

*Summary of Findings:*  
**Design and Testing of  
Truth in Lending Disclosures  
for Closed-end Mortgages**

July 16, 2009

Submitted to:  
Board of Governors of the  
Federal Reserve System

Submitted by:

**ICF MACRO**  
an ICF International Company

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# EXECUTIVE SUMMARY

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## BACKGROUND AND DESCRIPTION OF PROJECT

In 1968, Congress enacted the Truth in Lending Act (TILA) to protect consumers by requiring lenders to provide key pieces of information to consumers at various points in time. Congress assigned the Federal Reserve Board (the “Board”) the responsibility of implementing TILA, and the Board currently does so through its Regulation Z.

In 2004, the Board began the process of reviewing Regulation Z to determine whether revisions were necessary. In January 2009, the Board finalized amendments to Regulation Z’s rules applicable to open-end (not home secured) credit (e.g., general purpose credit cards, merchant-specific credit plans, and overdraft lines of credit).<sup>1</sup> The Board is currently in the process of reviewing disclosures under Regulation Z related to home-secured open-end credit—namely, home equity lines of credit, and closed-end mortgage disclosures. This report is related to the Board’s review of disclosures for closed-end mortgage loans. (ICF Macro has prepared a separate report relating to home-equity lines of credit).<sup>2</sup> One of the goals of this review is to ensure that the amended regulations lead to improved disclosures that consumers would most likely pay attention to, understand, and be able to use in their decision-making.

Currently, Regulation Z requires that potential borrowers be given three types of disclosures before consummation of a closed-end mortgage loan. The first is a Board publication titled “Consumer Handbook on Adjustable Rate Mortgages.” This publication (referred to in this report as the “CHARM booklet”) must be provided to potential borrowers who inquire about applying for an adjustable rate mortgage (ARM) at the time they are provided with an application form or are charged a nonrefundable fee, whichever is earlier. The CHARM booklet provides general information about how ARMs work, but does not provide any transaction- or program-specific information.

Regulation Z also requires every creditor to provide an ARM loan program disclosure under the same circumstances and at the same time as the CHARM booklet for each ARM program in which the consumer expresses an interest. The program disclosure gives details about a specific loan program, including the index used to determine adjustable rates, how often the index is adjusted, and any caps that apply to increases in the rate. It also includes a table showing a historical example of how rates and payments would have varied over the past 15 years for a hypothetical loan of \$10,000. Regulation Z currently prescribes no mandatory format for the ARM program disclosure except that it must be “clear and conspicuous,” in writing, and in a form that the consumer may keep.

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<sup>1</sup> As of the writing of this report, the Board is in the process of reviewing these rules in light of legislation passed by Congress in May 2009.

<sup>2</sup> Disclosures for reverse mortgages and rescission were not included in this stage of the review of Regulation Z mortgage disclosures.

Finally, Regulation Z requires that consumers applying for a closed-end mortgage loan receive a TILA statement that provides detailed transaction-specific information on the terms of their loan offer. This disclosure is provided to prospective borrowers within 3 days of application and typically again before loan closing.<sup>3</sup> Among other things, this disclosure includes the annual percentage rate (APR), finance charge, amount financed, total of payments, and a payment schedule that shows the number, timing and amounts of payments.

In addition to these pre-consummation disclosures, Regulation Z also requires creditors to give borrowers notice after consummation when the interest rate on an ARM changes. Currently, the content of this notice is prescribed, but no mandatory formatting is required.

In December 2007, the Board contracted with ICF Macro, an ICF International company, to assist it with its review and revision of closed-end mortgage disclosures. ICF Macro is a research and evaluation company with expertise in the design and cognitive testing of effective consumer communication materials. ICF Macro worked with the Board on its review of credit card disclosures and is also currently contributing to its review of TILA regulations related to home equity lines of credit.

ICF Macro's work thus far has consisted of two phases. In the background research phase, ICF Macro conducted four focus groups and six rounds of cognitive interviews, which were primarily focused on gaining knowledge about how consumers use the mortgage disclosures that they now receive, as well as revised disclosures that have been previously proposed. Through the focus groups, which took place in Greenbelt, MD, and Los Angeles, CA, ICF Macro gathered information about mortgage shopping, the types of information that consumers currently use for financial decision-making, and their perceptions of disclosures that are currently in use. Through the in-depth cognitive interviews, ICF Macro gathered more detailed information about how participants read disclosures and their level of comprehension of the content.

The second phase of the project was devoted to the development and testing of revised forms. This phase consisted of six additional rounds of cognitive interviews in different locations: Atlanta, GA; Bethesda, MD; Dallas, TX; Providence, RI; Denver, CO; and Bethesda, MD. For each round, ICF Macro developed a set of model disclosure forms to be tested. Interview participants were asked to review these forms and provide their reactions, and were then asked a series of questions designed to test their understanding of the content. Data were collected on which aspects of each form were most successful in providing information clearly and effectively. The findings from each round of interviews led to revisions to the models for the next round.

The findings from the consumer testing informed the Board's proposed revisions to Regulation Z rules for closed-end mortgages, which the Board will publish for public comment in July 2009. The revised disclosure forms that were developed and refined through the testing will be included as model forms and clauses with the proposal.

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<sup>3</sup> Currently, only applicants for home purchase loans would receive the disclosure within three days of application. Applicants for home equity loans or refinancing would receive the disclosure at closing. Under the Mortgage Disclosure Improvement Act amendments to TILA, all applicants must receive the disclosure within three business days of application, effective July 30, 2009.

## SUMMARY OF METHODOLOGY

Research participants were recruited by telephone using a structured screening instrument. Almost all participants had obtained a home mortgage in the past 2 years, either for the purposes of a home purchase or for refinancing. In later rounds, several participants were also recruited who were actively shopping for a mortgage but had not yet obtained one. The purpose of this was to evaluate the extent to which the forms were clear and informative for people who had not yet gone through the mortgage process.

The screening instrument included questions to ensure a range of participants in terms of gender, age, and ethnicity. It also included questions about respondents' current interest rates, as well as whether they had experienced a recent financial hardship or been denied credit or discouraged from applying. These criteria were used as proxies to ensure the inclusion of both prime and subprime borrowers as participants in the study. Since consumers' understanding of ARMs was a particular focus for this project, over half of participants had experience with an ARM, either as their current mortgage or a mortgage they had within the previous 5 years.

## SUMMARY OF KEY FINDINGS

The following is a summary of key findings from the cognitive testing, as well as the most significant design decisions. Some of the research focused on very specific aspects of the content or format of these forms, but this summary focuses primarily on the broader issues that were addressed during the testing process.

### Mortgage Shopping Behavior

- Only about half of research participants consulted more than one lender or broker when looking for a mortgage loan. The two most common reasons that participants did not shop more actively were a) because they trusted a particular lender or broker due to a personal relationship or prior business relationship; and b) because they were referred to a particular lender (e.g., by a real estate agent or home builder) and did not think to consult others.
- When participants were selecting lenders to contact, trust was one of their most important considerations. Most participants either began the mortgage shopping process by visiting their current lending institution to look at offers or going to a lender or broker recommended by friends, family members, or their realtors.
- Even among participants who shopped for mortgages, the shopping process almost always ended at the point of loan application. In some cases this was because of the cost in time and money required to complete another application; other participants who had found the shopping process tiring or frustrating seemed reluctant to revisit the process once they had applied; and a few were concerned that their credit scores would decrease as a result of multiple applications for credit. Whatever the reason, once a loan application was completed and accepted, very few participants ever revisited the shopping process and talked to other lenders—even after they learned that the loan they had been offered had terms they did not like, or that the terms of the offer had changed.



- Participants were most likely to select loans based on interest rate, monthly payment, and loan type (i.e., fixed rate vs. adjustable rate). Interest rate and monthly payment were by far the two most common terms that focus group and interview participants compared between lenders or brokers when shopping. The amount of closing costs and the presence of a prepayment penalty were other terms participants frequently mentioned considering during the shopping process.
- When participants were asked what was most difficult about their mortgage experience, the most frequent answer was the amount of paperwork involved. Many commented that because they were shown so many papers at closing they did not read any of them carefully—including their TILA and HUD-1 statements.<sup>4</sup> Some also complained about the amount of information lenders or brokers requested during the loan application process.
- Some participants felt external pressure to find a loan quickly, which limited their ability to shop. These participants included those who had found a home they wanted to purchase and had a limited amount of time before closing, and those who needed to refinance an ARM before the interest rate adjusted.
- A number of participants indicated that they were informed only at loan closing that the terms of their loan offer had changed. In almost all cases, these participants still completed the loan transaction despite any reservations they had. The most frequent reason mentioned was that they did not feel they had any options at that point in time—particularly in the case of home purchase loans. In other cases, participants accepted loans because they believed, or were advised by lenders, that they could easily refinance to better terms in the near future. Finally, several participants said they felt intimidated and rushed during the closing process and as a result found it difficult to object or raise questions.
- While most participants were satisfied with the loans they had received and said they would not have done anything differently when shopping for a loan, others said they wished they had spent more time shopping among lenders to obtain a better loan. Several had more serious concerns. For example, some had mortgage payments they were struggling to afford. Others had ended up with mortgages that included terms they had originally not wanted, such as adjustable rates, prepayment penalties, private mortgage insurance, and points paid at closing, which increased the costs of their loans.

## TILA Statements

- Almost all participants indicated that the interest rate was one of the most important terms they would consider when evaluating a loan offer. Several were confused by the fact that the interest rate was not included on the current TILA statement, or incorrectly assumed that the Annual Percentage Rate (APR) was the interest rate. As a result, the revised TILA statement displays the contract interest rate.

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<sup>4</sup> Under HUD's regulations implementing the Real Estate Settlement Procedures Act (RESPA), mortgage borrowers receive a Good Faith Estimate (GFE) of settlement costs after submitting a loan application and a HUD-1 statement of settlement costs at loan closing.

- Participants were generally confused by the fact that their contract loan amount was not displayed on the current TILA statement, and many incorrectly assumed that the “amount financed” was the amount of money they were borrowing. As a result, the loan amount was added into the Loan Summary section of the revised TILA statement.
- Participants consistently indicated they would want an estimate of their settlement charges as early as possible, and that it would be helpful to have these charges displayed in the context of their other loan terms (rather than on a separate document, such as their HUD-1 statement). As a result, settlement charges were added into the Loan Summary section of the revised TILA statement.
- Participants indicated that they would find the maximum interest rate and payment—two terms that are not disclosed on the current TILA statement—to be very helpful in assessing the affordability and riskiness of a loan offer. As a result, these terms were included in the proposed model forms and clauses.
- Three of the terms disclosed most prominently on the current TILA statement—the number of payments, total of payments, and finance charge—were not seen by participants as useful or important to their decision-making. In addition, almost all participants were confused by the “amount financed” and did not understand what the figure signified. As a result, these four terms are disclosed less prominently on the second page of the revised TILA statement.
- The meaning of the APR was generally not understood by participants. Almost all either assumed that this rate was the same as their interest rate, or understood that the two terms were different but could not explain how. Participants believed a change in the APR would not make much of a difference in their payment. Throughout multiple rounds of testing, ICF Macro designers attempted to clarify the meaning of the APR by using alternative labels and explanations, but were largely unsuccessful at improving participants’ comprehension of the term or concept. The TILA statement being proposed, therefore, focuses on providing context for consumers as to how the APR on their loan compares to others being offered to borrowers with similar loans nationwide. This context is based on the “Average Prime Offer Rate” (APOR) for mortgages of a comparable type (fixed or ARM) and maturity. The APOR is calculated weekly and provided on the Federal Financial Institutions Examining Council (FFIEC) website and is described on the form as “the average APR on similar loans offered to borrowers with excellent credit.” The proposed statement uses both a graphic scale and a narrative description to describe both the APOR and a “high cost zone,” which begins at 1.5 percentage points above the APOR for first lien loans.<sup>5</sup>
- Participants were generally confused by the payment schedule shown on the current TILA statement. For example, in examining a TILA statement for a hybrid ARM, several participants incorrectly assumed that the fact that payments in the table varied over time meant that they already reflected future changes in interest rates. As a result, the payment table was revised to demonstrate more explicitly the relationship between interest rates and payments. The table in the proposed model form and clauses for a hybrid ARM displays

<sup>5</sup> For subordinate lien loans, the high cost zone would begin at 3.5 percentage points above the APOR. ICF Macro and Board staff did not construct any tests involving subordinate lien loans.

these terms at three points in time: the introductory rate and payment, the maximum at first adjustment, and the maximum ever.<sup>6</sup>

- The revised TILA statement includes a new section labeled “Key Questions about Risk,” which provides information about up to nine potentially risky or costly features of mortgage loans, such as: adjustable interest rates; potential changes to payments; prepayment penalties; interest-only payments; balloon payments; negative amortization; whether the product is a “no-documentation” or “low-documentation” loan; whether the loan has a demand feature; and equity sharing. For each of these features, the form lists a question (e.g., “Can my interest rate increase?”) and the answer (either “Yes” or “No”).<sup>7</sup> All affirmative answers are accompanied by further explanation. This section of the form was received very positively by participants, who found the format clear and easy to understand.
- In the final two rounds of testing, ICF Macro tested a TILA statement that described a payment option mortgage. Because the details of payment option mortgages are so complex, ICF Macro and Board staff focused on developing a statement that would communicate to consumers that a) if they made the minimum payment their loan balance would increase; and b) their minimum payment can increase dramatically in the future. While interview participants did not necessarily understand exactly how payment option ARMs worked based on their review of the form, the statement was largely successful at meeting its two primary communication objectives.
- The proposed TILA model forms and clauses incorporate some of the technical information that is currently provided on ARM loan program disclosures—including information about the frequency of interest rate changes, caps on interest rates, and how the interest rate is calculated. This decision was made in part because the Board staff believes that this information was important for consumers to have when considering a specific loan offer, and in part because background research showed that consumers were unlikely to notice or use the information when it was included on the program disclosure.

## Other Mortgage Disclosures

- Participants who were shown the CHARM booklet generally indicated that they found the document useful and thought the information it contained was important – particularly for consumers with little experience with mortgages. However, a significant number of participants indicated that they would be unlikely to read the booklet because it was too long. Several participants indicated that they would be more likely to read a shorter and more concise disclosure.

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<sup>6</sup> The payment tables that are being proposed for loans other than hybrid ARMs (e.g., fixed rate loans or payment option ARMs) have a slightly different structure, reflecting the differences in the payment schedule for these products.

<sup>7</sup> Three of these features—adjustable interest rates, potential changes to payments, and prepayment penalties—are displayed on all TILA statements. The remaining six questions are included only on the form only if they apply to the loan being described.

- As a result, ICF Macro developed a new one-page early disclosure titled “Key Questions to Ask About Your Mortgage.” The goal was to summarize the most important information in the CHARM booklet in a shorter, more consumer-friendly format, and to warn consumers of certain risky loan features. This form lists seven questions related to potentially risky or costly features that prospective borrowers should ask their lenders about any loans they are offered. These questions pertain to interest rate, monthly payment, loan balance reduction, loan balance increase, prepayment penalty, balloon payment, and loan documentation. The questions on this disclosure are repeated on the TILA statement along with loan-specific answers to each question, to ensure that borrowers have information they need to determine whether to get that loan before they are committed. The Key Questions disclosure tested extremely well with participants; all indicated that they would find it useful, and almost all found it very clear and easy-to-read. As a result, the Board is proposing to require that lenders provide the Key Questions document to prospective borrowers before they submit a loan application.
- Participants who were shown a sample of a current ARM loan program disclosure found the document very difficult to read and understand. They found the narrative format difficult to navigate and the terminology extremely complicated. A large number misinterpreted the historical example table in the disclosure; for example, some thought that the historical rates shown in the table would apply to their loan in the future. As a result, ICF Macro developed a simpler revised program disclosure that focuses on four important distinguishing characteristics of an ARM program: the length of introductory period, the frequency of rate change, the index used to calculate the interest rate, and limits on rate changes. The revised program disclosure does not include a historical example table, but does include product-specific answers that parallel the Key Questions provided at application on the TILA statement.
- Along with the Key Questions document, ICF Macro developed another new early disclosure titled “Fixed vs. Adjustable Rate Mortgages.” This publication, which the Board is proposing be provided to all prospective borrowers, describes the features of ARMs and their relative advantages and disadvantages in relation to fixed-rate loan products. Interview participants found the form easy to understand, and indicated that it would be useful to them.
- In addition to those disclosures described above, ICF Macro developed and tested two additional disclosure forms and clauses to be provided after loan closing that the Board will propose in July 2009. The first is an ARM adjustment notice that would be provided to consumers at least 60 days before terms of their ARM changed and would explicitly describe the change to their interest rate and payment. The second is a disclosure to be included on periodic statements for loans with negative amortization, such as payment option ARMs. This monthly disclosure highlights the consequences that consumers’ payment decisions will have on their loan balance. In both cases, these disclosures tested extremely well—participants had little difficulty understanding their content, and indicated that the information would be meaningful and important to them.

# CHAPTER I: INTRODUCTION

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## BACKGROUND

In 1968, Congress enacted the Truth in Lending Act (TILA) to protect consumers by requiring lenders to provide key pieces of information to consumers at various points in time. Congress assigned the Federal Reserve Board (the “Board”) the responsibility of implementing TILA, and the Board currently does so through its Regulation Z.

In 2004, the Board began the process of reviewing Regulation Z to determine whether revisions were necessary. In January 2009, the Board finalized amendments to Regulation Z’s rules applicable to open-end (not home secured) credit (e.g., general purpose credit cards, merchant-specific credit plans, and overdraft lines of credit).<sup>8</sup> The Board is currently in the process of reviewing disclosures under Regulation Z related to home-secured open-end credit—namely, home equity lines of credit and close-end mortgage disclosures. This report is related to the Board’s review of disclosures for closed-end mortgage loans.<sup>9</sup> One of the goals of this review is to ensure that the amended regulations lead to improved disclosures that consumers would most likely pay attention to, understand, and be able to use in their decision-making.

Currently, Regulation Z requires that potential borrowers be given three types of disclosures before consummation of a closed-end mortgage loan. The first is a Board publication titled “Consumer Handbook on Adjustable Rate Mortgages.” This publication (referred to in this report as the “CHARM booklet”) must be provided to potential borrowers who inquire about applying for an adjustable rate mortgage (ARM) at the time they are provided with an application form or are charged a nonrefundable fee, whichever is earlier. The CHARM booklet provides general information about how ARMs work, but does not provide any transaction- or program-specific information.

Regulation Z also requires every creditor to provide an ARM loan program disclosure under the same circumstances and at the same time as the CHARM booklet, for each ARM program in which the consumer expresses an interest. The program disclosure gives details about a specific loan program, including the index used to determine adjustable rates, how often the index is adjusted, and any caps that apply to increases in the rate. It also includes a table showing a historical example of how rates and payments would have varied over the past 15 years for a hypothetical loan of \$10,000. Regulation Z currently prescribes no mandatory format for the ARM program disclosure except that it must be “clear and conspicuous,” in writing, and in a form that the consumer may keep.

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<sup>8</sup> As of the writing of this report, the Board is in the process of reviewing these rules in light of legislation passed by Congress in May 2009.

<sup>9</sup> Disclosures for reverse mortgages and rescission were not included in this stage of the review of Regulation Z mortgage disclosures.

Finally, Regulation Z requires that consumers applying for a closed-end mortgage loan receive a TILA disclosure that provides detailed transaction-specific information on the terms of their loan offer. This disclosure is provided to prospective borrowers within 3 days of application and typically again before loan closing.<sup>10</sup> Among other things, this disclosure includes the annual percentage rate (APR), finance charge, amount financed, total of payments, and a payment schedule that shows the number, timing and amounts of payments.

In addition to these pre-consummation disclosures, Regulation Z also requires creditors to give borrowers notice after consummation when the interest rate on an ARM changes. Currently, the content of this notice is prescribed, but no mandatory formatting is required.

In December 2007, the Board contracted with ICF Macro, an ICF International company, to assist it with its review and revision of closed-end mortgage disclosures. ICF Macro is a research and evaluation company with expertise in the design and cognitive testing of effective consumer communication materials. ICF Macro worked with the Board on its review of credit card disclosures and is currently contributing to its review of TILA regulations related to home equity lines of credit.<sup>11</sup>

The findings from ICF Macro's work informed the Board's proposed revisions to Regulation Z rules for closed-end mortgages, which the Board will publish for public comment in July 2009. The revised disclosure forms that were developed and refined through the testing will be included as model forms with the proposal.

## OVERVIEW OF THE PROJECT

The project thus far has consisted of two phases. In the background research phase, ICF Macro conducted four focus groups and six rounds of cognitive interviews, which were primarily focused on gaining knowledge about how consumers use the mortgage disclosures that they now receive, as well as revised disclosures that have been previously proposed. Through the focus groups, which took place in Greenbelt, MD, and Los Angeles, CA, ICF Macro gathered information about mortgage shopping, the types of information that consumers currently use for financial decision-making, and their perceptions of disclosures that are currently in use. Through the in-depth cognitive interviews, ICF Macro gathered more detailed information about how participants read disclosures and their level of comprehension of the content.

The second phase of the project was devoted to the development and testing of revised forms. This phase consisted of six additional rounds of cognitive interviews in different locations: Atlanta, GA; Bethesda, MD; Dallas, TX; Providence, RI; Denver, CO; and Bethesda, MD. For each round, ICF Macro developed a set of model disclosure forms to be tested. The model disclosures described loan transactions intended to be generally realistic for participants. The terms of the transactions were often constructed to facilitate testing of specific form elements and

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<sup>10</sup> Currently, only applicants for home purchase loans would receive the disclosure within three days of application. Applicants for home equity loans or refinancing would receive the disclosure at closing. Under the Mortgage Disclosure Improvement Act amendments to TILA, all applicants must receive the disclosure within three business days of application, effective July 30, 2009.

<sup>11</sup> ICF Macro has submitted a separate report to the Board describing its findings related to home equity lines of credit, which will also be published with its proposed rules.

did not necessarily reflect actual market terms and conditions. Interview participants were asked to review these forms and provide their reactions, and were then asked a series of questions designed to test their understanding of the content. Data were collected on which aspects of each form were most successful in providing information clearly and effectively. The findings from each round of interviews led to revisions to the models for the next round.

Appendix A provides an overview of the rounds of focus groups and cognitive interviews that have been conducted as part of this project, as well as the topics addressed in each round.

## RECRUITMENT OF RESEARCH PARTICIPANTS

Interview and focus group participants were recruited by telephone using a structured screening instrument developed by ICF Macro and Board staff. Participation was limited to people who were the primary mortgage decision-maker in their households, and who did not work for a bank or other financial institution or in the real estate or mortgage industry. Other questions ensured the recruitment of participants with a range of ethnicities, ages, education levels, and mortgage behavior. Nearly all participants had obtained a mortgage (either for a home purchase or through refinancing) in the past 2 years. Since consumers' understanding of ARMs was a particular focus for this project, over half of participants had experience with an ARM, either as their current mortgage or a mortgage they had within the previous 5 years.

In each of the last four rounds at least one participant was recruited who was actively shopping for a mortgage but had not yet obtained one. The purpose of this was to evaluate the extent to which the forms were clear and informative for people who had not yet gone through the mortgage process.

The recruiting screener used for interviews conducted in Providence, RI is provided as Appendix B; while the screener for other rounds varied slightly, the intent of the screening questions was essentially the same. Information about the demographic and background characteristics of the interview participants is provided as Appendix C.

One of the recruiting goals was to ensure that interviews were conducted with both prime and subprime borrowers. Because many consumers do not know their credit scores or are reluctant to share them, it was determined that a credit score could not be used as a screening variable for the purposes of recruiting. Therefore, participants were defined as "subprime" if they had: a) suffered a "financial hardship" such as bankruptcy, foreclosure, repossession or a tax lien in the past 7 years; b) been denied credit or discouraged from applying for credit in the past 2 years; or c) received an interest rate higher than 8 percent on their most recent first mortgage (or 10 percent on their most recent second mortgage). These cutoff points on the interest rate screening questions for borrowers with subprime loans were set to be roughly consistent with the Home Mortgage Disclosure Act (HMDA) APR-based thresholds for reporting higher-priced loans over the 2006-2007 period.<sup>12</sup> Fifty-nine of the 134 research participants qualified as "subprime" using the three criteria related to creditworthiness.

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<sup>12</sup> In January 2009, the cutoff points for this screening question were adjusted to 7.5 percent for first mortgages and 9.5 percent for second mortgages, to reflect the lower HMDA APR-based reporting thresholds over the 2007-08 period.

## STRUCTURE OF THIS REPORT

This report provides a summary of the work that has been carried out to date, the methodologies used, and the findings that influenced the development of the proposed model forms and clauses that will be released for public comment.

Chapters II and III describe the background research ICF Macro conducted with consumers prior to developing any new forms. Chapter II details ICF Macro's findings about how consumers currently shop for mortgages, while Chapter III presents research into the usability of several types of mortgage disclosures that are either currently provided to consumers or have been previously proposed.

Chapters IV through VII describe the second phase of the project, during which new disclosure forms were developed and tested. Chapter IV highlights the general design principles that ICF Macro form designers used during the course of the form development. Chapter V details the development and testing of revised TILA statements through six rounds of cognitive interviews, while Chapter VI describes the development and testing of several other types of disclosures related to mortgages that are provided at application or after closing. Finally, Chapter VII provides a brief summary of the project outcomes.



## CHAPTER II: FINDINGS ABOUT MORTGAGE SHOPPING

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One of the goals of ICF Macro's consumer research has been to obtain a better understanding of the extent to which consumers shop for mortgages (i.e., compare quotes from more than one lender or broker) and what kind of information they consider when doing so. Since one of the purposes of the Board's disclosures is to make consumers more effective shoppers for mortgages, it is important that the development of these documents is informed both by how consumers shop currently and by the obstacles that they encounter in trying to do so.

All rounds of focus groups and interviews conducted by ICF Macro included an introductory segment during which participants discussed their recent experiences shopping for mortgages. Participants were asked to describe how they had previously shopped for mortgages, including how many lenders or brokers they spoke to, how they identified potential lenders or brokers, and the factors they considered when choosing a mortgage. The following is a summary of ICF Macro's key findings about mortgage shopping.

### SHOPPING FOR A MORTGAGE

- **Only about half of research participants consulted more than one lender or broker when looking for a mortgage loan.** The two most common reasons that participants did not shop more actively were a) because they trusted a particular lender or broker due to a personal relationship or prior business relationship; and b) because they were referred to a particular lender (e.g., by a real estate agent or home builder) and did not think to consult others. Other reasons participants cited for not shopping included time constraints, a reluctance to have multiple lenders perform a credit check because of the impact it would have on their credit scores, concern about the amount of effort it would take to complete paperwork for multiple lenders, and in a few cases, a mistaken belief that all lenders would offer the same rates and terms.
- **When participants were selecting lenders to contact, trust was one of their most important considerations.** Most participants either began the mortgage shopping process by visiting their current lending institution to look at offers or going to a lender or broker recommended by friends, family members, or their realtors. Others selected a lender based on its general reputation as a financial institution. Several participants used the internet to compare loan products, using web resources that gave them multiple quotes from different lenders. A few contacted lenders to inquire about offers they saw in newspaper, radio, or television advertisements.
- **Participants who actively shopped for mortgages used a variety of methods to compare loans.** Some reported using internet tools to compare offers from different lenders. Others relied on offers that they received from different lenders over the phone. A few met in person with representatives from different banks. In general, these participants were more certain about what type of loan they wanted and what terms were most important to them.

- **Participants with poor credit were more likely to indicate they had difficulty finding financing.** Some participants indicated that because of poor credit or recent financial hardships, it was difficult for them to find a lender who would offer them a mortgage. These participants often indicated that in order to get a loan, they had to accept terms they felt were less than ideal, such as an adjustable rate mortgage (ARM) or a mortgage with a pre-payment penalty.
- **Even among participants who shopped for mortgages, the shopping process almost always ended at the point of loan application.** Even participants who actively shopped for their mortgage and solicited information from several lenders usually only applied for one loan. In some cases this was because of the cost in time and money required to complete another application; other participants who had found the shopping process tiring or frustrating seemed reluctant to revisit the process once they had applied. Whatever the reason, once a loan application was completed and accepted, very few participants ever revisited the shopping process and talked to other lenders—even after they learned that the loan they had applied for had terms they did not like, or when the terms of the offer changed.

## IMPORTANT FACTORS TO CONSUMERS WHEN SHOPPING

- **Participants were most likely to shop based on interest rate, monthly payment, and loan type.** Interest rate and monthly payment were by far the two most common terms that focus group and interview participants compared between lenders or brokers when shopping. Most participants said they were primarily interested in fixed rate mortgages. While some indicated that they would consider an ARM if they were sure they could refinance or sell before the rate adjusted, others said they would never apply for an ARM.<sup>13</sup> Other terms some participants considered when shopping were closing costs, prepayment penalties, discount points, whether private mortgage insurance was required, and balloon payments.

## EDUCATION ABOUT MORTGAGE PROCESS

- **Participants who educated themselves about the mortgage process primarily did so through an informal networking process with family, friends, and colleagues.** New homebuyers were more likely to have gathered information about the mortgage process before starting their search; in most cases participants who were getting their second or third mortgage felt that they were already knowledgeable and did not seek out additional information.
- **Some participants indicated that prior to getting their first mortgage they sought out information about the process on the Internet.** Fewer participants said they obtained information about the mortgage shopping process by reading magazines or newspapers or by attending workshops. A few also indicated they educated themselves by reviewing materials provided by their lending institution. Subprime participants were less likely to use the Internet and more likely to rely on information from family or friends.

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<sup>13</sup> It is important to note that much of the consumer research described in this report took place during the “mortgage crisis” of 2008-09. As a result, participants may have been more risk-averse and suspicious of ARMs and other alternative mortgage products than they would have been in previous years.

## FRUSTRATIONS AND SURPRISES

- **Most participants felt overwhelmed by the amount of paperwork involved in obtaining a loan.** When participants were asked what was most difficult about their mortgage experience, the most frequent answer was the amount of paperwork involved. Many commented that because they were asked to sign so many papers at closing they did not read any of them carefully—including their TILA and HUD-1 statements. Some also complained about the amount of information lenders or brokers requested during the loan application process. A few participants said they felt uncomfortable providing detailed financial information to a large number of lenders or brokers because of concerns about privacy. While none explicitly said so, this may have been an additional reason that some participants did not shop for mortgages more widely.
- **Time pressure was a particular concern among borrowers who were purchasing a home and those who felt a need to refinance before their mortgage rates adjusted.** Once participants found a home they wanted to purchase, many felt pressured to find a loan quickly, which limited their ability to shop. As one participant explained, “I found a house that I really loved in this neighborhood that I’ve been living in...Then a week later it was my home...I didn’t even know how to get a mortgage or anything so it all just happened really quickly.” Some participants said they felt pressure because they had an ARM and needed to re-finance before the interest rate adjusted. As a result, they did not talk to as many potential lenders as they might have otherwise.
- **Participants had difficulty acting on information they were provided for the first time at loan closing.** Several participants indicated they were surprised by important changes in their loan terms at the loan closing. In a few cases, for example, participants said that they had originally been offered a fixed-rate loan, but were told at closing their rate would be adjustable. In almost all of these cases, participants still completed the loan transaction despite their reservations. The most frequent reason mentioned was that they did not feel they had any options at that point in time—particularly in the case of home purchase loans. In other cases, participants accepted loans because they believed or were advised by lenders, that they could easily refinance to better terms in the near future. Finally, several participants said they felt intimidated and rushed during the closing process and as a result found it difficult to object or raise questions.
- **Some participants did not believe they were given enough information during the mortgage process.** For example, one participant complained their broker did not show him all of the loan offers for which he was qualified. Other participants felt their lender or broker should have explained the terms of their loan more clearly—for example, how and when rates and payments were going to vary. These complaints were more common among participants who were purchasing their first home; participants who had previous mortgage experience were much less likely to complain about a lack of information.

