***Submitted electronically***

February 25, 2013

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Re: Proposed Amendments to the Ability to Repay Standards under the Truth in Lending Act (TILA) and Regulation Z [Docket No. CFPB-2013-0002]

Dear Ms. Jackson:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the proposed rule published by the Consumer Financial Protection Bureau (CFPB) regarding the ability-to-repay mortgage standards required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). The CFPB adopted final rules implementing the ability-to-repay requirements on January 10, 2013. However, the CFPB stated that it believes several exemptions and modifications to the ability-to-repay requirements may be appropriate. The CFPB is also proposing two alternative

[1]The Independent Community Bankers of America®, the nation's voice for more than 7,000 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services.

With nearly 5,000 members, representing more than 24,000 locations nationwide and employing more than 300,000 Americans, ICBA members hold more than $1.2 trillion in assets, $1 trillion in deposits, and $750 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

comments to clarify the calculation of points and fees in a transaction involving loan originator compensation.

On May 11, 2011, the Federal Reserve published for notice and comment a proposed rule amending Regulation Z (Truth in Lending Act) to implement amendments made by the Dodd-Frank Act. The proposed rule addressed new ability-to-repay requirements that will apply to consumer credit transactions secured by a dwelling, and defined "qualified mortgages" that would be exempt from the ability-to-repay underwriting requirements. The Dodd-Frank Act transferred regulatory rule writing authority over this rulemaking to the CFPB on July 21, 2011. The original comment period to the proposed rule closed on July 22, 2011, but the CFPB reopened the comment period until July 9, 2012, to seek comment on several issues pertaining to loan underwriting and potential litigation risk for lenders. The CFPB published final rules on the proposal on January 10, 2013, but is seeking comment on additional changes to these rules.

**General Comments**

In general, ICBA is pleased that the final rule provides some flexibility for community banks to continue to offer mortgage loans, including balloon mortgages, to the consumers in their communities. ICBA also supports the proposed rule's creation of a new category of community bank qualified mortgages with additional flexibility for community banks. This flexibility reflects the Bureau's recognition of the key role that community banks play in providing credit safely to consumers who otherwise might not obtain credit from a large national lender which relies on selling loans into the secondary market. As the Bureau states in the preamble to the proposed rule:

> *The Bureau is proposing these changes because it believes they may be necessary to preserve access to responsible, affordable mortgage credit for some consumers. Small creditors are a significant source of loans that, for various reasons, do not qualify for government guarantee and insurance programs and cannot be sold for securitization. Larger creditors often are unwilling to make these loans because they involve consumers or properties with unique features that make them difficult to assess using larger creditors' underwriting standards or because larger creditors are unwilling to hold the loans in portfolio. Small creditors often are willing and able to consider these consumers and properties individually and to hold the loans on their balance sheets. Small creditors also may be the predominant source of credit in many rural areas where large creditors do not operate*.

ICBA remains concerned, however, that the exemptions and exceptions for community bank loans, particularly for balloon payment mortgage loans, do not cover nearly enough community banks and could end the mortgage business for many community banks across the country. It's important to note that community banks have always been responsible home mortgage lenders and did


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not participate in lending abuses that drove financial crisis. However, in a quest to prevent the events of the past from happening again, these laws and regulations developed to address the abuses of the past will force some community banks out of the mortgage lending business and reduce access to credit for their customers. Balloon payment mortgages have been originated safely and prudently for decades by local community banks and for many consumers these loans offered by community banks are the only way for them to buy or refinance a home.

