Consumer Federation of America
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October 30, 2013

Mr. Robert deV. Frierson
Secretary
Board of Governors of the
Federal Reserve System
Washington, DC 20551

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
Washington, DC 20429

Mr. Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
Washington, DC 20552

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
Washington, DC 20549

Rules Docket Clerk
Office of the General Counsel
Department of Housing &
Urban Development
Washington, DC 20410

Legislative and Regulatory Activities Division
400 7th St., SW Suite 3E-218 Mail Stop 9W-11
Office of the Comptroller of the Currency
Washington, DC 20219

RE: Proposed Rulemaking on Credit Risk Retention Requirements

Office of the Comptroller of the Currency
Docket Number OCC-2013-0010
RIN 1557-AD40

Federal Reserve System
Docket No. R-1411
RIN 7011-AD70

Federal Deposit Insurance Corporation
RIN 3064-AD74

Securities and Exchange Commission

Release No. 34-70277
RIN 3235-AK96

Federal Housing Finance Agency
RIN 2590-AA43

Department of Housing and Urban Development
RIN 2501-AD53

Dear Sir/Madame:

On behalf of our members, Consumer Federation of America (CFA) appreciates this opportunity to comment on the above-referenced proposed rulemaking on behalf of our nearly 300 member organizations. CFA was founded in 1968 to represent the consumer interest through research, advocacy, and education. We also joined with other industry and consumer groups in a comment filed by the Coalition for Sensible Housing Policy.

The proposed rulemaking on credit risk retention and the definition of a proposed "Qualified Residential Mortgage (QRM)" as required by Title IX of the Dodd-Frank Act is an important step in the reconstruction of the nation's mortgage system. CFA was an early and frequent critic of the loose and ultimately calamitous underwriting and securitization system that emerged in the late 1990's. The lack of alignment among originators, borrowers, creditors and investors led to high inflation in house prices, the growth of an "originate to sell" model of loan-making that fostered poor credit decisions, and the failure of many loans with dire economic consequences for borrowers, investors and communities. In theory, requiring a level of risk retention by securitizers can act to increase their diligence and care when choosing mortgages for securities.

We note, however, that risk retention in and of itself is an imperfect tool for insuring that safe and appropriate lending standards are developed and followed. During the recent mortgage boom, many securitizers held significant portions of risk, greatly in excess of the amounts that would be required under this proposed rulemaking.[1] Holding this risk alone did not generate the level of care that would have avoided the failure in hundreds of billions of dollars in these securities. Likewise, investors generally looked to rating agency grades on these mortgage bonds to assess their likely risk as a substitute for relying on counterparty risk-holding to mitigate investor exposure. But these investors soon found that the agencies themselves had done little or very poor due diligence to justify their ratings, and they ultimately were useless.

[1] "Before the financial crisis, many investment banks held a significant amount of the credit risk in their securitizations. To get many of these issues to market, banks needed to invest in the securities' so-called equity tranches— the pieces most exposed to default. Banks were also attracted to the high returns of these risky tranches. Thus, despite having lots of skin in the game, the securitizers still made huge errors. Requiring them to hold 5% of the credit risk may not hurt mortgage rates or credit availability, but it will also do little to improve the quality of securitization." *Skinny on Skin in the Game*, Mark Zandi and Christian deRitis, Special Report, Moody's Analytics, March 8, 2011, p. 2

We believe that the causes of the massive failures in subprime and Alt-A mortgages that have driven the housing market's collapse were clear and obvious well before the bonds backed by the mortgages actually failed. These included faulty appraisals; dangerous and unstable mortgage features like interest only loans, prepayment penalties, balloon payments, negative amortizations, and teaser ARM rates; fraudulent underwriting where incomes and assets – where assessed – were doctored, and well-known risk factors were layered together to create combustible loans that consumers were unlikely to be able to repay. Risk retention is one means of creating more accountability and alignment in the financing system. But we do not believe it alone is adequate to ensure safe securitizations. Far more important, we believe, is close regulation of mortgage underwriting, appraiser licensing and regulation, the compensation models through which loan originators are paid, servicing requirements focused on effectively and swiftly resolving delinquencies, and the product features that can be offered to consumers.

