

51

-----Original Message-----

From: Kaplan, Steven [mailto:skaplan@kl.com]

Sent: Wednesday, July 05, 2000 7:27 PM

To: 'public.info@ots.treas.gov'

Cc: Avrakotos, Costas A.; Garwood, Suzanne

Subject: Attention Docket No. 2000-34

TO: Manager, Dissemination Branch
Information Management and Services Division
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

Attention: Docket No. 2000-34

Dear Sir/Madam:

Attached please find a comment letter submitted on behalf of the law firm of Kirkpatrick & Lockhart LLP in connection with the Office of Thrift Supervision's advance notice of proposed rulemaking on responsible mortgage lending. This comment letter is submitted on behalf of certain of our clients, including those that are (i) federally chartered savings banks, (ii) operating subsidiaries of federally chartered savings banks, and (iii) lenders who would be considered "housing creditors" under the Alternative Mortgage Transaction Parity Act. We will also have a copy of the comment letter hand delivered to the OTS on July 6.

If you have difficulty accessing the attached comment letter, have any questions regarding the comment letter or desire additional information, please call me at (202) 778-9204 or Gus Avrakotos at (202) 778-9075. Thank you, Steve Kaplan.

<<8DTW01!.doc>>

COSTAS A. AVRAKOTOS
202-778-9075
cavrakotos@kl.com

July 5, 2000

VIA E-MAIL AND HAND DELIVERY

Manager, Dissemination Branch
Information Management and Services Division
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

Attention: Docket No. 2000-34

Dear Sir/Madam:

We appreciate the opportunity to comment on the Office of Thrift Supervision's (OTS) advance notice of proposed rulemaking (ANPR) on responsible mortgage lending. This comment letter is submitted on behalf of certain of our clients, including those that are (i) federally chartered savings banks, (ii) operating subsidiaries of federally chartered savings banks, and (iii) lenders who would be considered "housing creditors" as that term is defined under the Alternative Mortgage Transactions Parity Act (the "Parity Act"). All of these clients have a significant interest in any regulatory initiatives by OTS to amend its lending regulations.

The ANPR comes amid a flurry of activity from Congress and other government agencies such as the Department of the Treasury and the Department of Housing and Urban Development ("HUD") to both define the problem of "predatory lending" and suggest proposals to prevent such practices from causing harm to consumers in the marketplace. Although the OTS has indicated that the purpose of the ANPR is to solicit information as part of a larger effort to revise the agency's mortgage lending regulations, the agency's tone and approach throughout much of the proposal reveals the strong influence that predatory lending concerns had not only in prompting this rulemaking but shaping its focus. We respectfully urge the agency to avoid taking action that further would blur the distinction between alternative mortgages and predatory lending practices. Our concern is that not only will the absence of clarity between practices that prey upon unsophisticated borrowers and mortgage products with alternative pricing features result in a stigma being attached to responsible lenders engaged in alternative mortgage transactions, but that the OTS will take unnecessary regulatory action to limit the products that may be offered. With this perspective in mind, we submit the following suggestions regarding the OTS' proposed approaches to amending its mortgage lending regulations.

I. Should OTS Adopt Regulations on High-Cost Mortgage Loans?

Concerned that individuals in minority neighborhoods with limited access to prime mortgage lenders would fall prey to the potentially abusive nature of high-cost, high fee loans,

Congress in 1994 enacted the Home Ownership Equity and Protection Act ("HOEPA").¹ HOEPA amended the Truth-in-Lending Act ("TILA") by setting forth specific requirements for disclosures relating to high-cost mortgages and limiting the use of several loan pricing features, such as prepayment fees, negative amortization and balloon payments in connection with such mortgages. Since its inception, HOEPA has come under criticism regarding its effectiveness and ability to deter predatory lending practices.² Most recently, North Carolina and New York have taken action to adopt measures that regulators in those states believe will provide their residents with increased consumer safeguards involving high-cost mortgage loans.³

We recognize that there is growing public concern over predatory lending practices, and that the OTS wants to discourage lending practices that prey upon customers' lack of knowledge or options. We share these concerns and believe that any responsible lender would not seek to engage in harmful lending practices intentionally. Accordingly, we would support reasoned efforts by the OTS to provide effective consumer protections.

