October 9, 2000

VIA FACSIMILE AND OVERNIGHT MAIL.

Mr. Thomas J. Curry
Commissioner of Banks
Massachusetts Division of Banks
One South Station
Boston, Massachusetts 02110

RE: Proposed Massachusetts High Cost Home Loan Provisions Comment

Dear Mr. Curry:

We appreciate the opportunity to comment on the Massachusetts Division of Banks' (the "Division") proposed amendments to 209 CMR 32.00: Disclosure of Consumer Credit Costs and Terms and 209 CMR 42.00: The Licensing of Mortgage Lenders and Mortgage Brokers; and the adoption of proposed new regulations at 209 CMR 40.00: Unfair and Deceptive Practices In Consumer Transactions. This comment letter is submitted on behalf of Option Mortgage Corporation and its wholly owned subsidiary H&R Block Mortgage Corporation, each of which is licensed and regulated under the auspices of the Division in the provision of mortgage loan products to its clients within the Commonwealth of Massachusetts.

We share in the Division's concern over predatory lending abuses and concur with the common goal of eradicating such abuses. We are aware that such abuses exist, but we do not believe, and no evidence has been presented to suggest otherwise, that such abuses extend beyond a minority of participants. Moreover, it is clear that these participants effectively operate within the current regulatory schemes, which are intended to combat predatory abuses. Although success has been fruitful when enforcement actions have been initiated under the current regulatory schemes, we do not believe that this method has been employed to its full potential. In its stead, both federal and state authorities have determined a better method of curbing predatory abuses is to implement additional regulations aimed not at the participant minority, but to the mortgage finance industry as a whole. As to certain aspects of the Division's proposed regulations, we believe that with vigilant enforcement, our common goal will be advanced. Other aspects, however, may unwittingly limit a borrower's choice between a responsible lender and a predatory lender, and have an inapposite effect on the Division's stated intent not to

regulate or restrict responsible forms of lending. With this perspective in mind, we submit the following recommendations regarding selected provisions of the Division's proposed amendments.

209 CMR 32.32 (1)(a)1.c.

In determining whether an adjustable rate mortgage loan is a "high cost home loan" covered by Section 32.32 (1)(a)1, the proposed regulations require the creditor to calculate the annual percentage rate ("APR") threshold using "the interest rate that would be effective once the introductory rate has expired." In its Summary of 209 CMR 32.32 (1), the Division writes "...the threshold computation is to be based upon the fully indexed ARM rather than an introductory or "teaser" annual percentage rate." Our concern with this statement is that the APR calculation already takes the fully indexed rate into consideration. On a discounted ARM, the annual percentage rate is a composite rate, which fully considers the effect of adjustment from the initial rate to the fully indexed rate (based on today's index value). Because the initial rate is usually in effect for a short time period relative to the term of the loan, the fully indexed rate has a much greater impact on the APR than does the initial rate.

We believe that the current regulatory framework already provides adequate disclosure of the relationship between an introductory interest rate and the fully indexed rate. The payment schedule on the disclosure required by 209 CMR 32.18 (7) discloses payments at the initial rate as well as increasing payments until the fully indexed rate is reached. Additionally, creditors are required today to give variable rate disclosures under 209 CMR 32.19 (2) that further disclose the fact of a discounted initial interest rate.

We recommend that the final regulations not alter the existing annual percentage rate calculation. The method suggested by the proposed regulations would result in an annual percentage rate that does not reflect the true obligation and is likely to confuse, rather than aid, the consumer in understanding the cost of credit.

209 CMR 32.32 (1)(a)2.

The proposed amendment to Section 32.32 (1)(a)2 lowers the "points and fees" threshold for determining a high cost home loan from the greater of eight percent of the total loan amount, or $400.00, to five percent of the total loan amount, or $400.00. This provision does not take into account two fundamental tenets of mortgage origination: first, that the costs incurred in originating a mortgage loan are not dependent on the loan amount; and second, that lower loan amounts are less profitable than greater loan amounts. The provision requires a creditor to make a choice as to whether it should discontinue making lower amount loans, if unable to cover its cost to originate such

loans, or to increase the rate for such loans. We do not believe that either choice benefits the consumer.

With respect to limitations on points and fees, both Fannie Mae and North Carolina have rejected the fixed percentage test and recognized the adverse impact that such limitations would have to consumers on lower loan amounts. Specifically, Fannie Mae limits its purchase of loans with points and fees exceeding five percent of the loan amount, unless "the limitation would result in an unprofitable origination for the lender." In its predatory lending legislation, North Carolina adopted a tiered threshold approach which limited points and fees on loans over $20,000 to five percent; on loans $20,000, or less, to the lesser of eight percent of the loan amount or $1,000. We recommend that the final regulations provide for a tiered threshold approach, which would continue to allow lenders to provide such credit, while accommodating the costs of origination on lower loan amounts.

209 CMR 32.32 (6)(1)(a).

With the elimination of the exclusion from Section 32.32 for "residential mortgage transactions," the limitations of Subsection a on the financing of points, fees or charges assume a prominent role in a consumer's decision to purchase a home. Among other restrictions, this provision prohibits creditors from directly or indirectly financing points and fees payable to the creditor and certain charges payable to third parties, in an amount exceeding five percent of the loan amount. Beyond being coincident with the five percent threshold for points and fees in determining a high cost home loan, this limitation appears to have been arbitrarily selected. Each of the two calculations is separately and distinctly defined. The primary concern, however, should be this provision's removal of decision making authority from a consumer in financing an otherwise permitted mortgage transaction. Under the proposed provision, the bar to homeownership is no longer simply the consumer's understanding and personal assessment of the suitability of a high cost home loan, but now the imposition of a cash requirement. In addition to those consumers who are "cash-poor," this provision would adversely effect those consumers who simply decide that their accumulated cash is better spent or saved elsewhere, such as in home improvements or investments. We recommend that the final regulations exclude residential mortgage transactions from the reach of this provision.

