February 28, 2011

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

Re: Interim Mortgage Disclosure Improvement Act Rule to Clarify Certain Provisions of the September 2010 Interim Rule [Regulation Z, Docket No. R-1366]

Dear Ms. Johnson:

The American Financial Services Association ("AFSA") appreciates the opportunity to comment on the Interim Rule proposed by the Federal Reserve Board ("Board") which implements certain requirements of the Mortgage Disclosure Improvement Act of 2008 ("MDIA"). AFSA is the national trade association for the consumer credit industry, protecting access to credit and consumer choice. Its 350 members include consumer and commercial finance companies, auto finance/leasing companies, mortgage lenders, mortgage servicers, credit card issuers, industrial banks and industry suppliers.

AFSA appreciates the Board's willingness to address the issues raised in comment letters by issuing another interim final rule. We ask that the Board consider a few additional issues before implementing a final rule.

Payment Schedule

AFSA takes this opportunity to reiterate a few comments from our previous letter that we feel are particularly important. We respectfully request that the Board give lenders the option to use the new disclosure for fixed-rate loans to supplement the current Section 226.18(g) payment schedule, rather than replace it.

The Interim Rule replaces the payment schedule with a new interest rate and payment summary table for a transaction secured by real property or a dwelling, other than a transaction secured by a consumer's interest in a timeshare plan. The current payment schedule is well-understood by, and very important to, consumers because consumers can use the disclosure to see the exact number of payments, the amount of payments, and the date payments are due, in a very simple format. Eliminating that clear payment schedule for fixed rate (and especially amortizing) loans is unnecessary and will create confusion for consumers. These loans were not implicated in the mortgage crisis in any way. Because the current payment schedule is so helpful to consumers, lenders will likely want to continue providing it, but will now have to do so outside the "TILA Box." This will add more disclosure for consumers at a time when everyone, regulators and lenders, is working toward simplification.

Also, under Section 226.23, the payment schedule is a "material disclosure." The failure to disclose the schedule of payments, which has been taken out of the TILA Box in the Interim Rule, therefore subjects the creditor to possible rescission of the transaction for failure to provide (see footnote 48 of Section 226.23).

Additionally, there are many creditors who currently use the same Regulation Z "TILA Box" for both closed-end transactions that are secured by real property or a dwelling ("real estate secured transactions") and other non-real estate secured transactions. The impact of this Interim Rule is even greater on these creditors than on those who only make real estate secured transactions. These creditors will now have to program their systems to select the correct TILA Box disclosure, based on the types of security taken. Something as simple as no longer allowing the number of payments in the TILA Box for a real estate secured transaction is problematic for those creditors whose only reference in their forms to the number of payments and the amount of the payments is in the schedule of payments currently contained in the TILA Box. For those state-licensed creditors with that issue that do business in multiple states, not only will the Interim Rule impact the TILA Box disclosure, it will require most of their real estate secured loan agreements to change, requiring review of all loan agreements for real estate secured transactions and changes to all of those loan agreements for real estate secured transactions.

Buydowns

The Interim Rule has triggered concerns among a number of creditors and investors regarding how to disclose a loan that includes a temporary rate or payment buydown feature. As a result of those concerns and the risks attached to disclosing these programs incorrectly, many creditors and investors have decided not to offer or purchase loans that include a buydown feature until the rules are clarified.

In a buydown program, someone contributes a sum at the closing that the creditor deposits in a buydown account. The creditor agrees to apply a portion of the buydown funds to supplement the consumer's scheduled payments for a limited period of time, typically, the first two or three years of the loan. At the end of the buydown period, the consumer must pay the full scheduled payment amount. Buydown programs are useful to consumers because they reduce the consumer's monthly payment for a period of time while not subjecting the consumer to a balloon payment or negative amortization at some later time. Under a typical three-year buydown agreement, the consumer's scheduled payment increases at the end of each year by specified amounts. From the consumer's perspective, the loan looks like a step-rate loan or a fixed-rate, graduated payment loan.

The current rules on when to reflect a buydown program in the payment disclosures are outdated and do not seem helpful or useful to consumers. Under Paragraphs 17(c)(1)-3 through

5 of the Commentary, a creditor is required to reflect the buydown program in the payment disclosures if the consumer pays the buydown account funds at the closing. However, a creditor is required to ignore the buydown feature when preparing the same payment disclosures if the creditor or a third party (for example, a seller) pays the buydown account funds at the closing, unless the buydown agreement modifies the note rate. Most buydown agreements do not modify the note rate. Some disclose an "effective rate" or a "payment rate," but those rates simply reflect the rate that would have been in place if the loan was a true step-rate transaction and the consumer's portion of the scheduled payment was all that was owed under the note. In fact, under most buydown agreements, interest continues to accrue at the full note rate during the buydown period. For example, if a consumer paid the loan in full, the final payment amount would be determined based on the note rate and not the "effective rate" or "payment rate" in effect under the buydown agreement. As a result, the payment disclosures received by a consumer are radically different on transactions that, to the consumer, are the same transaction. We doubt that a consumer would understand why the payment disclosures are different. More to the point, we do not believe the differences are helpful to a consumer attempting to compare the programs. From the consumer's perspective, these transactions are the same. They each result in a step-rate or graduated payments during the buydown period. As a result, we believe that the longstanding rules on when buydown programs should be reflected in the payment disclosures should be simplified so that the information the consumer receives is the same regardless of who pays the buydown funds or whether the buydown agreement modifies the note rate.

Under the new rules in Section 226.18(s), a loan is disclosed as an adjustable rate transaction if the APR can increase after consummation. A loan must be disclosed as a step-rate transaction if the interest rate will change after consummation and the rates that will apply and the periods for which they will apply are known at consummation. If a loan is not an adjustable rate or a step-rate loan, then it must be disclosed as a fixed-rate transaction. As discussed above, most buydown programs do not change the interest rate owed under the note. As a result, the typical buydown agreement is not a step-rate transaction under this definition (the "interest rate" does not increase at specified times and by specified amounts). It is less certain whether the loan would be an adjustable rate transaction under the rule. If the borrower is the source of the buydown funds, a creditor is required to take the graduated payments into account when preparing the payment disclosures even if the note rate does not change. In that circumstance, some people believe that the annual percentage rate on the loan may increase (because the borrower's portion of the payments will increase) and some people believe it may not (because the interest rate and the total monthly payment never change). Others believe that the loan is a step-rate loan because the "effective rate" changes at specified times and by specified amounts.

Regardless of which analysis is correct, it strikes us that the current rules are unnecessarily confusing for creditors and unhelpful to the consumer. We suspect that if anyone ever sat the consumer down and showed the consumer the various ways buydown programs are required to be disclosed under the Interim Rule, the consumer would throw up his hands in frustration that the disclosures vary so wildly when the transactions are fundamentally the same to the consumer. As a result, we ask you to consider modifying the rules under Section 226.17(c)(1) and/or 226.18(s) so that creditors have clear instructions on how these transactions should be disclosed in the Interest Rate and Payment tables and so that consumers will receive consistent payment disclosures for buydown programs regardless of who pays the buydown funds or whether the buydown agreement modifies the note rate. It strikes us that the alternative that would provide the most meaningful information to consumers would be that the buydown plan be included in the definition of a step-rate transaction.

Conclusion

AFSA thanks the Board for the opportunity to comment on the Interim Rule and commends the Board for its work in protecting consumers. Please feel free to contact me with any questions at 202-296-5544, ext. 616 or bhimpler@afsamail.org.

Respectfully submitted,

Bill Himpler

Bill Himpler
Executive Vice President
American Financial Services Association