ICBA understands and appreciates the enormous job the CFPB had in drafting these final rules. Nevertheless, we are concerned that stringent regulatory requirements will disable community banks from being able to effectively provide mortgage loans, by restricting the availability of balloon payment mortgages, for consumers in their communities. The costs associated with increased litigation risk and compliance will lead many community banks to exit the consumer mortgage business altogether. The following comments received from a recent ICBA survey are typical of concerns raised by community bankers:

> W*e are very concerned about what we are going to do. Our options appear to be make no consumer mortgages, or offer ARMs instead of balloons and worry about the threat of lawsuits. We are in a rural area but our county which is very large has a big city in it, St. Cloud.*
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> *. . . . . . .*
>
> *Because of the increased regulatory burden related to mortgage lending, we no longer do mortgage loans; we exited the market in March 2012.*

Federal Reserve Governor Elizabeth Duke discussed the unique role that community bank mortgage lending provides in a speech in November of 2012:

> *Community banks have long been a source of loans that, for a variety of reasons, do not fit the parameters of conforming government-sponsored enterprise loans or eligibility for government-guaranteed programs. Community banks typically hold these loans on their balance sheets. They use higher interest rates to compensate for the lack of liquidity in these loans or to cover higher processing costs because community banks lack economies of scale, and they use balloon payments as a simple way to limit their interest-rate risk. To the extent that regulations require additional operational procedures for such loans that are prohibitively expensive, raise the liability associated with making them, or create capital requirements that are out of proportion to the riskiness of the loans, community banks could be closed out of these products altogether.*[2]

[2] Community Banks and Mortgage Lending, Speech by Federal Reserve Governor Elizabeth Duke at the Community Bankers Symposium, Chicago Illinois, November 9, 2012.



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This result will leave many consumers without access to mortgage credit as the large national financial institutions do not provide the type of portfolio mortgage loans necessary to address the unique properties and personal financial situations that a balloon payment mortgage does from a local community bank. For these customers, who do not meet secondary market criteria either due to their personal situation or the characteristics of the property to be mortgaged, a balloon loan from a community bank may be their only financing option. As such, we urge the Bureau to carefully consider our comments in this letter and make the appropriate changes to the ability-to-repay rule, so that community banks can continue to lend, and serve their customers and communities.

## Summary of ICBA's Recommendations

The following are ICBA's recommendations regarding the proposed rule as well as recommendations for adjustments to address other provisions of the final ability-to-repay rule.

- Expand the definition of qualified mortgage to include additional loans held in portfolio by small creditors, including balloon payment mortgages originated by small creditors in non-rural markets;
- Increase the limit for the number of mortgage loans originated and retained in portfolio to qualify as a community bank lender to 1,000 per year;
- Extend the safe harbor conclusive presumption of compliance for community bank mortgage loans held in portfolio with APRs up to the higher of APOR plus 3.5% or the community bank cost of funds plus 4%, subject to the HOEPA threshold;
- Expand the definition of "rural" for balloon mortgage loans and escrow requirements to include all counties outside metropolitan statistical areas and all towns with fewer than 50,000 residents;
- Grant QM safe harbor protection for refinancing balloon mortgage loans after the January 10, 2014 effective date, so that borrowers with balloon mortgages coming due are not left without refinancing opportunities; and
- Do not include mortgage loan originator compensation in the total points and fees calculation for loans that receive the QM designation.

## Specific Comments

### Expand Loans Held in Portfolio by Small Creditors to Include Balloon Payment Mortgages and Adjust Portfolio and APR Thresholds

The 2013 ability-to-repay final rule defines three categories of qualified mortgages. Qualified mortgages or QM loans are provided either a conclusive presumption of compliance (safe harbor) or a rebuttable presumption of compliance with the requirement that creditors make a reasonable, good faith determination of a consumer's ability to repay before originating a mortgage loan. In this proposal, the Bureau is proposing to define a new, fourth category of qualified mortgage, which would include certain loans originated by small creditors that have a total asset size of $2 billion or less and originate 500 or fewer first-lien covered transactions during the previous calendar year. This proposed new category would include only loans held in portfolio by these creditors. The loans also would have to conform to all of the requirements under the general definition of QM except the 43 percent limit on monthly debt-to-income ratio.

As proposed, for creditors that satisfy the above criteria, these mortgage loans would receive a safe harbor from the "ability to repay" requirements as long as the loan's annual percentage rate (APR) was no greater than 3.5 percentage points above the average prime offer rate (APOR). The Bureau is proposing this change because it believes it is necessary to preserve access to responsible affordable mortgage credit for some consumers. This change would also apply to balloon payment mortgage loans that would otherwise satisfy the QM definition.