Although certain practices detrimental to consumers have received considerable attention in the media, we do not believe those practices are prevalent among OTS-chartered institutions and their operating subsidiaries, nor generally widespread in the marketplace. For years, OTS-chartered institutions engaged in real estate finance activities have enjoyed the benefits of minimal regulation, increased flexibility, and uniformity in lending across state lines. The positive regulatory environment has enabled chartered institutions to stay healthy while offering competitively priced loan products that otherwise may not be available in the marketplace. The wide range of lenders, variety of loan products, and competitively priced financing has helped create the highest percentages of homeownership among American people in recent history.⁴ HOEPA, which applies to creditors generally, including those making loans pursuant to OTS regulations, provides a sufficient federal regulatory mechanism to govern the high-cost home lending activities of all lenders, including OTS-chartered institutions. Accordingly, we do not believe there is a need for OTS-chartered institutions to be subject to an additional layer of high-cost home loan regulation.

We share the Agency's apprehension that issuing regulations will have the unintended effect of closing off credit opportunities to individuals in underserved markets that may enable them to purchase houses, refinance high interest rate mortgages, or responsibly consolidate debt. Increased regulation by the OTS of its chartered institutions has a ripple effect, as it will affect the ability of their operating subsidiaries to engage in lending activities pursuant to their

¹ See DEP'T OF TREASURY/DEP'T OF HOUSING AND URBAN DEVELOPMENT, JOINT REPORT ON PREDATORY LENDING (June 2000).

² The failure of HOEPA to have the effect in the marketplace that was intended by Congress prompted the Federal Reserve Board to hold hearings in June 1997. The following year, the Federal Reserve Board and Department of Housing and Urban Development issued a report to Congress recommending that HOEPA be amended to, among other things, exclude the use of balloon payments and prohibit the advance collection of lump-sum credit insurance premiums. FED. RESERVE Bd./DEP'T OF HOUSING AND URBAN DEVELOPMENT, JOINT REPORT TO CONGRESS CONCERNING REFORM TO TILA AND RESPA 74 (1998).

³ See NEW YORK BANKING DEP'T PROPOSED REGULATIONS PART 41; N. C. 1999-332 (effective July 1, 2000).

⁴ DEP'T OF TREASURY/DEP'T OF HOUSING AND URBAN DEVELOPMENT, JOINT REPORT ON PREDATORY LENDING (June 2000). The Joint HUD/Treasury report issued earlier this month noted that "[i]n April, the home ownership rate reached a record high with 67.1% of American families owning their own homes." *Id.* at 1.

preemption authority and of nonfederally chartered creditors pursuant to the Parity Act. Such increased regulation also could influence the decision of the secondary markets to securitize such loan products. As we discuss herein, we also believe it would be ill advised to attempt to restrict the preemption authority of nonfederally chartered housing creditors under the Parity Act by limiting the preemption authority of OTS-chartered institutions, as it would penalize federal savings associations by taking away a benefit that they have long enjoyed.

In the event, however, the Agency finds it necessary to issue its own high-cost home mortgage regulations, there are certain guidelines that we believe the Agency should follow. First, we caution the Agency against taking a "one size fits all" approach to determine the amount of fees or points that are appropriate for mortgage loans. For every mortgage loan that a lender originates, there is a certain amount of overhead and fixed costs that must be absorbed in the pricing of each loan. By subjecting loans with low principal balances to inflexible fee ceilings, regulators are ensuring that lenders will not be able to fully recoup their costs in originating all loans. Regulations providing for "fee-capped loans" appear as an attractive solution to predatory lending abuses, but in the long run could prove detrimental to the credit needs of underserved communities. Ultimately, originating lenders will not be able to offer certain loan products if they incur losses due to arbitrary fee restrictions. When this happens in the subprime market, borrowers will be forced to look to alternative sources for much needed credit. We believe that the presence of responsible lenders is especially critical in the subprime market to ensure that borrowers have the benefit of robust competition and are not forced to accept credit on whatever terms are demanded.