- **Although most participants were satisfied with their loans, some had serious concerns about their mortgages.** Most participants were satisfied with the loans they had received and said they would not have done anything differently when shopping for a loan. However, some said that, in retrospect, they wished they had spent more time shopping among lenders to obtain a better loan. Several had more serious concerns. For example, some had mortgages they were struggling to pay. Others had ended up with mortgages that included terms they had originally not wanted, such as adjustable rates, prepayment penalties, private mortgage insurance, and points paid at closing.

## CHAPTER III: TESTING OF CURRENT AND PREVIOUSLY PROPOSED DISCLOSURE FORMS

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As noted earlier in this report, the first phase of ICF Macro’s consumer testing primarily focused on gaining knowledge about how consumers used the mortgage disclosures they now receive as well as testing selected disclosures that were previously proposed by other organizations. In this early phase of testing, ICF Macro tested three types of disclosures:

- **Transaction-Specific Disclosures:** These disclosures provide information about a specific loan offer from a lender. The transaction-specific disclosure that is currently required is known as the “TILA statement.” It is currently provided to consumers at two points in the mortgage process—an initial version is provided within 3 days of application and a final document is generally provided before loan closing.
- **ARM Loan Program Disclosures:** This disclosure is required when a consumer who has expressed interest in an ARM received an application form. The form provides information about ARM loan programs offered by the lender but not about specific loan terms based on the consumer’s creditworthiness.
- **The Consumer Handbook on Adjustable Rate Mortgages (the “CHARM booklet”):** Like the program disclosure, the CHARM booklet is required to be provided to consumers who have expressed interest in an ARM when they receive an application form. This booklet provides general information about ARMs and how they work as well as potential risks of getting an ARM.

The following chapter of the report describes ICF Macro’s consumer research findings related to these disclosures. It also includes the implications these findings had for subsequent disclosure design efforts.

### TRANSACTION-SPECIFIC DISCLOSURES

In addition to the TILA statement format that is currently in use, two other formats were tested during the background research phase of the project (Phase I). These included:

- A form proposed in 1998 by staff from the Department of Housing and Urban Development (HUD) and the Board (referred to in this report as the “joint form”);<sup>14</sup> and

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<sup>14</sup> Under a 1996 Congressional directive, the Board and HUD studied ways to simplify and improve the disclosures required by TILA and the Real Estate Settlement Procedures Act (RESPA). In July 1998, the Board and HUD submitted a Joint Report to the Congress that provided a broad outline intended to be a starting point for consideration of legislative reform of the mortgage disclosure requirements. The report included a proposed two-page disclosure that would largely include the information required by both laws. Information elements related to TILA were included on the first page; the second page included a breakout of settlement costs to fulfill the requirements of RESPA. The first page of this combined form was used in the background research phase of this project. The 1998 report the agencies submitted to Congress is available at <http://www.federalreserve.gov/boarddocs/rptcongress/tila.pdf>.

- A three-page form proposed by Alex Pollock of the American Enterprise Institute in 2007. This form, titled “The Basic Facts About Your Mortgage Loan,” is referred to in this report as the “Pollock form.” It contains one page of transaction-specific information and a two-page glossary.

ICF Macro and Board staff opted to study these two specific forms for several reasons. The joint form shared a number of common elements with the current TILA and thus supplemented benchmark testing of the TILA statement. In addition, this form reflected joint efforts by HUD and Board staff to combine informational elements from the Real Estate Settlement Procedures Act (RESPA) and TILA into a single disclosure. The Pollock form, on the other hand, utilized a significantly different format than the existing TILA and joint forms. This form also specifically addressed features of ARMs, which was a primary area of focus for this study.<sup>15</sup>

Usability information on the current TILA statement was collected through focus groups in Greenbelt, MD and Los Angeles, CA (Rounds 1 and 4), as well as through cognitive interviews in Baltimore, MD (Round 7). The Pollock and joint forms were tested through interviews in Washington, DC and Los Angeles, CA (Rounds 2 and 3). The forms that were shown to consumers during this background research phase are provided in Appendix D.

## Summary of Findings

### *Initial Reactions to the TILA Statement*

- Only a few participants from the background research testing recognized the current TILA statement, or knew that they had received this document previously. Those that did recognize the form usually commented on the four boxes at the top of the page containing the Annual Percentage Rate, Finance Charge, Amount Financed, and Total of Payments.
- Participants who did recognize the TILA statement were asked whether they had found the document useful when they received it previously. Most indicated that they had not, either because they had not understood it or because they had not paid attention to it at loan closing.

### *Loan Summary Information*

#### *Amount Financed/Loan Amount*

- Most participants who reviewed the current TILA statement incorrectly assumed the “amount financed” was the same as the loan amount or, as one participant said, “the cost of the house.”
- The Pollock and joint forms listed the loan amount, rather than the amount financed. All but one participant who reviewed these forms were able to correctly identify the loan amount.

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<sup>15</sup> This project focused primarily on disclosures related to ARMs and other more complex mortgage products. In 2007, the Federal Trade Commission (FTC) conducted research on consumer understanding of TILA and other disclosures in the context of fixed-rate mortgages.

### *Total of Payments*

- When reviewing the current TILA, most participants assumed the “total of payments” was equal to the sum of the finance charge and the amount financed.

### *Loan Term*

- The current TILA and joint forms did not display the loan term. Most participants who were asked to identify the loan term added up the number of payments shown in the payment schedule to calculate their answer. However, a few found it difficult to do so and as a result could not answer this question.
- All but one of the participants who were shown the Pollock statement were able to correctly identify the loan term (30 years).

### *Settlement Costs*

- When asked whether there was any information that did not appear on the current TILA statement that they thought should be displayed, several participants commented it would be helpful to see more detailed information about closing costs and/or settlement charges.
- All participants correctly identified the amount of the closing costs on both the Pollock and the joint forms. About half of the participants indicated they would want the closing costs to be itemized on the statement.

### ***APR and Finance Charge***

- Most participants who reviewed the current TILA and joint forms indicated the “finance charge” was the cost one would pay for getting the loan. It was unclear whether these participants understood that this figure was made up of both interest and fees.
- Almost all participants who were shown the current TILA statement or joint form did not understand what was meant by the APR.<sup>16</sup> Many assumed it was synonymous with the interest rate while others understood that the two terms were different they were unable to articulate how they differed.
- Some participants who saw the joint form (which provided an explanation of the APR) understood that this rate included both interest and fees. However, most of these participants only realized this after looking at the form for several minutes and even then did not understand how the term might be useful to them.
- Participants had various misinterpretations of the APR, such as that it reflected how the rate would adjust in the future, or that it was the maximum possible rate. These misinterpretations occurred even when participants were looking at the joint form, which included an explanation of the term.

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<sup>16</sup> The APR did not appear on the Pollock form.

## **Rate and Payment Information**

### *Understanding of Adjustable Rate*

- Over half of the participants who reviewed the current TILA statement understood the interest rate on the loan would change. However, several arrived at this conclusion because the payment schedule showed different monthly payments (which would not necessarily indicate that the loan had an adjustable rate) and not because the form was marked as having a “variable rate feature.” A few participants indicated they did not know whether the rate would change or not.
- Some participants who saw the current TILA commented that although the form used the term “variable rate,” they were more familiar with the term “adjustable rate.” In fact, a few did not realize that the fact that the “variable rate” box on the form was checked meant the rate could change.
- All participants who reviewed the joint form understood the loan had an adjustable rate. However, less than half understood the interest rate was fixed for the first 3 years. The remainder thought that the rate could vary within the first 3 years; several, in fact, thought that it could begin varying after only 1 month. Several others indicated the form did not provide any information about when the interest rate could adjust. Moreover, most participants did not know how often the interest rate could adjust; only a small number correctly indicated the interest rate could adjust annually after the first 3 years.
- Almost all participants who saw the joint and Pollock forms were able to identify the initial interest rate and most were able to also identify the maximum interest rate.
- All but one participant who reviewed the Pollock form realized the loan had an adjustable rate. Most understood the rate was fixed for 3 years and would begin to vary after that. However, only about half of participants were able to indicate the rate would change annually after the first 3 years. Moreover, a few participants incorrectly indicated that after 3 years, the rate would change to the maximum possible rate.
- When participants in several rounds of testing were queried as to what would cause their interest rate to go up or down, they gave a variety of responses, including “the market”; “the economy”; the “prime rate”; the “Fed rate”; and the Consumer Price Index. All of these responses seemed to reflect a common belief that rates would change based on external market forces over which they had no control. However, most participants did not understand the details of how this rate would be determined (i.e., that it would remain at a fixed margin above a given index rate).

### *Monthly Payments*

- Several participants commented they liked the payment schedule shown on the current TILA and joint forms because it provided specific and detailed information about their future payments. However, most incorrectly assumed the monthly payments shown in the payment schedule were their future monthly payments, rather than estimates that could change based



on the market. One participant explained, “I like the [the joint] form because it shows...the payment could change, but it shouldn’t be dramatically different.” This misconception led to some confusion among participants who questioned how the form could display their future monthly payments when the interest rate was adjustable.

- The joint and Pollock forms each disclosed the maximum rate and payment that could ever be charged on the loan, while the current TILA statement did not. Participants strongly supported the inclusion of this information on the form, because they felt it would help them make more informed decisions regarding the affordability and riskiness of adjustable rate mortgages.
- Almost all participants who saw the joint form were able to correctly identify the initial monthly payment and knew this payment could vary over time. However, as with interest rates, participants were confused as to when the payment could begin adjusting. While some participants correctly stated the payments could change after 3 years, others thought the payments could adjust as early as within 1 month.
- Almost all participants who reviewed the Pollock form correctly identified the initial monthly payment on the Pollock form. When looking at the Pollock form, most participants understood the monthly payments would be fixed for the first 3 years of the loan and then could vary.
- When asked if the Pollock form indicated what the payment would become after 3 years, about half of the participants identified the payment associated with the fully-indexed rate. However, it appeared that some participants correctly identified the fully-indexed rate because it was the only other payment displayed on the form, rather than because they understood the term. When asked to explain the meaning of “fully-indexed rate,” most participants were unable to do so (see the section “Terms Unique to Pollock Form” below).

#### *Taxes and Insurance (Escrow)*

- Most participants who saw the joint form incorrectly assumed that the payments shown in the payment schedule included escrow, even though there was a footnote stating otherwise. Some participants later saw the footnote and realized their mistake while others did not.
- The word “escrow” has different meanings in different parts of the country which led to confusion on the part of participants who reviewed the joint form. Most participants in Washington, DC. understood the term referred to additional funds for taxes and insurance that are added to the monthly payment. In California, however, the word “escrow” is used to refer to the process of closing on a loan.
- Some participants suggested the joint form provide an explanation of the word “escrow,” since they thought not everyone would be familiar with the term. Others suggested either adding another column in the payment schedule to include escrow or moving the information about escrow closer to the payment schedule.

- When asked which of the monthly payments shown on the Pollock form would be their initial monthly payment, most selected the payment that included taxes and insurance, while a few participants chose the payment with just principal and interest.<sup>17</sup> Participants who assumed that payments would not include escrow tended to be those who were younger and had less experience with mortgages.

### ***Other Required Disclosure Text***

#### *Prepayment Penalty*

- While most participants reviewing the current TILA understood the general meaning of the phrase “prepayment penalty,” about half thought the penalty would not apply if they sold the house or refinanced their loan. A few were confused by the language that indicated they would “not be entitled to a refund of part of their finance charge”; these participants thought if they paid off the loan they would still be responsible for paying the full finance charge shown on the top of the page.
- When looking at the joint form, almost all participants realized there was a prepayment penalty associated with the loan. However, some incorrectly assumed this penalty would only apply if the loan was paid off or if the house was sold, not if the loan was refinanced. A number of participants also commented that they would like the form to provide the amount of the penalty as well as the specific circumstances in which it would apply.
- When reviewing the Pollock form, almost all participants understood that a prepayment penalty would be charged and they were able to correctly identify the amount of that penalty.
- The version of the Pollock form used for testing in Washington, DC stated the prepayment penalty would be charged “if you refinance within the first three years.” Several participants who saw this version of the form did not realize that the penalty would also apply if they sold the house or otherwise paid off the loan. A version of the Pollock form used in Los Angeles was revised to read that the fee must be paid “if you pay off or refinance your loan.” This led to fewer misconceptions among participants, although one participant still questioned whether he would have to pay a penalty if he sold the house.

#### *Other Loan Terms*

- Very few of the participants who saw the current TILA understood the terms “security interest” and “demand feature.” About half of the participants who read the description of loan assumption understood what it meant; others were confused by this text. Several participants were surprised to learn that mortgages could be transferred in this way.
- Participants generally indicated that the information on the bottom half of the current TILA statement and joint form (e.g., information about security interest, late charges, loan assumption, demand feature, and hazard insurance) was much less important than that on the

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<sup>17</sup> The Pollock form did not indicate whether or not escrow was required, so none of these responses were correct or incorrect.

top half of the form (e.g., information about interest rates and payment). At least half did not understand what was meant by “security interest,” “assumption,” or “demand feature.”

- The two pieces of information on the bottom half of the current TILA statement that participants did indicate were important to them were whether or not the interest rate could change, and whether the loan included a pre-payment penalty.

### ***Terms Unique to Pollock Form***

The Pollock form had several terms and features not found on the current TILA or joint forms. The findings specific to Pollock terminology and features are described below.

#### *Type of Loan*

- The Pollock form used in testing listed the “type of loan” as a “3/1 LIBOR ARM.” Almost all participants were confused by this term and did not understand what was meant by either “3/1” or “LIBOR.”<sup>18</sup> Only one participant understood that “LIBOR” referred to the index being used to determine the interest rate; another understood this after seeing a reference to LIBOR in the glossary.

#### *Fully-Indexed Rate*

- Most participants did not understand that the fully-indexed rate was the level to which the interest rate would eventually adjust assuming there was no market fluctuation (i.e., no variation in the LIBOR index). Several simply thought this was what the interest rate would change to in 3 years, rather than an estimate. Other participants had even more serious misconceptions; for example, one thought the fully-indexed rate represented the fee that the mortgage broker would receive for his or her services.

#### *Payment-to-Income (PTI) Ratio*

- All participants correctly interpreted the payment-to-income ratio shown on the Pollock form as the percentage of their income that would be required to make their loan payments.
- Participants’ reactions to the inclusion of the PTI ratio on the form were mixed. Some thought this information would be useful to help them budget for their mortgage payments. Others, however, felt this ratio was not helpful because it did not account for other debts and bills. One participant commented that the PTI ratio was not a valuable measure because it might change dramatically in the event of a career change.
- Participants interpreted the income figure provided on the Pollock form differently; about half assumed the figures listed would be pre-tax, while the other half thought they would be post-tax. Because of this confusion, several participants suggested this be clarified on the form.<sup>19</sup>

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<sup>18</sup> “LIBOR” stands for the London Interbank Offered Rate, which is used as an index for determining the rate on some ARM loans.

<sup>19</sup> The Pollock form does not indicate whether the income shown is pre- or post-tax.

- When asked whether they would rather be shown pre- or post-tax income on this form, participants were again split. Some preferred to see post-tax income, since they felt this would make the ratio more useful. Others preferred to see pre-tax income, because that is the figure with which they are more familiar. The majority of participants also indicated it would be more useful to have monthly income listed on the form, as opposed to annual income.
- Participants had very different opinions of how high the PTI ratio would have to be before they would feel uncomfortable taking the loan. When asked what level would make them uncomfortable, participants gave responses ranging from 20 to 50 percent. Only one participant looked in the glossary and found the reference to the “industry standard” of 28 percent.

### *Glossary*

- Very few participants noticed the glossary when first reading the form and even fewer referred to the glossary when they came across terms they did not understand.
- When asked by the interviewer to review the glossary, participants were very positive toward it; they found it to be user-friendly and easy to understand.
- Participants suggested that more consumers would use the glossary if it appeared before the form, rather than after it.

## **Design Implications**

- There were several items that do not appear on the current TILA that participants consistently indicated they would want to see on a revised form. In some cases, these were terms that participants already use when shopping for a mortgage, and therefore including this information on the TILA statement would allow them to confirm that they received what they had been offered verbally. In other cases participants felt the information would be helpful for them to make informed decisions between loans. Therefore, all revised TILA forms developed for this project included following new terms: the loan amount, loan term, interest rate, settlement charges, and maximum rate and payment.
- Testing of the current TILA and joint forms showed that few participants understood the APR; many assumed it was the same as the loan interest rate, while those who knew that it differed from the interest rate were unsure why. In its subsequent revisions of the TILA statement, ICF Macro attempted to clarify the meaning of the APR by varying the labels and explanations used, changing the prominence and placement of the term, and in later rounds, including a graphic showing how the APR compares to that of similar loan offers to provide context.
- Testing clearly showed that the current TILA payment schedule is ineffective at communicating to consumers what could happen to their payments. One goal of the revised TILA was to portray more clearly what could happen to payments over time—while making it clear to consumers that in the case of an ARM, their actual payment could not be accurately predicted.

- Because participants indicated they were more familiar with the phrase “adjustable rate” rather than “variable rate” as it related to mortgages, and because a few did not realize that the fact that a loan had a “variable rate” meant that the interest rate could change, the phrase “adjustable rate” was used on all revised TILA forms.
- Because participants who saw the joint and Pollock forms were unsure whether escrow would be included in their monthly payments, the portion of the payment that went toward escrow was disclosed prominently in the payment table on the revised TILA forms.
- Because participants generally indicated that the bottom half of the TILA statement was significantly less useful to them, ICF Macro reformatted this section of the form significantly. The presence of an adjustable rate or prepayment penalty, both of which participants indicated were important, were disclosed prominently on all revised TILA forms. However, other information that was considered less important (such as the need for hazard insurance or the amount of a late payment fee), or that was confusing to consumers (such as information about loan assumption, a demand feature, or security interest) was reworded and removed from the TILA statement.

## ARM LOAN PROGRAM DISCLOSURE

ICF Macro tested an ARM loan program disclosure form through the two rounds of focus groups held in Greenbelt, MD and Los Angeles, CA (Rounds 1 and 4). This form, which is provided in Appendix D, was designed to be representative of forms that are currently in use. The following is a summary of findings related to this initial program disclosure.

### Summary of Findings

- None of the participants, including those who had recently shopped for an ARM, remembered ever receiving anything similar to the ARM loan program disclosure they were shown.
- Participants overwhelmingly indicated they would not find the program disclosure useful and that if given the form, they probably would not read it.
- Upon looking at the form, the first reaction of many participants was one of confusion. Several complained it was very difficult to read due to the terminology that was used. One commented, “You’ve got to be a financial expert to understand that. That’s ridiculous. That’s like the fine print on the credit card.” Another said that in order to understand the disclosure “you’d have to take a semester [course] in this.”
- Several focus group participants were concerned they could not find any information about what their actual interest rate would be. They indicated that in the absence of this rate, most of the other information provided was not important to them.
- The second page of the disclosure included a chart showing a historical example of how payments would have varied for a \$10,000 loan over the previous 15 years. Several participants did not realize this was only an historical example and assumed that the numbers

related to a loan they were actually being offered. Some participants who did understand the purpose of the chart commented that because the size of the loan was so low the information was not helpful. Others assumed that because the chart showed 15 years, it was showing a loan with a 15-year amortization period (in fact, the chart was for a 30-year loan).

- Several participants commented that the ARM loan program disclosure should show the best and worst case scenarios with regard to the interest rate and payment adjustments over the life of the loan. Other changes suggested by at least one participant included simplifying the terminology used on the form; enlarging the font size used in the disclosure; replacing the historical table with a line graph; and bolding or highlighting key terms from the first page for emphasis.

## Design Implications

- Because participant reactions to the current program disclosure were so negative, this disclosure was redesigned and tested again with consumers in Providence, RI (Round 11). The goal of this redesign was to use plainer language to simplify the form and to focus the disclosure more specifically on potentially risky features of ARMs. Research findings related to the revised program disclosure are provided in Chapter VI of this report.
- Based on the results of the focus groups, ICF Macro and Board staff felt that borrowers would be much more likely to pay attention to and use information that is provided in the context of an actual offer. Therefore, some specific information about how interest rates would adjust, such as the index and margin used to determine the rate and caps on rate change, were included in the revised TILA.

## CHARM BOOKLET

ICF Macro collected usability information about the CHARM booklet<sup>20</sup> through the two rounds of focus groups held in Greenbelt, MD and Los Angeles, CA (Rounds 1 and 4). This booklet was also shown to interview participants in Washington, DC and Kansas City, KS (Rounds 2 and 6). The following is a summary of findings related to this disclosure.

### Summary of Findings

#### *Consumer Familiarity with CHARM Booklet*

- Almost none of the participants had seen the CHARM booklet before testing. Even among participants who had recently obtained an ARM, very few indicated they had been given the booklet. A few thought they might have seen the booklet when they were shopping for loans, but did not have a clear memory of its contents or whether they had found the resource useful. Therefore, the majority of the reactions described in this report are based on participants' brief review of the booklet during testing.

#### *Initial Reactions to the CHARM Booklet*

- The majority of participants liked the information contained in the CHARM booklet because it was informative and educational. Several participants commented the booklet answered questions that some consumers might be reluctant to ask; as one said, "People don't like to ask questions, so this is good."
- Several participants noted that despite their risks, ARMs can be a useful tool for some consumers who need a low introductory rate or who plan to sell or refinance their loan before the interest rate adjusts. These participants felt the booklet would be particularly beneficial to this type of consumer because it would help them successfully implement their plan.
- There were specific aspects of the booklet that participants particularly liked:
  - One of the most frequently mentioned sections of interest to participants was the description of payment shock on page 20. A few participants thought the section was so important that it should have been moved to the front of the booklet. One participant was concerned that people would not read the section in its current location because it is "buried in the middle—you get bored after the 5th page, [and] you don't get that far." A few participants also liked the graph that gave an example of payment shock because it visually showed how much your payment could increase.
  - The cautionary bullets on the first page were cited as being particularly useful by several participants. They thought it was a good idea to mention the most important topics early in the booklet. Some participants also commented it was helpful that the bulleted items included page numbers so readers could easily find more information on the subject.

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<sup>20</sup> A PDF version of the CHARM booklet may be found at [www.federalreserve.gov/pubs/arms/armsbrochure.pdf](http://www.federalreserve.gov/pubs/arms/armsbrochure.pdf). A web summary is also available at [www.federalreserve.gov/pubs/arms/arms\\_english.htm](http://www.federalreserve.gov/pubs/arms/arms_english.htm)

- A large number of participants also identified the sections about prepayment penalties and negative amortization, the Mortgage Shopping Worksheet, and the glossary as being particularly important.
- Fewer participants found other parts of the booklet important. Those parts cited included the definitions of “lenders” and “brokers” on page 5, the description of payment caps on page 13, and the explanation of different types of ARMs beginning on page 15.

### ***Length of the CHARM Booklet***

- Although all participants thought the booklet contained useful information and would be beneficial to consumers who are considering ARMs, most thought the booklet was too long. Many participants said they would be more likely to read the booklet if it was shorter. A smaller number of participants disagreed and indicated that if the booklet were shortened it would actually be less useful because it would not include as much important information. There were even a few participants who thought the booklet was too short and should include more detail—for example, information about other loan products other than ARMs.
- Several participants suggested that multiple versions of the booklet could be developed—a shorter version, for people who were unlikely to read a longer document, and a longer version for those who wanted more detailed information. They felt this might be the best way to make sure everyone saw at least some information about ARMs.

### ***Reactions to the Mortgage Shopping Worksheet (CHARM Booklet pages 2 and 3)***

- Nearly all participants thought this worksheet would be a useful tool for someone who was shopping for a mortgage. Several commented that the worksheet would remind them of what loan terms and conditions might be important and that it could act as a guide to help them ask the necessary questions. Others focused on the fact that the worksheet would help them compare terms between loans.
- There was some disagreement among participants about whether the Mortgage Shopping Worksheet should be in electronic or paper format. Some participants preferred a paper format because they would be able to carry the worksheet to different banks and either complete it themselves or have the lender or broker complete it. However, other participants liked the electronic format because it would allow them to enter the data and complete calculations. Several participants felt it would be best to have both formats available.
- Participants provided only two concrete suggestions for improving the worksheet. The first was to define the acronym “ARM,” since consumers might use the worksheet independently of the rest of the booklet. A few participants also thought the worksheet should include a numerical example to illustrate how to complete the form.



### ***Reactions to the Glossary (CHARM Booklet pages 30 through 34)***

- Participants were specifically asked to comment on the usefulness of the glossary. All participants thought the glossary was a valuable part of the booklet because it included definitions and explanations of important terms that are sometimes difficult for consumers to find.
- Several participants gave suggestions for how the glossary could be made more effective, including bolding the words in the text that appear in the glossary, adding references to the glossary earlier in the booklet, including the definitions in the text as footnotes, or embedding definitions in the text itself.

### ***Participants' Suggested Revisions to the CHARM Booklet***

- Several participants said that including more explicit warnings about the risks of ARMs might make consumers read the information more carefully. Some of the suggested phrases included, “It’s really important for you to read this because your life depends on it,” or “Foreclosure is inevitable if you don’t understand what’s in this book.”
- A few participants suggested that including information on how mortgage rates are determined might help consumers forecast their future rates.
- Other content participants suggested adding to the booklet included:
  - Differences between fixed-rate versus ARM products;
  - Additional detail about late charges and prepayment penalties;
  - More emphasis on the need to refinance before the interest rate adjusts; and
  - A description of how taxes change as the interest rate changes.
- Some participants suggested improving the format of the booklet to make it clearer and easier to read. Specific ideas included adding a table of contents and bolding or highlighting specific sections to emphasize their importance.

### ***Dissemination of CHARM Information***

- To improve the likelihood of consumers seeing and understanding the information in the booklet, participants suggested providing it in alternative formats such as audiotapes or DVDs. One participant pointed out an added advantage of doing this would be that illiterate or semi-illiterate consumers would also be able to obtain the information. A large number of participants commented that the booklet should also be available online (as it currently is).

- One participant suggested that the Board should require lenders and brokers to review this information with their customers and then have them sign a document saying they received and understood the information. Another felt the Board should increase the amount of time consumers have before closing a loan so they will be able to read the booklet and other information.<sup>21</sup>
- A large number of participants said that in addition to creating resources like the CHARM booklet, the government should also take other steps to educate consumers. Suggestions included creating a “Real Estate 101” class for new home buyers, teaching high school students about loan products and home ownership, offering free seminars, and providing loan counselors who would be required to act in consumers’ best interest.

## Design Implications

- Because most participants indicated that the CHARM booklet was too long and many said that as a result they were unlikely to read it, the Board will propose in July 2009 that lenders no longer be required to provide this document to potential borrowers. However, the Board intends to continue to make this publication available for the purposes of consumer education, and plans to review it in the future to determine how it could be made more useful for consumers.
- Despite the fact that they felt it was too long, participants found a number of aspects of the CHARM booklet to be valuable and informative, such as explanations of negative amortization, payment shock and other potentially risky aspects of ARMs, and prepayment penalties. ICF Macro and Board staff incorporated this information into two new one-page mandatory disclosures that were developed through this project and will be included in the Board’s proposed rules, titled “Key Questions to Ask About Your Mortgage” and “Fixed vs. Adjustable Rate Mortgages.” For more information about the development of these new disclosures, see Chapter VI.

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<sup>21</sup> This participant may not have understood that the CHARM booklet should be given to consumers when they first inquire about an adjustable rate loan, before they even apply.

## CHAPTER IV: GUIDING PRINCIPLES FOR DISCLOSURE DESIGN

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Much of ICF Macro's design of revised disclosures was based directly on findings from cognitive testing. This reliance on direct consumer research is an important strategy for ensuring that disclosure forms are useful and understandable to their intended audiences. At the same time, there are a number of general principles to which ICF Macro's designers try to adhere whenever engaged in this or similar projects. These principals include:

- **Use plain language.** Jargon and technical language should be avoided whenever possible, and replaced with words that are more easily understood by consumers. The use of simple language is particularly important in the context of disclosures, because consumers that are at the greatest risk of being taken advantage of are often those with lower literacy levels. While readability metrics (such as the “grade level” of the writing) can be useful in this respect, the best way to determine whether language is truly understandable is through direct consumer testing.
- **Prioritize information, and structure disclosures so that the most important information for consumers is easiest for them to find.** Consumers frequently do not read disclosures carefully; those who look at them often only skim them quickly to look for a few key pieces of information. If consumers cannot quickly find the information they are looking for, they are likely to become frustrated and give up. Therefore, before any design work can begin there must be some discussion to identify the most important pieces of information on the form. Those should be located most prominently on the disclosure, to increase the likelihood that even consumers who skim the form quickly can find and understand that information.
- **Provide information in a format that makes it easy to compare terms between disclosures.** One purpose of mortgage disclosures is to serve as a tool to help consumers compare products from different lenders. Narrative text is often difficult to compare in this way, because consumers cannot always identify the equivalent information between forms. Providing information in more structured formats, such as tables with consistent labels and headings, facilitates this kind of shopping comparison.
- **Keep language and design elements consistent between forms so that information can be tracked over time.** In a disclosure regime like that currently in place for mortgages, consumers get information about the product for which they are applying at multiple points in time. One goal of these disclosures is to help consumers track the terms of their loan at each stage in the process to make sure nothing changes without their knowledge. To facilitate this, the structure and formatting of disclosure elements, as well as the language that is used to describe various aspects of the product, should be made consistent between disclosures whenever possible. For example, several aspects of the revised TILA statements were integrated into the initial program disclosures as well, to make it easy for consumers to confirm that the loan they were considering accepting matched what they had originally discussed with their lender.

- **Use headings and titles to make documents more navigable, and to help consumers find the information they are looking for.** When large amounts of text are included, plain language headings should be used to distinguish sections on different topics. In tables, rows and columns should have short, easy-to-read titles that accurately describe the information that is provided. This allows consumers to find information that they are looking for quickly and efficiently, and decreases the likelihood that they will become distracted by unrelated text.
- **Group related concepts and figures.** Mortgage disclosures, particularly TILA statements, contain a great deal of disparate information about a loan. Consumers are likely to find it easier to absorb and make sense of the information if it is grouped in a logical way so they do not have to constantly shift their mindset as they read. For example, the revised TILA statement groups all information about potentially risky features of the loan into a single section of the form.
- **When possible, provide information in multiple formats to accommodate different learning styles.** Current disclosures provide information in a mostly narrative format, accompanied by tables of figures. While this structure may be very appropriate for some consumers, others might benefit from an alternative presentation using graphics or other heuristics. While this strategy must be balanced with the desire to make efficient use of space, it can often have significant benefits for consumer comprehension. This approach was implemented in the APR section of the revised TILA statement, which uses a graphic scale to provide context for the loan's APR.
- **Build off of prior research whenever possible.** While each type of disclosure is different, findings from cognitive testing can often translate between different documents. The applicability of a disclosure format in a new context should always be confirmed through cognitive testing, but it often provides a useful starting point. For example, some of the revisions to the way the APR is described on the TILA statement were inspired by findings from ICF Macro's earlier testing of credit card disclosures for the Board. ICF Macro's design work was also informed by findings from its testing of disclosures related to broker compensation.<sup>22</sup>

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<sup>22</sup> Research on disclosures related to broker compensation was conducted during Rounds 2, 3, 5, and 6 of the background research phase of this project. ICF Macro submitted findings on this topic to the Board under separate cover; this report is available at <http://www.federalreserve.gov/newsevents/press/bcreg/20080714regzconstest.pdf>. ICF Macro's final reports related to its design and testing of credit card reports are available at <http://www.federalreserve.gov/newsevents/press/bcreg/20081218a.htm>.