ICBA strongly supports the proposed amendment for a new QM category for community bank portfolio loans. Community banks hold 100% of the credit risk on their portfolio loans, so they have every incentive to ensure they understand the borrower's financial condition and work with the borrower to structure the loan properly to make sure the borrower can afford it.

ICBA also urges the Bureau to broaden this new QM category as follows:

- Include balloon payment mortgages originated by small creditors in non rural markets;
- Increase the threshold for the number of mortgage loans originated and retained in portfolio to 1,000 per year; and
- Extend the safe harbor to mortgage loans with APRs up to the higher of APOR plus 3.5% or the community bank cost of funds plus 4%, subject to the HOEPA threshold.

As stated above, community banks have made balloon payment mortgages for decades, and are the product of choice for managing both credit and interest rate risk on mortgage loans held in portfolio. Many community banks do not have the ability to properly service ARM loans, which carry higher compliance costs and burdens. Further, the national indices used for setting ARM rates have little relation to a community bank's actual cost of funds. Balloon payment mortgages are easy for the borrower to understand, the payment schedule is fixed, and the borrower knows that the bank will be there to work with them to refinance or restructure the mortgage loan when it becomes due. To avoid disrupting the community bank mortgage market, balloon payment mortgages originated by community banks meeting the definition of small creditor as discussed above should receive the QM-safe harbor designation as part of the portfolio loan provision.

Further, recent data from an[3] ICBA member survey indicates that balloon payment mortgages comprise as much as 75% of community bank residential mortgage portfolios. Based on recent call report data, the assets of all community banks under $10 billion in assets equals $2.4 trillion, and those banks reported a total of $550 billion of residential 1-4 family mortgages on their books. Assuming that balloon payment mortgages accounted for 75% of the mortgage assets on community bank balance sheets, the result would be as much as $412 billion of balloon payment mortgages. Assuming an average loan amount of $75,000 this rule could impact over 5.5 million loans or as many as 5.5 million consumers in all areas of the United States. These portfolio loans should receive QM status and safe harbor protection for community banks. Not granting broad QM status to these loans will impact millions of American consumers, as they try to buy, sell or refinance their home without access to balloon-payment mortgages, as most of these loans will not qualify for sale in the secondary market.

ICBA also urges the Bureau to increase the annual originations threshold that defines a small creditor to 1,000 mortgage loans annually, and to apply this threshold only to loans retained in portfolio by the originating institution. Based on comments received from many community banks, the current threshold of 500 total originations would limit the number of eligible community banks, forcing them to curtail portfolio lending or secondary market sales in order to stay under the threshold. The purpose of the portfolio designation is to encourage portfolio mortgage lending and recognize the inherent incentives to ensure the ability to repay. Therefore, including loans sold in the secondary market in the origination threshold seems to be counterproductive. We urge the Bureau to make this adjustment to the threshold.

Finally, the Bureau's proposal to permit mortgage loans with APRs up to 3.5% over the APOR to receive the QM safe harbor designation will aid in making portfolio lending more attractive by exempting (qualifying) community banks from the additional escrow requirements on HPMLs. Also, community banks will be able to price their loans in a way that is aligned with their costs and the risks they take. For many community banks, the artificial APOR represents a metric that has no real bearing on their actual cost of funds. In fact, the APOR is heavily weighted towards the pricing that Fannie Mae and Freddie Mac set based on their ability to access capital and funding markets that community banks cannot. Community banks price all other types of credit based on their cost of funds plus their spread or margin. Banks that hold mortgage loans in portfolio should be able to do the same. As such ICBA suggests the Bureau modify its proposal to permit mortgage loans to receive the QM safe harbor designation where the APR is less than the ***higher*** of the APOR plus 3.5% or the community bank's cost of funds plus 4%, subject to the HOEPA threshold. To use this

[3] ICBA Mortgage Lending Survey, September 2012.

provision the community bank would have to be eligible as a small creditor. This will enable community banks to better price their portfolio loans reflecting the credit risk they are assuming and their cost of funds while providing protections to consumers.