Assuming that a fair and appropriate test can be devised for determining the loans that should be classified as high-cost loans, the OTS should not prohibit the financing of points or fees, or establish an inflexible ceiling as to the amount of fees that a borrower may finance. We realize that the financing of fees can increase the amount of the loan. We also recognize that if the lender has dealt dishonestly with the consumer, the financing of all fees could provide a means of concealing the true amount of the fees. Nevertheless, we are concerned that a restriction on financing points and fees could prevent creditworthy borrowers that do not have adequate cash on hand from obtaining a mortgage loan. Such a regulation in connection with high-cost home loans would have the effect of institutionalizing a discriminatory practice against low-income consumers, as borrowers generally would be free to finance points and fees of residential mortgage loans that are not classified as high-cost home loans.

Moreover, we believe that any action by the OTS to limit beyond HOEPA the extent to which loan products with prepayment fees may be offered by savings associations or other housing creditors is unwarranted and will deprive lenders and borrowers of a pricing feature that has proven to be mutually beneficial. As the OTS has noted, the authority to impose prepayment fees in connection with fixed rate loans or adjustable rate mortgage loans generally has not been abused by savings associations and has a valid and beneficial purpose in that it enables consumers to "negotiate a lower interest rate on their loans."⁵

⁵ 65 Fed. Reg. 17,813 (2000).

As lenders generally price the loan on a projected pay-off date, a loan with a prepayment fee feature will help offset the creditor's costs to make and hold the loan in portfolio, or to purchase the loan, should the loan be paid off in advance of projections. Like any feature of a loan, it is an option available to a consumer. The consumer can choose a lower interest rate loan without a prepayment fee feature or a slightly higher interest rate loan without a prepayment fee feature, depending on the consumer's personal circumstances. The opportunity to select a loan product with a lower interest rate and lower monthly payments in exchange for a prepayment fee condition that may never be triggered by an individual borrower should not be restricted. Ultimately, whatever restrictions are imposed on prepayment fees will be factored into the price of the loan and affect the consumer's choice in the marketplace.

Like any financial tool, loans with a prepayment fee can be abused. The combination of an unscrupulous lender and an uninformed borrower can turn prepayment fees from a flexible pricing feature which assists borrowers in achieving homeownership or responsibly using the equity in their homes, into a means of forcing borrowers to default on loans and eventually losing their homes.⁶ An unwary borrower can fall prey to this and other unsavory practices.

Accordingly, we believe that widespread education efforts for borrowers with poor credit history and a low Fair Isaac and Company (FICO) score⁷ will help minimize the opportunity for lenders to engage in many abusive lending practices. Mortgage financing remains a mystery to many borrowers, with even the most sophisticated of consumers needing help in understanding the costs associated with home purchase or equity financing. Education alone, however, will not solve the problem. A strong education campaign needs to be coupled with the imposition of tougher enforcement measures for lenders that intentionally disregard existing laws.

We urge OTS to refrain from either issuing new regulations or amending existing ones, as we believe that such action will be far more likely to limit the products that responsible housing lenders will choose to offer, rather than dissuade unscrupulous lenders from engaging in what already constitutes illegal behavior. Borrowing from the Agency's own words, we note that:

[R]egulations should be reserved for core safety and soundness requirements. Details on prudent operating practices should be relegated to guidance. Otherwise, regulated entities can find themselves unable to respond to market innovations because they are trapped in a rigid regulatory framework developed in accordance with conditions prevailing at an earlier time.⁸

⁶ Ironically, loans with a prepayment feature could counter the practice of "loan flipping," the practice of repeatedly refinancing mortgage loans within a short period of time with little or no benefit to the borrower, as borrowers would have a disincentive to refinancing.

⁷ In the Office of Federal Housing Enterprise Oversight's (OFHEO) 2000 report to Congress, it quoted statistics from Inside B&C Lending estimating that 73 percent of subprime loans originated in 1999 went to borrowers with a FICO score between 619 and 580, 13 percent went to borrowers with a score of 560 to 579, nine percent went to borrowers with a score between 540 and 559 and five percent went to borrowers with a score below 540. OFHEO 2000 REPORT TO CONGRESS 46 (2000).