# CHAPTER V: DEVELOPMENT AND TESTING OF REVISED TILA STATEMENTS

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## INTRODUCTION

After completing the background testing phase of the project, ICF Macro project staff met with Board staff to discuss key findings from consumer testing. Following this meeting, ICF Macro's design team developed several revised disclosures which were intended to address the weaknesses of the current forms. These forms were then tested through six rounds of cognitive interviews from November 2008 through May 2009. The specific forms that were tested changed in each round, but in each case the findings from one round informed revisions that were made to the forms for the next round. A more detailed description of each round of testing, as well as the topics that were covered, can be found in Appendix A.

The remainder of this report is focused on describing these iterative rounds of testing and form design. This chapter (Chapter V) focuses exclusively on the development and testing of revised TILA statements, which was the primary focus of these interviews. Chapter VI describes work that ICF Macro conducted on other types of mortgage disclosures provided at application or after closing.

For each round of testing that is presented in this chapter, the report begins by describing the objectives and methodology used in that set of interviews, including the different forms tested and the structure of the interview protocol. This is followed by an overview of key interview findings and a description of significant design decisions made following that round.

## ROUND 8: ATLANTA, GEORGIA (NOVEMBER 2008)

### Objectives and Methodology

In November 2008, ICF Macro conducted nine cognitive interviews in Atlanta, GA. These interviews focused primarily on testing two proposed formats for a revised TILA statement and gathering data on how consumers might shop between loans using these forms. The interview protocol included the following sections:

- Participants in the interviews were first asked to review a TILA statement in one of two formats (version A or B) that described a 3/1 ARM product. They were then asked a series of questions designed to test their comprehension of the content on the form.
- Next, participants were given a second form in the same format describing a different 3/1 ARM. They were asked to compare the two loans and decide which loan they would choose. The purpose of this exercise was to gather information on which terms participants considered when comparing two loans.

- After this shopping simulation, participants were shown the alternative version of the TILA statement and asked to compare several aspects of the two forms in terms of their clarity and usefulness.
- Finally, participants were shown a table and graph that explained in more detail what could happen to their monthly payments, and were then asked questions to test their comprehension of the information. This table and graph showed what would happen to monthly payments under two scenarios: if market rates stayed the same (Scenario A) and if rates increased to the maximum allowed each year (Scenario B).

This first round of developmental testing focused on key terms that would likely be most prominent on a revised TILA. Additional content was added to the TILA in subsequent rounds. Six forms were used during the interviews; all are provided in Appendix D:

- TILA statements A1 and A2 (both have the same format, but different loan terms);
- TILA statements B1 and B2 (same loan terms as their respective A forms, but with an alternative format); and
- A payment scenario graph and table showing how payments could change over the life of the loan.

## Key Interview Findings

### *Initial Reactions to the Form*

- Each interview participant was asked to “think aloud” when reading through the TILA statement. In general, participants immediately noticed the interest rate, maximum interest rate, and the prepayment penalty. Most also noticed the finance charges, although they did not express as much interest in this information. Two participants commented they liked to know in advance what their payments would be.

### *Loan Obligation*

- Most participants did not notice the text in the “Your Rights as a Borrower” section that indicated they were not obligated to accept the loan shown. However, even those who did not notice this text still understood they were under no obligation to accept the loan.

### *General Loan Information*

- All participants correctly identified the term of the loan (30 years) and understood that it was an adjustable rate mortgage.
- Participants were confused about the difference between the “loan amount” and the “amount financed.” When asked to identify the amount of money they were borrowing, five participants indicated it was \$200,000 (the “loan amount”) while four stated it was \$195,250 (the “amount financed”). Two participants indicated the difference between the two was due

to the amount of “prepaid finance charges” listed on the form, but it was unclear whether either understood what this meant.

### ***Settlement Charges***

- Participants were asked about their understanding of settlement charges as illustrated on the sample form. Four participants indicated they did not know what “total estimated settlement charges” were. Others indicated that settlement charges included a variety of costs associated with the loan, such as the appraisal fee, legal fees, prepaid items, loan fees, taxes, documents, escrow, loan origination fee, processing fee, and title charges.
- Three participants were asked to describe the difference between settlement charges and “closing costs”; all said that the two terms were interchangeable.
- Participants all understood that “cash to closing” was related to the amount of money they would be expected to bring to the closing. However, two participants thought they would also have to pay the settlement costs shown at closing—that is, they believed the two figures were distinct and did not overlap.
- Interview participants were asked why the “cash to closing” amount might be less than the total estimated settlement charges (as it was in the model form used in this round of testing). Three participants indicated that some settlement charges could have been rolled into the cost of the loan, while one said that the seller might be paying some of the settlement charges. The remaining participants did not understand why the “cash to closing” figure might be lower.
- Version B displayed the settlement charges and cash to closing at the top of the form, while version A showed these terms in a separate section at the bottom. All but one participant indicated that they preferred to have this information near the top of the page.

### ***APR and Finance Charge***

- When asked to explain what “finance charges” are, participants were generally unsure. Most thought the finance charges were equal to the amount of interest that the borrower would pay over time; only a few understood the finance charges shown on the form included fees as well as interest. At least one participant was unsure whether principal was also included in the figure for finance charges shown.
- When asked to explain what the “APR” was, most participants indicated they did not know. Several indicated that the APR was the same as their interest rate. Others knew the APR was different from the interest rate but were unable to articulate how. A few participants commented that they primarily thought of this term as relating to credit cards.
- Most participants did not read the definitions of finance charge and APR during their first review of the form. After being directed to read these definitions, some participants realized that the finance charge included fees. Even after reading the definition of the APR, however, participants were unable to explain in their own words what it was.

- Because the APR and finance charge are more useful shopping tools when they are calculated over the specific length of time the borrower expects to hold the loan, the forms used in this round showed these terms over three different time horizons: 3 years, 5 years, and 30 years. Most of the participants, however, expressed confusion as to why the APR would vary over time. A few said the APR would increase over time because the interest rate would increase at the end of the introductory period, but most had no explanation. Participants' confusion in this respect was generally due to the fact that they did not understand what the APR signified.
- When asked how they would use the finance charges or APR in their decision-making, most participants indicated that they would not. Almost all participants indicated they would be much more likely to compare loans based on the interest rate than on the APR. One commented that he thought the APR would be useful if they expected to be in a home for 15 to 30 years, but not in the shorter term. Two specifically stated that the APR was too confusing for it to be useful to them.

### ***Rate and Payment Information***

- All interview participants were able to correctly identify the initial interest rate (5.625%) and the period for which the rate would apply (3 years, or until 2011). However, participants were unsure what would happen after that point. A few participants said that the interest rate would definitely go up after 3 years, but this was usually based on a general assumption that interest rates for ARMs tend to increase. The remaining participants thought the rate could go up or down depending on the market. None of the participants understood that the loan described in the form offered a discounted introductory rate.
- When the interview participants were asked what would cause their interest rate to go up or down, they gave a variety of responses, including “the market”; “the economy”; the prime rate; the “Fed rate,” and the Consumer Price Index. All of these responses seemed to reflect a common belief that rates would change based on external market forces over which they had no control.
- All interview participants were able to correctly identify the maximum highest payment (\$2,165.97), the maximum interest rate (11.625%), and the year in which it could reach this amount (2013). Participants generally understood that the highest possible payment and rate were only maximums, and would not definitely be reached.
- Most participants understood the interest rates and respective payments shown on the form as initial and “maximum ever” terms. They were much less clear as to the meaning of the middle interest rate and payment, which represented the maximum at the first adjustment.
- Most participants indicated that the amount shown on the forms for “estimated taxes and insurance” included property taxes, county taxes, and local taxes. Most participants thought the term “insurance” related to homeowner’s insurance, while a few thought it might also include private mortgage insurance (PMI). All participants recognized that while this was shown as a fixed amount on the form, both taxes and insurance could also vary over time—although some commented that they would not expect this amount to vary much.



- Versions A and B of the TILA statement both included a table of interest rates and monthly payments, but these tables were formatted very differently. This difference did not have a noticeable effect on participants' comprehension of the information. However, most interview participants indicated that they preferred the payment table shown in version B because a) it allowed them add the different pieces of their monthly payment from top to bottom, rather than left to right; and b) it presented changes over time from left to right, rather than from top to bottom. Two participants also noted that version B used the term “introductory rate,” which they found more descriptive than “initial rate,” the term used in version A.

### ***Risk Factors/Key Questions***

Versions A and B both included a section labeled Risk Factors, but the sections were formatted very differently. Version A listed two potentially risky features of the loan—the fact that the interest rate was adjustable and the fact that the loan included a prepayment penalty. Version B, on the other hand, listed six “key questions” related to potential risks, such as “Can my interest rate increase?” “Could I owe a balloon payment?” and “Will I owe a balloon payment?” Each question was answered “Yes” or “No,” with additional explanation provided with “Yes” answers.

- Regardless of which version they were shown, all but one interview participant understood that the loan they were shown included a prepayment penalty.
- The four interview participants who reviewed version B were asked about their understanding of the six key questions listed on the form.
  - All of the participants understood the questions related to changing interest rates, changing monthly payments, and prepayment penalties.
  - While most participants understood what was meant by a “balloon payment” when they read the questions and answers, one thought it pertained to paying down principal on the loan.
  - Most participants were confused by the questions “Will my monthly payments cover only interest and no principal?” and “Can my loan balance increase?” While these questions refer to interest-only payments and negative amortization, respectively, very few participants understood what they meant. For example, one participant thought that his/her loan balance would increase if the interest rate increased, while another thought the question referred to whether or not the borrower would be able to refinance in the future for more money.
- Participants were asked to directly compare versions A and B and indicate which format they preferred. All participants indicated that they preferred the “key questions” format of version B because they found it easier to read and more informative. Several also liked the fact that version B showed which risk factors did not apply to the loan, as well as those that did.

## ***Mortgage Shopping Simulation***

In one portion of the interview, participants were asked to review two TILA statements that showed loans with different terms and indicate which they would choose and why. Loan 1 had lower settlement costs and slightly higher interest rates and monthly payments, while Loan 2 had higher settlement costs and lower interest rates and payments.

- Participants focused almost exclusively on the interest rate, monthly payment, and settlement charges, and cash due at closing when making their decisions. Very few compared the finance charges or APRs of the two loans.
- Participants were split as to which of the loans they would choose. Three participants stated they would choose Loan 1, while four said they would choose Loan 2. The remainder did not express a clear opinion or indicated they would choose the loan based on the period they planned to retain the loan. Most indicated they would have difficulty deciding between the two loans, because the differences between them were so small.
- Some participants indicated their choice between the two loans would depend on their situation—for example, whether they could afford to pay higher settlement charges, or whether they specifically needed lower monthly payments.
- When asked whether it would make a difference if they knew that they were going to hold the loan for either 3 years or 30 years, most participants said that it would not. A few participants, however, revised their selection based on the concept that trading higher settlement charges for lower payments makes more sense in the long term, while accepting higher payments in return for lower settlement charges would make more sense in the short term.
- Participants were generally confused to find that the APR and finance charges for one of the loans were lower than the other for a 3-year term but higher for a 30-year term. Most participants did not understand why this would be the case.

## ***Payment Change Scenario Table and Graph***

After they completed their first review of the TILA, participants were shown a graph and corresponding table showing more detail about how their monthly mortgage payment would change over time under two different scenarios. The terms shown in the graph and table matched those in the first TILA statement that participants were shown.

- All participants understood the distinction between the two scenarios shown in the table and graph (“market rates stay the same” vs. “maximum possible rate and payment”).
- All participants understood the “Year of Loan,” “Period Beginning,” and “# of Payments” columns in the table, although one commented that the number of payments was redundant and unnecessary.

- Almost all participants understood from both the table and graph that even if market rates stayed the same, their payment would increase after three years. Several indicated that this surprised them, because this was not apparent from the first page of the TILA. However, the table did not improve understanding of why rates would increase if market rates stayed the same; even after seeing both the table and graph none of the participants understood that the loan in question had a discounted introductory rate.
- When looking at the graph and table, all participants understood that their rate and payment would never be higher than the maximum shown. Some, however, incorrectly thought that the rate and payment could never go below than the amounts shown for Scenario A (the scenario under which market rates stayed constant). This misconception was particularly prevalent when participants were looking at the graph; several incorrectly assumed that their payment would always fall between the two lines shown.
- Most participants indicated that they found the table easier to understand than the graph; one said that he<sup>23</sup> would not look at information presented in graphical format because he would assume it was difficult to understand.

## Subsequent Design Decisions

### *Loan Summary Section*

- Because all but one participant in this round preferred to have information about settlement charges provided near the top of the form, all forms developed for subsequent rounds of testing included these charges in the Loan Summary section at the top of the page.
- Several participants did not understand the relationship between “cash to close” and settlement charges. To address this confusion, forms developed for the next round showed the arithmetic relationship between total settlement charges, cash to close, pre-paid fees, and fees that were rolled into the loan amount.

### *APR and Finance Charge*

- Participants in Atlanta had a great deal of difficulty interpreting the table showing APRs and finance charges for multiple time horizons; most, in fact, had no understanding of why APRs over different time periods would vary. Therefore, the decision was made to highlight only a single APR and finance charge.
- Some participants connected the term “APR” with its meaning in a credit card context, and as a result assumed that the APR was the same as their interest rate. To address this potential confusion, forms used in the next round used two different labels for the Annual Percentage Rate: “This Loan’s Price Tag” and “Total Cost.”

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<sup>23</sup> To protect participants’ confidentiality, this report will refer to individual participants as “he” regardless of the actual gender of the participant.

- Most participants in Atlanta found the lengthy description of the APR that was provided to be confusing. The forms tested in the next round used a simpler, shorter phrase to describe this term (“the interest rate when some closing costs are factored in”). Variations of this shorter description were used in forms for all subsequent rounds.
- Despite the explanation provided on the forms, some participants in Atlanta did not understand that the APR represented a combination of both interest and fees. Therefore, one of the forms tested in the following round tried to display this relationship more explicitly as an “equation” (interest rate + fees = APR).

### ***Rate and Payment Information***

- Participants found the rate and payment table used in version B (which showed payment components vertically and time periods and payment changes horizontally) significantly easier to understand. Therefore, all forms for subsequent rounds included a table with this format.
- Because several participants indicated they preferred the label “introductory rate” to “initial rate,” all subsequent forms used this phrasing.
- Several participants in this round had difficulty understanding how their rate could change over time, therefore, explanatory text was added under the heading “Rate Change.” This text disclosed the length of the introductory period, the index and margin that would be used to determine the rate after the introductory period ended, and the periodic and lifetime rate change caps. The new text also stated that the loan had a discounted introductory rate, since none of the participants in this round realized that this was the case. This “Rate Change” information was added below the Payment Summary table.
- Because several participants indicated they would not use the payment change scenario graph, and because it would take up a great deal of space on the form, this graph was not included in any subsequent forms.
- While several participants had difficulty understanding the payment change scenario table that was tested this round, there was some evidence that others did benefit from more specific information about how their rates and payments would change over time. Therefore, this table was included in one of the versions tested in the following round (version D).

### ***Risk Factors/Key Questions***

- Participants in this round responded positively to the question and answer format used in the Risk Factors section of version B. Therefore, this format was used in all subsequent forms.
- Participants also liked the fact that version B indicated which risk factors were not associated with the loan being described, as well as those that were. Therefore, the forms developed for the next round included all Key Questions, even those to which the answer was “No.” This issue was revisited in the Dallas round of testing (Round 10).

- Most participants who were shown version B had difficulty understanding the Key Questions related to interest-only payments and negative amortization. As a result, the wording of these questions was revised for the forms tested in the following round.

## **ROUND 9: BETHESDA, MARYLAND (JANUARY 2009)**

### **Objectives and Methodology**

In January 2009, ICF Macro conducted nine cognitive interviews in Bethesda, MD. As with the previous round of interviews, the Bethesda round focused primarily on testing two proposed formats for a revised TILA statement and gathering data on how consumers might shop between loans using these forms. The interview protocol included the following sections:

- Participants in the interviews were first asked to review a TILA statement in one of these two formats (versions C or D) that described a 3/1 or 5/1 ARM product. They were then asked a series of questions designed to test their comprehension of the content on the form.
- Next, participants were given a set of two TILA forms in the same format that described two fixed-rate loans. They were asked to compare the two loans and decide which they would choose. As in the previous round, the purpose of this exercise was to gather information about which terms participants consider when selecting between loans. The decision was made in this round to use fixed-rate loans rather than ARMs to simplify the comparison for participants.
- After this shopping simulation, participants were shown the alternative TILA statement and asked to compare several aspects of the two forms in terms of clarity and usefulness.
- After reviewing the TILA statements, participants were asked to review some text for additional required disclosures about possible lender actions, loan assumption, property insurance, demand features, and refund of finance charges. The goal of this section of the interview was to assess the extent to which participants understood this language.

Version D included some information that was not on version C, including a table providing more detail about future changes in rates and payments (the payment change scenario table tested in the previous round) and a table showing APRs and finance charges for three different time horizons. As a result, version D was printed on two letter-sized pages. Version C was printed on one legal-sized page, as were the forms used in the previous round.

All TILA statements for this round (Round 9) included a section labeled “Optional Features,” which contained information on credit life insurance, reduced documentation loans, and owner’s title insurance.

Seven forms were used in these sections of the interview; all are provided in Appendix D:

- TILA statements C1, C2, and C3 (all forms had the same format, but C1 was a 3/1 ARM while C2 and C3 were fixed-rate loans);

- TILA statements D1, D2, and D3 (same terms as C1, C1, and C3, but with an alternative format); and
- A separate page of additional required disclosures.<sup>24</sup>

## Key Interview Findings

### *Initial Reactions to the Form*

- When asked what information was most important to them on the TILA statement, participants most frequently mentioned the interest rate (3 participants), monthly payment (2), Key Questions About Your Loan (2), the loan type (2), and the loan amount (2). Other items mentioned as most important included the timing of the interest rate adjustments, the fact that taxes and insurance were included in the monthly payments, and the boldface language at the bottom of the form indicating not to sign the form if you do not understand the terms.
- When asked whether there was any information that was not on the form that they would want to know, some participants commented that they would want a more detailed breakdown of their settlement charges.

### *Loan Obligation*

- Most participants did not notice the text at the top of the form that indicated they were not obligated to accept the loan shown. However, most interview participants who did not notice this text still understood they were under no obligation to accept the loan.

### *Loan Summary Section*

- Eight of nine participants correctly identified the term of the loan (30 years). All participants understood that the loan being described was an adjustable rate mortgage.
- When asked to identify the amount of money they were borrowing, five of nine participants correctly identified the loan amount shown on the form. Two participants incorrectly subtracted from the loan amount the down payment shown on the form, while one thought he was borrowing the “amount financed.” The remaining participant thought he was borrowing the amount financed plus the finance charge.
- When asked if they could identify the price of the home they were purchasing, most participants added the loan amount and down payment together to obtain the price of the home. None answered this question correctly, which would have required subtracting the closing costs that were included in the loan amount.

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<sup>24</sup> For the second day of testing, these disclosures were integrated into the TILA statements rather than being shown on a separate page.

- Generally, interview participants did not understand the concept of the “amount financed.” The two participants who came closest to correctly explaining this term said that it was the loan amount less the closing costs—although both noticed that based on the numbers shown on the form, this was not true. Others gave a variety of incorrect explanations for the amount financed, including that it was “how much escrow they would have,” the amount they would have to pay back, or the amount that they borrowed.
- Both versions of the TILA tested in this round broke closing costs into three categories: “paid before closing,” “included in loan amount,” and “due at closing.” In general, most participants did not understand the significance of these categories. For example, only four of the nine participants understood that the “due at closing” figure was what they would have to pay at settlement, and only three understood that they were effectively borrowing the costs “included in loan amount.”
- At least four participants confused the phrase “closing costs” with the amount that they would have to pay at closing when in fact some would be paid before closing. This misunderstanding persisted despite the fact that the costs “due at closing” were listed on the form.
- When asked whether they preferred the use of the term “settlement charges” or “closing costs,” most participants thought the two phrases had identical meanings. One thought settlement charges were a subset of closing costs, while another suggested “loan fees” as an alternative term.

### ***APR and Finance Charge***

- Only one of the nine participants understood that the APR included both interest and fees. About half thought that the terms APR and interest rate were identical in meaning, while others knew the APR was different but could not articulate how.
- When participants were asked how they would use the APR, all but two indicated they would not use the term. Of the two that indicated they would use it for shopping and comparing loans, one misinterpreted the APR as the “average interest rate” over time.
- Comprehension of the finance charge was higher than that of the APR; all but one participant was able to correctly describe what the finance charges signified. However, only one of the nine participants indicated that he would find this information useful.
- Versions C and D displayed the APR and finance charge in two very different formats. On version C, the APR and finance charge were provided in a box labeled “This Loan’s Price Tag.” Version D included a horizontal box across the page labeled “Total Cost” that presented the initial interest rate, settlement charges, APR and finance charge in the form of an equation.<sup>25</sup> Participants were split when asked which format they preferred; four preferred this aspect of version D while three preferred version C. However, regardless of which form participants were shown comprehension of the APR was minimal.

<sup>25</sup> The equation was stated as follows: interest rate + estimated closing costs = APR & finance charge.

- As in the previous round, participants were generally confused by the table on the second page of version D that showed the APR and finance charge over 3, 5, and 30 years. Few could explain why the APR would vary based on the time horizon used. Almost all participants ignored this table, except when specifically asked questions about it.

## ***Rate and Payment Information***

### *Understanding of Adjustable Rate*

- All but one participant were able to correctly identify both the initial interest rate and when the first rate adjustment could take place. Six of the nine were able to indicate how often the interest rate would change.
- All participants understood that the loan described by the versions C1 and D1 had an adjustable rate. However, only two understood that their initial rate was discounted, so a rate increase after the introductory period was very likely.
- Most participants believed that it was much more likely that their rate would increase than that it would decrease. However, this was based on a general distrust of adjustable rate products, rather than anything they saw on the form.
- When participants were asked why their interest rate would fluctuate, most correctly stated it was the “market” or “market rate.” As in previous rounds of testing, participants had a variety of explanations for what this “market rate” was based on, including the housing market, the “average going rate” for mortgages, and “the economy.” One participant correctly stated that the “market rate” was based on the rate the banks paid to borrow their money.
- All interview participants were able to correctly identify the maximum interest rate, and eight of nine were able to identify the year in which it could first reach this amount. However, most participants did not recognize the relationship between the year the maximum could be hit and the periodic caps described on the form.

### *Payment Summary Table*

- The Payment Summary tables used in versions C and D both showed the introductory and “maximum ever” rate and payment for the loan. Version C also included a third column that showed the maximum rate and payment at first adjustment. Two participants were confused by the difference between the “maximum at first adjustment” and “maximum ever” columns in the table. However, several other participants commented that the information about what could happen at the first adjustment was very important to them.
- Most participants indicated that when evaluating a loan, the maximum payment would be more important to them than the initial payment because they would want to make sure they could afford the highest possible payment. Two, however, said that the initial payment was more important because they would expect to refinance out of the loan before it hit the maximum.



- When specifically asked to read the information under the heading “Rate Change,” participants generally understood the text about rate caps. Most also seemed to understand the concept of an index and margin, although none understood the term “LIBOR.”<sup>26</sup>

#### *Taxes and Insurance (Escrow)*

- All participants understood that they would be required to pay taxes and insurance as part of their monthly payment. All but two recognized that the cost of taxes and insurance could change over time and that the amount on the form was only an estimate.
- When asked what was included in the amount shown for taxes and insurance, most indicated that it included property taxes and homeowner’s insurance. Two participants thought it might include costs shown elsewhere in the form, such as title insurance or credit life insurance. Another thought it included private mortgage insurance (PMI).
- The term “escrow” was shown on the form next to the itemization of taxes and insurance. All but two participants understood what this term meant. In almost all cases, however, this understanding was based on prior knowledge rather than the description provided on the form.

#### *Payment Change Scenario Table (Version D1)*

- The payment change scenario table on version D1 did not significantly improve participants’ understanding of what would happen to their rate and payment. Even after reviewing this table most participants did not understand that their introductory rate was discounted and would likely increase at the end of the introductory period.
- When reviewing the payment change scenario table, most participants understood that over time their rate and payment could be between the figures shown for Scenarios A and B, and also that they could not be above the amount shown for Scenario B. As in the previous round, however, some incorrectly thought that the rate and payment could not go below the amount shown for Scenario A (the scenario under which market rates stayed constant).
- When asked to assess the importance of the payment change scenario table, most participants indicated that it was not important because it largely repeated information provided elsewhere on the form. A few, however, commented that this table provided useful detail and showed more clearly that the interest rate could increase even if the market rates stayed the same.

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<sup>26</sup> In Version C, the “Rate Change” text was immediately following the Payment Summary table. In Version D, this text was on the second page, above the Payment Change Scenario table.

## ***Key Questions Section***

- All participants understood they would be charged a pre-payment penalty if they paid off the loan, refinanced, or sold the property within 3 years. All also understood the questions related to rate and payment change and late payment fees.
- Participants' understanding of the term "balloon payment" was inconsistent. Five were able to accurately define a balloon payment, while four gave a variety of incorrect definitions of the term, such as a higher payment due to a rate increase or a final loan payment that is lower than previous payments. One person confused a balloon payment with a jumbo loan.
- All participants understood the meaning of the question related to interest-only mortgages. However, several who were unfamiliar with this type of loan were confused as to why payments would ever be interest-only.
- Only two of the nine participants understood the question "Can my balance increase even after I've made payments?" Others had a variety of misinterpretations; some, for example, thought that the question referred to whether the lender could add a late fee to the loan principal or whether the borrower could borrow more money in the future, such as with a line of credit. Others thought this question was redundant with the question related to interest-only payments.
- When asked about the relative importance of the questions shown, several participants commented that the information about late payment fees would be less valuable to them because they would already expect to be charged a fee for making a late payment.

## ***Credit Life Insurance and Other Optional Features***

- About half of participants did not understand that this section showed features that were already included in their hypothetical loan. Instead, they thought these features were being offered to them at this point.
- When specifically asked what they could do to lower the cost of the loan, most participants did not understand that the credit insurance product was optional and could be declined in order to lower the cost of the loan.
- None of the participants understood what was meant by a "No Doc or Low Doc" loan. About half understood the meaning of "credit life insurance" and "owner's title insurance," although several thought that title insurance was a required, not optional, feature.

## ***Mortgage Shopping Simulation***

In one portion of the interview, participants were asked to review two TILA statements that showed loans with different terms and indicate which they would choose and why. Loan 3 had a higher interest rate (6.5% vs. 6.25%), and a slightly higher monthly payment. Loan 2, however, included a large amount of closing costs that were included in the loan amount. As a result, Loan 2 had a higher APR than Loan 3. Both were fixed-rate loans and did not require the borrower to pay anything at closing.

- Seven of the nine participants selected Loan 3, while two selected Loan 2.
- The two participants selecting Loan 2 stated they chose this loan because of the lower monthly payment and lower interest rate. Neither noticed the \$15,470 in closing costs that were rolled into the loan amount.
- Most of the participants who selected Loan 3 based their decision at least in part on the fact the APR for that loan was lower. However, as they discussed their decision it was clear that most of these participants did not understand what the APR represented. For example, two pointed to the APR and indicated that the “interest rate” was lower for Loan 3, when in fact this was not the case.
- When it was pointed out to participants that Loan 2 had a higher APR but a lower interest rate, almost none of the participants were able to explain how this could be.
- When asked if the length of time they planned to hold the loan would make a difference in their selection of the loan, almost all indicated that it would not. Only one participant who was comparing version D forms looked at the table on the second page that showed APRs and finance charges for different time horizons.

## ***Other Required Disclosure Text***

In addition to testing revised TILA statements, another goal of this round was to assess participants’ understanding of text related to other required disclosures. On the first day of interviews, participants were shown these statements on a separate sheet of paper. On the second day, the statements were integrated into the TILA statements used in the shopping simulation.

- Seven of the nine participants understood language indicating that the lender could demand the borrower pay off the loan at any time. All of those who understood the statement indicated it was an important piece of information.
- Seven of the nine participants understood a statement that early payoff of the loan could result in a refund of interest or fees. Participants who understood this text indicated that it was important information to them, although most indicated it would likely not have an impact on whether or not they accepted the loan.

- Seven of the nine participants understood a sentence indicating that the borrower “can obtain insurance from anyone that is also acceptable to the lender.” One of the two who misunderstood this sentence thought it meant that he was being charged PMI. Among those who understood the meaning of this text, most indicated it was not important because they already knew this information.
- Only four of nine participants understood language indicating that the loan could be assumed. One thought the text referred to the lender “selling” the mortgage to another lender, while another thought assumption could only take place if the original borrower defaulted. Two thought that the fact that a buyer could assume the loan would be a negative feature for the original borrower.

## Subsequent Design Decisions

### *Loan Summary Section*

- Some participants were confused by the fact that the down payment was shown on the TILA statement, and incorrectly thought that the amount they would be borrowing would be the “loan amount” shown on the page less their down payment. Therefore, the down payment was removed to simplify the form and improve comprehension.
- The description of “Loan Type” on the forms used in Bethesda included information about rate changes, including the length of the introductory period and the frequency with which the rate would adjust. This information was redundant with other sections of the form; therefore, the TILA statements used in the next round of testing did not include these details. Instead, they simply described the sample loan as a “3/1 Adjustable Rate Mortgage (ARM).”
- The mathematical relationship that was shown between total settlement charges, cash to close, pre-paid fees, and fees rolled into the loan amount did not improve consumer understanding of how these terms were related. Therefore, this section of the statement was eliminated from forms tested in the next round (Dallas). Instead, the Loan Amount section of these forms displayed the portion of the loan amount that was applied to settlement charges.
- Participants in the first two rounds (Rounds 8 and 9) generally did not understand the meaning of the amount financed. In addition, several participants in the first two rounds mistakenly thought the amount financed was the amount of money they would be borrowing. Therefore, for the next round the amount financed was removed from the Loan Summary section and the prepaid finance charge (the figure that is subtracted from the loan amount to determine the amount financed on the form) was placed in a footnote on the bottom of the page.
- Some participants expressed a desire to see a more detailed breakdown of their settlement charges. Therefore, all TILA statements used in subsequent rounds included a reference to “See your Good Faith Estimate for details.”