We believe that the so-called "ability to repay" and Qualified Mortgage (QM) provisions in Dodd-Frank's Title XIV were adopted specifically for these reasons. We consider these to be far more important than the risk retention rules in encouraging safe and stable mortgage lending. They apply at the point of contact with consumers, when loan terms are negotiated and agreed upon. They are designed to regulate loan originators' behavior and discourage them from selling consumers product features that are dangerous and not in the consumer's best interest. They will be universal in their coverage, applying to all loan originations regardless of their ultimate destination in a security or a portfolio. The inclusion of the so-called "qualified mortgage (QM)" provision to provide a safe harbor or rebuttable presumption of compliance with the ability to repay rules should create a clear and, we believe, appropriate bucket of loans whose strong performance is well-documented. Long history in the mortgage finance field has shown these sensible standards, especially the exclusion of unstable product features, to be reliable and dependable.

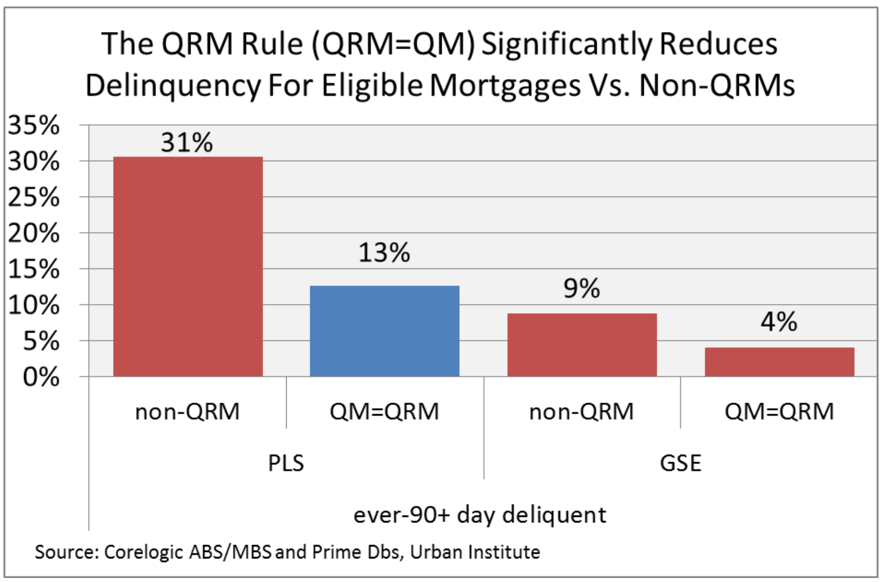
Since the initial proposal of the risk retention rules in 2011, the Consumer Financial Protection Bureau (CFPB) has promulgated final regulations executing the Title XIV provisions of Dodd-Frank. **We strongly support the new proposed risk retention rule's adoption of the QM standard for meeting the Qualified Residential Mortgage (QRM) definition included in Title IX of Dodd-Frank.**

The incorporation by reference of the QM definition appropriately aligns these two important parts of the mortgage process. We believe that the combination of prohibited product features, documentation and verification of income and employment, limitations on prepayment penalties and points and fees establish a robust level of protection for consumers and investors alike. The alignment of the QM and QRM definitions will simplify creditors' business processes by enabling them to apply one set of criteria as loans move through the origination to securitization pipeline. We believe the exclusion of the loans that demonstrated the highest failure rates in the housing boom period, along with the other important protections in the QM definition, is a powerful means to assure that investors can rely on the quality of the loans backing securities. QRM was intended by Congress to establish a standard that could be easily understood and applied by lenders, securitizers and investors for purposes of waiving the risk retention requirements that apply to non-QRM loans. We believe that the QM standard fulfills this intention.

We strongly oppose the alternative proposed "QM-Plus" approach. While significantly altered from the original proposal, we believe that this alternative would raise costs for non-QRM securities and loans for those unable to raise the significant down payment threshold in the proposal. The trade-off between additional performance quality and potential reduced access to credit in QM-Plus is, we believe, unjustified and would cause a hardship on many low and moderate income consumers by increasing the costs of their mortgages, or reducing their access to mortgage credit at all.