⁸ 61 Fed. Reg. 1,164 (1996).

Although we do not believe a regulatory initiative that rewrites the rules by which federally chartered savings associations and their operating subsidiaries may engage in mortgage finance activities is necessary, we believe the OTS must address the extent to which legislative and regulatory remedies being adopted by the states apply to federally chartered savings associations and their operating subsidiaries. Widely disparate state solutions to combat predatory lending practices threaten certain goals that have long guided the manner in which the OTS regulates the lending activities of its chartered institutions and their operating subsidiaries. Individual state adoption of measures to fight predatory lending will (i) generate uncertainty with lenders as to the extent to which the OTS has exclusive authority to regulate the lending activities of its chartered institutions and their operating subsidiaries, (ii) undermine efforts by the OTS to keep federally chartered savings associations competitive with other lenders; (iii) negate the OTS uniform system of regulation, examination, and supervision that enables federal chartered savings associations and their operating subsidiaries to conduct their lending operations consistently and efficiently across state lines; and (iv) significantly increase the regulatory burden placed on federally chartered savings associations and their operating subsidiaries in conducting their lending activities.⁹

We recognize that the preemption from state lending restrictions afforded federal savings associations under 12 C.F.R. § 560.2, and their operating subsidiaries by virtue of 12 C.F.R. §§ 559.3(h) and (n), is broadly worded. Nevertheless, issues could arise as to whether certain novel state provisions to regulate predatory lending practices are preempted. For example, under North Carolina's statutory high-cost home provisions, lenders must obtain a certification from borrowers of certain loans that the borrower has obtained counseling about the loan. Additionally, both North Carolina's statutory provisions and New York's proposed regulatory provisions require the lender to make a determination as to the suitability of a "high-cost loan" for a particular consumer.¹⁰

Although we believe these and other requirements will not have the salutary effect anticipated by the states, and in the case of a "suitability test" will subject lenders to litigation irrespective of whether they approve or deny a loan, we believe it is important for states to recognize that such requirements are not within the purview of the state to impose on federally chartered savings association and their operating subsidiaries. Therefore, in any rulemaking conducted by the OTS, the OTS should clearly and unequivocally (i) restate that it has the plenary authority to regulate the lending activities of federally chartered savings associations and their operating subsidiaries, (ii) reconfirm that federally chartered savings associations and their operating subsidiaries conduct their lending activities exclusively under the regulations and supervision of the OTS, and (iii) conclude that any state restrictions or requirements involving the capacity, ability, authority or conditions to make, broker, acquire, sell, service, or enforce residential mortgage loans, regardless of their nature, are preempted for federally chartered savings associations and their operating subsidiaries.

⁹ 65 Fed. Reg. 17812 (2000).

¹⁰ See N.C. 1999-332 (effective July 1, 2000) and N.Y. Banking Dept. Proposed Regulations, Part 41.

II. Should the OTS Modify its Regulations Implementing the Alternative Mortgage Transactions Parity Act.

The OTS has requested comments on whether all of the regulations that it has deemed "appropriate and applicable" to alternative mortgage transactions under the Parity Act should continue to be so designated. Specifically, the OTS asks "[s]hould only those OTS regulations that apply exclusively to alternative mortgage transactions be designated appropriate and applicable (the approach taken by the Bank Board in 1982)?" In the alternative, the OTS asks "[s]hould every regulation that imposes conditions or restrictions on a federal savings association's ability to make an alternative mortgage transaction be designated appropriate and applicable, even if the regulation applies to a broader category of loans (the approach taken by OTS in 1996)?"¹¹

We recognize that the OTS is concerned that nonfederally chartered housing creditors, which are not subject to examination and supervision by a federal agency, are using their authority under the Parity Act to impose certain fees or engage in certain practices that may be detrimental to consumers. Nevertheless, given the express authority of the Parity Act, we do not believe the concerns of the OTS can be addressed by revising its regulations without harming the interests of its chartered federal savings associations. The Parity Act places nonfederally chartered housing creditors on the same level playing field as federally chartered savings associations in being able to assert preemption from state laws when making, purchasing, or enforcing alternative mortgage transactions. We are concerned, therefore, that the tenor of the ANPR suggests that the OTS may be moving to adopt a regulation that either will (i) deviate from its consistent application of the Parity Act to treat nonfederally chartered housing creditors equally with federally chartered savings associations when preempting state laws impeding alternative mortgage transactions, or (ii) limit the longstanding preemption of state laws available to its chartered institutions and their operating subsidiaries as a means of restricting the extent to which nonfederally chartered housing creditors may preempt state law when making alternative mortgage transactions pursuant to the Parity Act.

