous, high-pressure, and fraudulent actions will not be tolerated. And like the "tinmen" of aluminum siding infamy, it will take FTC action to reform a significant segment of this industry that operates outside of federal and state banking regulation.

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[4] 12 CFR 560.2(c).

The ABA has publicly stated its condemnation of predatory lending practices.[5] The anecdotal experiences recounted are replete with current law and regulation violations and cry out for a two-pronged approach that pairs enforcement with education. Indeed, Federal Reserve Board Governor Edward M. Gramlich highlighted the need for this dual approach in his remarks before the Fair Housing Council of New York earlier this year. He noted that "a significant component of predatory lending involves outright fraud and deception, practices that are clearly illegal." Further he stated that "[m]ortgage provisions that are generally desirable, but complicated, are abused."[6] Consumer education must go hand in glove with enforcement.

For example, the Federal Trade Commission has several brochures that highlight "best practices" for consumers to follow when considering home equity and other loans. One of the more recent releases issued in cooperation with AARP by the FTC, Bureau of Consumer Protection, Office of Consumer and Business Education, outlines several "early warning signs" that home equity borrowers should watch for. The brochure encourages borrowers to avoid lenders who:

- Tell borrowers to falsify information on loan applications such as listing the loan for business purposes when it is not.
- Pressure borrowers to apply for loans for more money than needed.
- Pressure borrowers into accepting monthly payments that they can't make.
- Fail to provide required loan disclosures or tell borrowers not to read them.

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[5] Statement of Edward L. Yingling, Exec. Dir., ABA, May 25, 2000, "ABA condemns predatory lending practices. Predatory practices – such as guaranteeing the borrower one-loan rate and putting a second, higher rate in the mortgage contract – are illegal. Lenders who engage in what are defined as predatory practices are criminals and should be held accountable for their actions through the strict enforcement of existing laws and criminal statutes. Lenders who engage in these illegal activities deserve to have the book thrown at them. Law enforcement and regulators already have the tools necessary to purge predatory practices from the complex lending marketplace. Any additional changes to the marketplace should be considered in the context of a broader reform of mortgage lending activities. Attempts to add new laws or regulations to address predatory practices should be tempered by careful consideration of the impact on subprime borrowers. The subprime market, with its risk-based pricing, plays an important role in providing access to credit for borrowers who don't met traditional credit standards. Policy makers must be vigilant not to harm those borrowers by restricting lenders' flexibility in serving this market. All borrowers deserve fair prices and appropriate disclosures. Stronger enforcement of existing laws would help diminish the activities of unscrupulous lenders and help the legitimate lenders as they continue to serve consumers with less than perfect credit histories."

[6] Remarks of Governor Edward M. Gramlich, Federal Reserve Board of Governors, before the Fair Housing Council of New York, Syracuse, New York, April 14, 2000.

- Misrepresent the type of loan, such as calling a one-time loan a line of credit.
- Promise one set of terms when the borrower applies and provides a different set of terms at the loan closing with no explanation.
- Tell borrowers to sign blank forms for the lender to fill in later.
- Refuse to provide copies of signed documents. [7]

What is remarkable about the list is that, with the exception of the loan and monthly payment amount, each of the listed practices is already illegal. There are more examples of clear, borrower-friendly, educational materials already in existence. One option would be to use a consumer education program much like the Y2K effort to inform consumers and send them to reliable sources of information. While not foolproof, this type of approach empowers the consumer to seek assistance and make informed choices.

Voluntary consumer counseling programs are preferable to mandated courses. Requiring certain types (or even all) borrowers to seek consumer counseling in an effort to reach the vulnerable risks patronizing the very borrowers the regulators seek to assist and may result in yet another barrier to credit. Few borrowers, particularly parents of young and school-aged children, would agree that they have time available to attend mandatory credit training. Others would argue correctly that they are well informed and fully capable of entering a loan contract, no matter its terms. The upshot of a broad requirement for mandatory credit counseling would be the potential creation of an underground market for credit that circumvents well-meaning attempts to require the equivalent of a "financial driver's license" before borrowers would be allowed to make credit decisions.

