



July 22, 2011

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-1417: Regulation Z; Truth in Lending (RIN 7100-AD75)

Dear Ms. Johnson:

On behalf of the state Housing Finance Agencies (HFAs) it represents, the National Council of State Housing Agencies (NCSHA) appreciates the opportunity to comment on the Federal Reserve Board's May 11, 2011 proposal to amend Regulation Z. NCSHA urges you to provide enough flexibility in the final rule to ensure that lenders are able to offer a wide range of appropriate and responsible financing vehicles to potential home buyers. We also request that you exempt HFA-financed subordinate loans from the rule's requirements for the reasons put forward below.

HFAs issue mostly tax-exempt bonds to finance affordable housing for home buyers and renters. HFAs also administer a wide range of affordable housing and community development programs, including the Low Income Housing Tax Credit, HOME, Section 8, down payment assistance, homebuyer education, loan servicing, homeless assistance programs, and state housing trust funds.

We generally concur with the proposed rule's ability-to-repay standard and support the inclusion of the proposed standard's eight underwriting components. They are all integral to a sound assessment of mortgage default risk.

We urge you, however, as you prepare the final rule, to provide enough flexibility to allow for a common-sense underwriting review. Such a review takes into account and evaluates the totality of a borrower's circumstances and the interaction of the various risk factors as a whole, including compensating factors.

We are pleased the proposed rule does not impose specific quantitative standards for these underwriting components. If, as the rule's explanation suggests, you are considering establishing quantitative standards for these components, we urge you to retain flexibility and avoid rigid limits or formulas that would exclude borrowers on the basis of one or a few factors based on such standards.

#### **Increase Points and Fees Flexibility**

NCSHA recommends an increase in the proposed rule's limit on per-loan points and fees to at least 3.5 percent of the loan amount for small loans, with a definition of small loans that includes loans greater than \$75,000. Without such relief, lenders that cannot cover their costs or achieve a reasonable

return on their efforts may refrain from originating smaller loans and thus restrict credit to important potential consumers. We also recommend that loan size limits be adjusted annually to reflect inflation.

We further recommend that federal regulators exclude discount points from the points and fees calculation. These are points the borrower pays voluntarily in exchange for a lower interest rate.

### **Expand Exemption for Loans in Rural and Underserved Areas**

We also urge you to consider expanding the proposed rule's exemption for creditors operating predominantly in rural and underserved areas to facilitate greater extension of credit to potential home buyers in these hard-to-serve areas. We particularly recommend broadening the definition of rural so more areas classified as rural under the Department of Agriculture's rural home loan programs are eligible for the proposed rule's relief.

### **Expand Exemption for Subordinate Loans**

NCSHA also urges federal regulators to take advantage of the opportunity this rule presents to codify and expand an exemption for subordinate loans HUD established last year. On October 6, 2010, HUD Secretary Donovan issued a memorandum exempting certain HUD program-assisted subordinate loan transactions from the requirements in sections 4 and 5(c) of the Real Estate Settlement Procedures Act of 1974 (RESPA). We urge you to expand this exemption to all HFA-financed subordinate loans and to modify the exemption's criteria as described below.

NCSHA appreciates HUD's efforts to exempt certain subordinate loan transactions from the burdensome and unnecessary requirements outlined in sections 4 and 5(c) of RESPA. However, many HFAs have indicated that the exemption may fail to meet HUD's objectives because the majority of the subordinate loans offered under HFA-assistance programs fail to meet some of the exemption's eligibility criteria.

In order for a subordinate loan to qualify for the RESPA exemption, "Requirement E" in the exemption notice states that, "the total of settlement costs assessed to the recipient for the subordinate loan [must be] less than 1 percent of the amount of the subordinate loan and includes, at most, charges for the following items: recordation fee; application fee; and/or housing counseling fee." Most subordinate loans offered under HFA-assistance programs cannot meet this requirement.

The total settlement costs assigned to recipients of subordinate loans under HFA-assistance programs vary, but they are typically low and affordable. Despite this, they can still easily exceed 1 percent because most subordinate loans HFAs finance are small.

Many of the settlement costs associated with subordinate loans offered under HFA-assistance programs are state or county recording or documentation fees or taxes. These recording or documentation fees or taxes typically cannot be modified by HFAs, as they are determined by state or municipal laws or regulations. Because these modest and reasonable fees or taxes cannot be controlled by HFAs, we feel it is unfair and inappropriate to include them in the exemption's eligibility criteria.

If excluding these fees and taxes from the eligibility criteria is not possible, we ask the exemption extend to loans that include "customary and reasonable fees" or for an increase in the maximum allowable level of settlement costs required to qualify for the RESPA exemption from "less

than 1 percent of the amount of the subordinate loan,” to at least, “less than 3.5 percent of the amount of the subordinate loan.”

Another cost included in the exemption language’s definition of “settlement costs” is the lender application fee. Lender application fees are typically negotiated between HFAs and their lending partners. While they are usually minimal, they allow lenders to receive a small fee for their services, which is necessary to provide an appropriate incentive for lender participation and to facilitate a productive and healthy HFA-lender partnership. If HFAs attempt to modify or eliminate these fees, they risk losing important lending partners and restricting the flow of credit to responsible home buyers.

Additional costs that are not explicitly included in the exemption language’s definition of “settlement costs,” but which require further clarification, are the fees associated with the non-industry standard processing and inspection requirements of subordinate liens offered under the HOME program. Federal HOME regulations require a property inspection and an environmental review of properties that HOME program recipients receive subordinate loans to purchase. Most HFAs allow lenders to charge program recipients processing and inspection fees to help cover the costs required to comply with federal HOME requirements. It is unclear if the processing fees or the property inspection fees are considered application fees under the exemption language’s definition of “settlement costs.” NCSHA recommends that these additional costs be allowed on exempted loans.

NCSHA also believes that HUD, the Federal Reserve Board, or the Consumer Financial Protection Bureau, as appropriate, needs to clarify how the RESPA exemption impacts the HUD-1 settlement statement for the primary mortgage. HFA lending partners have indicated that because there are settlement expenses associated with the second mortgage, “Requirement F” of the exemption language would obligate them to provide a HUD-1 settlement statement for the second mortgage. If lenders are required to provide a HUD-1 settlement statement for the second mortgage, the RESPA exemption would be useless. NCSHA requests that the exemption notice explicitly state that any fees associated with a subordinate lien that are included in the exemption language’s definition of “settlement costs” should be reported on the HUD-1 settlement statement for the first mortgage.

Thank you for your consideration. We would be happy to discuss these issues with you at your convenience.

Sincerely,

A handwritten signature in black ink, appearing to read "Garth B. Rieman", with a long horizontal flourish extending to the right.

Garth B. Rieman  
Director, Housing Advocacy and Strategic Initiatives  
National Council of State Housing Agencies