With this concern in mind, we want to offer our comments on the application of the Parity Act, and address certain statements made in the ANPR that merit clarification as to the OTS position regarding the Parity Act.

A. What is the Congressional Purpose in Enacting the Parity Act?

In enacting the Parity Act, Congress found that alternative mortgage transactions are essential to an adequate supply of residential financing, and that the federal agencies had adopted regulations authorizing federally chartered depository institutions to engage in alternative mortgage financing. Therefore, Congress enacted the Parity Act in order "to eliminate the discriminatory impact that those regulations have upon nonfederally chartered housing creditors and provided them with parity with federal chartered institutions by authorizing

¹¹ 65 Fed. Reg. 17815 (2000)

all housing creditors to make, purchase and enforce alternative mortgage transactions so long as the transactions are in conformity with regulations issued by the Federal agencies."¹²

The purpose of the Parity Act is to achieve parity between chartered financial institutions and nonfederally chartered housing creditors in making, purchasing, and enforcing alternative mortgage transactions. The OTS consistently has indicated that it is appropriate to look to the purposes that underlie the Parity Act, to prevent discrimination against state-chartered depository institutions and other nonfederally chartered housing creditors.¹³ Any regulation that benefits federally chartered savings association over nonfederally chartered housing creditors in making, purchasing, or enforcing alternative mortgage transactions undermines the purpose of the Parity Act. Any regulations adopted by the OTS for purposes of implementing the Parity Act must maintain parity between its chartered institutions and nonfederally chartered housing creditors.

B. How Does the Parity Act Apply to State Law?

The Parity Act authorizes nonfederally chartered housing creditors to make alternative mortgage transactions "notwithstanding any State constitution, law, or regulation," if made in accordance with "the regulations governing alternative mortgage transactions as issued by the [OTS] for federally chartered savings associations," as such regulations have been authorized by the rulemaking authority of the OTS for its chartered federal associations under laws other than the Parity Act.¹⁴ As the OTS indicates in the ANPR, the Parity Act grants housing creditors with the same power as federal savings associations in the context of alternative mortgage transactions.¹⁵ Based on the plain language of the Parity Act, this broad preemption authority extends to any state law, if the housing creditor follows the rules that OTS-chartered institutions could apply to alternative mortgage transactions. Nothing in the Parity Act limits the preemption available for nonfederally chartered housing creditors to those state provisions that exclusively apply to alternative mortgage transactions.

The underlying approach to the Parity Act was simple. If federally chartered thrifts can make alternative mortgage loans in accordance with the rules of their federal regulator and preempt state laws that would limit such ability, then nonfederally chartered housing creditors also should have such authority. Contrary to the sentence in the ANPR that "state law governs those aspects of a housing creditor's operations not covered by regulations designated as applicable to alternative mortgage transactions under the Parity Act,"¹⁶ state law may apply only to the extent it would apply to the federal savings association. Accordingly, if federally chartered thrifts can preempt a state law of general applicability when it makes an alternative mortgage transaction, then nonfederally chartered housing creditors are equally entitled to preempt such a state law when making an alternative mortgage transaction. The Parity Act has not been amended to change this basic premise.

¹² 12 U.S.C. 3801

¹³ OTS Op. Chief Counsel at 4 (April 30, 1996).

¹⁴ 12 U.S.C. 3803.

¹⁵ 65 Fed. Reg. 17815 (2000).

¹⁶ Id.