**Expand the Definition of "Rural" for Balloon Mortgage Loans and Escrow Requirements**

ICBA also strongly urges the Bureau to amend the current definition of "rural" for purposes of the balloon mortgage QM exception and the escrow requirements for higher-priced mortgage loans. The current definition of "rural" would exclude many community banks that operate in truly rural areas with very small populations and limited financial resources. As it is currently written, the definition includes counties that are not in a metropolitan statistical area (MSA) or micropolitan statistical area adjacent to a metropolitan statistical area. There are many rural areas across the United States that do not satisfy this definition and would not be considered rural for purposes of the QM and escrow requirements. The attached maps illustrate this concern. Areas colored yellow are non-rural areas, and areas colored in blue are rural areas, based on the Bureau's definition.

Attachment 1 is a stark example of this issue.The state of Ohio a state with large agricultural areas, yet only 20 out of 88 counties or a little over 22% of Ohio would meet the Bureau's definition of rural. Attachment 2 highlights this issue is also prevalent in larger states such as Oregon, where out of 36 very large counties, 20 would not meet the Bureau's definition of rural. Attachment 3 shows that this problem is magnified in smaller states like Maryland. While Maryland is home to the two large overlapping metro areas of Washington, D.C. and Baltimore, 20 out of 23 counties in the state would not meet the Bureau's definition of rural yet there are many community banks in areas, especially on eastern shore of Maryland or in the northern sections of the state that are very rural in nature. These areas are also served by the Farm Credit System, a GSE which can lend in these markets without restriction, yet as presently defined, many community banks will not be able to offer the types of mortgage loans they traditionally have without taking on additional risk of litigation, and will have to comply with costly escrow requirements where they did not before. Clearly this is not what Congress intended.

Comments received from an ICBA survey conducted in February 2013 indicated that at least 44% of the responding banks characterized their markets as rural and themselves as rural community banks, but would not meet the bureaus definition of rural:[4]

*If the definition of rural includes a micropolitan county then our bank is going to have serious problems. We operate in Randolph County, Missouri*

[4] ICBA QM Banker Survey, February 2013.


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*which has an approximate population of 25,000. To consider us anything other than rural is absurd.*

ICBA urges the Bureau to adjust its rural definition to match the Farm Credit System. A Government Sponsored Enterprise that is exempt from the QM statue should not have a competitive advantage over a community bank. There are over 7,500 community banks in the U.S., and the vast majority of these banks are located in communities of 50,000 or fewer residents.

ICBA urges the CFPB to instead change the definition of rural to include any county outside of an MSA, or any town with fewer than 50,000 residents, his would be consistent with the lending territory of the Farm Credit System, which is a GSE specializing in lending in rural areas.

**Grant QM Safe Harbor Protection for Refinancing Balloon Mortgage Loans After the January 10, 2014 Effective Date**

ICBA is also very concerned that consumers who currently have balloon mortgage loans will be unable to refinance or restructure these loans after the January 10, 2014 effective date of the rule, because their current community bank will not satisfy the criteria for providing balloon mortgage loans with QM status.

As discussed previously, community banks provide balloon mortgage loans to their customers, because in many cases the borrower would not qualify for a secondary market loan. If community banks can no longer provide these loans because they do not satisfy the "rural" or "underserved" exceptions, or the Bureau chooses not to include balloon payment loans under in the safe harbor for portfolio loans, or the community bank holding the balloon payment loan exceeds the thresholds to be considered a small creditor and does not want to assume the risk of providing a non-QM loan, those customers with current balloon mortgage loans will have few options available to them to refinance their loans once the balloon mortgage becomes due.

We urge the Bureau to allow customers with balloon mortgage loans, originated before January 10, 2014, the ability to refinance into another balloon mortgage loan without requiring the bank to satisfy the ability-to-repay or QM balloon exception standards. Further, we urge the Bureau to extend QM safe harbor protection for these loans as long as they are held in portfolio by the originating community bank. Any other policy will place consumers in a difficult financial situation that could be devastating. In addition, this situation could place community banks in a position of having to choose between the safety and soundness of their bank operations and fulfilling QM and ability-to-repay compliance requirements. As stated earlier community banks and their customers should not have to suffer for the lending abuses committed by others.