### ***APR and Finance Charge***

- As in the previous round, participants were generally confused by a table that showed APRs and finance charges for three different time periods. In addition, only one of nine participants referred to this table when choosing between two loans. As a result, this table was not included in any forms for subsequent rounds.
- Neither label used for information about the APR and finance charge (“This Loan’s Price Tag” or “Total Cost”) led to improved comprehension of these terms by participants. As a result, the forms used in the next round of testing (Dallas) used different labels for the APR: “True Cost Factor” and “Overall Rate of Fees and Interest.”
- Explicitly displaying the relationship between interest rates, settlement charges, APR and finance charge, as was done on version D, did not have a discernable impact on consumer understanding of the APR. Because of this, as well as concerns that this format gave too much prominence to the initial interest rate, this “equation format” was not used in subsequent TILA versions.
- Participants in this and previous rounds generally disregarded the finance charge when reading their TILA statements, other than commenting that the number was very large. Several commented that this information was not useful, since they had no choice but to pay a large finance charge if they wanted to purchase a home. Therefore, on subsequent versions of the form the finance charge was deemphasized and moved from the top of the first page to the “More Information About Your Payments” section under the heading “Total Payments.”

### ***Rate and Payment Information***

- When asked to compare the Payment Summary tables on versions C and D, several participants commented that the columns providing information about the maximum rate and payment at first adjustment was important to them. Therefore, all versions for subsequent rounds included this column in the Payment Summary table.
- The presence of the more detailed Payment Change Scenario table on the second page of version D did not noticeably improve most participants’ understanding of what would happen to their rate and payment over time. Most participants indicated that this table was not important to them, because it was largely redundant with other parts of the form. For this reason, this table was not included in any subsequent forms.

### ***Key Questions Section***

- As in previous rounds, participants continued to respond positively to the question and answer format used in the Key Questions section of the TILA statement. As a result, this format was retained in the forms for all subsequent rounds of testing.
- Some participants did not realize that the Key Questions shown on the form were describing potentially risky loan features. Therefore, on forms for all subsequent rounds the title of this section was changed from “Key Questions About Your Loan” to “Key Questions About Risks.”

- For Round 9, an additional question about late payment fees had been added to the forms being tested. However, several participants indicated that this information was less important to them. Based on these results, all subsequent forms did not include this question.
- As in Atlanta, some participants in this round had difficulty understanding the difference between the questions related to interest-only payments and negative amortization. As a result, the wording of these questions was revised again for the following round.

### ***Credit Life Insurance and Other Optional Features***

- Because participants generally did not understand the Optional Features section of the forms used in this round, this section of the TILA was significantly restructured for the next round of testing. References to reduced documentation and owner's title insurance were dropped, and the credit life insurance disclosure was revised to clarify that the product is optional and could be declined.

### ***Other Required Disclosure Text***

- Participants indicated that information about loan demand features was particularly important to them, so the decision was made to include this information on the TILA statement in the Key Questions section.

## ROUND 10: DALLAS, TEXAS (FEBRUARY 2009)

### Objectives and Methodology

In February 2009, ICF Macro conducted 10 cognitive interviews in Dallas, TX. As in previous rounds, this round of interviews focused primarily on testing two proposed formats for a revised TILA statement and gathering data on how consumers might shop between loans using these forms.

As part of the interview, participants were shown several alternatives for how the APR could be displayed. All of these alternatives provided context for how the loan's APR compared to that of other similar loans. All disclosed the boundary between prime and higher-priced loans; that boundary is 1.5 percentage points over the "average prime offer rate" (APOR) calculated by the Board for first lien loans and published each week.<sup>27</sup> Some of the APR presentations also disclosed the APOR itself, which was described as the average rate "on comparable loans recently offered to borrowers with excellent credit."

The interview protocol included the following sections:

- Participants in the interviews were first asked to review a TILA statement in one of two formats (versions E or F) that described a 3/1 ARM product. They were then asked a series of questions designed to test their comprehension of the content on the form.
- Next, participants were given a second form describing a different 3/1 ARM in the same format, but with different terms. They were asked to compare the two loans and decide which they would choose. As in previous rounds, the purpose of this section of the interview was to gather information about which terms participants consider when selecting between two loans.
- After this shopping simulation, participants were shown the alternative TILA statement and asked to compare several aspects of the two forms in terms of their clarity and usefulness.
- After completing their review of the TILA statements, participants were then shown the alternative APR presentations and asked a series of questions designed to measure their comprehension of the information.
- As in the previous round, after reviewing the TILA statements participants were asked to review some additional text for required disclosures about possible lender actions, loan assumption, property insurance, refund of finance charges, and late payment fees.

The TILA statements tested in this round included two new items in the Key Questions section. These questions related to loan demand features ("Can my lender demand full repayment at anytime?") and equity sharing features ("Do I have to share any equity I gain?").

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<sup>27</sup> The boundary is 3.5 percentage points for subordinate lien loans.

Six forms were used in these sections of the interview; all are provided in Appendix D:

- TILA statements E1 and E2 (both have the same format, but different terms);
- TILA statements F1 and F2 (same terms as E1 and E2, but with an alternative format);
- A variety of alternate approaches to displaying the APR; and
- Additional text for required disclosures.

All TILA statements used in this round of testing were printed on one legal-sized page.

## **Key Interview Findings**

### ***Initial Reactions to the Form***

- After participants first reviewed the TILA statement, they were asked what pieces of information on the form were most important. Participants most often mentioned the monthly payment (5 participants), loan type (4), interest rate (4), key questions (3), loan amount (3), and term of loan (3).

### ***Loan Obligation***

- Most participants did not notice the text that indicated they were not obligated to accept the loan shown. However, all but one participant still understood they were under no obligation.

### ***Loan Summary Section***

- All participants correctly identified the term of the loan (30 years) and the amount borrowed.
- When asked how much of the \$200,000 loan they could apply to the price of the home they were purchasing, only three participants understood that \$198,000 would go toward the home purchase and the remaining \$2,000 would be used to pay for closing costs.
- When asked if the Total Settlement Charges listed on the form included their down payment, half of the participants incorrectly stated that it did, while three more indicated they did not know.

### ***APR***

- Two different labels were used for the APR in this round of testing; on version E the term was labeled “True Cost Factor,” while version F used the phrase “Overall Rate of Fees + Interest.” When asked to explain in their own words the definition of this term, only two participants provided an explanation related to its actual meaning. All other participants were confused by the term; for example, several thought the APR represented an “average” or “overall” interest rate. None of the participants were able to successfully explain how the “True Cost Factor” or “Overall Rate of Fees plus Interest” differed from the interest rate.



- Version E displayed the APR (called the “True Cost Factor”) without a percentage sign. This variation was an attempt to decrease the extent to which participants confused this term with their interest rate. However, this had no noticeable impact on participant understanding; in fact, even participants who saw version E discussed the True Cost Factor as if it was a percentage and confused it with their interest rate.
- When asked to indicate whether they preferred the treatment of the APR on version E or F, about half of participants selected each form. As in the previous round, however, participant comprehension of the APR was extremely low regardless of which version participants were shown.

### ***Rate and Payment Information***

#### *Understanding of Adjustable Rate*

- All interview participants were able to correctly identify the initial interest rate. All participants also understood that the loan had an adjustable rate and that the rate and payment would be fixed for the first three years. Participants also were able to correctly identify the size of their payment during that time.
- Most participants understood that the rate could change annually after the third year, but two did not know how often the rate could change.
- Almost all participants were able to correctly identify the maximum interest rate of the loan. One participant was confused by the text below the table that indicated the rate could increase by 2% each year, and mistakenly thought this meant there was no maximum rate.

#### *Payment Summary Table*

- Several participants mistakenly thought the different columns in the payment table represented what would happen to their rate and payment, rather than what could happen. For example, at least two thought that in 2012 and 2014 their rate and payment would increase to the amount shown in those columns of the table, and did not understand that their rates and payments might actually be lower than those shown.
- When asked whether the initial or maximum payment would be more important to them when considering an adjustable-rate loan, eight of the ten participants indicated that the maximum payment would be more important.
- Underneath the Payment Summary table, both versions of the TILA statement used in this round included some explanatory text. Version E included an additional sentence that did not appear on version F: “If the market rate does not change, at the end of this period your interest rate will increase by 2.00%, adding approximately \$250.00 to your monthly payment.” The inclusion of this statement did not have any noticeable effect on participant understanding.

- Almost all participants understood that the interest rate would change based on the “market rate” (the term used in the statement). When asked to explain what is meant by the “market rate,” participants gave a variety of answers, including the stock market, the price of homes in a community, and “how the economy is doing.” One participant understood the term “LIBOR.”
- Most participants had difficulty connecting the rates shown in the payment table with the information about periodic and lifetime caps below the table. In fact, for a few participants the presence of this explanatory text seemed to decrease comprehension of the table; these participants initially understood what was shown in the table, but then became confused when reading the text.
- Almost all participants understood the information provided under the heading “Total Payments,” including the number of payments, total of payments, and finance charge. When asked how they would use this information, most participants indicated that they would not.
- No participants commented on the footnote providing the prepaid finance charge during their first reading of the form. When the interviewer pointed out this footnote and asked participants to explain what the “prepaid finance charges” signified, none were able to do so.

#### *Taxes and Insurance (Escrow)*

- All but one participant indicated they had heard the term “escrow” previously. Most seemed to have a thorough understanding of the term before reading the form.
- All participants understood the amount they would pay for taxes and insurance could change over time. However, three participants did not realize that the amount shown in the table was estimated, and would not necessarily be accurate when they closed on the mortgage.
- All but two participants assumed that the “insurance” referred to in the payment table was homeowner’s insurance. One thought this figure might include private mortgage insurance (PMI), while another thought it could include other types of insurance but did not specify which kinds.

#### **Key Questions Section**

- Eight of ten participants understood from the Key Questions section that the lender could demand repayment of the loan at any time. However, two of the eight mistakenly thought that the lender could only do so if they became delinquent.
- Half of the participants misunderstood the question related to equity-sharing. Several were confused by the last sentence of this section (“In exchange, we are giving you a lower interest rate”) and mistakenly thought the form was indicating they would receive a lower interest rate at the point when they sold their home. Regardless of whether they fully understood the information provided, all participants stated that an equity-sharing feature would be a negative feature for the borrower.

- Version F showed eight key questions in this section, each with an answer of “Yes” or “No.” Version E only showed those questions whose answers reflected risky features of the loan, and then provided a concise statement listing other features not present in the loan terms. All but two participants indicated they preferred to be shown all eight key questions, even when the answer showed that a given feature did not apply to the loan. Two participants preferred to be shown only those questions whose answers implied risk.
- Version E included “interest-only payments” in a list of features that did not apply to the loan, while version F listed the question “Will my monthly payments reduce my loan balance?” and indicated that the answer was “Yes.” In both forms, the intent was to indicate that this loan did not include interest-only payments. However, participants’ comprehension of this fact was slightly higher when viewing version F.
- A few participants commented they did not like the fact that the answers to the Key Questions related to rate and payment change were simply “Yes.” They indicated that more explanation should be provided to help borrowers understand their loan more completely.

### ***Credit Life Insurance***

- Almost all participants were somewhat familiar with credit life insurance before seeing the form; only one indicated that he had never heard of this feature before.
- Almost all interview participants understood from their reading of this section of the form that credit life insurance is not required. All understood that this insurance would have a monthly cost associated with it and that this cost was not included in the monthly payments shown elsewhere on the form.
- After reading this section of the form, several participants commented that credit life insurance sounded like an important loan feature and indicated that they would want to enroll.

### ***Mortgage Shopping Simulation***

Participants were asked to review two TILA statements that described different 3/1 ARMs. Loan 1 had a higher interest rate and monthly payment, while Loan 2 had higher settlement charges and a slightly higher APR. Participants were asked to select one of the loans and provide reasons for why they chose it.

- Eight of the ten participants selected Loan 2 (i.e., TILA version E2 or F2). These participants generally realized the loan had higher settlement charges, but felt that the lower interest rate and monthly payments outweighed the higher up-front costs.
- Two participants selected Loan 1 (version E1 or F1). They did so primarily because of its lower settlement charges, although one also considered the APR (see below).

- Only one person considered the APR when choosing between the two loans. This participant chose F1, because it had a lower “Overall Rate of Fees + Interest” (APR) and lower settlement charges. When other participants were asked why they had not used the APR, most indicated they did not understand what the term meant.
- When asked if the length of time they planned to hold the loan (3 vs. 30 years) would make a difference in which loan they selected, just over half indicated that it would not. Four participants, however, indicated that the first loan would be the better choice over 3 years while the second loan would be preferable over 30 years. Their reasoning was that over a longer period of time it made sense to pay a larger up-front charge in exchange for a lower interest rate, which was what the second loan offered.

### ***Alternative APR Presentations***

- As part of the interview, each individual was shown two alternative presentations of the APR that provided context for how the loan compared to others in the market. One version included a graphic that placed the APR on a scale, along with a line distinguishing “prime” and “subprime” loans. The second version did not include a graphic, but included text that listed both the cut-off between “prime” and “subprime” loans and the average APR received by people with “excellent credit.”
- When looking at either the graphic or text-based versions, participants generally understood that a lower APR was better for them and that people with better credit would be offered loans with a lower APR. However, it was not clear to what extent this understanding was based on the material presented to them or on prior knowledge.
- Both versions used the word “subprime” in their descriptions. While almost all thought the word had a negative connotation and indicated they would not want a “subprime loan,” several did not understand the meaning of this term.
- In general, participants found the text-based presentation of the APR easier to understand. The primary reason for this was that the text-based presentation listed the average APR received by people with excellent credit, while the graphic presentation did not.
- A few participants suggested the graphic and text be used in combination to explain the information more fully.

### ***Other Required Disclosure Text***

- All or almost all participants understood the disclosure text related to possible lender actions, property insurance, refunds of interest and fees, and late payment fees.
- As in previous rounds, several participants had difficulty understanding the text about loan assumption. In some cases this confusion was due to the fact that the phrase “take over your mortgage” was seen as threatening or a negative feature of the loan.

## Subsequent Design Decisions

### *Loan Summary Section*

- Some participants in this round of testing were confused as to whether the amount shown for “settlement charges” included their down payment, so a statement was added to the TILA statement indicating that the down payment was not included in the settlement charges.
- Most participants did not understand after reading the forms that a portion of the loan amount would go toward settlement charges. Therefore, the forms developed for the next round more explicitly broke the loan amount into two portions: the amount applied toward fees and the amount available for the borrower’s own use.

### *APR*

- Neither of the labels used for the APR (“True Cost Factor” and “Overall Rate of Fees and Interest”) led to improved comprehension of the term. As a result, forms used in subsequent testing used the original label “Annual Percentage Rate” for this term. Rather than varying the label used, the form designers focused on improving the presentation this term.
- Displaying the APR without a percentage sign had no discernable effect on consumer understanding, so the percentage sign was used in subsequent versions of the TILA statement.
- Participants in Dallas generally reacted positively to the new alternative presentations of the APR they were shown. Therefore, the forms used in the following round of testing included both text-based and graphic context for how the APR compared to that of other loans.

### *Rate and Payment Information*

- Some participants in this and previous rounds had difficulty relating the rate caps to the maximum rates shown in the payment table. Therefore, one of the versions designed for the next round (version G1) included text that explicitly connected the lifetime cap to the maximum interest rate.

### *Key Questions Section*

- Most participants in this round preferred to have all Key Questions shown, even those to which the answer was “No.” However, ICF Macro and Board staff were concerned that listing all eight Key Questions might not be an efficient use of space, since affirmative answers to some of the questions (such as that related to a demand feature) would be rare. Therefore, the decision was made to require that Key Questions related to rate and payment changes, pre-payment penalties, interest-only payments and balloon payments would be required on the form, whether the answer to the question was affirmative or negative. Key Questions related to negative amortization, equity-sharing, and a demand feature would only be required if the answer was affirmative. This policy was implemented in all forms designed for subsequent rounds of testing.

- Due to continued lack of participant understanding of the Key Question related to interest-only payments, the wording of this question was revised slightly on forms for the following round.
- Because some participants commented they did not like the fact that the responses for the first two Key Questions stated simply “Yes” with no explanation, in subsequent forms a short explanation accompanied all affirmative answers.

### ***Credit Life Insurance***

- Based on the findings from this round, the Board staff was concerned that the presence of information about credit life insurance on the first page of the TILA statement increased awareness of the product, but did not make consumers aware that they might not qualify for the product’s benefits. Therefore, the decision was made to remove this information from the TILA statement and to add language to alert consumers that they might not be eligible for benefits from the insurance.

### ***Other Required Disclosure Text***

- Because participants had difficulty understanding the disclosure text describing loan assumption, this text was revised and tested again in the next round of interviews.

## ROUND 11: PROVIDENCE, RHODE ISLAND (MARCH/APRIL 2009)

### Objectives and Methodology

On March 30 and April 1, 2009, ICF Macro conducted 10 cognitive interviews in Providence, RI. Unlike previous rounds of interviews, which focused primarily on hybrid ARMs, the TILA statements tested in this round described more complex mortgage products. Loan G was an interest-only 5/1 ARM that included PMI. Loan H was a 3-year fixed-rate mortgage with a balloon payment. Loan H also had an equity-sharing feature, which was disclosed in the Key Questions section. Loan G had a subprime APR, while Loan H had an APR just under the cutoff for subprime. Two different versions of the TILA statement were developed and tested for each of these two loan products.

To avoid having the statements appear cramped or dense, forms for this round were laid out on two letter-sized pages rather than one legal-sized page. The “Key Questions” section was moved to the second page, as was some descriptive text about rate and payment changes (under the heading “More Information About Your Payments”).

The interview protocol included the following sections:

- Participants in the interviews were first asked to review one of the TILA statements that described an interest-only ARM product (version G1 or G2). They were then asked a series of questions designed to test their comprehension of the content on the form.
- Next, participants were given a TILA statement that described the second loan product (version H1 or H2). They were asked to review this loan and asked several questions about its content.
- After reviewing the TILA statements, participants were asked to review some additional text for required disclosures about assumption, negative amortization, and reduced documentation loans.

For the Providence round of testing and all subsequent rounds, the footnote for prepaid finance charges was deleted. Instead, the amount financed was shown under the heading “Total Payments,” in the “More Information about Your Payments” section on the second page of the statement.

Five forms were used in these sections of the interview; all are provided in Appendix D:

- TILA statements G1 and G2 (both have the same terms, but a different format);
- TILA statements H1 and H2 (both have the same terms, but a different format); and
- A separate page with additional text for required disclosures.

## Key Interview Findings

### *Loan Obligation (Loan G)*

- All but one participant understood that when they received this form they would not be obligated to accept it. As in previous rounds, this understanding was based more on prior knowledge than on the fact it was stated on the form.
- Three participants incorrectly believed that by signing the TILA statement they would be committing themselves to the loan. Another participant commented that even though the form specifically states that a signature only indicates receipt of the form, the cautionary language above the signature line makes it appear binding.

### *Loan Summary Section (Loan G)*

- All participants correctly identified the term of the loan (30 years) and the amount borrowed.
- When asked if they could identify how much of the \$200,000 loan they could apply to the price of the home they were purchasing, about half of participants correctly indicated that \$198,000 would go toward the home purchase. The remaining participants were not able to answer this question correctly.
- Only three participants understood that the \$2,000 that had been rolled into the loan amount for Loan G was included in the amount shown for Total Settlement Charges. Others thought this \$2,000 would be an additional charge or were not sure.
- Almost all participants understood from the form the down payment was not included in settlement charges.

### *APR (Loans G and H)*

- Several participants initially confused the APR with their interest rate. When asked to explain the difference between the interest rate and APR, only two participants were able to explain that the APR included settlement charges—even though the APR was described on the page as “Your interest rate with settlement charges included.”
- Despite the fact that participants did not generally understand what the APR was, most realized from the graphic that the APR for Loan G fell in the “subprime” category, and that this meant their loan was more costly than a prime loan. These participants indicated this made them feel more negatively about the loan.
- All participants were shown Loan H and asked how they would react to the loan if they had excellent credit. About half indicated that if they had excellent credit they would expect to get a lower APR closer to the average prime offer rate (APOR). The other half did not seem concerned that their APR was different from the APOR, and did not indicate that this fact would affect their decision whether to accept the loan.



- Five participants were asked to explain the graphic on Version G-1 or H-1—in particular, the significance of the two dotted lines on the graph. Four of the five participants understood that one dotted line represented the APOR, while the other represented the lower end of the range labeled “subprime.” Two of the five, however, thought the graphic divided the range of possible APRs into three categories—one for people with excellent credit (below the APOR), one for people with “average” credit (between the APOR and “subprime” cutoff), and one for people with poor credit (the area labeled “subprime”). This was not the intent of the graphic, since this interpretation misrepresents the significance of the APOR.
- Although the word “subprime” had a negative connotation for them, only a few participants understood that a subprime loan was a higher-priced loan usually given to borrowers with poor credit. Two participants thought the term “subprime” meant the loan had a rate lower than the prime rate.
- The APR graphic in versions G1 and H1 was slightly different than that on versions G2 and H2. In G1 and H1, the APOR was represented by a dotted line, while the APR for the loan being described was represented by a diamond. In G2 and H2, the APOR was represented by a star, and the loan being described was represented by an inverted triangle and labeled “this loan.” About three quarters of participants indicated they preferred the latter format. Some commented that a star was an appropriate symbol for the APOR, since it represented a very good rate.

### ***Rate and Payment Information***

#### *Understanding of Adjustable Rate (Loan G)*

- When asked to identify the initial interest rate of the loans, several participants mistakenly pointed to the APR. This seemed to be largely due to the prominence of this figure on the form.
- All participants understood the rate would change, and all but one understood that the first rate adjustment would occur after 5 years (2014). However, most did not realize their initial rate was discounted.
- Only three of the ten participants understood that the rate would change annually after the first 5 years.
- When participants were asked what determined how the rate would change over time, three participants understood the rate was based on an index. Most other participants indicated the rate change was based on the “market rate” or the “national rate.”

### *Payment Summary Table (Loan G)*

- The maximum interest rate was correctly identified by eight of ten participants. Four of five participants who saw version G1 understood that the interest rate could increase no more than 2 percentage points each year.<sup>28</sup>
- All participants were able to identify the amount of the first monthly payment and all knew the payment would be same for the first 5 years.
- When asked what was more important to them in terms of the payments, six participants indicated the “maximum ever” payment was more important than the initial or first adjustment payments.
- As in previous rounds, several participants were unsure what would happen to their payment after the introductory period ended. Some assumed the payment would definitely increase to the amount shown in the “maximum at first adjustment” column, while others understood that their payment could be lower than that shown.

### *Interest-Only Payments (Loan G)*

- Only two of the ten participants realized during their first review of Loan G that their payments would be interest-only during the first 5 years. All participants eventually understood this feature of the loan, but in most cases only after being prompted by the interviewer to re-read portions of the form.

### *Taxes and Insurance (Escrow) (Loans G and H)*

- On versions G1 and G2, only one participant thought the amount for taxes and insurance shown in the payment summary table was the actual amount he would pay; all others understood this figure was an estimate. Almost all participants also understood that taxes and insurance could change over time.
- Almost all participants understood Loan H did not include an escrow account and that as a result they would have to pay taxes and insurance on their own. In all cases, this understanding was based on the inclusion of the words “not included” in the escrow row of the Payment Summary table; fewer participants noticed this information in the More Information About Your Payments section.

### **Key Questions Section (Loans G and H)**

- All participants understood that Loan G included a prepayment penalty if they paid off the loan within the first 2 years.
- When asked to read the Key Question related to interest-only payments, almost all participants understood they would not be paying any principal for the first 5 years they made payments. All

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<sup>28</sup> Form G2 did not include information about the periodic cap on rate change.

realized that this could be a risky feature, although one participant commented he might still accept an interest-only loan if that were the only type he could afford.

- When looking at Loan H, only three of ten participants noticed the equity-sharing feature in their first review of the form. Four others eventually saw this information in the Key Questions section, while three never did.

### ***“More Information About Your Payments” Section (Loan G)***

- All participants had heard of PMI previously. However, only two of the ten participants noticed the text under the heading Escrow that indicated that they would be paying PMI with this loan.
- Version G1 included information about periodic and lifetime rate change caps, while version G2 did not. Participants who saw G1 showed a greater understanding of how their rate could change over time. For example, some participants who saw G1 were able to use the periodic rate change cap information to determine what their maximum rate would be in 2015, while no participants who saw G2 were able to correctly answer this question. When asked whether information about rate caps would be important to them and should be included on the form, most participants responded affirmatively.
- Almost all participants correctly identified the number of payments and total of payments, as well as the amount that would go to interest and fees. As in previous rounds, none were able to explain what was meant by the “amount financed,” although this did not affect their comprehension of other parts of the form.

### ***Balloon Payment (Loan H)***

- Almost all participants realized in their initial review of Loan H that it included a balloon payment. All understood that the “balloon payment” was a large payment that they would have to make after 3 years.
- Most noticed the information about the balloon payment in the Payment Summary table. Only one noticed it first in the Key Questions section.
- Versions H1 and H2 provided information about the balloon payment in two different ways. H1 showed the balloon payment in a separate column in the Payment Summary table, while H2 showed the balloon payment in a separate row below the table. The format that was used did not have a discernable effect on participant understanding; almost all participants noticed the balloon payment regardless of which form they saw. Participants were evenly split in terms of which of the two formats they felt was the clearest presentation of the balloon payment.

## ***Other Required Disclosure Text***

- At the end of the interview, participants were asked to review three different disclosures and describe what they meant in their own words. The first disclosure was revised text related to loan assumption. The results were more positive than in previous rounds; most participants understood what was meant by the fact that the lender could “permit the new buyer to take over the payments” on their mortgage and that this could be a positive feature for a borrower.
- In addition to the language about loan assumptions, participants were also asked to review two disclosures in the “Q&A” format used in the “Key Questions About Risk” section of the TILA. The first described negative amortization by indicating that the loan balance for the loan could increase over time, even if the borrower made payments. All stated that this was not a feature that they would want on their loan. While few participants had previously heard the phrase “negative amortization,” almost all understood that if this disclosure were true they could potentially end up owing more money than they had originally borrowed.
- The other “Key Question” disclosure participants were asked to review described no- or low-documentation loans. It indicated that the loan had a higher rate or fees because the borrower did not document his or her employment, income, or other assets. While several were surprised at the disclosure because they assumed that documentation always had to be provided, almost all understood its meaning.

## **Subsequent Design Decisions**

### ***Loan Summary Section***

- Although the breakout of the loan amount into two amounts—the amount applied towards fees and the amount available for the borrower’s own use—was more successful than previous attempts to communicate information, almost half of the participants were still confused by this portion of the form. As a result, this reference was removed from the Loan Amount section. Instead, underneath the settlement charges a reference was added referring to what portion of the fees were included in the loan amount.

### ***APR***

- Two different versions of the APR graphic were tested in Providence. Generally, participants reacted more positively to the graphic used in versions G2/H2, which included more explicit labels for the APOR and the APR of the loan offered. As a result, this basic graphic template was used in forms for subsequent rounds of testing.
- Several participants were confused by the word “subprime” as it was used in the APR section, so this word was not used in forms for the next round. Instead, the “subprime” portion of the APR range in the graphic was labeled “high cost.”
- Several participants in Providence and previous rounds of testing expressed a belief that a small difference in APR would not likely make a significant difference in their monthly payment. To combat this misconception, a reference was added to forms for the following

round (Denver) that indicated the monthly dollar amount a 1 percent decrease in APR could save a borrower.

### ***Rate and Payment Information***

- Because participants continued to struggle to understand what would happen to their payment at the end of the introductory period, for the next round of testing information was added to the first page of the form describing what would happen if market rates did not change. This text appeared as a “Teaser Rate Notice” under the payment summary table.
- Most participants did not notice the disclosure in the “More Information about Your Payments” section that indicated their loan included private mortgage insurance. Therefore, the forms for the next round of testing included this information in the heading of the escrow row in the Payment Summary Table on the first page.
- Because most participants did not initially realize that payments for Loan G would be interest-only for the first 5 years, in the next round a reference to “interest-only payments” was added under Loan Type to make this feature more prominent.
- In the model forms and clauses it releases in July 2009, the Board will propose that in most cases the balloon payments be displayed in a separate row at the bottom of the payment table (as in version H2). Since participants had no clear preference between the different formats tested, the rationale for this decision was that it may be easier to add a row to the payment table rather than a column since space is more likely to be limited horizontally on a page.

### ***Key Questions Section***

- In an attempt to improve comprehension among participants, the wording of the affirmative answer to the Key Question related to interest-only payments was revised slightly on forms for the following round.
- Several participants did not understand that interest rate adjustments for the sample loan could occur on an annual basis, so a reference to the frequency of adjustment was added to the answer to the first Key Question (“Can my interest rate change?”).

## ROUND 12: DENVER, COLORADO (APRIL 2009)

### Objectives and Methodology

In April 2009, ICF Macro conducted 10 cognitive interviews in Denver, CO. The TILA statements tested in this round described two different mortgage products: an interest-only ARM and a payment option ARM. The goal of the interviews was to assess how clearly the revised statement described the terms of these more complex products.

The interview protocol included the following sections:

- Participants in the interviews were first asked to review one of two TILA statements that described an interest-only ARM (versions J-IO or K-IO). As in previous rounds, they were then asked a series of questions designed to test their comprehension of the content on the form.
- Next, participants were given the alternate interest-only TILA statement, which varied only in the way in which APR information was presented on the form. Participants were asked to compare the APR sections on the two forms and indicate which format they felt was clearer and more informative. In order to minimize learning effects, the order in which participants were shown the two interest-only TILA statements was rotated between participants.
- Participants were then shown a TILA statement that described a payment option ARM product (versions J-PO or K-PO). Again, participants were then asked a series of questions designed to test their comprehension of the content on the form. They were subsequently shown the alternate payment option TILA statement and asked which aspects of each form they found clearer. As with the interest-only loans, the order in which the participants were shown the two payment option TILA statements was rotated.
- After reviewing the TILA statements, participants were shown some additional text related to credit life insurance and were asked questions to test their understanding of the content.

Five forms were used in these sections of the interview; all are provided in Appendix D:

- TILA statements J-IO and K-IO, which described interest-only ARM products (identical except for the format of the APR section);
- TILA statements J-PO and K-PO, which described payment option ARM products (identical except for the format of the APR and Payment Summary sections); and
- A page with an additional disclosure about credit life insurance.

Versions J-IO and K-IO displayed an APR of 7.59%, which fell into the “high cost” (i.e., subprime) area shown on the form. Versions J-PO and K-PO displayed an APR of 6.01%, which was close to, but not in, the high cost range shown on the form.

Prior to this round, ICF Macro and Board staff determined that the Payment Summary table tested in prior rounds would not be appropriate to use for a payment option ARM. Because payment option ARMs are significantly different products, the table being used for other types of loans would not have disclosed several important pieces of information, such as the fact that multiple payment options were available each month. Therefore, versions J-PO and K-PO include a new Payment Summary section that was customized for this specific type of product. Because of the complexity of payment option ARMs, ICF Macro did not attempt to describe all details of the loan product. For example, the TILA statement that was developed did not display all payment options available for this type of loan; it only provided information about the full and minimum payments. The primary goals of the statement were to communicate to consumers that: a) making the minimum payment each month would cause their loan balance to increase; and b) their minimum required payment could increase dramatically in the future.

## Key Interview Findings

### *Loan Summary Section*<sup>29</sup>

- All participants correctly identified the term of the loan (30 years). All but two correctly identified the amount that was being borrowed; the remaining two incorrectly thought they were borrowing the “amount financed” shown on the second page of the form.
- Almost all participants understood that the settlement charges shown on the form did not include any down payment they would owe.
- TILA statements used in Denver indicated that \$2,000 of the settlement charges had been “rolled into” the loan amount. All five participants who were shown these forms were confused when this language was pointed out to them; most thought this meant the loan amount would be different than the amount shown (\$200,000). On the second day of testing, participants were shown an alternative wording for this portion of the disclosure (“\$2,000 of these charges is already included in your loan amount above”). Participants found this phrasing much clearer; all understood that the \$2,000 was part of the \$200,000 loan amount shown on the form.