The single biggest advantage to lending under the Parity Act is the same benefit available to federally chartered thrifts making any real estate-secured loans, uniformity and consistency in offering alternative mortgage products across state lines. The hodgepodge of state regulation that could apply to alternative products would make it impossible for a nonfederally chartered housing creditor to offer competitively priced alternative mortgage loans if not for the Parity Act. Without being able to rely on the Parity Act, state law would prohibit certain alternative mortgage transactions, such as mortgage loans with a balloon feature or shared appreciation mortgages, limit the types of indices used as the basis for interest rate adjustments, require individual state-specific disclosures, and impose different fee requirements. Rather than having one product in compliance with one set of rules governing the product that could be offered universally, nonfederally chartered housing creditors would need to have 51 variations of the product to ensure compliance with the laws of each state and the District of Columbia. The costs to comply with 51 jurisdictions and the limitations on alternative mortgage products in different jurisdictions would ensure that nonfederally chartered housing creditors are economically disadvantaged when competing with federally chartered lenders. This could lead many nonfederally chartered housing creditors to abandon alternative mortgage products, tightening the availability of credit, restricting accessibility to creditors, and ultimately increasing the cost of the credit to the consumer. Congress recognized these concerns when it enacted the Parity Act.

Moreover, the secondary mortgage marketplace that has developed since the Parity Act was enacted would be undermined if regulations applicable to alternative mortgage transactions were different between nonfederally chartered housing creditors and federally chartered housing creditors. As the Parity Act authorizes nonfederally chartered housing creditors to make, purchase, and enforce alternative mortgage transactions on an equal footing with chartered financial institutions, it has had the effect of facilitating a steady stream of capital to finance diverse mortgage products. If nonfederally chartered housing creditors had one set of rules and federally chartered housing creditors had another set of rules when making, purchasing and enforcing alternative mortgage products, then the secondary mortgage markets would be disrupted as issues about the enforceability of alternative mortgage products would arise. For example, could a nonfederally chartered housing creditor purchase an alternative mortgage product from a federally chartered thrift and enforce a prepayment fee provision contained in the note in a state that prohibits prepayment fees if the nonfederally chartered housing creditor could not rely on the Parity Act to preempt the state restriction to the same extent as the federally chartered thrift? Such uncertainty about the enforceability of alternative mortgage products would lead to a tightening of housing credit.

C. What Purpose do the Regulations Adopted by the OTS Serve in Implementing the Parity Act?

The ANPR states that the Parity Act authorizes housing creditors to make alternative mortgage loans as long as the transactions are "in accordance with" appropriate and applicable OTS regulations."¹⁷ In discussing this regulatory authority under the Parity Act, the ANPR

¹⁷

65 Fed. Reg. 17815 (2000).

seems to suggest that the OTS can adopt regulations specifically and exclusively applicable to nonfederally chartered housing creditors making alternative mortgage transactions.

The authority of the OTS under the Parity Act to issue implementing regulations, however, is limited when considered in the context of its Congressional purpose to prevent discrimination against nonfederally chartered housing creditors when making, purchasing, or enforcing alternative mortgage transactions. Nonfederally chartered housing creditors subject to the OTS rules for Parity Act purposes are entitled to assert preemption from state requirements to the same extent as federal savings associations. For nonfederally chartered housing creditors to be able to exercise their Parity Act authority, they must make their alternative mortgage transactions in accordance with the OTS regulations under which federally chartered savings associations may engage in such transactions.¹⁸ Accordingly, the Parity Act requires the OTS to identify, describe, and publish those portions or provisions of its regulations governing its chartered institutions that are inappropriate and thus inapplicable, or that needed to be conformed, for the use of such nonfederally chartered housing creditors exercising their Parity Act preemption authority.¹⁹