**Do Not Include Mortgage Loan Originator Compensation in the Total Points and Fees Calculation for Loans that Receive the QM Designation**

The Bureau has requested comment regarding the inclusion of loan officer compensation as part of the 3% maximum cap on points and fees, that are not bona-fide third party charges or discount points. As proposed, this cap would include amounts paid to companies for settlement services, appraisers or appraisal management firms that are owned or affiliated with the lender originating the loan. The Bureau's concern is that borrowers are being steered into using these firms and are not permitted to shop for these services from other firms, and thereby may not be getting the best price for these services. Further, the Bureau believes the lender, through its affiliation with these firms, benefits financially, including the mortgage loan officer. Additionally the Bureau is endeavoring to implement a poorly written provision of the Dodd-Frank statute requiring all compensation paid directly or indirectly by a consumer to a mortgage loan originator be included in the calculation of points and fees. The goal was to provide complete transparency of the costs of the mortgage transaction and hopefully encourage the borrower to shop around for the best deal. The Bureau has proposed two separate alternatives to deal with the issue. Unfortunately, neither alternative is workable.

Including the mortgage loan originator compensation in the points and fees calculation will not lower the borrower's costs at all; in fact, it increase them as firms raise their interest rates on mortgage loans to cover their compensation costs. This of course will make it more difficult for some borrowers to qualify for a loan since higher interest rates equate to higher monthly payments.

To solve this issue, ICBA urges the Bureau to exclude mortgage loan originator compensation from the points and fees calculation for any mortgage loan that meets the QM definition. Non-QM loans which may have higher rates, or cross the HOEPA thresholds would be required to include all compensation in the points and fees calculation. This approach is very clear and easy to implement and for regulators to monitor.

**Conclusion**

ICBA appreciates the Bureau's recognition that there needs to be a separate QM category for loans held by community banks in portfolio. We strongly support the intent of this amendment to the ability-to-repay rule.

As stated above, ICBA urges the Bureau to include balloon payment loans as a QM loan product when held in community bank portfolios including for community banks located in non-rural areas. Community banks have demonstrated their ability to successfully manage these loans, and they are a


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necessary product in all markets for consumers that cannot qualify for a secondary market mortgage loan.

ICBA and its community bank members are very concerned that the Bureau's definition of rural is too narrow and will result in too many community banks being ineligible to receive QM safe harbor treatment of balloon payment loans they make for portfolio and will be subject to implementing costly escrow requirements. This will force many community banks to exit the mortgage business leaving their communities without an important source of mortgage credit. ICBA urges the Bureau to expand its definition of rural to include any county outside of an MSA or any town with fewer than 50,000 residents.

ICBA recommends that the Bureau grant QM-safe harbor status to any community bank that refinances a maturing balloon payment mortgage that they continue to hold in their portfolio, regardless of the location of the property or the size of the community bank.

ICBA urges the Bureau to increase the threshold for annual originations for small creditors to 1,000 mortgage loans annually, and that this threshold only apply to loans originated and held in portfolio, and not include loans sold in the secondary market.

ICBA urges the Bureau to extend the safe harbor to community bank mortgage loans held in portfolio with APRs up to the higher of APOR plus 3.5% or the community bank cost of funds plus 4%, subject to the HOEPA threshold.

Finally, ICBA strongly urges the Bureau not to include mortgage loan originator compensation into the total points and fees calculation for loans that receive a QM designation.