### **APR**

- As in previous rounds, participants continued to confuse the APR with their interest rate; several, in fact, referred to the APR as the interest rate during their initial review of the form. When participants were asked to explain why the APR and interest rate listed on the form were different, only two correctly indicated that the APR includes settlement charges. All others were either unable to explain the difference or provided an incorrect explanation; two, for example, thought the APR was the average of the interest rates they would be charged over time.

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<sup>29</sup> Participants answered questions about the loan term and settlement charges while reviewing the interest-only loan.

- The forms used in this round included a graphic that showed a range of possible APRs. The APOR was identified on this range, and labeled the “Avg. Best APR.” The range of subprime APRs was shaded darker on the scale, and was labeled “high cost.” All participants were able to correctly explain what the “Avg. Best APR” and shaded regions meant. Most also understood that participants with poor credit were likely to be offered loans with APRs that were identified as “high cost.”
- The APR for the interest-only loan used in this round was 7.59%, which placed it in the range labeled “high cost.” Most participants realized that the APR fell into the “high cost” category based on their review of the graphic. However, not all indicated this would be a factor in whether or not they accepted the loan. For example, some who confused the APR with the interest rate said that 7.59% seemed like a good interest rate to them, because it was lower than what they had on their current mortgage. Others commented that they would not accept the loan, because their current interest rate was lower than 7.59%. These participants were clearly relating the APR shown on the form to their own personal experience, rather than the context provided by the form.
- Six of the ten participants indicated they would be less likely to accept the interest-only loan based on the information in the APR section, while the remaining four indicated this information would be unlikely to affect their decision. However, in some cases it was clear that participants’ attitudes toward the loan were being driven by factors other than the APR, such as the fact that it had an adjustable rate or that payments were interest-only.
- The TILA statements describing a payment option loan displayed an APR of 6.01%, which was just below the boundary of “high cost” loans. Again, most participants understood the content of the APR section—for example, they knew that the average APR offered to borrowers with excellent credit was 4.75%. However, when asked what they would do if they had excellent credit and received this form from their lender, half expressed concern that their APR was too high. These participants indicated that they would go to another lender to get another offer, or would ask their lender to give them a lower APR. Others, however, did not seem to be bothered by the fact that they had not been offered the lower APR and indicated that the information on the form would not influence their decision whether to accept the loan.
- All forms also included a statement informing readers that a 1% APR reduction would result in a savings of \$167 a month for the first 5 years. Most participants did not notice this information; when asked if the form contained any information about how much money they would save with a lower APR, only two participants referenced this statement on the form.
- When participants were asked to compare the APR sections of versions J and K, six participants indicated that they preferred version K, while only one preferred version J. The remaining three participants did not express a preference. The aspects that participants liked about version K included the fact that the APR was displayed in a larger font, the fact that the explanatory text was below the graphic rather than beside it, and the fact that the definition of the APR was provided right next to the actual term, rather than in smaller font below.



## ***Rate and Payment Information***

### *Interest-Only ARM*

- All interview participants correctly identified the initial and maximum interest rates, as well as the period of time during which the rate would remain fixed.
- All but one participant indicated their rate and payment would likely increase at the end of the first 5 years. However, their responses seemed to be based mostly on a distrust of ARMs and an assumption that rates on these loans usually increase. Only two participants referenced the information in the Teaser Rate Notice; they indicated the rate would likely increase because it was discounted for the introductory period.
- Only three participants understood how often the interest rate could change after the first 5 years; the remainder did not see that information in the Key Questions or More Information About Your Payments sections.
- About half of participants were able to identify the maximum their rate could increase in a single year (2%); the remainder did not see this information in the More Information About Your Payments section.
- All participants correctly identified the initial monthly payment, and all but two understood that this payment would remain constant for 5 years (except for potential changes in escrow).
- Almost all participants could identify the maximum their payment would be when it first adjusted after 5 years. However, some participants mistakenly thought their payment would definitely increase to the maximum at that time. This misconception appeared to be in part because of a misreading of the table and in part because of general distrust of ARM products.
- When the Teaser Rate Notice was pointed out to them, a few participants reacted negatively to the use of the word “teaser.” Some commented that lenders would be very unlikely to use this word when communicating with consumers; others felt the use of the word was demeaning or insulting.
- Only six of the participants realized during their initial review of the form that the loan included interest-only payments; the remaining four did not.
- In some cases, participants were not concerned to find out that payments for the first 5 years were interest-only. They seemed to think this was a traditional loan in which the amount of principal paid during the first few years is very small. Because of this misunderstanding, these participants indicated that the fact that initial payments were interest-only would not affect how they felt about the loan.

### *Payment Option ARM*

- Two participants had previously heard of a payment option mortgage; one of the two had held this type of mortgage previously.
- After their first review of the TILA statement, about half of participants commented they definitely would not accept this type of loan. Two others indicated they found the terms of the loan confusing.
- All participants understood the interest rate could change and all but two understood it could begin changing after the first month.
- Half of the participants were able to identify the initial interest rate of the loan (1.5%). Four of the other five participants incorrectly referenced the APR when asked this question. Participants who saw version K were more successful in identifying the initial rate because it was displayed in the Payment Summary table rather than in the explanatory text above the table.
- All but two participants were able to identify the maximum interest rate for the loan (10.5%).
- All but one participant understood that their minimum payment would increase over time, and increase dramatically in June 2011.
- Most participants understood based on their first review of the form that if they made only the minimum payment each month, their loan balance would increase because of unpaid interest.
- The Payment Summary tables were significantly different on versions J-PO and K-PO. Participants were shown both forms and asked which version of the table they found clearer and more informative. Most participants indicated that they preferred the table on version K to that on version J. The most frequent reasons given by participants were that they liked the fact the column headings identified specific points in time (rather than “Year 1,” “Year 2,” etc.); they liked the fact that the table in version K listed the interest rate at different points in time as well as the payment; they liked the references to “1st adjustment” and “2nd adjustment” that were provided; and they liked the placement of the description of the full and minimum payment options.

### ***Taxes and Insurance (Escrow)***

#### *Interest-Only ARM*

- All but two participants were able to explain the term “escrow.” Of the other two, one said that they had heard of the word but did not know what it meant, while the other had never heard the term.
- Seven participants understood that the amounts shown for taxes and insurance on the form were only estimates. Eight understood that these amounts could change over time.

- Half of the participants had previously heard of PMI; the remainder had not.
- Although the Payment Table listed PMI as part of the estimated taxes and insurance, only six of the ten participants realized they would be paying PMI on this loan. One reason that awareness was fairly low may have been that half of the participants had never heard of PMI before.

#### *Payment Option ARM*

- When reviewing the payment option ARM, half of the participants saw the reference that taxes and insurance were included in the payments shown in the Payment Summary section. The remaining participants indicated that taxes and insurance were not included or stated they did not know.

### **Key Questions Section**

#### *Interest-Only ARM*

- All participants understood that the interest-only loan they were shown had a prepayment penalty.
- When directed to read the Key Question about interest-only payments, most participants understood that payments for the first 5 years would not cover any principal, and that they would begin paying down the loan principal in year 6.

#### *Payment Option ARM*

- When reviewing the payment option forms, most participants generally understood the content of the Key Questions related to interest-only payments and negative amortization. However, a few confused the information that was provided about interest-only payments and negative amortization, and mistakenly thought that the information in the Key Question about interest-only payments related to the minimum payment option.

### **“More Information About Your Payments” Section**

#### *Interest-Only ARM*

- When asked to read the text under the Rate Calculation heading, about half of the participants were able to explain how their rate would be determined after the introductory period. Some participants were confused by the term “LIBOR,” while others had difficulty understanding the concept of how an index and margin would be used to calculate their rate.
- When asked to read the text under the Rate Change Limits and Total Payments headings, all participants generally understood the information provided. However, several participants did not notice this information until they were specifically asked to read it (e.g., the periodic rate cap).

### *Payment Option ARM*

- Most participants did not understand the information under the heading Rate and Payment Change Limits in the More Information About Your Payments section of the form. Two participants seemed to generally understand the information about the caps on payments and the loan balance, although the extent to which they understood exactly how the caps worked was unclear. Other participants were clearly confused by this text.

### **Loan Obligation**

- Despite the fact the forms included a statement consumers were not obligated to accept the loan in addition to a statement “By signing below, I acknowledge receipt of this form,” about half of the participants mistakenly thought if they signed the statement they would be indicating acceptance of the loan terms.

### **Credit Life Insurance**

- All participants understood after reading the text that there was an additional cost for credit life insurance.
- When asked whether they would sign up for credit life insurance based on the notice they were shown, three indicated that they would. Two said that they would consult their own life insurance policies first to see whether additional coverage was necessary. The remaining participants were unsure whether they would sign up.
- Only three participants noticed the language that indicated even if you pay for credit life insurance, you may not receive any benefit from the policy.
- All interview participants noticed the reference to the Board website in the credit life statement. Most indicated that they would be likely to visit this site if they had questions about this product.
- Although most participants also saw the reference to a housing counselor, only four indicated they would be likely to contact a counselor to obtain more information. Others said they would be more likely to go to the website shown.

## **Subsequent Design Decisions**

### **Loan Summary Section**

- As in the previous round, some participants were unsure how often their rate and payment could change after the introductory period ended. Therefore, the forms developed for the following round of testing included the adjustment frequency in the Loan Type section.
- Because the alternate language used on the second day describing settlement charges that were included in the loan amount was clearer to participants, this language was used on forms for the following round of testing.

## **APR**

- Because some participants continued to confuse the APR with their interest rate, forms for the next round did not describe the APR as “your interest rate with settlement charges included.” Instead, the revised forms used the phrase “overall cost of this loan” or “fee-inclusive cost of this loan.”
- Although participants understood that the right side of the APR range represented “high cost” loans, some participants in this round did not express concern that their APR fell into this range. Therefore, the graphic used in forms for the subsequent round of testing in Bethesda attempted to demonstrate the importance of this range by coloring it black and labeling it the “high cost zone.” Also, an explanatory note about “high cost” loans that had been removed from forms in this round was added back in, along with a reference that loans falling in this range are usually provided to consumers with poor credit.
- Most participants preferred the format of the APR section shown in version K to that of version J, therefore, this format was used in all subsequent forms.

## **Rate and Payment Information**

- The Teaser Rate Notice was simplified in forms for the next round of testing, because of concerns that the number of different rates and payments displayed on the first page could confuse consumers. Specifically, the amount of the rate increase and the reference to a new monthly payment amount were removed.
- A few participants reacted negatively to the use of the word “teaser,” so on subsequent forms the Teaser Rate Notice was renamed the Introductory Rate Notice.
- Some participants continued not to notice that their loan included PMI, so a bullet was used to emphasize this fact in the left-hand column of the Payment Summary table. In addition, information about private mortgage insurance was given its own heading in the More Information About Your Payments section on the second page.

## **Interest-Only Payments**

- Several participants in this round of testing did not realize they would be paying only interest during the introductory period, while some others did not realize that the fact that payments were interest-only made this product different than traditional loans. To emphasize that payments were interest-only, the number “0” in the first column of the Payment Summary table was replaced with the word “None.”

## **Payment Option ARM**

- When reviewing forms for the payment option loan, participants strongly preferred all aspects of the Payment Summary table used in version K to that used in version J. Therefore, this format was used in the forms designed for the next round of testing.

- Because some participants confused the interest-only payments described in the Key Questions section with the minimum payment, the description of the minimum payment option was revised slightly for the next round of testing. The revised text was adapted from the payment option monthly payment disclosure that was also tested this round (see Chapter VI).
- Several participants did not realize escrow payments were included in the sample monthly payments shown in the Payment Summary table, so this fact was made more prominent in the forms tested in the following round.
- Most participants struggled to understand the information in the “More Information about Your Payments” section under the heading “Rate and Payment Change Limits.” Therefore, on forms for the following round of testing, this text was broken into two different headings: “Rate Change Limits” and “Payment Change Limits.”

### ***Key Questions Section***

- Although understanding of the Key Questions related to interest-only payments and negative amortization was better than in previous rounds, there were still a few participants who were confused by this text. Therefore, the wording of these questions and answers was revised for the following round.

### ***Credit Life Insurance***

- While participants understood most of the content in the credit life insurance disclosure tested this round, most did not realize that purchasing this insurance might not provide them with any additional benefits. Therefore, this information was made more prominent in the version of this disclosure tested in the next round.

## ROUND 13: BETHESDA, MARYLAND (MAY 2009)

### Objectives and Methodology

In May 2009, ICF Macro conducted nine cognitive interviews in Bethesda, MD. One goal of this round was to continue testing how effectively the revised TILA could describe the terms of complex loan products, such as interest-only and payment option ARMs. Another goal was to continue testing the extent to which the text and graphic in the APR section provided participants with useful context for comparing their APR to that being offered to other consumers.

The interview protocol included the following sections:

- Participants in the interviews were first asked to review one of two TILA statements describing fixed-rate loans. The primary focus of this portion of the interview was to assess participants' reaction to and understanding of the APR section. The decision was made to use fixed-rate loans for this portion of the interview because in previous rounds of testing participants' reactions to forms they were shown were often driven by other loan features, such as an adjustable rate or a prepayment penalty, rather than by the APR. As a result, it was often difficult to isolate participants' reactions to a high APR. By testing the APR in the context of a simpler loan, ICF Macro and Board staff could assess how a relatively high APR would affect participants' evaluation of a loan they might otherwise accept.
- Next, participants were given a TILA statement that described an interest-only ARM product. They were then asked a series of questions designed to test their comprehension of information on the form.
- Participants were next given a TILA statement describing a payment option ARM product, and again were asked a series of questions designed to test their comprehension of the information.
- After reviewing the TILA statements, participants were asked to review a revised disclosure related to credit life insurance.

Five forms were used in these sections of the interview; all are provided in Appendix D:

- TILA statements L1 and L2 (describing fixed-rate loans; they were identical except for the information in the APR section);
- TILA statement M (describing an interest-only ARM);
- TILA statement N (describing a payment-option ARM); and
- Additional text about credit life insurance.

## Key Interview Findings

### *Loan Summary Section (Versions L1 and L2)*

- All participants correctly identified the term of the loan (30 years) and the amount borrowed (\$306,000).
- Six of nine participants understood the settlement charges shown on the form did not include any down payment they would owe; one participant did not answer this question.
- Four participants were confused by the statement that \$3,000 of their settlement charges were included in the loan amount shown. Some thought this statement might mean that they were actually borrowing a different amount than that listed on the form. The remaining participants understood that the \$3,000 of their settlement charges were already included in the loan.
- Almost all participants in this round understood that the \$3,000 of settlement charges that were included in the loan amount were already reflected in the “total estimated settlement charges” listed on the form.

### *APR (Versions L1 and L2)*

- As in previous rounds, several participants initially confused the APR with the interest rate; several referred to the APR as the “interest rate” throughout their review of the form. When it was pointed out to participants that the APR and interest rate were different, only one was able to explain that the APR was higher because it included settlement charges. Others either indicated that they did not know why the terms were different or provided incorrect explanations.
- Most participants understood the dot on the scale labeled “Avg. Best APR” represented the average APR offered to applicants with excellent credit. All but one understood that the “high cost zone” labeled on the scale represented the range of more costly APRs that would likely be offered to consumers with poor credit.
- When shown version L1, which showed an APR that was in the “high cost zone,” four of five participants indicated that this information made them view the loan more negatively and would make them less likely to accept the loan. Among those who were shown L2, which had an APR just below the “high cost zone,” three of five participants indicated concern about the APR.
- Among all participants, about half said that if they had excellent credit, they would want to make sure that they got an APR close to the “average best” APR shown on the form. The remaining participants indicated that the APR graphic did not seem to consider this an important goal.



- Half of the participants noticed the reference on the form that a 1% APR reduction would result in a savings of \$194 a month. Other participants said they understood that decreasing their APR would save them money, but did not notice the information on the form about the specific amount they could save.
- All but two participants understood there was no limit to how high the APR could be on a loan. The remaining two thought that the end of the scale (10.75%) represented the maximum APR that could be offered.
- The L forms described the APR as the “overall cost of the loan, including interest and settlement charges.” Participants were asked whether replacing the word “overall” in this description with the phrase “fee-inclusive” would change their perception of what the APR signified. Almost all participants indicated this change would not affect their understanding of the APR. Most indicated that they found the term “overall cost” to be clearer than “fee-inclusive cost”; a few said that they found the reference to fees confusing. One participant, however, did appear to understand the meaning of the APR better when given the “fee-inclusive” language.

### ***Rate and Payment Information***

#### *Fixed-Rate Mortgage (Versions L1 and L2)*

- All participants understood their interest rate and payment would not change over time (except if the amount for taxes and insurance changed).

#### *Interest-Only ARM (Version M)*

- Most participants were able to identify the initial interest rate of the loan, although two incorrectly identified the APR as the interest rate. All participants understood that the interest rate could change after the 5-year introductory period.
- All but two participants could identify the maximum interest rate; the remaining two incorrectly thought the rate could increase above the maximum shown in the Payment Summary table.
- All participants correctly identified the maximum their interest rate could be in Year 6. Aside from the maximum, however, participants seemed unclear as to what could happen to their rate. Some seemed to think their rate would definitely increase in Year 6 to the amount shown in the table while others understood their rate could also be lower than the amount shown.
- Most participants indicated that they thought their interest rate was likely to increase after the introductory period ended in March 2014. However, only a few participants referenced the information in the Introductory Rate Notice, which indicated that the initial rate was discounted and that the interest rate would increase after the introductory period, even if the market rate did not change. Most participants did not notice this information or did not realize how it related to future rate and payment changes.

- All but two participants understood their rate could adjust annually. The remaining two assumed the rate would adjust every two years after the introductory period ended, because that was the length of time between the second and third columns in the Payment Summary table.
- Half of the participants were able to identify the maximum amount their rate could increase in a single year; others did not notice this information in the More Information About Your Payments section.
- Half of the participants realized during their initial reading of the form that payments during the introductory period would be interest-only. All others noticed this information after reviewing the form further. Overall, the word “None” in the Payment Summary table seemed to make the fact that these payments were interest-only more prominent.

#### *Payment Option ARM (Version N)*

- Two participants had heard of a payment option mortgage prior to their interview.
- After their initial review of the TILA statement, most participants expressed concern with some aspect of the payment option loan. Some features that participants mentioned included: the fact that their loan balance could increase; the fact that minimum payments would not pay off any principal; and the fact that the interest rate was adjustable. When asked if anything concerned them about this loan, one participant responded “everything.” Another commented that the loan would make it “too easy” for a borrower to get into trouble if they made only the minimum payments.
- All participants understood that their interest rate was adjustable and could begin changing as soon as the second month.
- All but one participant correctly identified the initial interest rate; the remaining participant confused the initial interest rate with the APR. All but one was also able to identify the maximum interest rate.
- All but two participants understood their minimum payment would increase over time, and could increase dramatically in June 2011 when the loan would require a fully amortizing payment.
- Most participants understood the minimum payment covered only some interest and no principal, while the full payment covered both. Two participants understood that the minimum payment covered no principal, but mistakenly thought that it covered all interest.
- All but two participants understood that making the minimum payments would cause the loan balance to increase over time. Not all understood why this occurred, however; a few indicated that the loan balance would increase because the principal was not being paid off, rather than because of unpaid interest.

- After being directed to read the statement at the bottom of the page that explained making minimum payments would lead to an increase of \$29,943.00 to the loan amount, all participants indicated that this information would make them less likely to make minimum payments.

### ***Taxes and Insurance (Escrow)***

#### *Interest-Only ARM*

- Although all participants indicated they had previously heard the term “escrow”; when asked to describe it, however, only six were able to do so accurately.
- All but two of the participants realized the payments for the interest-only loan included PMI. Most saw this information in the More Information About Your Payments section on the second page, rather than in the note about PMI in the Payment Summary table.

#### *Payment Option ARM*

- As in the previous round, most participants did not realize taxes and insurance were included in the monthly payments shown on the form. Only three participants in this round of testing understood that this was the case, while other participants either assumed that taxes and insurance were not included or were not sure.

### ***Key Questions Section***

#### *Interest-Only ARM*

- All participants realized, based on their initial review of the form, that the interest-only ARM had a prepayment penalty feature. Most of the participants noticed this feature on the first page of the form, rather than from the Key Questions on the second page of the form.
- When asked to read the Key Question related to interest-only payments, all but one participant understood the information clearly. One incorrectly thought that making interest-only payments would cause the loan balance to increase.

#### *Payment Option ARM*

- Participants were asked to read the Key Questions related to interest-only payments and negative amortization and explain what they said. Most participants understood both features and the impact that they would each have on the loan balance over time. However, as in previous rounds a few participants confused the two. For example, two participants indicated that making interest-only payments would cause the loan balance to increase.

## **“More Information About Your Payments” Section**

### *Interest-Only ARM*

- When asked to read the text under the Rate Calculation heading, almost all participants were able to explain that their rate would be equal to the LIBOR index plus 5%. While some had never heard of the LIBOR index, most generally understood the concept that their rate would vary based on a market rate.
- All but one participant understood the annual and periodic rate change caps described under the heading Rate Change Limits. However, as noted above about half of the participants did not see this information until it was pointed out to them.
- As in previous rounds, almost all participants understood the text under the heading Total Payments, although none understood what the “amount financed” signified.

### *Payment Option ARM*

- Almost all participants were able to explain the information under the heading Rate Change Limits on the payment option ARM statement, including that their rate could increase to a maximum of 10.5% and that it could start adjusting the first month after consummation. This was an improvement from the previous round, when participants did not understand this text.
- As in the previous round of testing, participants were generally confused by the information under the heading Payment Changes. While some understood that their payments could increase no more than 7.5% a year at the beginning of the loan, they generally did not understand the relationship between caps on payments and the loan balance or what would happen after the loan balance cap was reached.

## **Credit Life Insurance**

- All participants understood after reading the notice that credit life insurance was not a required feature.
- Participants generally understood the first two bulleted statements. Most participants were surprised by the third statement, which stated that even if they paid for the insurance they may “not qualify to receive benefits in the future.” A few indicated they did not understand how they could pay for the coverage and then receive no benefits. Despite their surprise, participants seemed to understand the statement; all but two correctly indicated that if they purchased the coverage and then died, the insurance would not necessarily pay off their loan. Most assumed that the reason a borrower would not be covered would be because of pre-existing medical conditions or suicide.
- When asked whether they would purchase credit life insurance, all but one participant indicated they would not—in fact, one participant had recently purchased credit life insurance and was planning to re-read the paperwork after the interview. The remaining participant, however, indicated he would purchase credit life insurance after reading the notice.

- When asked how much credit life insurance would cost for a \$200,000 loan, five of seven participants correctly answered \$144 per month. The remaining two gave the figure shown on the form (\$72 per month), which was the incremental cost for each \$100,000. Two participants were not asked this question.
- Most participants indicated they would be likely to visit the website shown on the notice if they had additional questions about credit life insurance.

### ***Loan Obligation***

- Because the forms used in this round specifically stated that a signature on the part of the borrower merely indicates receipt of the form, six participants understood that by signing they would not be committing themselves to the loan terms. However, three participants incorrectly thought that signing the form would indicate a commitment to the lender.

## **Subsequent Design Decisions**

### ***Loan Summary Section***

- Because participant understanding of the frequency of rate and payment change was higher than in the previous two rounds, the decision was made to include this information under the Loan Type heading, as was done in this round.

### ***Rate and Payment Information***

- For interest-only loans, the use of the word “none” in the Payment Summary table indicating none of the payment would be used to pay principal seemed to make this information clearer and more noticeable to participants. Therefore, this notation was used in the final TILA statement models and clauses.

### ***APR***

- Most participants in this round indicated that the term “overall cost” was a clearer descriptor of the APR than “fee-inclusive cost”; there was no clear difference between the two terms in how well they explained the meaning of the term. Therefore, the decision was made to use the phrase “overall cost” in the final model forms and clauses.
- The revised format of the APR graphic—particularly the use of the term “high cost zone”—appeared to improve its effectiveness at communicating to participants the costs of having a high APR. Compared to the previous round of testing in Denver, more participants in this round indicated that if they had excellent credit they would expect to get an APR near the “average best APR” shown on the scale. Therefore, this basic format was used in the APR section of the final model forms and clauses.

### ***“More Information About Your Payments” Section***

- Because participants were more likely in this round to realize the interest-only loan they reviewed included PMI, the decision was made to retain the separate heading “Private Mortgage Insurance” in this section of the forms and clauses.
- Although participants who reviewed the payment option ARM still did not understand the relationship between the caps on payments and the loan balance, their understanding of the rate change limits was significantly better than in the previous round. Therefore, the decision was made to retain separate headings for “Rate Change Limits” and “Payment Change Limits” on the model forms and clauses for payment option ARMs.

## CHAPTER VI: DEVELOPMENT AND TESTING OF OTHER TYPES OF MORTGAGE DISCLOSURES

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Although the primary focus of most rounds of interviews for this project was on testing current and revised TILA statements, ICF Macro and Board staff also developed and tested several other types of disclosures. These included several new early disclosures, a revised initial program disclosure, a rate adjustment notice for ARMs, and a payment option monthly payment disclosure explaining the consequences of making less than the full payment each month. In most cases, these disclosures were developed by ICF Macro and tested in only one round of interviews, after which small changes in wording were made to address any comprehension issues that had become apparent through testing.

This chapter of this report describes the development and testing of these other disclosures.

### NEW EARLY DISCLOSURES ABOUT MORTGAGE RISKS

#### “Mortgage Risk Worksheet”

For the round of interviews held in Baltimore, MD (Round 7), ICF Macro developed a new early disclosure called the “Mortgage Risk Worksheet.” This document listed six mortgage features that are potentially risky or costly: an adjustable rate, balloon payment, interest-only payments/negative amortization, prepayment penalty, no-documentation or low-documentation loans, and direct payment of taxes and insurance. For each of the six features, the form provided a description of the feature and the potential benefits, risks, and costs. In each case, the participant was asked to decide whether or not they were comfortable with the risk and to indicate if their comfort level by checking a box. Since the intent of the Mortgage Risk Worksheet was to ensure that individuals were affirmatively “opting in” to risky loan features, the form did not include a box for participants to check if they were not interested in a particular feature.

Participants in the Baltimore interviews were shown the Mortgage Risk Worksheet and asked to provide initial reaction and feedback. They were then asked to explain several portions of the form, to learn the extent to which they understood the content. Finally, they were asked to describe how, if at all, they would use this worksheet in their own mortgage shopping process. The form that was shown to participants is provided in Appendix D.

#### *Key Findings*

- The Mortgage Risk Worksheet was received favorably by most participants. However, some more experienced participants indicated the Worksheet would be of minimal value to them because they already understood the risks associated with these loan features.

- Most participants indicated they learned something from reading the form. Most often, participants said they had learned something about balloon payments, negative amortization, or “no-doc”/“low-doc” loans.
- Participants generally understood most of the content on the form. However, several were confused by the difference between an “interest-only loan” and one with negative amortization. This confusion may have been exacerbated by the fact that these two loan features were combined into a single row in the worksheet.
- Some participants were confused by the last row of the worksheet, which related to “direct payment of property taxes and homeowner’s insurance.” The source of this confusion seemed to be that while most rows addressed the presence of a risky loan feature, this last row addressed the absence of an escrow account. As a result, several participants mistakenly thought that by checking the box in the right-hand column they were indicating they did want an escrow account—when in fact a checkmark meant that they would consider a loan that required them to save for taxes and insurance themselves.
- A few participants had difficulty understanding the row on “no-doc”/“low-doc” loans. In most cases, participants confused by this row seemed to understand the content but were surprised that these types of loans existed.
- Several participants suggested additional features be added to the worksheet, such as fixed rate loans and PMI. Others suggested the document should provide a full glossary of loan terminology. Based on these suggestions, it was clear the participants did not understand that the Mortgage Risk Worksheet was designed specifically to alert consumers about loan features that might be particularly risky or costly. Instead, they viewed it as a source of general information about mortgage terms.
- Participants generally understood how the form was intended to be used—that is, that potential borrowers were to read and complete the worksheet and then use it as a basis for discussion with their lender or broker. However, most participants indicated they would be unlikely to complete the worksheet or bring it to meetings with their lenders or brokers. Participants seemed to feel that the usefulness of the form lay in the information it provided and that actually completing it would provide minimum additional value for them.
- Several participants did not like the fact that the worksheet only offered a checkbox to indicate they were comfortable with the risk. They felt a second checkbox should be provided in each row indicating that the potential borrower is not comfortable with the risk associated with that feature.
- Several participants commented that a worksheet like this would only be valuable if lenders and brokers were held accountable for collecting it and keeping consumers’ stated preferences in mind when presenting loan offers. A few even recommended that the form include a signature line for the potential borrower and lender, to show that consumers’ preferences had been collected and discussed.



## ***Subsequent Design Decisions***

- While participants indicated that much of the content in this disclosure was important and helpful to them, most said they would not use the form as intended. As a result, the decision was made at this time not to require lenders to provide this type of worksheet to all potential borrowers.
- Because ICF Macro and Board staff believed that the content of the Mortgage Risk Worksheet was important in helping consumers understand and assess the risk associated with adjustable-rate and other loan products, a new early disclosure was designed for the following round of testing. This new document, which was titled “Six Key Questions to Ask About Your Mortgage,” moved away from the “worksheet” structure of the original form but provided much of the same information about potentially risky loan terms.

## **“Key Questions to Ask About Your Mortgage” Disclosure**

The disclosure titled “Six Key Questions to Ask About Your Mortgage,” which was developed following the Baltimore round of testing, listed six questions consumers should ask their lender about a loan offer, as well as an explanation for why each question is important.

The Key Questions early disclosure was designed to be provided to consumers when they first inquire with a lender or broker about getting a mortgage. However, the questions shown on the form mirrored those shown on the revised TILA statement. The intent of this parallel construction was that during the shopping stage, consumers would ask their lender or broker these questions about the loan they were being offered. Once they applied for the loan, the TILA statement would allow them to confirm the answers they had been given.

This early disclosure was tested with participants in the Atlanta round of interviews in November 2008 (Round 8). Based on findings from this round, the disclosure was revised and tested again with participants in Dallas in February 2009 (Round 10). Content was added to the form for this round; the version of the Key Questions disclosure tested in Dallas lists nine questions instead of the original six.

Participants in both rounds (Atlanta and Dallas) were shown the Key Questions disclosure near the end of the interview and asked to provide initial reactions and feedback. They were then asked to explain several items on the form, to gather data on the extent to which they understood the content. Both versions of the Key Questions disclosure are provided in Appendix D.

## ***Key Findings***

- When asked to rate the usefulness of the Key Questions document on a scale of 1 (“not at all useful”) to 10 (“extremely useful”), almost all participants in both rounds of testing gave the document a rating of 9 or 10. No participants gave the form a rating lower than 7.
- Participants liked the “question and answer” format and thought the content would be particularly helpful for first-time buyers.

