American Bankers Association
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October 25, 2010

Ms. Jennifer J. Johnson
Secretary, Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Docket No. R-1392, RIN No. AD 7100-AD54

Dear Ms. Johnson:

The American Bankers Association (ABA) welcomes the opportunity to provide comments on the Board's proposal regarding jumbo loans and mandatory escrow requirements, amending Regulation Z, as published in the Federal Register, Vol. 75, No. 185, on Friday, September 24, 2010. The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $13 trillion banking industry and its two million employees. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities.

In response to section 1421 of the Dodd-Frank Act (hereinafter "Dodd-Frank" or "DFA"), the Board proposes a higher threshold for mandatory escrow accounts for mortgage loans that exceed the maximum allowable purchase price by Freddie Mac and Fannie Mae. Accordingly, "for a transaction with a principal balance at consummation that exceeds the maximum principal obligation in effect as of the date the transaction's interest rate is set for such a transaction to be eligible for purchase, by Freddie Mac pursuant to Section 305(a)(2) of the Federal Home Loan Mortgage Corporation Act, 12 U.S.C. 1454 (a)(2), the coverage threshold [for mandatory escrow] shall be 2.5 or more percentage points greater than the applicable average prime offer rate."[1]

The Board initially amended Regulation Z, section 226.35 under the authority of the Home Ownership and Equity Protection Act (HOEPA), at which time, among a number of other things, the Board defined "higher priced loans" and established as a threshold for mandatory escrow—those loans with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 percentage points for loans secured by a first lien on a dwelling.[2] ABA commented on the Board's proposed rule in Docket No. R-1305 in April 2008, and provided further comment in August 2008, in Docket No. R-1321, amending rules for reporting pricing information on higher priced loans.[3] ABA additionally

[1] Proposed section 226.35(b)(3)(v), Federal Register/ Vol. 75. No. 185, 58508.

[2] 12 CFR Section 226.35.

[3] See ABA Comment dated April 8, 2008, Docket No. R-1305, and ABA Joint Comment (filed collectively with American Financial Services Association, the Consumers Bankers Association, The Consumer Mortgage Coalition, and the Mortgage Bankers Association), dated August 29, 2008.

wrote a letter to the Chairman in November 2009, regarding the practical market impact of the Regulation Z amendments.

Implementation of Proposed Section 226.35 (b)(3)(v)

As indicated above, ABA has long held the position that jumbo loans should be considered separately from, or at the very least have a different average prime offer rate spread than, defined higher priced mortgages when determining threshold application of mandatory escrow requirements. The proposed relief notwithstanding, ABA is concerned about the piecemeal approach being taken by the Board as to section 1461 and other mortgage related provisions of the DFA, and the overall compliance cost issues that banks will confront as future mortgage regulations are put into place.

As you are aware, the regulatory framework affecting mortgage lending has been undergoing intense reformation for the past two years, and the DFA will add additional restructurings, including a wholesale reorganization to integrate the Truth in Lending Act (hereinafter "TILA") and the Real Estate Settlement Procedures Act (hereinafter "RESPA") rules. These changes are significant, and there is a very real risk that intermittent and uncoordinated rulemaking will overwhelm lender systems.

Without question, banks will have to make changes to their internal systems based on the relief given under the proposed rule. However, it is anticipated that banks will be required to make similar and additional changes to those same systems, many times over, due to future rule drafting in response to passage of the DFA, including those rules that will be promulgated by the Consumer Financial Protection Bureau. It is imperative that the Board fully appreciate the cost and regulatory burden associated with not coordinating and harmonizing the finalization of all rules related to escrow, higher priced mortgage loans and RESPA, inasmuch as would be allowed under the DFA.

Evidence of anticipated regulatory burden associated with disharmonized rulemaking is apparent in the provisions of section 1461 of the DFA on which the Board is not issuing rules at this time.[4] In section 129D(h), the DFA identifies mandatory disclosure requirements associated with higher priced and jumbo loans. However, the Board in its present rulemaking has chosen not to amend TILA or RESPA escrow disclosure requirements in coordination with its proposal to amend section 226.35, although the new DFA disclosure mandates are different than what exist in present regulations.