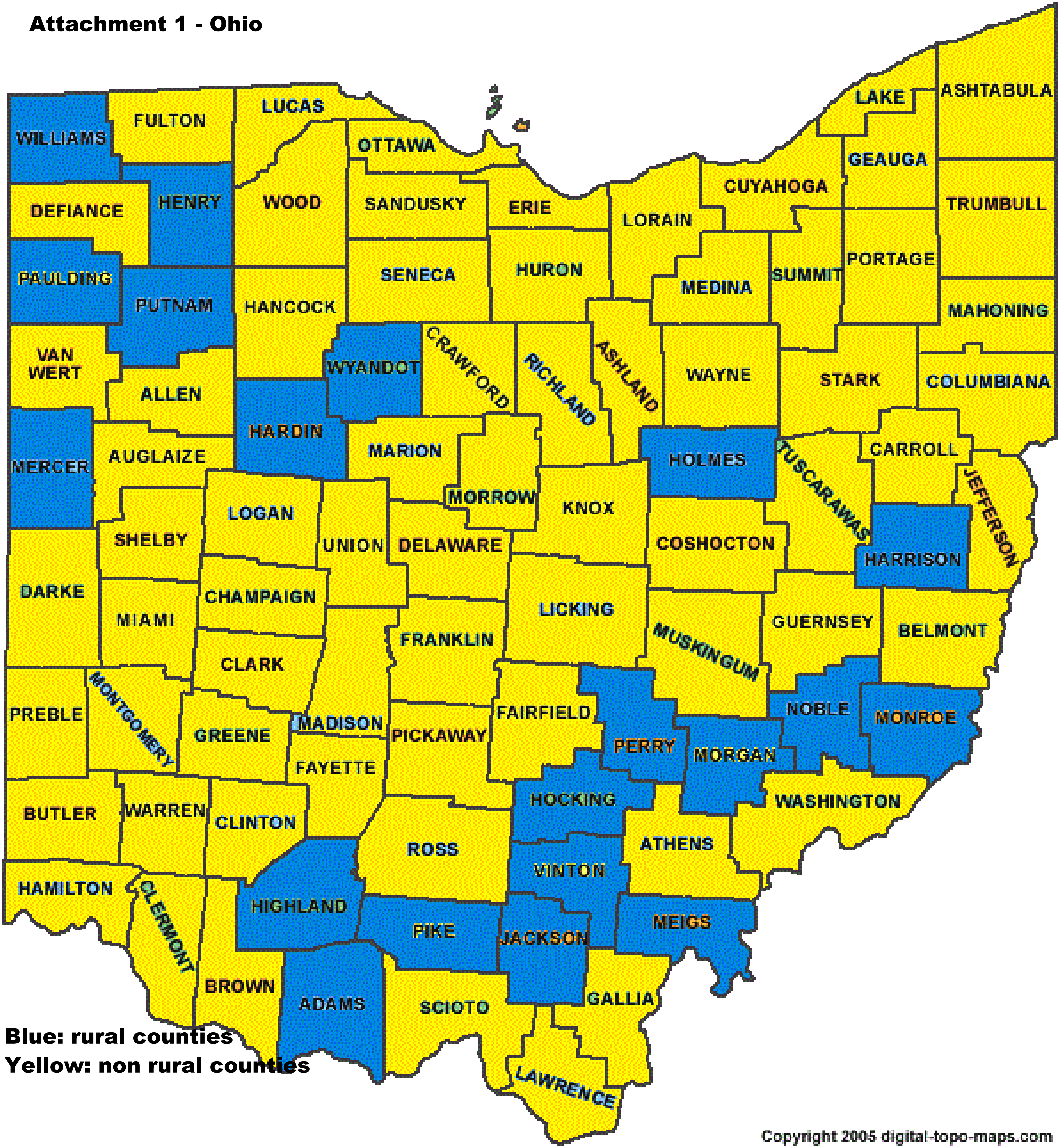
We appreciate the Bureau's outreach to community bankers and to ICBA on these issues, and ask that the Bureau carefully consider the contents of this letter when finalizing its proposal. We look forward to working with the Bureau to implement these rules in a manner that will help community banks continue to meet the needs of consumers in their communities.

If you have any questions regarding these comments please contact me at 202-821-4436 or ron.haynie@icba.org.