The OTS has identified certain regulations that are appropriate and applicable to the exercise of this authority and all other regulations not so identified are deemed inappropriate and inapplicable. Although regulations deemed inappropriate and inapplicable need not be followed by nonfederally chartered housing creditors, those regulations that benefit federal savings association because they preempt state law that may apply to alternative mortgage transactions are by operation of the Parity Act applicable to other housing creditors. Given that the purpose of the Parity Act is to establish parity between nonfederally chartered housing creditors and federally chartered institutions in alternative mortgage financing, we believe the Parity Act provides that nonfederally chartered housing creditors subject to the OTS rules for Parity Act purposes (i) must comply with all of the regulations identified by the OTS that apply to alternative mortgage transactions in order to exercise Parity Act authority, (ii) do not need to comply with any other OTS regulations not so identified, and (iii) can assert preemption from any state law that would prohibit, affect, restrict or impede their ability to make, purchase, or enforce alternative mortgage transactions to the same extent as federally chartered savings associations. Simply because the OTS has stated that all of its regulations not identified as appropriate and applicable to the exercise the Parity Act preemption authority are deemed inappropriate and inapplicable, does not negate the statutory right of nonfederally chartered housing creditors to preempt state laws affecting alternative mortgage transactions to the same extent as a preemption can be asserted by federally chartered savings associations. Accordingly, even if the requirement to follow the constraints of section 560.33 governing late charges and section 560.34 governing prepayments were not identified in section 560.220 as rules that are appropriate and applicable to the exercise of the Parity Act authority, a nonfederally chartered housing creditor still would be entitled to assert a preemption from a state late fee or prepayment fee restriction that could apply to an alternative mortgage transaction if a federally chartered savings association could assert a preemption from such restriction.

¹⁸ 12 U.S.C. 3803(a)(3).

¹⁹ 12 U.S.C. 3801 note.

Moreover, with respect to its regulations implementing the Parity Act, the OTS should recognize that its rules might be more restrictive than state law. For example, the OTS rules only allow a late fee to be imposed after a 15-day grace period has elapsed, whereas some states allow a late fee to be imposed after a 10-day grace period. As we understand, a nonfederally chartered housing creditor would need to apply all of the OTS Parity Act rules to gain the benefit of Parity Act preemption for a particular loan product.

D. The Preemption Authority of Nonfederally Chartered Housing Creditors Making Alternative Mortgage Transactions Cannot Be Less Than The Preemption Authority for Federally Chartered Savings Associations.

The OTS is given authority under the Parity Act to determine which of its regulations applicable to its chartered savings associations engaged in alternative mortgage transactions are inappropriate and, thus, inapplicable to other housing creditors seeking to rely on the Parity Act. However, this authority cannot be applied arbitrarily to limit the extent to which nonfederally chartered housing creditors can rely on the Parity Act. As the OTS set forth in the ANPR, in determining appropriate and applicable regulations, the OTS must keep the overall congressional goals of parity in mind.²⁰ As the Parity Act is intended to provide nonfederally chartered housing creditors with the authority to make, purchase, and enforce alternative mortgage transactions on the same basis as federally chartered institutions, the OTS rules that nonfederally chartered housing creditors must follow for purposes of the Parity Act cannot be any more restrictive than the rules applicable to OTS-chartered institutions. Otherwise, the Congressional goal in enacting the Parity Act is defeated.

Accordingly, given the wording of the Parity Act and the express intent of Congress to eliminate the discriminatory impact experienced by nonfederally chartered housing creditors in connection with alternative mortgage financing, the authority of the OTS to modify the Parity Act rules that are appropriate and applicable to nonfederally chartered housing creditors is limited. Without a legislative change, the authority of nonfederally chartered housing creditors and OTS-chartered financial institutions and their subsidiaries to engage in alternative mortgage transactions is intertwined. The OTS cannot adopt rules that benefit its chartered institutions and their operating subsidiaries making alternative mortgage products, but restrict such rules so that they do not apply to nonfederally chartered housing creditors as it would be contrary to the purpose of the Parity Act. The OTS could change the rules that apply to its chartered institutions and their operating subsidiaries, and by doing so, limit the rules that would be appropriate and applicable to other housing creditors for purposes of the Parity Act. Such an approach would be inadvisable, as it would unduly restrict the flexibility and competitiveness of OTS-chartered institutions and their operating subsidiaries in the marketplace, and ultimately their safety and soundness. Consequently, any rulemaking initiative by the OTS to modify its regulations that apply the Parity Act to nonfederally chartered housing creditors must be very circumspect.

E. Qualifying Housing Creditors Under the Parity Act

²⁰ 65 Fed. Reg. 17816.