- Participants in both rounds of testing generally understood the intended purpose of the disclosure. While many indicated they would not necessarily ask their lender the exact questions shown on the page, some said they would use the information on the form to develop their own list of questions.
- When asked whether they had learned anything from reading the form, about half of the participants indicated that they had. In Atlanta, participants most frequently said they had learned something about negative amortization, interest-only payments, or balloon payments. In Dallas, participants most frequently indicated they had learned something about equity-sharing features, demand features, and “no-doc”/“low-doc” loans—in fact, several said they had never heard of these three features before reading the Key Questions disclosure.
- Participants in both rounds generally understood the questions related to variable interest rates, payment changes, and prepayment penalties; these were all terms and concepts with which participants were already familiar.
- In general, the questions that were least understood by participants were those relating to interest-only payments and negative amortization. Several participants confused these two features and were unclear as to the difference between them. This was particularly true in Atlanta, when the question about negative amortization immediately preceded the question related to interest-only payments. The order of these two questions was flipped in Dallas, which appeared to alleviate the confusion between them—although some participants continued to struggle to distinguish the two.

### ***Subsequent Design Decisions***

- Between the Atlanta and Dallas rounds, several small changes were made to the wording of both the questions and the answers. These revisions, along with the reversal of the order of questions relating to negative amortization and interest-only payments, seemed to improve comprehension of the document slightly.
- Because participants in both the Atlanta and Dallas rounds reacted so positively to the Key Questions disclosure, and indicated that they would find the information useful, the Board is proposing that this document be provided to all prospective borrowers. The final model form includes seven of the nine Key Questions listed on the version used in Dallas.<sup>30</sup>

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<sup>30</sup> Two Key Questions relating to loan features that are relatively rare in the market (equity sharing and demand features) were removed from the form, because of concerns that if the disclosure were too long fewer consumers would read it.

## REVISED ARM LOAN PROGRAM DISCLOSURE

As described in Chapter III, ICF Macro tested the current version of the ARM loan program disclosure through focus groups in Greenbelt, MD and Los Angeles, CA (Rounds 1 and 4). Participants' reaction to the disclosure was fairly negative; most indicated they found it difficult to understand and that, because the content was so general, the form would not help them shop between products or lenders.

Prior to the round of interviews in Providence, RI (Round 11), ICF Macro developed a revised program disclosure form. This form included four terms that are important distinguishing characteristics of an ARM program: the length of the introductory period, the frequency of rate change, the index used to calculate the rate, and limits on rate changes. It also provided answers to the Key Questions used on the TILA statement. The intended timing of this disclosure was the same as the current ARM program disclosure; consumers would be provided with the document at the point before they have applied for a loan. The revised program disclosure form that was tested in Providence is provided in Appendix D.

Participants in the Providence interviews were asked to read the revised program disclosure and provide general comments on the extent to which they would find the form useful. They were then asked a series of questions designed to test their understanding of the content.

### Key Findings

- Participants understood that the purpose of the ARM loan program disclosure was to provide general information about a lender's loan program. They understood that this disclosure differed from transaction-specific documents like the TILA, because the lender could not provide specific information about interest rates before application.
- Six participants understood that the information on the form was being provided by the lender. Three were not sure who was responsible for the information provided, while one thought the information on the form was coming from "the government."
- Comprehension of the information on the program-specific page was generally high. All but one participant understood that their rate could begin changing after 3 years, and all knew that their rate would change annually after that point. Three participants mistakenly thought that the maximum interest rate on the loan would be 6%; in fact, this was the maximum increase in the interest rate. When asked if anything was confusing to them, two participants indicated they found the LIBOR index and margin as well as limits on the rate change and interest caps difficult to understand.
- Eight participants understood without prompting that the loan being described had both demand and equity-sharing features. Once they had read the information about these features, all participants understood them clearly. All participants indicated that these features would make them less likely to accept the loan; several were surprised because they had not known that mortgages could have these features.

## Subsequent Design Decisions

- Because participants' understanding and perceived usefulness of the revised program disclosure form were dramatically higher than the current version, the Board will propose to include the revised form in its proposed regulations.
- Because a few participants mistakenly thought that the reference to a "6% lifetime cap" referred to a limit on the interest rate itself rather than the change in the rate, the wording of this reference was revised following the Providence round of testing to state that the interest rate can increase "no more than 6% total for the life of the loan."

## NEW EARLY DISCLOSURE: "FIXED VS. ADJUSTABLE RATE MORTGAGES"

For the round of interviews held in Providence, RI (Round 7), ICF Macro developed a new early disclosure. This one-page document provided information about the relative advantages and disadvantages of an ARM compared to a fixed-rate loan, most of which currently appears in the CHARM booklet. The intent was that this publication would be provided to consumers at the point when they first expressed interest in a mortgage. The document that was tested is provided in Appendix D.

Participants in the Providence interviews were given this new early disclosure together with the revised program disclosure described above. They were asked to comment on the extent to which they would find this information useful, and were then asked questions designed to test their understanding of the form.

## Key Findings

- Participants understood that the purpose of this disclosure was to provide them with information about ARMs, and about the relative advantages and disadvantages of this type of loan product compared to a fixed-rate mortgage.
- Participants generally had a favorable reaction to the page comparing fixed rate to adjustable rate mortgages. Participants commented that the information was clear and easy-to-understand, and they did not identify anything that they found unclear or confusing. Several participants particularly liked the box that directly compared the two products and provided suggestions for when to consider each of them.
- Half of the participants understood the information on this page was coming from the Board, as opposed to a lender or broker. Other participants understood this was the case only after the Board logo and heading ("Federal Reserve Board Consumer Protection Resources") were pointed out to them.

## Subsequent Design Decisions

- Because participants generally understood the information on this disclosure and indicated that the information would be useful to them, lenders would be required to provide these forms to potential borrowers.

## ARM ADJUSTMENT NOTICE

Currently, Regulation Z requires lenders to notify ARM borrowers of a change to the interest rate; if the borrower's payment will change, the lender must send the notice in advance of the change. Regulation Z does not contain a model form for this disclosure.

Prior to the round of interviews in Providence, RI (Round 11), ICF Macro developed a model notice to inform borrowers that their interest rate had been changed and would change their monthly payment. The specific terms shown on the notice also indicated that the borrower would begin paying interest, whereas previous payments had been interest-only. The notice shown to participants is provided in Appendix D.

Participants in the Providence interviews were asked to review this notice and provide initial reactions and comments. They were then asked a series of questions designed to test their understanding of the content.

## Key Findings

- Participants generally understood the form content and recognized all aspects of the loan that would be changing. All interview participants correctly identified the amount of the new payment, as well as the date that it would be due. Almost all participants recognized without prompting that their rate was increasing, the amount they pay for taxes and insurance was increasing, and their new payments would begin paying off the loan principal.
- All but one participant saw the information on the form indicating that if they tried to refinance into another loan, they would be subject to a prepayment penalty.
- When asked what they would do if they realized they would be unable to make their new payments, six participants indicated they would call their lender, while four said they would use one or more of the resources listed at the bottom of the form. Two participants said that they most likely would not seek out any type of assistance because they did not believe doing so would be helpful.

## Subsequent Design Decisions

- Because comprehension of this notice was generally very high, the model ARM adjustment notice published by the Board with its proposed rules in July 2009 will be almost identical to that which was tested with consumers.<sup>31</sup>

## PAYMENT OPTION MONTHLY PAYMENT DISCLOSURE

Prior to the round of interviews in Denver, CO (Round 12), ICF Macro developed a model disclosure to include with monthly statements for payment option mortgages. This disclosure describes a borrower's payment options for that month, along with the impact that each would have on their loan balance and future payments. The disclosure shown to participants is provided in Appendix D.

Participants in the Denver interviews were asked to review this disclosure and provide initial reactions and comments. They were then asked a series of questions designed to test their understanding of the content.

## Key Findings

- All participants understood that the purpose of this disclosure was to inform them of their payment options, along with the consequences of selecting a particular payment.
- Participants felt the information was very clearly presented; they had no questions following their review of the disclosure. One participant, however, expressed doubt that lenders would ever be this honest when describing the consequences of making minimum payments.
- Most interview participants understood if they made the minimum payment they would be borrowing more money and increasing their loan balance. Most also understood that if they made minimum payments they would have to make much larger payments in the future.
- All but two participants understood that if they made an interest-only payment they would be paying only interest and would not be paying off principal. The remaining two participants confused the consequences of an interest-only payment with those of the minimum payment, and indicated that making an interest-only payment would also cause the loan balance to increase.

## Subsequent Design Decisions

- Because comprehension of the content was generally very high, the model payment option monthly payment disclosure published by the Board with its proposed rules in July 2009 will be almost identical to that which was tested with consumers in this round.

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<sup>31</sup> The model form published by the Board will also show loan balance and other loan features where applicable, such as interest rate carryover.

## NEW EARLY DISCLOSURE: MORTGAGE SHOPPING CHECKLIST

For the round of interviews held in Baltimore, MD (Round 7), ICF Macro developed another early disclosure. Called the “Mortgage Shopping Checklist,” the goal of this one-page document was to provide consumers with six action steps they should take before applying for a mortgage loan. These action steps were intended to make consumers more knowledgeable about mortgages, and to improve their ability to shop effectively between lenders. The disclosure was designed with the intent that it would be provided to consumers when they first contacted a lender or broker about obtaining a mortgage.

Participants in the Baltimore interviews were shown the Mortgage Shopping Checklist and asked to provide initial reaction and feedback. They were then asked to explain several sections of the form, to gather data on the extent to which they understood the content. The Checklist shown to participants is provided in Appendix D.

### Key Findings

- About half of participants indicated they would find this document helpful if they were in the process of looking for a mortgage. Some said if they had been given this information when they bought their first home it would have saved them time and money.
- Participants who indicated that the document would not be useful to them tended to be more experienced borrowers who had been through the mortgage process multiple times. Several believed they were already effective shoppers and did not need additional guidance. Some of these participants, however, thought the Checklist would be a useful resource for first-time borrowers.
- One participant commented the document would be more useful if it actually provided information about mortgages, rather than simply recommending other resources.
- Several participants expressed surprise that the Federal Reserve Board would produce a document like this for consumers, because they did not know this was one of the Board’s roles. Others had not known that the Board offered resources such as consumer-oriented websites.
- Approximately half the participants said they would be likely to call the phone number listed at the bottom of the page and request the “Mortgage Shopping Package.” Others said they would be unlikely to do so, because they did not believe that this information would be useful to them.
- Some participants indicated that in addition to the six items on the checklist, they would like more information on topics including: the timeline of the mortgage process; how to identify reputable lenders and/or brokers; an explanation of closing costs; suggestions on how to improve your credit score; and how to read and understand mortgage disclosures.
- Several participants suggested that if the Board produced a resource like this, they should be sure to promote it to increase awareness of its availability.

- A few participants commented that in addition to this form, the Board should also provide in-person workshops and mortgage counseling.
- One participant indicated that he would be unlikely to get quotes from multiple lenders if doing so required that he pay multiple application fees.

### **Subsequent Design Decisions**

- Because half of the participants indicated they did not find the content of this disclosure to be helpful, the decision was made not to require that a Mortgage Shopping Checklist be provided to all potential borrowers. However, because other participants—particularly less experienced borrowers—said that a checklist like this would be useful, the Board plans to explore options for how to provide this information through consumer education materials.



## CHAPTER VII: SUMMARY

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This report summarizes work conducted by ICF Macro from December 2007 through June 2009 in support of the Board's efforts to revise Regulation Z rules pertaining to closed-end mortgage disclosures. The outcomes of this work include the development of:

- A significantly revised TILA statement that:
  - Emphasizes potential changes in rates and payments;
  - Highlights potentially risky or costly loan features;
  - Helps consumers verify key terms they might have considered before applying for a particular loan; and
  - Provides context for how the loan APR compares with what other recent borrowers have been offered;
- A new document titled “Key Questions to Ask About Your Loan,” a concise and easy-to read disclosure for potential borrowers that provides guidance on what questions they should ask their lenders;
- A new disclosure titled “Fixed vs. Adjustable Rate Mortgages,” which will be provided to potential borrowers to explain the relative advantages of fixed and adjustable rate loan products;
- A revised ARM loan program disclosure that is simpler and more useful to consumers than that which is currently in use;
- A revised ARM adjustment notice that describes future interest rate and payment changes; and
- A new payment option monthly payment disclosure for consumers with payment option and other negative amortization mortgages that describes the consequences of making less than the full payment each month.

The results of the research described in this report will inform the Board's proposed revisions to Regulation Z, which are scheduled for release in July 2009. The disclosure forms developed through iterative testing will be released with the proposal as model forms and clauses. By relying heavily on direct consumer testing in the development of these forms, the Board hopes to ensure that its new regulations will lead to financial disclosures that will be easier for consumers to read and understand, and as a result will help them make well-informed financial decisions.

# **APPENDIX A: Research Timeline**

Round #	Location	Date(s)	Type of Testing	Topics Addressed
1	Greenbelt, MD	February 20, 2008	Focus Groups (2)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• Current disclosures (CHARM booklet, ARM loan program disclosure, TILA statement<sup>1</sup>)</li> </ul>
2	Washington, DC	March 4 & 6, 2008	Interviews (7)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• Mortgage broker compensation disclosures<sup>2</sup></li> <li>• Pollock and joint (HUD-Fed) forms</li> </ul>
3	Los Angeles, CA	March 25-26, 2008	Interviews (7)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• Mortgage broker compensation disclosures</li> <li>• Pollock and joint (HUD-Fed) forms</li> </ul>
4	Los Angeles, CA	March 25-26, 2008	Focus Groups (2)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• Current disclosures (CHARM booklet, ARM loan program disclosure, TILA statement)</li> </ul>
5	Washington, DC	April 30 & May 1, 2008	Interviews (10)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• Mortgage broker compensation disclosures</li> <li>• CHARM booklet</li> </ul>
6	Kansas City, KS	May 13-14, 2008	Interviews (11)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• Mortgage broker compensation disclosures</li> <li>• CHARM booklet</li> </ul>
7	Baltimore, MD	August 20-21, 2008	Interviews (10)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• New early disclosures (Mortgage Checklist, Mortgage Risk Worksheet)</li> <li>• Current TILA statement</li> </ul>
8	Atlanta, GA	November 5-6, 2008	Interviews (9)	<ul style="list-style-type: none"> <li>• Mortgage shopping behavior</li> <li>• New early disclosure (“Key Questions” disclosure)</li> <li>• Revised TILA statements</li> <li>• Payment scenario table and graph</li> </ul>
9	Bethesda, MD	January 27 & 29, 2009	Interviews (9)	<ul style="list-style-type: none"> <li>• Revised TILA statements</li> </ul>
10	Dallas, TX	February 24-25, 2009	Interviews (10)	<ul style="list-style-type: none"> <li>• Revised TILA statements</li> <li>• Alternate presentations of APR</li> <li>• “Key Questions” disclosure</li> </ul>
11	Providence, RI	March 31 & April 1, 2009	Interviews (10)	<ul style="list-style-type: none"> <li>• Revised TILA statements (interest-only ARMs and fixed rate loans with balloon payments)</li> <li>• Revised ARM loan program disclosure</li> <li>• ARM adjustment notice</li> </ul>
12	Denver, CO	April 21-22, 2009	Interviews (10)	<ul style="list-style-type: none"> <li>• Revised TILA statements (interest-only and payment option ARMs)</li> <li>• Payment option monthly payment disclosure</li> </ul>
13	Bethesda, MD	May 6-7, 2009	Interviews (9)	<ul style="list-style-type: none"> <li>• Revised TILA statements (fixed-rate loans, interest-only and payment option ARMs)</li> </ul>

<sup>1</sup> Unless noted otherwise, testing of current and revised TILA statements focused on statements that described hybrid ARMs.

<sup>2</sup> Findings related to the disclosure of mortgage broker compensation were presented to the Board in a separate report in July 2008, which is available at <http://www.federalreserve.gov/newsevents/press/bcreg/20080714regzconstest.pdf>.

**APPENDIX B:  
Sample Recruitment  
Screenener**

**Participant Screener for Federal Reserve Board In-Depth Interviews**  
**Providence, RI**  
**March 31-April 1, 2009**

**Recruiting Script**

Hello, I am calling on behalf of the United States Federal Reserve Board. As you may know, recently many Americans have had problems with their mortgages. In response to the recent mortgage issues, the Federal Reserve Board is sponsoring a series of consumer interviews in your area so that we can learn more about how people make decisions regarding their mortgages. We will use what we learn from these interviews to help improve the information consumers receive when they get a mortgage loan.

Q1: Have you obtained a new mortgage or refinanced a mortgage in the past two years?

- Yes → *Participant may qualify for Category A; continue to Q2*
- No → *Participant may qualify for Category B; skip to Q9*

Great. We will be holding interviews in Providence on Tuesday, March 31<sup>st</sup> and Wednesday, April 1<sup>st</sup>. Participants will receive \$75 in exchange for their time and input on this important topic. I was wondering if you would be interested in attending.

- Yes → Continue to screening questions
- No → *Record reason (not interested, not available on that date, etc); thank them politely and end call.*

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***Questions for Category A Candidates***

Q2: Was this mortgage related to a property for your own use, or a property you purchased solely as an investment?

- Own use → *Continue*
- Investment → *Thank respondent politely and end call.*

Q3: Were you the person in your household who was responsible for making decisions related to this mortgage?

- Yes → *Continue*
- Yes, in cooperation with my [spouse, partner, etc.] → *Continue*
- No → *Thank respondent politely and end call.*

Q4: Do you work or have you ever worked for a bank or other financial institution, or in the real estate or mortgage industry?

- Yes → *Thank respondent politely and end call.*
- No → *Continue*

Q5: ARTICULATION QUESTION: In a few sentences, could you describe the process through which you found your current mortgage lender?

- If respondent indicates that he/she got their mortgage through a family member or close friend who was a broker or worked at a bank → *Thank respondent politely and end call.*

In all other cases...

- If respondent gives a thoughtful, articulate answer → *Continue to Q6*
- If respondent does not give a thoughtful, articulate answer → *Thank respondent politely and end call.*

At this point, I am going to ask you a few questions that pertain to financial information that you might find personal or private. However, I want to assure you that none of this information will be shared outside the group conducting this research, and all information will be kept anonymous—your name will never be used in any reports.

Q6: How many mortgages do you currently have on your primary residence?

- One (*skip to Q8a*)
- Two or more

Q7: Was the mortgage that you obtained in the past two years the larger or smaller of these mortgages?

- a) Larger (1<sup>st</sup> mortgage)
- b) Smaller (2<sup>nd</sup> or 3<sup>rd</sup> mortgage) [*NOTE: No more than 2 among interviews*]
- c) Both [*Direct respondent to answer remaining questions based on larger (1<sup>st</sup>) mortgage*]

If answer is  
"a" or "c" ↓

Q8a: What is the current interest rate on this mortgage?

- 7.5% or below
- Above 7.5% → **Qualifies as SP**
- Don't know

If answer is  
"b" ↓

Q8b: What is the current interest rate on this mortgage?

- 9.5% or below
- Above 9.5% → **Qualifies as SP**
- Don't know

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### ***Questions for Category B Candidates***

Q9: Have you ever owned a home?

- Yes → *Thank respondent politely and end call.*
- No → *Continue*

Q10: Have you looked into buying a home in the last year?

- Yes → *Continue*
- No → *Thank respondent politely and end call.*

- Q11: In the past year, have you spoken to a mortgage lender or a broker about buying a house?
- Yes → *Continue*
  - No → *Thank respondent politely and end call.*
- Q12: Do you work or have you ever worked for a bank or other financial institution, or in the real estate or mortgage industry?
- Yes → *Thank respondent politely and end call.*
  - No → *Continue*
- Q13: ARTICULATION QUESTION: If you find a house you are interested in buying, how do you think you will go about finding a mortgage loan?
- If respondent gives a thoughtful, articulate answer → *Continue*
  - If respondent does not give a thoughtful, articulate answer → *Thank respondent politely and end call.*
- Q14: Are you the person in your household who would be responsible for making decisions related to a mortgage?
- Yes → *Participant qualifies in Category B; continue to Q15*
  - Yes, in cooperation with my [spouse, partner, etc.] → *Participant qualifies in Category B; continue to Q15*
  - No → *Thank respondent politely and end call.*

**Note: No more than 2 participants can qualify in Category B; all other participants must qualify in Category A based on a “Yes” answer to Q1.**

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- Q15: Have you experienced any of the following financial hardships in the past seven years: bankruptcy, foreclosure, repossession, or a tax lien?
- Yes → Respondent qualifies as SP
  - No
- Q16: In the past two years, have you been turned down for credit or have you been discouraged from applying for credit?
- Yes → Respondent qualifies as SP
  - No

Screening Criteria	Interviews
<i>Does participant qualify as “SP”?</i>	<ul style="list-style-type: none"> <li>• At least 4 recruits must be SP</li> <li>• At least 4 recruits must NOT be SP</li> </ul>

<p>Q17: [Category A only] Was the mortgage that you obtained used to re-finance an existing mortgage?</p> <p>a) Yes (<i>skip to Q19</i>) b) No</p>	<ul style="list-style-type: none"> <li>• No more than 4 recruits should answer “a”</li> </ul>
<p>Q18: [Category A only] Was this the first home you ever purchased?</p> <p>a) Yes b) No</p>	<ul style="list-style-type: none"> <li>• At least 4 recruits should respond “a”</li> </ul>
<p>Q19: Some mortgages have an adjustable interest rate. Does your new mortgage have a rate that is adjustable or will become adjustable in the future?</p> <p>a) Yes, adjustable b) No, not adjustable → Have you had an adjustable rate mortgage in the past five years? <i>If Yes, then count as “a”</i> c) Don’t know</p>	<ul style="list-style-type: none"> <li>• No more than 3 recruits should respond “b” or “c”</li> </ul>
<p>Q20: What is your age?</p> <p>a) 18 to 25 b) 26 to 35 c) 36 to 50 d) 51 or above</p>	<ul style="list-style-type: none"> <li>• At least 3 recruits should respond “a” or “b”</li> <li>• At least 3 recruits should respond “c” or “d”</li> </ul>
<p>Q21: Which of the following categories best reflects your race or ethnicity? You can choose more than one category. [<i>Respondents who wish to choose more than one category should be counted as minorities, even if one race mentioned is White.</i>]</p> <p>a) White b) Black or African-American c) Hispanic or Latino d) Asian e) Native American or Pacific Islander</p>	<ul style="list-style-type: none"> <li>• At least 3 recruits should respond “a”</li> <li>• At least 3 recruits should respond “b”, “d”, or “e”</li> <li>• At least 2 recruits should respond “c”</li> </ul>
<p>Q22: What is the highest level that you reached in school?</p> <p>a) Some high school b) High school graduate c) At least some college work d) College graduate e) At least some graduate school</p>	<ul style="list-style-type: none"> <li>• At least 3 recruits should respond “a” or “b”</li> <li>• At least 3 recruits should be “c”</li> </ul>
<p>Q23: <i>Gender</i></p>	<ul style="list-style-type: none"> <li>• At least 3 recruits of each gender</li> </ul>



**APPENDIX C:  
Participant Demographic  
and Background  
Information**

Round 1	Round 2	Round 3	Round 4	Round 5	Round 6	Round 7
Greenbelt, MD (Feb. 2008 Focus Groups)	Washington, DC (Mar. 2008 Interviews)	Los Angeles, CA (Mar. 2008 Interviews)	Los Angeles, CA (Mar. 2008 Focus Groups)	Washington, DC (Apr. 2008 Interviews)	Kansas City, KS (May 2008 Interviews)	Baltimore, MD (Aug. 2008 Interviews)

## Personal Information

### Gender

Male	5	2	4	8	3	4	3
Female	11	5	3	8	7	7	7

### Age

18-35	1 <sup>1</sup>	3	3	2	1	4	6
36+	13	4	4	14	9	7	4

### Race

Caucasian	6	1	3	5	3	9	5
African-American	10	6	1	3	6	2	5
Hispanic	0	0	3	8	1	0	0
Other	0	0	0	0	0	0	0

### Education Level

High school or less	2	1	0	4	1	2	3
Some college or more	14	6	7	12	9	9	7

### Financial Hardship (e.g., bankruptcy, foreclosure) in Past 7 Years<sup>2</sup>

Yes	8	0	0	4	0	1	2
No	8	7	7	12	10	10	8

### Denied Credit or Discouraged From Applying in Past 2 Years<sup>2</sup>

Yes	4	2	1	5	2	2	3
No	12	5	6	11	8	9	7

### Creditworthiness<sup>2</sup>

Subprime	9	2	2	8	3	3	4
Prime	7	5	5	8	7	8	6

Round 1	Round 2	Round 3	Round 4	Round 5	Round 6	Round 7
Greenbelt, MD (Feb. 2008 Focus Groups)	Washington, DC (Mar. 2008 Interviews)	Los Angeles, CA (Mar. 2008 Interviews)	Los Angeles, CA (Mar. 2008 Focus Groups)	Washington, DC (Apr. 2008 Interviews)	Kansas City, KS (May 2008 Interviews)	Baltimore, MD (Aug. 2008 Interviews)

### Information About Loan History

#### Reason for Most Recent Loan

Refinance	9	1	3	8	9	7	6
Home purchase	7	6	4	8	1	4	4
No previous loan	0	0	0	0	0	0	0

#### First-Time Home Buyer<sup>3</sup>

Yes	6	3	2	6	0	2	3
No	1	3	2	2	1	2	1

#### Current Number of Mortgages on Primary Residence

One	14	7	6	8	8	10	7
Two or more	2	0	1	8	2	1	3

#### Had Adjustable Rate Mortgage in Past 5 Years?

Yes	10	6	5	12	4	7	7
No	6	1	2	4	6	4	3

#### Method of Obtaining Most Recent Loan

Through broker	3	2	3	10	1	3	4
Directly from lender	8	3	4	5	9	8	6
Don't know	5	2	0	1	0	0	0

#### Most Recent Loan: FHA or VA?

Yes	3	1	0	2	2	2	4
No	13	6	7	14	8	9	4
Don't know	0	0	0	0	0	0	2

#### Current Interest Rate Above Threshold<sup>2,4</sup>

Yes	0	0	1	2	1	2	1
No	16	7	6	14	9	9	9

Round 8	Round 9	Round 10	Round 11	Round 12	Round 13	Grand Total <sup>5,6</sup>
Atlanta, GA (Nov. 2008 Interviews)	Bethesda, MD (Jan. 2009 Interviews)	Dallas, TX (Feb. 2009 Interviews)	Providence, RI (Mar. 2009 Interviews)	Denver, CO (Apr. 2009 Interviews)	Bethesda, MD (May 2009 Interviews)	

### Personal Information

Personal Information							
<b>Gender</b>							
Male	5	4	4	6	4	3	<b>55 (41%)</b>
Female	4	5	6	4	6	6	<b>79 (59%)</b>
<b>Age</b>							
18-35	2	2	2	5	5	3	<b>39 (30%)</b>
36+	7	7	8	5	5	6	<b>93 (70%)</b>
<b>Race</b>							
Caucasian	5	5	3	8	6	5	<b>64 (48%)</b>
African-American	4	3	4	1	0	2	<b>47 (35%)</b>
Hispanic	0	1	2	1	3	2	<b>21 (16%)</b>
Other	0	0	1	0	1	0	<b>2 (1%)</b>
<b>Education Level</b>							
High school or less	2 <sup>7</sup>	0	1	1	1	2	<b>20 (15%)</b>
Some college or more	6	9	9	9	9	7	<b>113 (85%)</b>
<b>Financial Hardship (e.g., bankruptcy, foreclosure) in Past 7 Years<sup>2</sup></b>							
Yes	4	2	4	1	3	1	<b>30 (22%)</b>
No	5	7	6	9	7	8	<b>104 (78%)</b>
<b>Denied Credit or Discouraged From Applying in Past 2 Years<sup>2</sup></b>							
Yes	4	3	7	2	6	3	<b>44 (33%)</b>
No	5	6	3	8	4	6	<b>90 (67%)</b>
<b>Creditworthiness<sup>2</sup></b>							
Subprime	4	4	7	2	8	3	<b>59 (44%)</b>
Prime	5	5	3	8	2	6	<b>75 (56%)</b>

Round 8	Round 9	Round 10	Round 11	Round 12	Round 13	Grand Total <sup>5,6</sup>
Atlanta, GA (Nov. 2008 Interviews)	Bethesda, MD (Jan. 2009 Interviews)	Dallas, TX (Feb. 2009 Interviews)	Providence, RI (Mar. 2009 Interviews)	Denver, CO (Apr. 2009 Interviews)	Bethesda, MD (May 2009 Interviews)	

## Information About Loan History

### Reason for Most Recent Loan

Refinance	3	3	4	5 <sup>8</sup>	4	3	65 (49%)
Home purchase	6	6	5	2	5	5	63 (47%)
No previous loan <sup>9</sup>	0	0	1	2	1	1	5 (4%)

### First-Time Home Buyer<sup>3</sup>

Yes	3	4	2	2	3	4	40 (63%)
No	3	2	3	0	2	1	23 (37%)

### Current Number of Mortgages on Primary Residence

One	4	7	8	8	6	4	97 (75%)
Two or more	5	2	1	0	3	4	32 (25%)

### Had Adjustable Rate Mortgage in Past 5 Years?

Yes	3	5	6	2	7	5 <sup>10</sup>	79 (61%)
No	6	4	3	6	2	3	50 (39%)

### Method of Obtaining Most Recent Loan

Through broker	3	5	4	4 <sup>11</sup>	4	2	48 (38%)
Directly from lender	4	4	5	3	4	5	68 (53%)
Don't know	2	0	0	0	1	1	12 (9%)

### Most Recent Loan: FHA or VA?

Yes	4	2	0	2 <sup>12</sup>	1	1	24 (19%)
No	5	7	9	5	4	6	97 (76%)
Don't know	0	0	0	0	4	1	7 (5%)

### Current Interest Rate Above Threshold<sup>2,4</sup>

Yes	0	1	3	1	3	1	16 (12%)
No	9	8	6	7	6	7	113 (88%)

<sup>1</sup> In this round of testing, two participants did not provide their age.

<sup>2</sup> Participants' responses to three questions were used to categorize them as likely prime or subprime borrowers. Participants were categorized as "subprime" if they had: a) suffered a "financial hardship" such as bankruptcy, foreclosure, repossession or a tax lien in the past 7 years; b) been denied credit or discouraged from applying for credit in the past 2 years; or c) the current interest rate on their loan was higher than established HMDA thresholds (see Footnote 4 below).

<sup>3</sup> Only respondents whose most recent mortgage was for a home purchase (as opposed to a refinance) answered this question.

<sup>4</sup> The interest rate thresholds that were used to classify respondents as "subprime" were set to be roughly consistent with the Home Mortgage Disclosure Act (HMDA) APR-based thresholds for reporting higher-priced loans. For Rounds 1 through 8, the 2007-08 HMDA thresholds were used: 8 percent for a first mortgage and 10 percent for a second or third mortgage. For Rounds 9 through 13, these rates were adjusted to the 2008-09 HMDA thresholds: 7.5 percent for a first mortgage and 9.5 percent for a second or third mortgage.

<sup>5</sup> Percentages of participants by demographic category may contain a small rounding error, of less than to 1%.

<sup>6</sup> Some interviews were conducted with couples who indicated that they made mortgage decisions together. In these cases, the personal information shown in this table was collected from the member of the couple who responded to the recruitment screening questions.

<sup>7</sup> In this round of testing, one participant did not provide their education level.

<sup>8</sup> In this round, one participant did not provide the reason for their most recent loan.

<sup>9</sup> Participants that had never obtained a mortgage loan were not asked any of the subsequent questions about their loan history.