209 CMR 32.32 (6)(f).

Our comment to Subsection f applies generally to the scope of Section 32.32. The introductory summary to 209 CMR 32.32 (6) states, in part, that "this section identifies and proscribes 13 predatory lending practices as unfair high cost home loan acts and

practices." Specifically, the proposed Section (6)(1) states, in part, that "(i)t is an unfair act or practice for a creditor to engage in any of the following for any transaction subject to 209 CMR 32.32." (emphasis added). Subsection f prohibits a creditor from "(m)aking a high cost home loan with rates or fees that violate 940 CMR 8.06 ... or otherwise charge interest rates or fees ... that significantly deviate from industry standards or that are otherwise unconscionable." The provision further establishes a burden on the creditor to prove that such charges and fees do not violate this Subsection f.

We support the Division's initiative in identifying and proscribing certain recognized predatory abuses. We do not, however, understand the Division's full allocation of culpability and responsibility to creditors. To our knowledge, no evidence has been produced which exculpates the mortgage broker community or other settlement service providers from the practice of such abuses. Our commitment as an industry, and we would suggest the Division's as a regulator, should be to eradicate such abuses whenever and by whomever they are practiced. Although we recognize the Division's efforts in bringing all "licensees" under the coverage of 209 CMR 32.32 in the proposed amendment to 209 CMR 42.00, we do not believe the remedial measures set forth therein should be exhaustive. In testimony given before the U.S. House of Representatives' Committee on Banking and Financial Services, Laura J. Borrelli, Past President of The National Home Equity Mortgage Association, presented data which confirmed that mortgage brokers originate greater than fifty percent of subprime loans. This high percentage underscores the compelling argument that mortgage brokers should be subject to these regulations and not simply policed by the creditors with whom they do business.

As drafted, Subsection f is unclear as to whether the Division would require a creditor to justify the fees negotiated between a consumer and a mortgage broker, or other settlement service provider. We recommend that the final regulations more explicitly recognize that the commitment to responsible lending is not solely within the purview of the creditor, but should also be resident with every service provider, including mortgage brokers, in completing a mortgage transaction.

209 CMR 32.32 (6)(m)2.

We recognize that potential for predatory abuses to occur weighs disproportionately with those segments of the population without access to informational and educational resources. Predators are aware of the vulnerability of less sophisticated borrowers. We share in the Division's concern for these vulnerable segments of the population and we support regulatory and industry efforts to provide informational and educational resources to these segments of the population. We are concerned, however, with regulatory provisions which indirectly bar an informed borrower's access to credit.

Section 32.32 requires creditors to take or refrain from taking certain actions when making high cost home loans. This provision seemingly prohibits a creditor from taking a particular action; however, it actually requires an action – but not of the creditor. The affirmative action is required of selected individuals who are not regulated by the Division, but have simply attained the age of sixty. We hold no misconception that our seniors are immune from the prey of predators. We do, however, dispute the notion that all or a majority of seniors are unsophisticated borrowers and we bristle at that thought of having to communicate to our senior customers that we cannot accept their informed decisions. We disagree with the correlation for mandatory counseling which the Division sets forth between a reverse mortgage and a high cost home loan. A reverse mortgage is a highly sophisticated mortgage product that is designed for senior borrowers. In the unlikely event that the product becomes desirable to younger borrowers, we believe that its sophistication would warrant counseling at any age. A high cost home loan is not a mortgage product, but a function of the annual percentage rate or the applicable points and fees. It is not defined as predatory and is, in some situations, desirable to consumers regardless of age. The regulations promulgated against predatory abuses, which are sometimes associated with high cost home loans, should likewise apply, regardless of age of the consumer. We believe that seniors, even those on fixed incomes, are sufficiently protected under the Division's proposed regulations, including those protections we support at 209 CMR 32.32 (5) prohibiting "collateral based loans," without the Division subjectively determining their ability to understand and make a personal assessment of the suitability of a high cost home loan. We recommend that the Division remove the requirement for senior's counseling from the final regulations.

Finally, prior to the implementation of the final regulations, we urge the Division to develop tangible methods of measuring their effect on the flow of credit to consumers having legitimate credit needs and their effectiveness in combating predatory abuses. We believe that the lack of attention given to measuring the effects of similar regulations, such as the Homeownership Equity and Protection Act, is such regulations' failing. As previously mentioned, it is clear that predators effectively operate within the confines of the current regulatory schemes. In fact, such regulations may have increased the incident of predatory abuses in the high cost home loan market by driving out responsible lenders. We recommend that the Division not rely solely on the protections potentially afforded under the final regulations, but that it also advocate vigilant enforcement of such regulations and educational programs to assist consumers to recognize predatory practices.

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Thank you for your consideration of our comments and recommendations. If you or other members of the Division staff have any questions, we would be pleased to discuss them with you.

Respectfully submitted,

Option One Mortgage Corporation &
H&R Block Mortgage Corporation

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