Another example is found in section 129D(d) governing the duration of mandatory escrow accounts. TILA presently provides that a borrower may cancel a mandatory escrow account, but not sooner than 365 days from consummation of the original mortgage. Dodd-Frank provides a different requirement, increasing the period of mandatory escrow to five years, unless and until

[4] See section 129D(c)- Exemptions; 129D(d)- Duration of Mandatory Escrow; 129D(g)- Administration of Mandatory Escrow; 129D(h)- Disclosure Related to Mandatory Escrow; Section 1461(b)- Exemptions and Modifications. Also see Section 1462 of the DFA- Disclosure Notice Required for Consumers Who Waive Escrow, et al.

identified events occur, such as the borrower's having sufficient equity in the dwelling securing the transaction.[5]

Additionally, section 1461 grants the Board authority to exempt certain creditors from the mandatory provisions and additional broad authority to make changes to section 129D(b), if the Board determines such changes would be in the public interest.[6] It only makes sense that the Board would also identify the exemptions and changes it recommends related to section 129D at the same time it drafts the rule governing the threshold average-price offer rate (APOR) spread that would trigger mandatory escrow for jumbo loans, including further consideration for exempting those lenders that portfolio their mortgages. This would allow banks to comply with all regulatory changes in an economical and efficient manner. As it presently stands, banks will make changes pursuant to the existing proposal, and later make additional changes based on the exemptions. This will lead to training and regulatory compliance costs that could have otherwise been avoided, which will result in higher costs for consumers.

Most troubling is that the Board also proposes to change the metric for identifying higher priced mortgage loans.[7] The Board proposed the metric change on the same date it requested comments on amending the escrow threshold for jumbo loans. In the former, the Board stated in its supplementary information, " [t]he Board recognizes that any new metric would impose some costs, including training staff and modifying software and other systems." The supplementary information continues, "[t]he Board believes, however, that these costs should be relatively small because the proposal would necessitate only a one time modification to creditors' systems." However, if the implementation date of the proposed metric change is not appropriately coordinated with other changes to those same systems, including changes associated with mandatory escrow for jumbo loans, what the Board identifies as minimum costs could indeed become monumental for both creditors and consumers alike.

While lenders can easily make changes to their systems pursuant to some of the provisions of Dodd-Frank, there is no guarantee that a lender's interpretation will coincide with the Board's or Bureau's later interpretive rule drafting. In fact, to best ensure legal compliance and be protected from liability, banks are not likely to *sua sponte* make preemptive systematic and operational changes on a regulatory feature on which the Board or Bureau are likely to promulgate rules.

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[5] Section 129D(d) of section 1461 of the DFA specifically provides that the requisite mandatory escrow accounts shall remain in existence for a minimum of five years, beginning with the date of loan consummation, unless and until "(1) such borrower has sufficient equity in the dwelling securing the consumer credit transaction so as to no longer be required to maintain private mortgage insurance; (2) such borrower is delinquent; (3) such borrower otherwise has not complied with the legal obligation, as established by rule; or (4) the underlying mortgage establishing the amount is terminated.

[6] See section 129D(c) of section 1461 of the DFA and section 1461(b) of the DFA.

[7] See Proposed Rule to amend Regulation Z, Truth in Lending, Docket No. R-1390, Federal Register/ Vol. 75 No. 185, September 24, 2010, 58661.

Section 1461 of the Dodd-Frank Act

Section 1461 of Dodd-Frank, among other things, codifies in statute the definition of higher priced and jumbo mortgages, and establishes the requirement for mandatory escrow accounts associated with loans that meet the requisite definitions. Some readers of section 1461 have suggested that the statutory language places a mandatory escrow on all mortgages; however, this is not how ABA understands the intent of the drafters. Section 1461 specifically limits mandatory escrow only to those mortgages that meet the definition of higher priced loans as defined in section 129D(b)(3)(A), and TILA section 226.35, and to mortgages that meet the criteria in 129D(b)(3)(B), and the proposed rule to amend TILA, section 226.35(b)(3)(v), with exceptions, as identified in section 1461 of the DFA. ABA requests that the Board make clear in its final rule that it does not interpret section 1461 to place a mandatory escrow requirement on all mortgages.