Sincerely,

Ron Haynie
Vice President, Mortgage Finance Policy

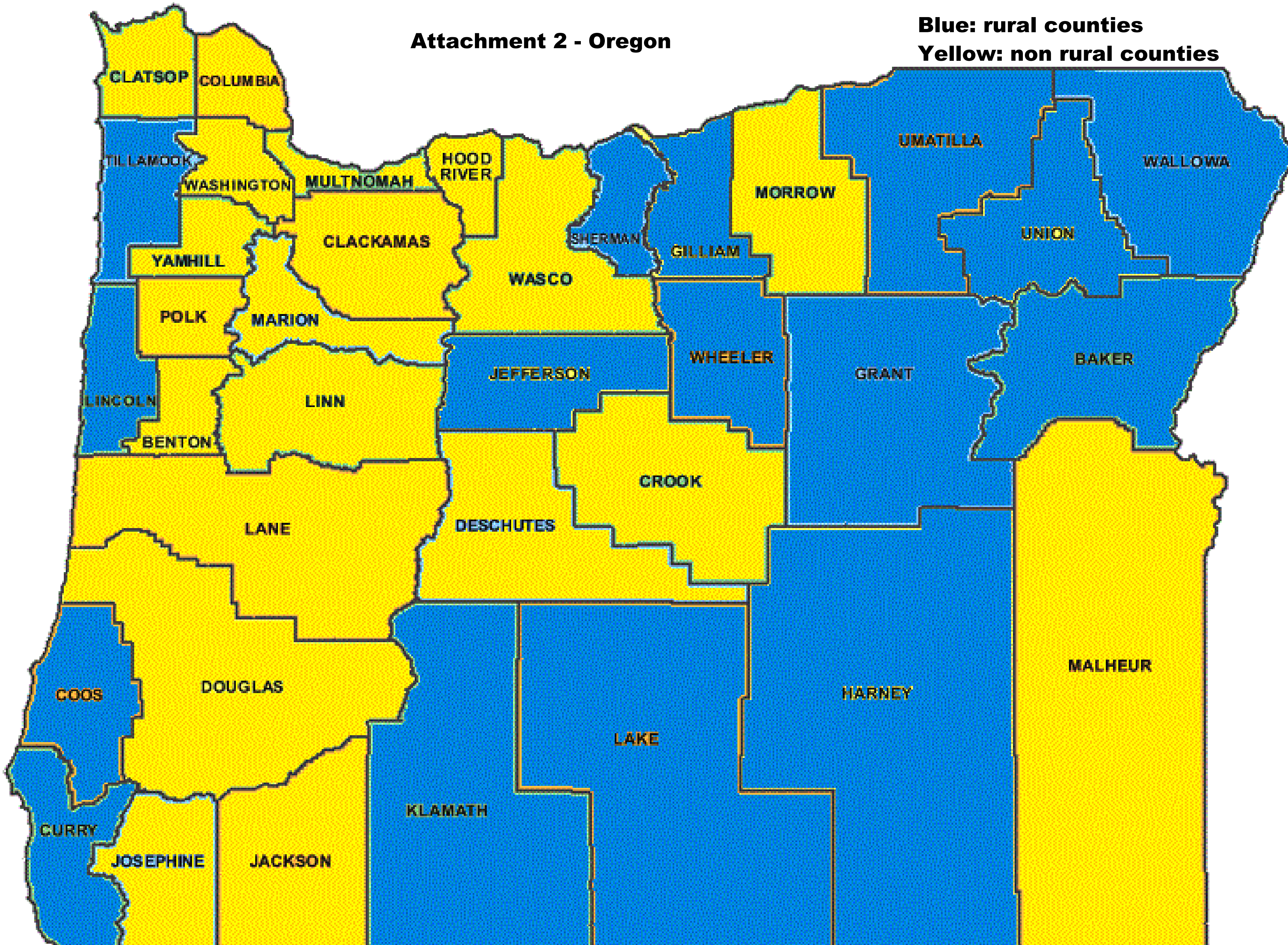
**Attachment 1 - Ohio**




**Blue: rural counties**
**Yellow: non rural counties**