The ABA urges the OTS and the other federal agencies to work with existing voluntary credit counseling organizations to reach as many consumers as possible in order to empower borrowers to make the credit decisions that work best for their particular situation. Enhancing consumer trust by partnering with church-based and other voluntary community-based organizations worked in the Y2K context and should be more fully explored for a long-term commitment. Voluntary education has the ability to react more quickly to changing economic circumstances and can assist borrowers to chose wisely in both favorable and unfavorable inflationary times.

Taking the two-pronged approach of increased enforcement and consumer education provides a more flexible and targeted method for dealing with the issues rather than

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[7] "Need a Loan? Think Twice About Using Your Home as Collateral," May 2000, AARP and Office of Consumer and Business Education, Bureau of Consumer Protection, Federal Trade Commission.

banning certain types of loan products. For instance, the balloon payment loan works well in a high inflationary environment. The "no doc" loan was developed to meet the rising demand of consumers for greater convenience. The OTS has applied the AMTPA to state restrictions imposing maximum and/or minimum loan amounts, limits on the term to maturity, authorizing only add-on precomputed finance charges, imposing dollar limitations under which ARM transactions cannot be consummated, requirements for equal payments of principal and interest, and direct limitations on variable rate transactions.[8] For the most part, OTS's implementation of the AMTPA has increased the variety and type of loan products available and encouraged competition in the loan marketplace.

Specific Questions Raised

The ANPR raises a number of specific questions about predatory lending and the practical effects of OTS's implementation of AMTPA. While the above general discussion answers many of the questions posed, the following responds more particularly to a few of the issues posed.

1. Should the OTS modify its regulations implementing the AMTPA?

   No. The AMTPA regulations balance the conflicting interests and faithfully implement the statutory provisions. Federal preemption in lending in particular is a hallmark of the savings association charter. The OTS has a recognized expertise that has fostered innovation to the benefit of both federal and state chartered depository institutions through thoughtful application of its preemption doctrine. Rather than take a broad based approach that could weaken the strength of federal preemption, ABA urges the OTS to pursue a dual approach of targeted enforcement and increased consumer education in partnership with state and local authorities and community-based organizations. For the worst perpetrators, only direct enforcement efforts will be effective.

2. Should OTS adopt regulations on high-cost mortgages?

   No. HOEPA is quite clear as to its requirements. Further regulation would limit flexibility Congressionally granted. The key to HOEPA is enforcement and education. The existence of HOEPA has not diminished the entrepreneurial spirit of the unscrupulous. Further regulation will only burden the law abiding.

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[8] OTS Op. Chief Counsel (Feb. 10, 1997).

3. Should the OTS impose limits on prepayment penalties and associated fees?

No. In addition to the negative impact such limits would have on the federal preemption doctrine of *de la Questa* and its progeny, OTS needs to remain mindful of the impact such requirements could have on the subprime market. Prepayment penalties and other permissible fees allow originators to recoup the cost of origination and to reflect risk. In the conventional market, it can take as long as two years of servicing to recoup the cost of origination. The subprime market, reflecting higher risk and, often, smaller loan amounts, has proportionately higher fees. It is a matter of pricing risk in a safe and sound manner. Limitations on fees only serve to discourage law-abiding lenders from serving segments of the subprime market thereby clearing the field for the predatory lender. This is not the result that OTS seeks in its ANPR.

As OTS Director Ellen Seidman noted in her remarks to the Interagency Conference on CRA, there are three parts to the solution of alternative credit: "enforcement, education and encouragement of responsible lending." [9] The ABA concurs with Director Seidman's suggested solution and urges the OTS to use the ANPR process as the basis to further this approach.

The ABA appreciates this opportunity to comment and stands willing to work with the agency to increase consumer and lender awareness. If there are any questions on the issues raised by this letter, please do not hesitate to contact Paul A. Smith, Sr. Federal Administrative Counsel at (202) 663-5331 or C. Dawn Causey, Director, Financial Institution Affairs and Counsel at (202) 663-5434.

Sincerely,

James D. McLaughlin

[9] Ellen Seidman, Director, OTS, "Puzzling Through: Approaching Alternative Credit Responsibly," remarks to the Interagency Conference on CRA, San Francisco, CA, April 17, 2000.