<sup>10</sup> In this round, one participant did not indicate whether he had an ARM in the past 5 years.

<sup>11</sup> In this round, one participant did not indicate the method through which they obtained their most recent mortgage.

<sup>12</sup> In this round, one participant did not indicate whether his most recent loan was obtained through the FHA or VA.

**APPENDIX D:  
Disclosure Forms Used  
in Testing**

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# **Round 1: Greenbelt, MD February 20, 2008**

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- **Current TILA Statement**
- **Current ARM Loan Program Disclosure**



**Truth in Lending Disclosure Statement**

<b>Date</b> January 2007	<b>Loan Number</b> 23879562
<b>Lender</b> Universal Mortgage	
<b>Borrower(s)</b> Emily Johnson	
<b>Property Address</b> 79 Sussex Court Wilmington, DE 19808	

**Final Disclosure**

ANNUAL PERCENTAGE RATE	FINANCE CHARGE	Amount Financed	Total of Payments
The cost of your credit as a yearly rate.	The dollar amount the credit will cost you.	The amount of credit provided to you or on your behalf.	The amount you will have paid after you have made all payments as scheduled.
12.1515 %	\$ 205,908.94	\$ 71,617.84	\$ 277,526.78

**Payment Schedule: Payments will be due monthly**

Number of Payments	Amount of Payment	Payments Begin
024	\$ 638.24	03/01/07
335	780.44	03/01/09
001	761.62	02/01/37

- Variable Rate**      Your loan  does  does not contain a variable-rate feature. Disclosures about the variable rate feature have been provided to you earlier.
- Security**            You are giving a security interest  in the real property, and fixtures and rents if indicated in the rider mortgage  shares of stock evidencing ownership of the cooperative unit, at the property address referenced above.
- Late Charge**        If a payment is more than 15 days late, you will be charged 5% of the payment.
- Assumption**        Someone buying your house  may, subject to conditions,  cannot be allowed to assume the remainder of the loan on the original terms.
- Prepayment**        If you pay off your loan early, you  may,  will not have to pay a penalty.  
If you pay off your loan early, you  may,  will not be entitled to a refund of part of the finance charge.\*
- Demand Feature**     If checked, your loan includes a demand feature.
- Hazard Insurance**   Hazard Insurance is required and may be obtained through any company of your choice that is acceptable to the Lender.

You should refer to your Note, Mortgage and other documents for additional information about non-payment, default, and required repayment in full before the scheduled date, prepayment rebates, and penalties.

*\*If you pay off your loan early, you will not receive a refund of part of the finance charge that you have already paid.*

**I (We) acknowledge receipt of this Disclosure Statement.**                      Date: \_\_\_\_\_

\_\_\_\_\_

Date: OCTOBER 19, 2006

Borrower Name: JOHN DOE

Property Address: 1234 MAIN STREET, SCOTTSDALE, ARIZONA 85254

## **ADJUSTABLE RATE MORTGAGE LOAN PROGRAM DISCLOSURE 2 YEAR LIBOR ARM**

This disclosure describes the features of an Adjustable Rate Mortgage (ARM) program you are considering, which is called the 2 YEAR LIBOR ARM. The interest rate and payment of this loan may each change during the term of this loan. Information on other ARM programs available from the lender will be provided upon request.

### ***HOW YOUR INTEREST RATE AND PAYMENT ARE DETERMINED:***

- Beginning on the first Interest Rate Change Date, your interest rate will be based on an index rate plus a margin. Please ask us for our current interest rate and margin.
- Your initial interest rate will not be equal to an index rate plus a margin. If the initial interest rate is below the then current index plus margin ("the fully indexed rate"), then the initial interest rate will be a "discounted" interest rate. Please ask us about the amount of the current discount.
- The index rate is the average of interbank offered rates for six-month U.S. dollar-denominated deposits in the London market ("LIBOR"), as published in The Wall Street Journal. Index rate values are shown below for the first business day of each month and year shown. The example shows how your payment would have changed based on actual changes in the index from 1992 to the present. If this index is no longer available at any Interest Rate Change Date, the lender will choose a new index that is based on comparable information and will give you notice of this change.
- When your interest rate changes, your new interest rate will equal the index rate, which is the most recently available index rate as of the first business day of the month immediately preceding the Interest Rate Change Date, plus the margin rounded to the nearest one-eighth percent (.125%).
- When your payment changes, your new payment will be based on the interest rate, loan balance, and remaining loan term. The new payment will be an amount sufficient to repay the loan balance at the new interest rate in substantially equal payments over the remaining loan term. Therefore, **NO NEGATIVE AMORTIZATION WILL EVER OCCUR** under this loan program.

### ***HOW YOUR INTEREST RATE CAN CHANGE***

- Your interest rate can change on your 24th payment date and every 6 months thereafter (the "Interest Rate Change Date") to a rate equal to the index value plus the margin, rounded to the nearest .125%, subject to the following limits:
  - Your interest rate cannot increase by more than three percentage points (3.00%) at the first Interest Rate Change Date and cannot increase or decrease by more than one percentage point (1.00%) at each Interest Rate Change Date thereafter (the "Periodic Rate Cap").
  - Your interest rate over the life of the loan cannot increase by more than six percentage points (6.00%) above the initial interest rate (the "Lifetime Rate Cap").
  - Your interest rate will never be less than a minimum, or floor, rate equal to the initial interest rate (the "Lifetime Floor Rate").

### ***HOW YOUR PAYMENT CAN CHANGE***

Your payment may change on the first payment date after the first Interest Rate Change Date and every 6 months thereafter. For example, on a \$10,000, 360-month loan with an initial interest rate of 9.000%, (i.e., the index plus the margin shown for 2006 in the Historical Example on page 2, rounded to the nearest .125% and reduced by the initial discount of 3.0%), the maximum amount that the interest rate could rise under this program is 6.000% above the initial interest rate of 9.000% up to 15.000% and the payment amount could rise from the beginning payment of \$80.46 to a maximum of \$124.89 (at payment 43). You will be notified in writing 30 days before a payment adjustment may be made. This notice will contain information about the index and interest rates, payment amount, and loan balance.

**EXAMPLE OF A 1992 \$10,000 LOAN USING HISTORICAL INDEX VALUES:**

The example below shows how your payments would have changed under the ARM program based on actual changes in the index from 1992 to 2006. This does not necessarily indicate how your index will change in the future. For simplicity, the example is based on these assumptions:

Loan Amount: \$10,000 Interest Adjustment: Every 6 Months (beginning with the 24th payment date)  
 Amortization Period: 360 Months Payment Adjustment: Every 6 Months (beginning with the 25th payment date)  
 Interest Rate Margin: 7.250%\* Initial Interest Rate: 8.500%\*\*

YEAR	INDEX VALUE	MARGIN	INTEREST RATE	MONTHLY PAYMENT	LOAN BALANCE
January 1992	4.19%	7.25%	8.500% **	12 @ \$76.89	\$9,924.42
January 1993	3.69%	7.25%	8.500%	12 @ \$76.89	\$9,842.16
January 1994	3.56%	7.25%	10.750%	12 @ \$92.81	\$9,783.65
January 1995	7.00%	7.25%	12.750% ***	12 @ \$107.45	\$9,739.12
January 1996	5.47%	7.25%	12.750%	12 @ \$107.45	\$9,688.57
January 1997	5.63%	7.25%	12.875%	12 @ \$108.36	\$9,632.42
January 1998	5.56%	7.25%	12.750%	12 @ \$107.47	\$9,567.18
January 1999	.5.07%	7.25%	12.375%	12 @ \$104.84	\$9,488.69
January 2000	6.23%	7.25%	13.500%	12 @ \$112.62	\$9,413.69
January 2001	5.36%	7.25%	12.625%	12 @ \$106.67	\$9,316.64
January 2002	1.99%	7.25%	10.625% ***	12 @ \$93.80	\$9,174.13
January 2003	1.35%	7.25%	8.625%	12 @ \$ 81.95	\$8,974.22
January 2004	1.21%	7.25%	8.500%	12 @ \$ 81.26	\$8,753.44
January 2005	2.96%	7.25%	10.250%	12 @ \$ 90.78	\$8,552.02
January 2006	4.81%	7.25%	12.000%	12 @ \$100.38	\$8,363.56

\* This is a margin we have used recently. Your margin may be different.

\*\* This interest rate reflects an initial discount of 3.0% and is rounded to the nearest one-eighth percent (.125%). Your initial interest rate may reflect a different discount from the fully-indexed rate.

\*\*\* This interest rate reflects a one (1) percentage point periodic interest rate cap.

To see what your payments (excluding impounds or escrow payments for taxes, insurance and other purposes relating to the security property) would have been during a period reflected in the chart, divide your mortgage amount by \$10,000, then multiply the loan payment reflected in the chart for that period, by that amount. For example, in 2006 the loan payments for a mortgage amount of \$60,000 taken out in 1992 would be:  $\$60,000/\$10,000 = 6 \times \$100.38 = \$602.28$ .

Borrower \_\_\_\_\_  
 Date Consumer Handbook on  
 Adjustable Rate Mortgages and  
 disclosure received

Borrower \_\_\_\_\_  
 Date Consumer Handbook on  
 Adjustable Rate Mortgages and  
 disclosure received

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**Round 2:  
Washington, DC  
March 4 & 6, 2008**

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- **Proposed Pollock Form**
- **Proposed Joint (HUD-Fed) Form**

# THE BASIC FACTS ABOUT YOUR MORTGAGE LOAN

Borrower: Jane and Karl Rover Property address: 4 Interview Lane  
Lending, MD 20815

Lender: XYZ Bank

Amount of loan: \$ 200,000.00, which is 80 % of the property's appraised value.

Your loan is for 30 years.

The type of loan you have: 3/1 LIBOR ARM

Your beginning interest rate is 5.625 %. This rate is good for 36 months/years. The rate and your payment can go higher on Aug 2010 and each 12 months after that.

Today's estimate of how high the rate will go, called the fully indexed rate, is 7.75 %.

The maximum possible rate on your loan is 11.625 %.

THIS LOAN IS BASED ON YOUR MONTHLY INCOME OF \$ 6,250.00

Your beginning rate = a monthly loan payment of \$ 1,151.31 = 18.42 % of your income.

-including taxes and insurance this is about \$ 1,422.15 = 22.75 % of your income.

The fully-indexed rate = a loan payment of \$ 1,412.83 = 22.61 % of your income.

-including taxes and insurance this is about \$ 1,683.66 = 26.94 % of your income.\*

\*This is called your fully indexed housing expense ratio.

## Special factors you must be aware of:

-A prepayment fee of up to \$4,500 must be paid if you refinance within the first three years.

-A "balloon payment" of \$ \_\_\_\_\_ to pay off your loan will be due on \_\_\_\_\_.

-You ~~do~~/do not have a "payment option" loan. If you do, make sure you really understand what this means.

Start with the definition on page 3.

Total "points" plus estimated other costs and fees due at closing are \$ 7,347.00

FOR QUESTIONS CONTACT: Name: Albert Lender

Phone: (301) 496-0000 e-mail: alender@mortgage.com

**See definitions of underlined terms and guidelines on pages 2-3.  
DO NOT SIGN THIS IF YOU DON'T UNDERSTAND IT!**

_____	_____	_____	_____
Authorized Signer of Lender	Date	Borrower	Date

## The Basic Facts about Your Mortgage Loan

This form gives you the basic facts, but some mortgage forms may use terms not listed here. For a good, borrower-friendly information source, try the Mortgage Professor online ([www.mtgprofessor.com](http://www.mtgprofessor.com)), which includes detailed explanations of the technical mortgage terms in its glossary and much other helpful information.

### Definitions and Guidelines Used in This Form

The *appraised value* is what a professional appraisal estimates the house could be sold for in today's market.

The *type of loan* determines whether and by how much your interest rate can increase. If it can, your monthly payments will also increase—sometimes by a lot. For example, in a thirty-year fixed rate loan, the interest rate is always the same. In a one-year ARM, it will change every year. Other kinds of loans have various patterns, but the interest rate may go up a lot. Make sure you understand what type of loan you're getting.

The *beginning interest rate* is the interest you are paying at the beginning of the loan. Especially if it is a low introductory or "teaser" rate, it is the rate which you will hear the most about from ads and salespeople. But how long is it good for and when will rates increase? In many types of loans, the rate will go up by a lot. You need to know.

The *fully-indexed rate* is an essential indicator of what will happen to your interest rate and your monthly payments. It is today's estimate of how high the interest rate on an adjustable rate mortgage will go. It is calculated by taking a defined "index rate" and adding a certain number of percentage points, called the "margin." For example, if your formula is the one-year Treasury rate plus 3 percent, and today the one-year Treasury rate is 5 percent, your fully-indexed rate is  $5\% + 3\% = 8\%$ . At the time the loan is being made, the fully indexed rate will *always* be higher than a beginning "teaser" rate.

The index rates are public, published rates, so you can study their history to see how much they change over

time. If the index rate stays the same as today, the rate on your loan will automatically rise to the fully-indexed rate over time. Since the index rate itself can go up and down, you cannot be sure what the future adjustable rate will be. In any case, you must *make sure you can afford the fully-indexed rate*, not just the beginning rate, which is often called a "teaser" rate for good reason.

The *maximum possible rate* is the highest your interest rate can go. Most loans with adjustable rates have a defined maximum rate or "lifetime cap." You need to think about what it would take to make your interest rate go this high. How likely do you think that is?

Your *monthly income* means your gross, pre-tax income per month for your household. This should be an amount which you can most probably sustain over many years. Make sure the monthly income shown on this form is correct!

Your *monthly payment including taxes and insurance* is the amount you must pay every month for interest, repayment of loan principal, house insurance premiums, and property taxes. Expressed as a percent of your monthly income, this is called your housing expense ratio. Over time, in addition to any possible increases in your interest rate and how fast you must repay principal, your insurance premiums and property taxes will tend to increase. Of course, your monthly income may also increase. How much do you expect it to?

Your *fully-indexed housing expense ratio* is a key measure of whether you can afford this loan. It is the percent of your monthly income it will take to pay interest at the fully-indexed rate, plus repayment of principal, house insurance, and property taxes. The time-tested market standard for this ratio is 28 percent; the greater your ratio is, the riskier the loan is for you.

A *prepayment fee* is an additional fee imposed by the lender if you pay your loan off early. Most

mortgages in America have no prepayment fee. If yours does, make sure you understand how it would work before you sign this form.

A “*balloon payment*” means that a large repayment of loan principal is due at the end of the loan. For example, a seven-year balloon means that the whole remaining loan principal, a very large amount, must be paid at the end of the seventh year. This almost always means that you have to get a new loan to make the balloon payment.

A “*payment option*” loan means that in the years immediately after securing a mortgage loan, you can pay even less than the interest you are being charged. The unpaid interest is added to your loan, so the amount you owe gets bigger. This is called “negative amortization.” The very low payments in early years create the risk of very large increases in your monthly payment later. Payment option loans are typically advertised using only the very low beginning or “teaser” required payment, which is less than the interest rate. You absolutely need to know four things: (1) How long is the beginning payment good for? (2) What happens then? (3) How much is added to my loan if I pay the minimum rate? (4) What is the fully-indexed rate?

“*Points*” are a fee the borrower pays the lender at closing, expressed as a percent of the loan. For example, two points mean you will pay an upfront fee equal to 2 percent of the loan. In addition, mortgages usually involve a number of *other costs and fees* which must be paid at closing.

*Closing* is when the loan is actually made and all the documents are signed.

The *For Questions Contact* section gives you the name, phone number, and e-mail address of someone specifically assigned by your lender to answer your questions and explain the complications of mortgage loans. Don’t be shy: contact this person if you have any questions.

Finally, *do not sign this form if you do not understand it*. You are committing yourself to pay large amounts of money over years to come and pledging your house as collateral so the lender can take it if you don’t pay. Ask questions until you are sure you know what your commitments really are and how they compare to your income. Until then, do not sign.

# Federal Disclosure Statement for Home-Secured Loans

BORROWERS: Mary and James Focus

CREDITOR: ABC Bank

PROPERTY ADDRESS: 3 Group Lane, Homeloan, MD 20790

DATE: 06/25/07

LOAN NO.: 123

LOAN AMOUNT	INTEREST RATE	REQUIRED CLOSING COSTS (including points)	MONTHLY PAYMENT
You are borrowing \$ <u>\$200,000</u> .	Your interest rate is <u>5.625%</u> . <input type="checkbox"/> fixed <input checked="" type="checkbox"/> variable*	Your required closing costs (including points) are estimated to total \$ <u>7,347.00</u> .	Your monthly principal and interest payment is <u>\$1,151.31</u> .

\* If checked, your loan contains a variable rate feature. During the term of your loan, the highest your interest rate could increase is to 11.625% , resulting in monthly payments of \$ 1,924.97 . See the variable rate disclosures separately provided to you for further information about how your rate, payment, and loan term may be adjusted.

**Finance Charge and Annual Percentage Rate (APR):** The dollar cost of borrowing \$ 200,000 for 30 years is \$ 303,767.47 (the finance charge). The cost of credit as a yearly rate (the APR) is 7.41% . The APR reflects interest (including points) and other costs required to obtain the loan. Taxes, escrow amounts and hazard insurance premiums are not included. You can use the APR to compare loan products among different lenders.

**Your Scheduled Payments for Principal and Interest Will Be:**

Number of Payments	Monthly Payments**	Total of Scheduled Payments
36	\$ 1,151.31 beginning Aug. 1, 2007	\$ 41,447.16
12	\$ 1,397.15 beginning Aug. 1, 2010	\$ 16,765.80
311	\$ 1,412.83 beginning Aug. 1, 2011	\$ 439,390.13
1	\$ 1,414.38 beginning Jul. 1, 2037	\$ 1,414.38

\*\*This amount does not include taxes or insurance.

**Security:** Your home is the security for this loan. **You may lose your home** if you do not make your payments.

**Late Charge:** If a payment is late, you will be charged \$ 50.00 .

**Prepayment Penalty:** If you pay your loan off early, you  will be charged a penalty.  
 will not be charged a penalty.

**Transfer of Servicing:** We may assign, sell, or transfer the servicing of your loan (the right to collect payments from you).

**Private Mortgage Insurance (PMI):** PMI  is required for your loan.  
You  may cancel when your balance is \_\_\_\_\_% of the home's value, or by paying an additional fee of \$ \_\_\_\_\_.  
You  may not cancel PMI.  
 is not required for your loan.

**Escrow Account:** You  will be required to have an escrow account for payment of taxes and hazard insurance. Your escrow account will add \$270.84 to your initial monthly payments listed in the payment schedule above.

You  may pay \$ \_\_\_\_\_ to cancel the escrow requirement.

You  may not cancel the escrow requirement.

will not be required to have an escrow account.



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**Round 3:  
Los Angeles, CA  
(Interviews)  
March 25-26, 2008**

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- **Proposed Pollock Form**
- **Proposed Joint (HUD-Fed) Form**

# THE BASIC FACTS ABOUT YOUR MORTGAGE LOAN

Borrower: Jane and Karl Rover Property address: 4 Interview Lane  
Lending, MD 20815

Lender: XYZ Bank

Amount of loan: \$ 360,000.00, which is 80 % of the property's appraised value.

Your loan is for 30 years.

The type of loan you have: 3/1 LIBOR ARM

Your beginning interest rate is 5.625 %. This rate is good for 36 months/years. The rate and your payment can go higher on Aug 2010 and each 12 months after that.

Today's estimate of how high the rate will go, called the fully indexed rate, is 7.75 %.

The maximum possible rate on your loan is 11.625 %.

THIS LOAN IS BASED ON YOUR MONTHLY INCOME OF \$ 9,166.67

Your beginning rate = a monthly loan payment of \$ 2,072.36 = 22.6 % of your income.

-including taxes and insurance this is about \$ 2,559.86 = 27.9 % of your income.

The fully-indexed rate = a loan payment of \$ 2,543.10 = 27.7 % of your income.

-including taxes and insurance this is about \$ 3,030.60 = 33.1 % of your income.\*

\*This is called your fully indexed housing expense ratio.

## Special factors you must be aware of:

-A prepayment fee of up to \$8,100.00 must be paid if you pay off or refinance your loan within 3 years .

-A "balloon payment" of \$ \_\_\_\_\_ to pay off your loan will be due on \_\_\_\_\_ .

-You do/do not have a "payment option" loan. If you do, make sure you really understand what this means.

Start with the definition on page 3.

Total "points" plus estimated other costs and fees due at closing are \$ 11,980.00 .

FOR QUESTIONS CONTACT: Name: Albert Lender

Phone: (301) 496-0000 e-mail: alender@mortgage.com

**See definitions of underlined terms and guidelines on pages 2-3.  
DO NOT SIGN THIS IF YOU DON'T UNDERSTAND IT!**

Borrower Date

Authorized Signer of Lender Date Borrower Date

## The Basic Facts about Your Mortgage Loan

This form gives you the basic facts, but some mortgage forms may use terms not listed here. For a good, borrower-friendly information source, try the Mortgage Professor online ([www.mtgprofessor.com](http://www.mtgprofessor.com)), which includes detailed explanations of the technical mortgage terms in its glossary and much other helpful information.

### Definitions and Guidelines Used in This Form

The *appraised value* is what a professional appraisal estimates the house could be sold for in today's market.

The *type of loan* determines whether and by how much your interest rate can increase. If it can, your monthly payments will also increase—sometimes by a lot. For example, in a thirty-year fixed rate loan, the interest rate is always the same. In a one-year ARM, it will change every year. Other kinds of loans have various patterns, but the interest rate may go up a lot. Make sure you understand what type of loan you're getting.

The *beginning interest rate* is the interest you are paying at the beginning of the loan. Especially if it is a low introductory or "teaser" rate, it is the rate which you will hear the most about from ads and salespeople. But how long is it good for and when will rates increase? In many types of loans, the rate will go up by a lot. You need to know.

The *fully-indexed rate* is an essential indicator of what will happen to your interest rate and your monthly payments. It is today's estimate of how high the interest rate on an adjustable rate mortgage will go. It is calculated by taking a defined "index rate" and adding a certain number of percentage points, called the "margin." For example, if your formula is the one-year Treasury rate plus 3 percent, and today the one-year Treasury rate is 5 percent, your fully-indexed rate is  $5\% + 3\% = 8\%$ . At the time the loan is being made, the fully indexed rate will *always* be higher than a beginning "teaser" rate.

The index rates are public, published rates, so you can study their history to see how much they change over

time. If the index rate stays the same as today, the rate on your loan will automatically rise to the fully-indexed rate over time. Since the index rate itself can go up and down, you cannot be sure what the future adjustable rate will be. In any case, you must *make sure you can afford the fully-indexed rate*, not just the beginning rate, which is often called a "teaser" rate for good reason.

The *maximum possible rate* is the highest your interest rate can go. Most loans with adjustable rates have a defined maximum rate or "lifetime cap." You need to think about what it would take to make your interest rate go this high. How likely do you think that is?

Your *monthly income* means your gross, pre-tax income per month for your household. This should be an amount which you can most probably sustain over many years. Make sure the monthly income shown on this form is correct!

Your *monthly payment including taxes and insurance* is the amount you must pay every month for interest, repayment of loan principal, house insurance premiums, and property taxes. Expressed as a percent of your monthly income, this is called your housing expense ratio. Over time, in addition to any possible increases in your interest rate and how fast you must repay principal, your insurance premiums and property taxes will tend to increase. Of course, your monthly income may also increase. How much do you expect it to?

Your *fully-indexed housing expense ratio* is a key measure of whether you can afford this loan. It is the percent of your monthly income it will take to pay interest at the fully-indexed rate, plus repayment of principal, house insurance, and property taxes. The time-tested market standard for this ratio is 28 percent; the greater your ratio is, the riskier the loan is for you.

A *prepayment fee* is an additional fee imposed by the lender if you pay your loan off early. Most

mortgages in America have no prepayment fee. If yours does, make sure you understand how it would work before you sign this form.

A “*balloon payment*” means that a large repayment of loan principal is due at the end of the loan. For example, a seven-year balloon means that the whole remaining loan principal, a very large amount, must be paid at the end of the seventh year. This almost always means that you have to get a new loan to make the balloon payment.

A “*payment option*” loan means that in the years immediately after securing a mortgage loan, you can pay even less than the interest you are being charged. The unpaid interest is added to your loan, so the amount you owe gets bigger. This is called “negative amortization.” The very low payments in early years create the risk of very large increases in your monthly payment later. Payment option loans are typically advertised using only the very low beginning or “teaser” required payment, which is less than the interest rate. You absolutely need to know four things: (1) How long is the beginning payment good for? (2) What happens then? (3) How much is added to my loan if I pay the minimum rate? (4) What is the fully-indexed rate?

“*Points*” are a fee the borrower pays the lender at closing, expressed as a percent of the loan. For example, two points mean you will pay an upfront fee equal to 2 percent of the loan. In addition, mortgages usually involve a number of *other costs and fees* which must be paid at closing.

*Closing* is when the loan is actually made and all the documents are signed.

The *For Questions Contact* section gives you the name, phone number, and e-mail address of someone specifically assigned by your lender to answer your questions and explain the complications of mortgage loans. Don’t be shy: contact this person if you have any questions.

Finally, *do not sign this form if you do not understand it*. You are committing yourself to pay large amounts of money over years to come and pledging your house as collateral so the lender can take it if you don’t pay. Ask questions until you are sure you know what your commitments really are and how they compare to your income. Until then, do not sign.

# Federal Disclosure Statement for Home-Secured Loans

BORROWERS: Mary and James Focus

CREDITOR: ABC Bank

PROPERTY ADDRESS: 3 Group Lane, Homeloan, MD 20790

DATE: 06/25/07

LOAN NO.: 123

LOAN AMOUNT	INTEREST RATE	REQUIRED CLOSING COSTS (including points)	MONTHLY PAYMENT
You are borrowing \$ <u>\$360,000</u> .	Your interest rate is <u>5.625%</u> . <input type="checkbox"/> fixed <input checked="" type="checkbox"/> variable*	Your required closing costs (including points) are estimated to total \$ <u>11,980.00</u> .	Your initial monthly payment including principal, interest, taxes and insurance is <u>\$2,559.86</u> .

\* If checked, your loan contains a variable rate feature. During the term of your loan, the highest your interest rate could increase is to 11.625%, resulting in estimated monthly payments of \$ 3,952.44, including principal, interest, taxes and insurance. See the variable rate disclosures separately provided to you for further information about how your rate, payment, and loan term may be adjusted.

**Finance Charge and Annual Percentage Rate (APR):** The dollar cost of borrowing \$ 360,000 for 30 years is \$ 548,176.78 (the finance charge). The cost of credit as a yearly rate (the APR) is 7.45% . The APR reflects interest (including points) and other costs required to obtain the loan. Taxes, escrow amounts and hazard insurance premiums are not included. You can use the APR to compare loan products among different lenders.

**Your Scheduled Estimated Payments for Principal, Interest, Taxes and Insurance Will Be:**

Number of Payments	Monthly Payments**	Total of Scheduled Payments
36	\$ 2,559.86 beginning Aug. 1, 2007	\$ 92,154.96
12	\$ 3,002.37 beginning Aug. 1, 2010	\$ 36,028.44
311	\$ 3,030.60 beginning Aug. 1, 2011	\$ 942,516.60
1	\$ 3,026.78 beginning Jul. 1, 2037	\$ 3,026.78

\*\*This amount DOES include an estimate of \$ 487.50 for escrow of taxes and insurance.

**Security:** Your home is the security for this loan. **You may lose your home** if you do not make your payments.

**Late Charge:** If a payment is late, you will be charged \$ 100.00 .

**Prepayment Penalty:** If you pay off or refinance your loan within 3 years, you  will be charged a penalty of up to \$ 8,100.00  
 will not be charged a penalty.

**Transfer of Servicing:** We may assign, sell, or transfer the servicing of your loan (the right to collect payments from you).

**Private Mortgage Insurance (PMI):** PMI  is required for your loan.  
You  may cancel when your balance is \_\_\_\_\_% of the home's value, or by paying an additional fee of \$ \_\_\_\_\_.  
You  may not cancel PMI.  
 is not required for your loan.

**Escrow Account:** You  will be required to have an escrow account for payment of taxes and hazard insurance. An amount of \$ 487.50 has been included in the payments above to reflect the initial amount of your escrow. The amount of your escrow payment is likely to rise over time.  
You  may pay \$ \_\_\_\_\_ to cancel the escrow requirement.  
You  may not cancel the escrow requirement.  
 will not be required to have an escrow account.

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**Round 4:  
Los Angeles, CA  
(Focus Groups)  
March 25-26, 2008**

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- **Current TILA Statement**
- **Current ARM Program Disclosure**

**Truth in Lending Disclosure Statement**

<b>Date</b> January 2007	<b>Loan Number</b> 23879562
<b>Lender</b> Universal Mortgage	
<b>Borrower(s)</b> Emily Johnson	
<b>Property Address</b> 79 Sussex Court Wilmington, DE 19808	

**Final Disclosure**

<b>ANNUAL PERCENTAGE RATE</b>	<b>FINANCE CHARGE</b>	<b>Amount Financed</b>	<b>Total of Payments</b>
The cost of your credit as a yearly rate.	The dollar amount the credit will cost you.	The amount of credit provided to you or on your behalf.	The amount you will have paid after you have made all payments as scheduled.
12.1515 %	\$ 205,908.94	\$ 71,617.84	\$ 277,526.78

**Payment Schedule: Payments will be due monthly**

<b>Number of Payments</b>	<b>Amount of Payment</b>	<b>Payments Begin</b>
024	\$ 638.24	03/01/07
335	780.44	03/01/09
001	761.62	02/01/37

- Variable Rate**      Your loan  does  does not contain a variable-rate feature. Disclosures about the variable rate feature have been provided to you earlier.
- Security**            You are giving a security interest  in the real property, and fixtures and rents if indicated in the rider mortgage  shares of stock evidencing ownership of the cooperative unit, at the property address referenced above.
- Late Charge**        If a payment is more than 15 days late, you will be charged 5% of the payment.
- Assumption**        Someone buying your house  may, subject to conditions,  cannot be allowed to assume the remainder of the loan on the original terms.
- Prepayment**        If you pay off your loan early, you  may,  will not have to pay a penalty.  
If you pay off your loan early, you  may,  will not be entitled to a refund of part of the finance charge.\*
- Demand Feature**       If checked, your loan includes a demand feature.
- Hazard Insurance**      Hazard Insurance is required and may be obtained through any company of your choice that is acceptable to the Lender.

You should refer to your Note, Mortgage and other documents for additional information about non-payment, default, and required repayment in full before the scheduled date, prepayment rebates, and penalties.

***\*If you pay off your loan early, you will not receive a refund of part of the finance charge that you have already paid.***

**I (We) acknowledge receipt of this Disclosure Statement.**      Date: \_\_\_\_\_

\_\_\_\_\_

Date: **OCTOBER 19, 2006**

Borrower Name: **JOHN DOE**

Property Address: **1234 MAIN STREET, SCOTTSDALE, ARIZONA 85254**

## **ADJUSTABLE RATE MORTGAGE LOAN PROGRAM DISCLOSURE 2 YEAR LIBOR ARM**

This disclosure describes the features of an Adjustable Rate Mortgage (ARM) program you are considering, which is called the 2 YEAR LIBOR ARM. The interest rate and payment of this loan may each change during the term of this loan. Information on other ARM programs available from the lender will be provided upon request.