The Proposed Rule will Encourage and Support Responsible Lending

By equating QRM with QM, regulators have provided clear rules that allow for robust markets that meet the needs of creditworthy borrowers in a safe and sound manner. The new proposed QRM will reduce the risk of default and delinquency as illustrated below.



An analysis by researchers at the Urban Institute[2] of mortgages in private label securities originated in or prior to 2013, the "ever 90-day delinquency rate" (loans that have ever been 90 days or more delinquent) for all loans that did not meet the re-proposed QRM standard was 30.6 percent. The delinquency rate for purchase and refinance loans that met the new QRM proposal was nearly two thirds lower at 12.6 percent.[3]

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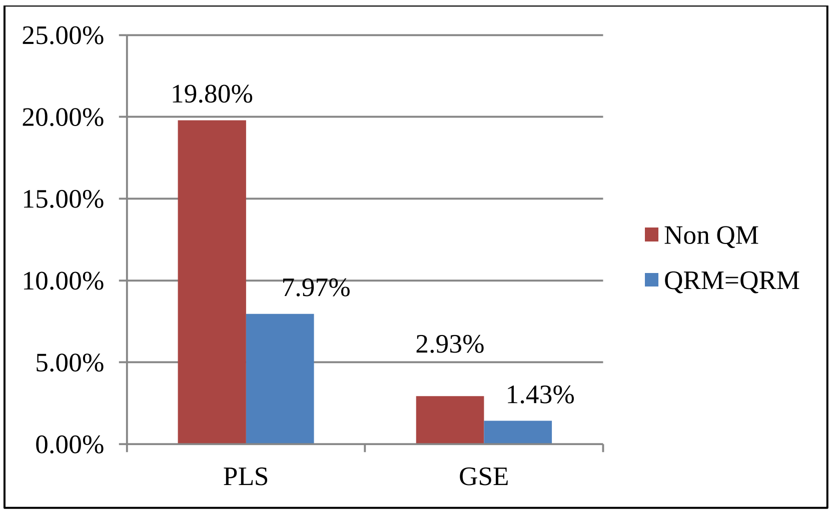
[2] See blog post by Laurie Goodman and Ellen Seidman and Jun Zhu. "QRM, Alternative QRM: Loan default rates." http://blog.metrotrends.org/2013/10/qrm-alternative-qrm-loan-default-rates/?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+MetrotrendsBlog+%28MetroTrends+Blog%29

[3] To account for prepayment penalties, the authors of the Urban Institute's study filtered from their QM definition mortgages with prepayment penalties incurred more than three years after origination, but they were unable to screen those mortgages with penalties that exceeded the limit of 2 percent of the amount prepaid, which would be

Loans purchased by Freddie Mac and Fannie Mae that met the re-proposed QRM standard of QM had default rates of 4.1 percent as compared to 8.7 percent for mortgages that did not qualify for QM status. The study's authors point out that using an alternative measure of performance such as ultimate termination of the mortgage gives a more complete picture of loan performance, taking into account cures during the mortgages' lives. Using this measure, Urban found that 7.87% of the PLS mortgages and 1.43% of the GSE mortgages that met the proposed QRM standard using QM for loans issued before 2013 were terminated. By contrast, 19.8 percent of the PLS and 2.9 percent of the GSE loans that did not meet the new proposed standard were terminated.

Terminated Loans, Non-QRM and QRM=QM



Source: CoreLogic/MBS and Prime Dbs, Urban Institute

Furthermore, as pointed out by researchers at the UNC Center for Community Capital, several recent studies of performance for QM and non-QM loans vary in scope by time frame and mortgage features included, but all indicate that the QM standard significantly reduces risk, while providing broader access to credit than a QRM that includes a down payment requirement.[4]

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considered disfavored HOEPA loans. The analysis did not exclude prepayment penalties on adjustable-rate mortgages or higher-priced mortgage loans, neither of which are permitted under Dodd-Frank, nor did the data permit it to screen out loans with prepayment penalties that, along with upfront points and fees, exceeded the 3 percent cap for QM loans. Likewise, data limitations precluded their ability to screen hybrid ARM products for a maximum rate reset in the first 5 years. Mortgages with these features may have been screened from the QM definition for other reasons, but some were likely included and thus estimates for delinquency rates for QM loans would have been lower.

