



CHARTER ONE® BANK F.S.B.

July 6, 2000

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

Attention: Docket No.2000-34

Re: Advance Notice of Proposed Rulemaking - Responsible Alternative Mortgage Lending

Gentlemen:

Charter One Bank, F.S.B., on behalf of itself and its lending affiliates and subsidiaries (collectively, the "Bank"), is pleased to comment on the questions and issues (the "Issues") raised by the above-referenced advance notice of proposed rulemaking ("APNR") published by the Office of Thrift Supervision (collectively, the "OTS"). The Bank is a federally-chartered savings bank and a wholly-owned subsidiary of Charter One Financial Inc. (a \$31 billion asset financial holding company) with branch operations in the states of Ohio, Michigan, New York, Illinois, Massachusetts, and Vermont with residential mortgage lending and non-prime residential mortgage lending operating subsidiaries among others. These operating subsidiaries purchase significant volumes of loans from third-party originators. The total lending operations of the Bank including the subprime lending operations conducted by subsidiaries are integral to the Bank's profitability. In conducting its lending operations the Bank and its operating subsidiaries rely significantly upon the preemption of state laws granted by the Alternative Mortgage Transactions Parity Act (the "Parity Act") and its implementing regulations.

At the outset it is important to remember that subprime lending or high cost lending is not in and of itself "predatory." Certain mortgage loan attributes, standing alone, have often been identified as "predatory;" however, there are often sound business reasons for their inclusion in any given mortgage loan. For example: higher rates and fees are used to compensate lenders for increased credit risk, prepayment premiums are used to compensate lenders for loans with no or low closing costs or fees which are granted to borrowers who are unable to afford the out-of-pocket expenses otherwise associated with mortgage loans. We ask the OTS to carefully consider the ramifications of any future

regulation in this area to the ability of its regulated entities to provide mortgage loans in a prudent, safe, sound **and profitable** manner.

The Bank submits the following comments concerning the following Issues raised in the ANPR:

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

The expansion of traditional mortgage lending markets into subprime and non-prime markets has no doubt provided additional consumers an opportunity to obtain mortgage loans that would not have otherwise been available in traditional lending markets. While the OTS does not want to discourage such lending, the agency is understandably concerned about the protection of non-traditional borrowers.

The ANPR discusses the possibility of adopting specific regulations governing "high-cost mortgage loans." The primary component of such regulation would be the expansion of the definition of "high-cost mortgage loans," as currently defined by the Home Ownership Equity and Protection Act of 1994, Pub. L. 103-325, Title I, Subtitle B (Sept. 23, 1994) ("HOEPA"). Apparently, additional regulation in this area would apply to any loan falling within the definition of "high-cost mortgage loan," thus establishing a reasonable definition is critical. The ANPR discusses the approaches adopted by the legislatures of North Carolina and New York, and solicits comments on the possibility of a similar OTS definition. The respective North Carolina and New York legislative definition of "high-cost loans" is unnecessarily restrictive, serving to encompass and regulate broad group of loans, and placing additional regulatory and/or disclosure burden on responsible lenders who are not engaging in predatory practices.

The imposition of a lower point and fee threshold than as defined HOEPA would significantly negatively affect the wholesale mortgage loan business of regulated lenders.

2. *Should OTS impose limits on financing of certain fees or charges?*

A limitation or restriction on the financing of fees and points may unnecessarily restrict fees which are bona fide and reasonable in relation to services actually performed or provided, by either the lender or a third party, or both.

3. *Are limits on refinancing appropriate?*

An absolute requirement that the borrower receive an annual percentage rate that is less than the existing note rate when the institution is refinancing its own or an affiliate's mortgage would be unnecessarily restrictive since the borrower may receive some other form of material benefit from a refinance other than a reduction in rate. This is particularly true in the current market rate environment, in which cost of funds and the resultant mortgage rates are rising. It is also particularly true in subprime markets, where borrowers' credit standing may not necessarily improve over time.