We also want to bring to the attention of the OTS a quotation offered in the ANPR that will leave readers with the wrong impression of the application of the Parity Act, and should be amended to reflect accurately the language of the Parity Act. The ANPR states that "in order to qualify as a housing creditor and take advantage of the Parity Act's preemption, the creditor must be licensed under applicable state law and [remain or become] subject to the applicable regulatory requirements and enforcement mechanisms provided by state law."²¹ Contrary to this sentence, the Parity Act does not require housing creditors to be licensed to take advantage of the Parity Act. Rather, the Parity Act expressly provides that an entity is

not a housing creditor with respect to a specific alternative mortgage transaction if, in order to enter into that transaction, "the person would be required to comply with licensing requirements imposed under state law, unless such person is licensed under applicable state law . . ."²²

Thus, the requirement to be licensed under applicable state law to take advantage of the Parity Act only arises if such entity would be required to comply with state licensing requirements. If an entity is not required to be licensed under state law because it is exempt from licensing, it still can take advantage of the Parity Act. This provision of the Parity Act recognizes that every state did not license entities engaged in mortgage finance activities, and that every state licensing statute provides a number of express statutory exemptions from licensing for, among other entities, affiliates or subsidiaries of federally chartered thrifts; FHA, VA, FNMA, FHLMC, or GNMA approved lenders; insurance companies; or securities broker/dealers.

III. Is Differential Regulation Appropriate?

OTS specifically has requested comment on the advisability of pursuing the adoption of a regulation that would condition a housing creditor's ability to make loans under the Parity Act on the OTS' determination of whether the lender has met certain standards of eligibility. Assuming that any new regulation would be modeled after Part 516 of the OTS' regulations we do not believe that housing creditors would necessarily be foreclosed from making loans, but would be subject to either a review by the agency or required to provide evidence of their compliance with OTS regulations prior to or in the course of making alternative mortgages in accordance with OTS regulations. We strongly urge the OTS to refrain from further pursuing this approach.

Following the enactment of the Parity Act, the Federal Home Loan Bank Board (FHLBB) (predecessor to the OTS) issued a final rule implementing regulations under that Act applicable to federal savings associations as well as other housing creditors. The FHLBB clearly understood the limitations that Congress had placed on its jurisdiction over housing creditors and made a point of quoting Congressional intent on this point in the preamble to the final rule. The FHLBB noted that, "Title VIII 'does not place nonfederally chartered housing creditors under the supervision of the federal agencies, but instead merely enables them to follow a federal

²¹ 65 Fed. Reg. 17813 (2000).

²² 12 U.S.C. 3802.

Manager, Dissemination Branch
Office of Thrift Supervision
July 5, 2000
Page 12

program as an alternative to state law."²³ The ANPR reiterates that the OTS "does not have licensing, supervision, examination, or enforcement authority over [nonfederally chartered] housing creditors."²⁴ Accordingly, we are unclear as to why the OTS would seek to be the arbiter of compliance with the Parity Act. We find Congress' intent to keep housing creditors free from the OTS' oversight to be clear and urge the OTS to abandon an approach that would put the Agency in a position of examining a non-federally chartered housing creditor's safety and soundness.

Moreover, state regulation and examination of nonfederally chartered housing creditors is significant. A number of state mortgage financing licensing agencies annually examine loan files of licensees, and actively investigate consumer complaints. State regulators can enforce violations of the Parity Act without the OTS needing to step in and supervise the activities of nonfederally chartered housing creditors. Housing creditors subject to investigation, license suspension or revocation in one state often are required to provide notice of such action with regulators in other states in which they may be licensed, and state regulators routinely circulate notice of such action to their colleagues.

*

*

*

We would like to thank you for the opportunity to comment and for your consideration of our suggestions. If you or other members of the OTS staff have any questions, we would be pleased to discuss them with you.

Sincerely,

Costas A. Avrakotos

²³ 48 Fed. Reg. 23, 053 (1983) (citing S. Rep. No. 97-463, 97th Cong., 2d Sess. 55).
²⁴ 65 Fed. Reg. 17812 (2000).