[4] Reid, Carolina and Roberto Quercia. "Risk, Access, and the QRM Reproposal." UNC Center for Community Capital. September 2013.

The alignment of the QM definition with the QRM definition results in a construct that excludes risky product features and low or no-documentation lending that are closely correlated with increased probability of default. Appropriately, the definition of QM is not limited based on down payment. Although data show that the risk of default increases as down payments decrease, this does not necessitate the inclusion of down payment in QRM, as we described in greater detail in our comments on the original proposed rule. Much like the private market operates today, investors can choose to purchase MBS of QRMs based on down payments if they choose to. Aligning QRM with QM allows market participants to assess and allocate risk within boundaries that will ensure stability to the market and a wide degree of credit access.

Recent market trends show that the QRM rule is unlikely to lead to a flood of zero down payment loans, as some critics of the proposed rule have suggested. Creditors currently are requiring borrowers to put significant amounts down in order to qualify for a loan before any risk retention rules are in effect yet. Both Fannie Mae and Freddie Mac recently raised their minimum down payments for most loans to five percent, and charge significant premiums and require mortgage insurance for those with down payments below 20 percent. The inclusion of a down payment requirement in the QRM rule is, therefore, unnecessary. Nonetheless, if it were included it would set a rigid standard not amenable to adjustment by individual securitizers based on experience and market trends. Moreover, it would give the government's imprimatur to an underwriting factor. That was not Congress's intent and would exclude far too many borrowers from QRM loans. As Laurie Goodman of the Urban Institute states,

> "The default rate for 95 to 97 percent LTV mortgages is only slightly higher than for 90 to 95 LTV mortgages, and the default rate for high FICO loans with 95 to 97 LTV ratios is *lower* than the default rate for low FICO loans with 90 to 95 percent LTV ratios. . . For mortgages with an LTV ratio above 80 percent, credit scores are a better predictor of default rates than LTV ratios."[5]

The proposed rule seeks comment on whether the incorporation of the QM definition should make any distinction between loans that receive a "safe harbor" status under QM or those that receive a "rebuttable presumption" of compliance because they are "high cost" loans. We do not believe that this is necessary. We strongly supported applying only a rebuttable presumption to QM loans in our comments on that rule. But for purposes of the QRM, we believe that it makes sense in serving the market and making responsible credit as widely available as possible within the rules that both types of loans should be included in QRM. We also support the proposal to allow the co-mingling of "safe harbor" and "rebuttable presumption" QMs in QRM-qualified pools.

The agencies requested comment on the proposed certification requirements. We strongly support these. The purpose of the risk retention rule is to "bend" the market's attention to safer loans and to allow investors a level of confidence in the quality of the assets backing the securities they purchase. The extensive documentation and verification required by QM is meant

[5] See Laurie Goodman and Taz George, Fannie Mae reduces its max LTV to 95: Does the data support the move?, The Urban Institute, MetroTrends Blog (September 24, 2013) (available at http://blog.metrotrends.org/2013/09/fannie-mae-reduces-max-ltv-95-data-support-move/).

to assure that the creditor knows and can assess the quality of the most important information relevant to making a judgment about the borrower's ability to repay the debt. Allowing QM loans that are not performing at the time of securitization would undermine the central purpose of aligning the two definitions, e.g., assuring investors of the assets' quality. The bundling of faulty or nonperforming loans into securities was a significant factor in the poor quality and performance of private label securities issued in the mortgage boom. It is reasonable and appropriate to require securitizers to certify to the quality of the assets in their securities in order to avoid having to retain a measure of risk on them.

Once again, thank you for the opportunity to comment on this important proposed regulation. Please do not hesitate to contact me at Consumer Federation of America if you have any questions or comments about this submission.

Sincerely,

/s

Barry Zigas

Director of Housing Policy