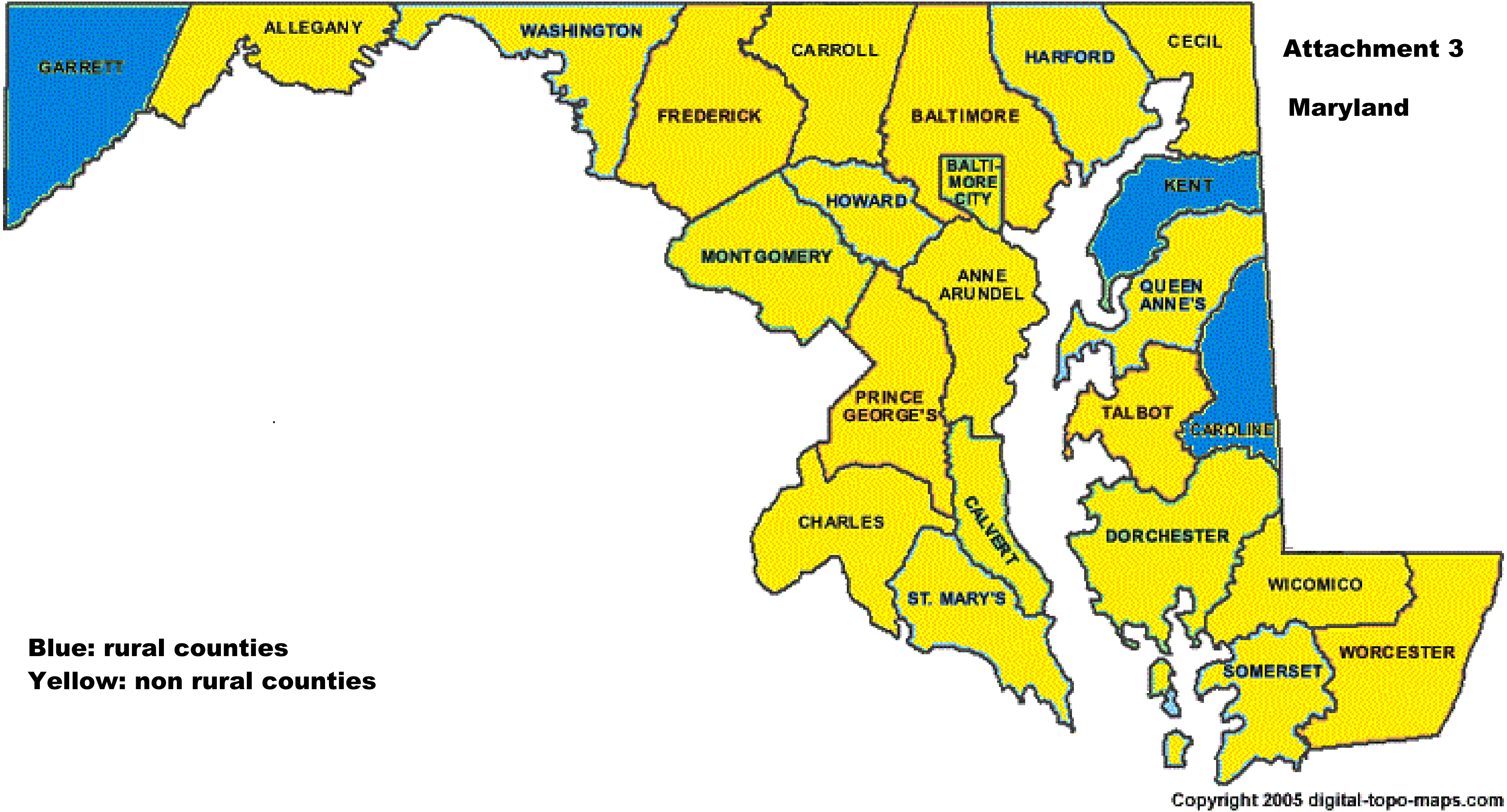
**Attachment 2 - Oregon**

**Blue: rural counties**
**Yellow: non rural counties**



Attachment 3

Maryland




**Blue: rural counties**
**Yellow: non rural counties**