4. *Are prepayment premiums or fees appropriate for high-cost loans?*

A subprime mortgage loan may have significant closing costs and fees which are advanced by the lender at origination (as, for example, in the case of a no-cost loan) which, from an accounting perspective, are not recognized as income at time of origination. Rather, the fees are amortized over the life of the loan. In instances in which a borrower pays off a loan early, the prepayment fee then becomes the lender's only means of recouping such advanced costs and fees. If such a loan is paid-off early, the lender will incur a loss on the loan absent the imposition of a prepayment fee.

In the case of whole loans purchased on the secondary market, prepayment fees may be used to offset loan origination premiums paid out to other lenders or brokers at the acquisition. The restriction or prohibition of such fees would again likely result in a loss to the lender.

5. *What limits on balloon payments, negative amortization, post-default interest rates and mandatory arbitration clauses would be appropriate for high cost loans?*

One instance in which negative amortizing loans can be advantageous to the borrower is the case of graduated payment mortgage loans that allow borrowers, to grow into their mortgage payment over time.

Balloon payment loans can provide benefit to the borrower by providing a lower rate than a fully amortizing loan. Additionally, due to certain state restrictions on prepayment fees on loans which are not originated directly with the customer by the OTS regulated lender (but rather originated by state regulated mortgage brokers), balloon loans, as a type of "Alternative Mortgage Transaction" under the Parity Act, are one type of loan which allows the lender the opportunity to include a prepayment fee on the loan and provides the borrower with a loan at a rate that might not otherwise be available.

6. *Should OTS require lenders to determine the suitability of a mortgage loan product for a particular borrower?*

The ability of the customer to repay the requested loan is a critical consideration, equally, if not more essential to the loan decision procedure than the borrower's credit history or the quality of the collateral. Such a requirement in a level playing field would be appropriate.

One problem that is probably unique to subprime lending is that consideration of a borrower's ability to repay, and an initial determination that the borrower does not qualify, often results in a loan exception, such as a debt-to-income exception, which ultimately results in a higher interest rate and higher monthly payments for the borrower.**

7. *Should OTS require lenders to determine the suitability of a mortgage loan product for a particular applicant?*

Whether conforming, prime, high-cost or sub-prime loans OTS regulated lenders are required by regulation to have and follow underwriting guidelines and standards. Borrowers in subprime or high-cost loan markets may have limited access to general financial and mortgage specific information. They should be encouraged to seek additional information and guidance on loan choices prior to loan closing. This will enable borrowers to make an informed decision, and to preserve the objective of the OTS in creating a lending environment of negotiation between the lender and an informed borrower.

8. *Is Differential Regulation appropriate?*

OTS regulations in this regard that do not reach state-regulated housing creditors would potentially result in a "playing field" that is not level. Presently, the OTS should have sufficient regulations and guidance to monitor the activities of its regulated entities in this area of lending.

9. *How should OTS deal with potential lending issues raised by thrift subsidiaries or affiliates?*

The OTS presently has significant supervisory and regulatory authority over thrifts and their subsidiaries, additional regulation is not warranted and the OTS through the ANPR has not provided instances where increased regulations may be of benefit.

10. *Should OTS impose certain due diligence requirements?*

We believe that the OTS presently has sufficient and significant opportunities to address the concerns through present regulations, interagency guidance and a regular examination process. To impose any such due diligence requirement while seeming to be reasonable and appropriate (to the extent that such a requirement advances the safety and soundness objectives of the OTS and does not unduly restrict the lender's ability to diversify its asset portfolio through secondary market acquisitions), its potential impact may well be to cause OTS regulated institutions to become *de facto* regulators of the loan correspondents and brokers with which it does business.

The Bank appreciates the opportunity to comment on the Issues raised by the ANPR. Should you have any questions regarding this letter, please contact the undersigned at 1-800-553-8981, extension 5382.

Very truly yours,

Daniel J. Tredent
Senior Vice President
Charter One Bank, F.S.B
Consumer Lending
and
Chief Executive Officer
Charter One Credit Corporation