Additional clarification is required in that section 129D(b)(3)(B) of the DFA identifies loans that exceed the maximum limitation "*pursuant to the sixth sentence of section 305(a)(2) [of] the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1454(a)(2)*" as those loans which require mandatory escrow.[8] The "*sixth sentence*" refers specifically to the base conforming limits (BCL). Subsequent sentences in paragraph (2) refer to methods used when making adjustments to the BCL, and further define when super conforming limits (SCL) are applicable. However, when drafting the proposed rule, the Board did not distinguish between the *sixth sentence* and subsequent language in paragraph 2 of section 305(a). ABA asks that the Board make clear whether it intends to apply mandatory escrow to those loans that exceed the BCL, as could be interpreted from the DFA, or also to those loans that exceed the SCL.

Implementation Period

Due to the necessary system changes and related training in response to the proposed TILA amendments, ABA recommends that the Board not opt for an immediate effective date following issuance of the final rule. ABA again urges that the Board place very high priority to the proper coordination of the various regulatory components inherent in the regulatory reforms mandated by the DFA. However, should the Board select to proceed with the proposed rule, ABA estimates that banks will require at least a six-month period to provide full compliance. ABA further requests that should the Board propose additional rules regarding section 1461 of the DFA prior to the six-month implementation date, the Board delay section 226.35(b)(3)(v) implementation to coincide with future section 1461 effective dates. In the alternative, the Board should allow for voluntary compliance of the proposed rule, until such time of the effective date of all required rules under section 1461 or when section 1461 becomes effective by law, whichever is first. The Board should further ensure harmonization of all rules under the DFA that directly or indirectly impact compliance of proposed section 226.35(b)(3)(v). This result would address some of the concerns about piecemeal implementation of mortgage regulations.

[8] Emphasis added.

The Board should also be certain to ensure that the implementation date is after July 21, 2011, the earliest possible effective date of subtitle D of Title X, governing preservation of state laws. As the Board noted in its supplemental information, some jurisdictions may prohibit mandatory escrow, or possibly assign differing disclosure requirements to escrowed loans. While such provisions or prohibitions might be preempted by federal regulations prior to July 21, 2011, it would seem that these state laws may not be preempted after that date. The requirement to amend systems prior to the effect of the preservation of state laws and to then again make system adjustments after, should be avoided.

Conclusion

ABA thanks the Board for providing an opportunity to comment on proposed amendments to TILA, section 226.35(b)(3)(v). In prior comments, ABA has proposed that the Board view jumbo loans different than and outside of the definition of higher priced mortgage loans. The proposed rule to amend section 226.35 of TILA is a positive step in addressing the concerns of ABA and banking industry. However, isolating section 226.35(b)(3)(v) amendments from other provisions of the DFA, including other provisions within section 1461, will result in more burden than benefit.

ABA respectfully requests that the Board seriously consider delaying mortgage lending rulemaking on all aspects of the DFA, until such time that rulemaking under the DFA can be sufficiently harmonized, inasmuch as this is practical under DFA statutory effective dates. Alternatively, ABA requests that the Board allow for voluntary compliance with section 226.35(b)(3)(v) until such time that DFA compliance is required by statute or when all mortgage lending rulemaking has been harmonized, whichever comes first. At the very least, the Board should indentify an implementation period that provides the least burden to creditors and greatest of benefits to consumers.

Thank you for the opportunity to comment on this important matter. Should you have any questions, please contact the undersigned, or Rod Alba at 202-663-5592 or ralba@aba.com, or Vincent Barnes at 202-663-5230 or vbarnes@aba.com

Sincerely,

Robert R. Davis