### ***HOW YOUR INTEREST RATE AND PAYMENT ARE DETERMINED:***

- Beginning on the first Interest Rate Change Date, your interest rate will be based on an index rate plus a margin. Please ask us for our current interest rate and margin.
- Your initial interest rate will not be equal to an index rate plus a margin. If the initial interest rate is below the then current index plus margin ("the fully indexed rate"), then the initial interest rate will be a "discounted" interest rate. Please ask us about the amount of the current discount.
- The index rate is the average of interbank offered rates for six-month U.S. dollar-denominated deposits in the London market ("LIBOR"), as published in The Wall Street Journal. Index rate values are shown below for the first business day of each month and year shown. The example shows how your payment would have changed based on actual changes in the index from 1992 to the present. If this index is no longer available at any Interest Rate Change Date, the lender will choose a new index that is based on comparable information and will give you notice of this change.
- When your interest rate changes, your new interest rate will equal the index rate, which is the most recently available index rate as of the first business day of the month immediately preceding the Interest Rate Change Date, plus the margin rounded to the nearest one-eighth percent (.125%).
- When your payment changes, your new payment will be based on the interest rate, loan balance, and remaining loan term. The new payment will be an amount sufficient to repay the loan balance at the new interest rate in substantially equal payments over the remaining loan term. Therefore, **NO NEGATIVE AMORTIZATION WILL EVER OCCUR** under this loan program.

### ***HOW YOUR INTEREST RATE CAN CHANGE***

- Your interest rate can change on your 24th payment date and every 6 months thereafter (the "Interest Rate Change Date") to a rate equal to the index value plus the margin, rounded to the nearest .125%, subject to the following limits:
- Your interest rate cannot increase by more than three percentage points (3.00%) at the first Interest Rate Change Date and cannot increase or decrease by more than one percentage point (1.00%) at each Interest Rate Change Date thereafter (the "Periodic Rate Cap").
- Your interest rate over the life of the loan cannot increase by more than six percentage points (6.00%) above the initial interest rate (the "Lifetime Rate Cap").
- Your interest rate will never be less than a minimum, or floor, rate equal to the initial interest rate (the "Lifetime Floor Rate").

### ***HOW YOUR PAYMENT CAN CHANGE***

Your payment may change on the first payment date after the first Interest Rate Change Date and every 6 months thereafter. For example, on a \$10,000, 360-month loan with an initial interest rate of 9.000%, (i.e., the index plus the margin shown for 2006 in the Historical Example on page 2, rounded to the nearest .125% and reduced by the initial discount of 3.0%), the maximum amount that the interest rate could rise under this program is 6.000% above the initial interest rate of 9.000% up to 15.000% and the payment amount could rise from the beginning payment of \$80.46 to a maximum of \$124.89 (at payment 43). You will be notified in writing 30 days before a payment adjustment may be made. This notice will contain information about the index and interest rates, payment amount, and loan balance.



**EXAMPLE OF A 1992 \$10,000 LOAN USING HISTORICAL INDEX VALUES:**

The example below shows how your payments would have changed under the ARM program based on actual changes in the index from 1992 to 2006. This does not necessarily indicate how your index will change in the future. For simplicity, the example is based on these assumptions:

Loan Amount: \$10,000 Interest Adjustment: Every 6 Months (beginning with the 24th payment date)  
 Amortization Period: 360 Months Payment Adjustment: Every 6 Months (beginning with the 25th payment date)  
 Interest Rate Margin: 7.250%\* Initial Interest Rate: 8.500%\*\*

YEAR	INDEX VALUE	MARGIN	INTEREST RATE	MONTHLY PAYMENT	LOAN BALANCE
January 1992	4.19%	7.25%	8.500% **	12 @ \$76.89	\$9,924.42
January 1993	3.69%	7.25%	8.500%	12 @ \$76.89	\$9,842.16
January 1994	3.56%	7.25%	10.750%	12 @ \$92.81	\$9,783.65
January 1995	7.00%	7.25%	12.750% ***	12 @ \$107.45	\$9,739.12
January 1996	5.47%	7.25%	12.750%	12 @ \$107.45	\$9,688.57
January 1997	5.63%	7.25%	12.875%	12 @ \$108.36	\$9,632.42
January 1998	5.56%	7.25%	12.750%	12 @ \$107.47	\$9,567.18
January 1999	.5.07%	7.25%	12.375%	12 @ \$104.84	\$9,488.69
January 2000	6.23%	7.25%	13.500%	12 @ \$112.62	\$9,413.69
January 2001	5.36%	7.25%	12.625%	12 @ \$106.67	\$9,316.64
January 2002	1.99%	7.25%	10.625% ***	12 @ \$93.80	\$9,174.13
January 2003	1.35%	7.25%	8.625%	12 @ \$ 81.95	\$8,974.22
January 2004	1.21%	7.25%	8.500%	12 @ \$ 81.26	\$8,753.44
January 2005	2.96%	7.25%	10.250%	12 @ \$ 90.78	\$8,552.02
January 2006	4.81%	7.25%	12.000%	12 @ \$100.38	\$8,363.56

\* This is a margin we have used recently. Your margin may be different.  
 \*\* This interest rate reflects an initial discount of 3.0% and is rounded to the nearest one-eighth percent (.125%). Your initial interest rate may reflect a different discount from the fully-indexed rate.  
 \*\*\* This interest rate reflects a one (1) percentage point periodic interest rate cap.

To see what your payments (excluding impounds or escrow payments for taxes, insurance and other purposes relating to the security property) would have been during a period reflected in the chart, divide your mortgage amount by \$10,000, then multiply the loan payment reflected in the chart for that period, by that amount. For example, in 2006 the loan payments for a mortgage amount of \$60,000 taken out in 1992 would be:  $\$60,000/\$10,000 = 6 \times \$100.38 = \$602.28$ .

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# **Round 7: Baltimore, MD August 20-21, 2008**

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- **Current TILA Statement**
- **Proposed Early Disclosure: “Mortgage Shopping Checklist”**
- **Proposed Early Disclosure: “Mortgage Risk Worksheet”**

**Truth in Lending Disclosure Statement**

<b>Date</b> June 25, 2007	<b>Loan Number</b> 102030405
<b>Lender</b> Gravel Bank	
<b>Borrower(s)</b> Joe Smith & Jane Doe	
<b>Property Address</b> 1234 Main Street Anytown, ST 12345	

**Final Disclosure**

ANNUAL PERCENTAGE RATE	FINANCE CHARGE	Amount Financed	Total of Payments
The cost of your credit as a yearly rate.	The dollar amount the credit will cost you.	The amount of credit provided to you or on your behalf.	The amount you will have paid after you have made all payments as scheduled.
7.41 %	\$ 303,767.47	\$ 195,250.00	\$ 499,017.47

**Payment Schedule: Payments will be due monthly**

Number of Payments	Amount of Payment	Payments Begin
36	\$ 1,151.31	08/01/2007
12	1,397.15	08/01/2010
311	1,412.83	08/01/2011
1	1,414.38	07/01/2037

- Variable Rate**      Your loan  does  does not contain a variable-rate feature. Disclosures about the variable rate feature have been provided to you earlier.
- Security**            You are giving a security interest  in the real property, and fixtures and rents if indicated in the rider mortgage  shares of stock evidencing ownership of the cooperative unit, at the property address referenced above.
- Late Charge**        If a payment is more than 15 days late, you will be charged 5% of the payment.
- Assumption**        Someone buying your house  may, subject to conditions,  cannot be allowed to assume the remainder of the loan on the original terms.
- Prepayment**        If you pay off your loan early, you  may,  will not have to pay a penalty.  
If you pay off your loan early, you  may,  will not be entitled to a refund of part of the finance charge.\*
- Demand Feature**       If checked, your loan includes a demand feature.
- Hazard Insurance**    Hazard Insurance is required and may be obtained through any company of your choice that is acceptable to the Lender.

You should refer to your Note, Mortgage and other documents for additional information about non-payment, default, and required repayment in full before the scheduled date, prepayment rebates, and penalties.

*\*If you pay off your loan early, you will not receive a refund of part of the finance charge that you have already paid.*

I (We) acknowledge receipt of this Disclosure Statement.      Date: \_\_\_\_\_

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# Mortgage Shopping Checklist

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Small differences in mortgage terms can cost you thousands of dollars over the life of your loan. So **take the time to shop wisely**. Preparing for the mortgage shopping process can save you money and stress.

## Before applying for a mortgage loan you should:

- Get your free credit report**, and check it for errors. If you find errors on your credit report, request that they be corrected immediately because these mistakes can cause you to pay more for your loan and can take up to several weeks to fix. To get your free credit report, go to [www.annualcreditreport.com](http://www.annualcreditreport.com), or call 1-877-322-8228.
- Decide how much of your savings you can afford to put into your home**. Putting more money into a down payment may give you more loan options and get you a better interest rate. However, be sure to leave yourself with enough savings to cover unexpected expenses at closing, or in case your home needs repairs.
- Read *Shop Wisely: Understanding Your Mortgage Choices***. This short booklet from the Federal Reserve Board provides an overview of **what you need to know** before talking to lenders and brokers, including definitions of mortgage terms and sales tactics to watch out for. The booklet is available online at [www.federalreserveconsumerhelp.gov/shopwisely](http://www.federalreserveconsumerhelp.gov/shopwisely).
- Complete the Federal Reserve Board's "Mortgage Risk Worksheet."** Loans have a wide variety of features, and some features are more risky or costly than others. Make sure that you understand the risks and costs of different loan features before talking to lenders and brokers, so that you don't end up paying more than you have to for your loan. You can download the Mortgage Risk Worksheet from [www.federalreserveconsumerhelp.gov/loanrisk](http://www.federalreserveconsumerhelp.gov/loanrisk).
- Compare quotes from at least two brokers or lenders**. When you have what you believe is a reasonable quote, **get a second opinion**. Remember that a broker or lender is a salesperson with no obligation to get you the best loan or interest rate. Also, the more lenders and brokers you talk to the more choices you will have. There are hundreds of mortgage products on the market, and no one broker or lender offers all of them.
- Seek help if you need it before you get stuck with a loan you can't afford**. Do not let anyone talk you into a loan with terms you do not understand or payments you cannot afford. HUD-approved counseling agencies can help you evaluate loan offers and tell you about special programs you might qualify for. For a list of HUD-approved counseling agencies, see [www.hud.gov/homebuyers/counseling](http://www.hud.gov/homebuyers/counseling).

In addition to using the websites above, you can also get print copies of the booklets and worksheet referenced above by calling 1-888-MY-MONEY and requesting the "Mortgage Shopping Package."



# Mortgage Risk Worksheet

Some mortgages have features which make them more risky or costly, and these features can be combined in many ways. This worksheet provides an overview of some common features you should know about. For more information on these terms, see the booklet *Shop Wisely: Understanding Your Mortgage Choices*, or visit [www.federalreserveconsumerhelp.gov/shopwisely/](http://www.federalreserveconsumerhelp.gov/shopwisely/).

How to use this worksheet:

1. **Fill it in.** Read through the explanations of the particular terms, as well as the descriptions of the potential benefits and risks of each term. If you think you could be comfortable taking that risk, check the box in the right-hand column.
2. **Shop it around.** Show a copy of this worksheet to each mortgage broker or loan officer you speak with about a loan. Discuss with them what types of products you want—and what types you want to avoid.
3. **Check this form against any offer(s) you receive** to make sure you are getting what you wanted.

Mortgage Term	Explanation	Are you comfortable with the risk?
<b>Adjustable Rate Mortgage (ARM)</b>	<p><b>What it is:</b> These loans have payments that can go up or down because the interest rate changes. Some have rates that can change just a few months after you take out the loan.</p> <p><b>Benefits:</b> You may get a lower interest rate and lower monthly payments at first. If interest rates go down, your monthly payment may go down.</p> <p><b>Risks or Costs:</b> If interest rates go up, your payment could go up significantly.</p>	<input type="checkbox"/> <b>Yes,</b> I would consider a mortgage with an adjustable interest rate.
<b>Balloon Payment</b>	<p><b>What it is:</b> These loans allow you to make small payments for a while, with a large payment due at the end of the loan.</p> <p><b>Benefits:</b> You may get lower monthly payments initially.</p> <p><b>Risks or Costs:</b> At the end of the loan, even after years of making payments, you will owe a large sum of money.</p>	<input type="checkbox"/> <b>Yes,</b> I would consider a mortgage with a balloon payment.
<b>Interest Only Loan/Negative Amortization Loan</b>	<p><b>What it is:</b> An interest only loan allows you to make smaller monthly payments initially, because you are paying only the interest owed every month. A negative amortization loan also allows you to make smaller payments that do not pay down your loan balance, but unlike an interest only loan, your payment does not cover all the interest you owe.</p> <p><b>Benefits:</b> You may get lower monthly payments initially.</p> <p><b>Risks or Costs:</b> With both interest only and negative amortization loans, your low initial payments only cover some or all of the interest on the mortgage—they do not pay off any of the principal. In the case of negative amortization loans, the amount you owe actually grows over time. With both loan types, you will eventually have to pay off the loan principal, and then your payments will go up—often by a lot.</p>	<input type="checkbox"/> <b>Yes,</b> I would consider an interest only loan. <input type="checkbox"/> <b>Yes,</b> I would consider a negative amortization loan.



# Mortgage Risk Worksheet

Mortgage Term	Explanation	Are you comfortable with the risk?
<b>Prepayment Penalty</b>	<p><b>What it is:</b> Loans with prepayment penalties require you to pay the lender an extra fee if you sell the home, refinance the loan, or pay some or all of the principal off earlier than a specified time.</p> <p><b>Benefits:</b> You may get a lower interest rate.</p> <p><b>Risks or Costs:</b> It could cost you several thousand dollars to refinance your loan or sell your house, if you do so before the prepayment penalty period ends.</p>	<input type="checkbox"/> <b>Yes</b> , I would consider a mortgage with a prepayment penalty.
<b>“No Doc” (No Documentation) and “Low Doc” (Low Documentation) Loans</b>	<p><b>What it is:</b> These loans require you to provide less proof of your employment, income, and/or assets to get a loan.</p> <p><b>Benefits:</b> The loan process may go more quickly, especially for people who have difficulty documenting their income or assets.</p> <p><b>Risks or Costs:</b> A No-Doc or Low-Doc loan usually involves paying a higher interest rate or higher fees. Note: It is illegal to provide false information on a loan application.</p>	<input type="checkbox"/> <b>Yes</b> , I would consider a “No Doc” or “Low Doc” loan.
<b>Direct Payment of Property Taxes and Homeowner’s Insurance</b>	<p><b>What it is:</b> Many mortgages include property taxes and homeowner’s insurance in the regular monthly payments. (This mortgage feature is sometimes called an “escrow account” or an “impound account”). If your mortgage payment does not include taxes and insurance, you must remember to save and pay these expenses yourself.</p> <p><b>Benefits:</b> Loans with no escrow or impound account have lower monthly payments only because they do not include the insurance and tax payments you will owe. Homeowners who save up for their property tax and insurance payments may earn interest on their savings.</p> <p><b>Risks or Costs:</b> Taxes and insurance can cost hundreds of dollars per month. Homeowners without escrow/impound accounts who do not save money for taxes and insurance may not be prepared for these large expenses.</p>	<input type="checkbox"/> <b>Yes</b> , I would consider a mortgage that required me to save for property taxes and homeowner’s insurance and pay them myself.

Borrower’s Signature

Date

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# **Round 8: Atlanta, GA November 5-6, 2008**

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- **Revised TILA Statement Version A1**
- **Revised TILA Statement Version A2**
- **Revised TILA Statement Version B1**
- **Revised TILA Statement Version B2**
- **Proposed Payment Scenario Graph and Table**
- **Proposed Early Disclosure: “Six Key Questions to Ask About Your Mortgage”**

# STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: September 23, 2008

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

## YOUR RIGHTS AS A BORROWER

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

## LOAN SUMMARY

- This is a **30 Year** loan for **\$200,000.00**.
- **The interest rate is adjustable**; it will change in 2011 and can adjust either up or down every year after.
- The amount financed (the loan amount less prepaid finance charges) is **\$195,250.00**.

Initial & Maximum Interest Rate	Monthly Principal + Interest	Monthly Estimated Taxes + Insurance (Escrow)	TOTAL Estimated Monthly Payment
<b>5.625%</b> initial rate until first adjustment (2009 – 2011)	\$ 1,151.31 +	\$ 241.00 =	<b>\$ 1,392.31</b>
<b>7.625%</b> max. rate at first adjustment (Nov. 2011)	\$ 1,397.15 +	\$ 241.00 =	<b>\$ 1,638.15</b>
<b>11.625%</b> maximum rate ever (can be reached as early as 2013)	\$ 1,924.97 +	\$ 241.00 =	<b>\$ 2,165.97</b>

## RISK FACTORS

- ⚠ **This loan has an adjustable interest rate**, which means that your required monthly payment could go up after the first three years, and could also increase every year after. See the Payment Schedule on page 2 for more details.
- ⚠ **This loan has a prepayment penalty**, which means you could be charged a penalty of up to **\$4,000** if you pay off your loan, refinance, or sell this property within three years.

## THE COST OF THIS ADJUSTABLE RATE LOAN OVER TIME

If market rates did not change, and you kept this loan for:

- **3 years**, the *finance charge* would be **\$37,833.70** and the *APR* would be: **6.46%**
- **5 years**, the *finance charge* would be **\$66,965.51** and the *APR* would be: **6.89%**
- **30 years**, the *finance charge* would be **\$303,767.47** and the *APR* would be: **7.41%**

“*The Finance Charge*” is the interest plus other fees you’ll pay over the life of the loan.

“*APR*” is the annual percentage rate, which is interest plus other fees such as points and closing costs as a percentage of the loan amount, factored over the term of the loan. Since the APR includes much of the cost associated with the loan, it is a good tool to use to compare loans to each other. A lower APR generally means a less expensive loan.

## SETTLEMENT COSTS

Total Estimated Settlement Charges: \$5,400.00 (See your Good Faith Estimate for details)  
Cash to bring to closing: \$3,940.00

The Federal Truth in Lending Act requires lenders to mail or deliver this form to borrowers within three days of receiving the application and at least seven days prior to closing (signing for) the loan.



# STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: September 23, 2008

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

## YOUR RIGHTS AS A BORROWER

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

## LOAN SUMMARY

- This is a **30 Year** loan for **\$200,000.00**.
- **The interest rate is adjustable**; it will change in 2011 and can adjust either up or down every year after.
- The amount financed (the loan amount less prepaid finance charges) is **\$193,250.00**.

Initial & Maximum Interest Rate	Monthly Principal + Interest	Monthly Estimated Taxes + Insurance (Escrow)	TOTAL Estimated Monthly Payment
<b>5.375%</b> initial rate until first adjustment (2009 – 2011)	\$ 1,119.94 +	\$ 256.00 =	<b>\$ 1,375.94</b>
<b>7.375%</b> max. rate at first adjustment (Nov. 2011)	\$ 1,362.67 +	\$ 256.00 =	<b>\$ 1,618.67</b>
<b>11.375%</b> maximum rate ever (can be reached as early as 2013)	\$ 1,885.28 +	\$ 256.00 =	<b>\$ 2,141.28</b>

## RISK FACTORS

- ⚠ **This loan has an adjustable interest rate**, which means that your required monthly payment could go up after the first three years, and could also increase every year after. See the Payment Schedule on page 2 for more details.
- ⚠ **This loan has a prepayment penalty**, which means you could be charged a penalty of up to **\$4,000** if you pay off your loan, refinance, or sell this property within three years.

## THE COST OF THIS ADJUSTABLE RATE LOAN OVER TIME

If market rates did not change, and you kept this loan for:

- **3 years**, the *finance charge* would be **\$38,334.27** and the *APR* would be: **6.59%**
- **5 years**, the *finance charge* would be **\$66,450.27** and the *APR* would be: **6.89%**
- **30 years**, the *finance charge* would be **\$293,408.32** and the *APR* would be: **7.25%**

“*The Finance Charge*” is the interest plus other fees you’ll pay over the life of the loan.

“*APR*” is the annual percentage rate, which is interest plus other fees such as points and closing costs as a percentage of the loan amount, factored over the term of the loan. Since the APR includes much of the cost associated with the loan, it is a good tool to use to compare loans to each other. A lower APR generally means a less expensive loan.

## SETTLEMENT COSTS

Total Estimated Settlement Charges: \$7,400.00 (See your Good Faith Estimate for details)  
Cash to bring to closing: \$4,090.00

The Federal Truth in Lending Act requires lenders to mail or deliver this form to borrowers within three days of receiving the application and at least seven days prior to closing (signing for) the loan.

## STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: September 23, 2008

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

### LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b>	Total Estimated Settlement Charges:	<b>\$5,400.00</b>
Loan Term:	<b>30 years</b>	Cash to Bring to Closing:	<b>\$3,940.00</b>
Adjustable or Fixed Rate?	<b>Adjustable</b> <i>(beginning in 2011)</i>	Amount Financed <i>(loan amount less prepaid finance charges):</i>	<b>\$195,250.00</b>

	INTRODUCTORY Rate & Est. Payment <small>(for first 3 years)</small>	MAXIMUM at FIRST ADJUSTMENT <small>(Nov. 2011)</small>	MAXIMUM EVER <small>(as early as 2013)</small>
Interest Rate	<b>5.625%</b>	<b>7.625%</b>	<b>11.625%</b>
Principal + Interest	\$ 1,151.31	\$ 1,397.15	\$ 1,924.97
Estimated Taxes + Insurance*	+ \$ 241.00	+ \$ 241.00	+ \$ 241.00
<b>Total Est. Monthly Payment</b>	<b>\$1,392.31</b>	<b>\$ 1,638.15</b>	<b>\$ 2,165.97</b>

\* Taxes and Insurance could be significantly higher than the estimates shown here.

### RISK FACTORS – key questions to ask about your loan

<i>Can my interest rate increase?</i>	<b>YES.</b> Your interest rate can go up beginning in 2011 and can increase every year after, up to a maximum of <b>11.625%</b> as early as 2013.
<i>Can my monthly payment increase?</i>	<b>YES.</b> Your monthly payment can go up beginning in 2011 and can increase every year after, to an estimated maximum of <b>\$2,165.97</b> as early as 2013.
<i>Will my monthly payments cover only interest and no principal?</i>	No.
<i>Can my loan balance increase?</i>	No.
<i>Could I owe a prepayment penalty?</i>	<b>YES.</b> If you pay off your loan, refinance, or sell this property within <b>3 years</b> you could pay a penalty of up to <b>\$4,000.00</b> .
<i>Will I owe a balloon payment?</i>	No.

### THE COST OF THIS ADJUSTABLE RATE LOAN OVER TIME – compare this APR to the APR of other loan offers

If market rates did not change, and you kept this loan for:	The <b>Finance Charge</b> would be:	The <b>APR</b> would be:
3 years	\$ 37,833.70	6.46%
5 years	\$ 66,965.51	6.89%
30 years	\$ 303,767.47	7.41%

The **Finance Charge** is the interest plus other fees you'll pay over the life of the loan.

The **APR** is the annual percentage rate, which is interest plus other fees such as points and closing costs as a percentage of the loan amount, factored over the term of the loan. Since the APR includes much of the cost associated with the loan, it is a good tool to use to compare loans to each other. A lower APR generally means a less expensive loan.

The Federal Truth in Lending Act requires lenders to mail or deliver this form to borrowers within three days of receiving the application and at least seven days prior to closing (signing for) the loan.

## STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: September 23, 2008

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

### LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b>	Total Estimated Settlement Charges:	<b>\$7,400.00</b>
Loan Term:	<b>30 years</b>	Cash to Bring to Closing:	<b>\$4,090.00</b>
Adjustable or Fixed Rate?	<b>Adjustable</b> <i>(beginning in 2011)</i>	Amount Financed <i>(loan amount less prepaid finance charges):</i>	<b>\$193,250.00</b>

	INTRODUCTORY Rate & Est. Payment <small>(for first 3 years)</small>	MAXIMUM at FIRST ADJUSTMENT <small>(Nov. 2011)</small>	MAXIMUM EVER <small>(as early as 2013)</small>
Interest Rate	<b>5.375%</b>	<b>7.375%</b>	<b>11.375%</b>
Principal + Interest	\$ 1,119.94	\$ 1,362.67	\$ 1,885.28
Estimated Taxes + Insurance*	+ \$ 256.00	+ \$ 256.00	+ \$ 256.00
<b>Total Est. Monthly Payment</b>	<b>\$1,375.94</b>	<b>\$ 1,618.67</b>	<b>\$ 2,141.28</b>

\* Taxes and Insurance could be significantly higher than the estimates shown here.

### RISK FACTORS – key questions to ask about your loan

<i>Can my interest rate increase?</i>	<b>YES.</b> Your interest rate can go up beginning in 2011 and can increase every year after, up to a maximum of <b>11.375%</b> as early as 2013.
<i>Can my monthly payment increase?</i>	<b>YES.</b> Your monthly payment can go up beginning in 2011 and can increase every year after, to an estimated maximum of <b>\$2,141.28</b> as early as 2013.
<i>Will my monthly payments cover only interest and no principal?</i>	No.
<i>Can my loan balance increase?</i>	No.
<i>Could I owe a prepayment penalty?</i>	<b>YES.</b> If you pay off your loan, refinance, or sell this property within <b>3 years</b> you could pay a penalty of up to <b>\$4,000.00</b> .
<i>Will I owe a balloon payment?</i>	No.

### THE COST OF THIS ADJUSTABLE RATE LOAN OVER TIME – compare this APR to the APR of other loan offers

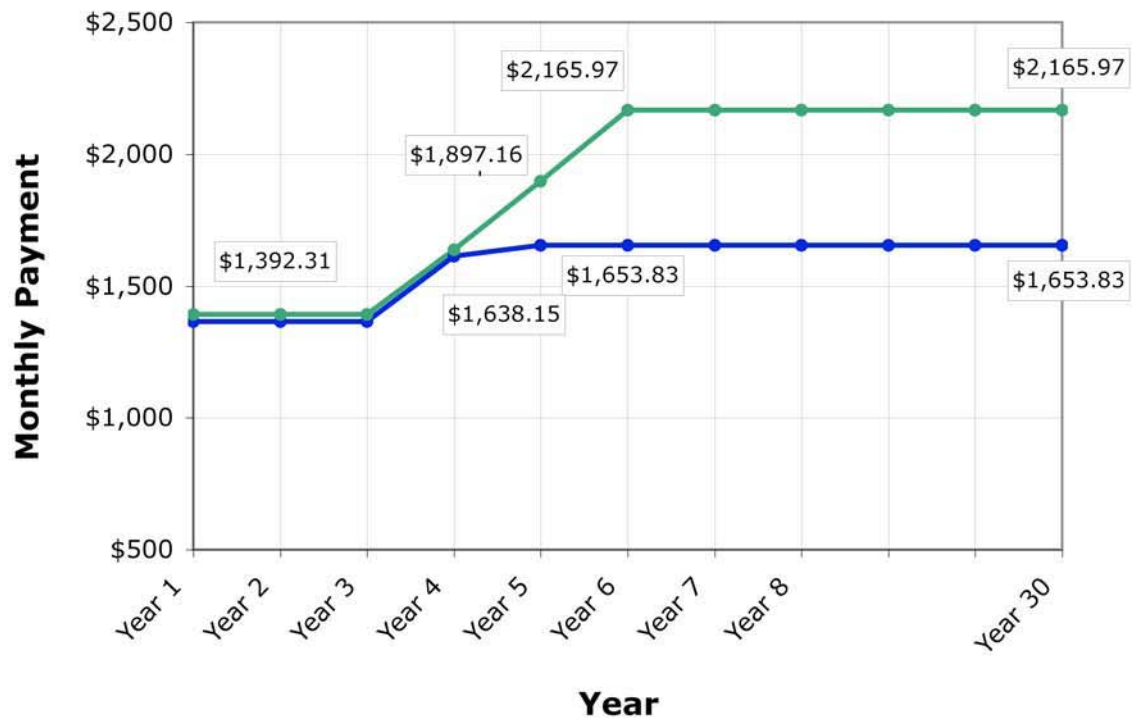
If market rates did not change, and you kept this loan for:	The <b>Finance Charge</b> would be:	The <b>APR</b> would be:
3 years	\$ 38,334.27	6.59%
5 years	\$ 66,450.27	6.89%
30 years	\$ 293,408.32	7.25%

The **Finance Charge** is the interest plus other fees you'll pay over the life of the loan.

The **APR** is the annual percentage rate, which is interest plus other fees such as points and closing costs as a percentage of the loan amount, factored over the term of the loan. Since the APR includes much of the cost associated with the loan, it is a good tool to use to compare loans to each other. A lower APR generally means a less expensive loan.

The Federal Truth in Lending Act requires lenders to mail or deliver this form to borrowers within three days of receiving the application and at least seven days prior to closing (signing for) the loan.

## How Your Monthly Payment Can Change



- SCENARIO A: If Market Rates Stayed The Same
- SCENARIO B: Maximum Possible Rate Increases

						SCENARIO A: If Market Rates Stayed The Same as Today		SCENARIO B: Maximum Possible Rate Increases	
Year of Loan	Period Beginning	# of Payments	Taxes + Insurance (Escrow)	Interest Rate	Monthly Payment*	Interest Rate	Monthly Payment*		
1 to 3	11/1/2008	36	\$241	5.625%	\$1,392.31	5.625%	\$1,392.31		
4	11/1/2011	12	\$241	7.625%	\$1,638.15	7.625%	\$1,638.15		
5	11/1/2012	12	\$241	7.750%	\$1,653.83	9.625%	\$1,897.16		
6 to 30	11/1/2013	300	\$241	7.750%	\$1,653.83	11.625%	\$2,165.97		

\* The Monthly Payment Amounts in this chart include an estimate for taxes and insurance based on today's costs. In actuality, the cost of taxes and insurance will likely increase over time.



# 6 Key Questions to Ask About Your Mortgage

**When you are shopping for a loan, ask the lender the six questions below.** Some loans have risky features that could make it difficult for you to repay your mortgage loan. Understand the loan terms and the risks you could face. If you are not comfortable with certain risks, ask about another loan product. For more information about risky loan features, read *Shop Wisely: Understanding Your Mortgage Choices* available at [www.federalreserveconsumerhelp.gov/shopwisely](http://www.federalreserveconsumerhelp.gov/shopwisely).

1

## Can my interest rate increase?

With an adjustable rate mortgage (ARM), your interest rate can go up or down after a short period. This can result in increased monthly payments.

2

## Can my monthly payment increase?

With some loans your monthly payment can increase after a period of time, often by hundreds of dollars, because you have a lower introductory rate, an adjustable rate, or a monthly payment that does not cover all that you owe.

3

## Can my loan balance increase?

Some loans give you the choice to pay **less than** the interest owed each month. The unpaid interest is added to your loan balance and increases the total loan amount you owe. This could cause you to lose equity in your home.

4

## Will my monthly payments reduce my loan balance?

Some loans allow you to pay **only** the interest on your loan each month. You pay nothing to reduce the amount you borrowed, and so you may not build any equity in your home.

5

## Can I refinance or pay off my loan early without a fee?

Some loans will charge you a large fee, even thousands of dollars, if you pay off your loan, refinance it, or sell your home within the first few years of the loan.

6

## Will I owe a balloon payment?

Some loans require a very large payment at the end of the loan (e.g., tens of thousands of dollars). If interest rates rise, if the value of your property drops, or if lending requirements change you may not be able to refinance before having to make this large payment.

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# **Round 9: Bethesda, MD January 27 & 29, 2009**

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- **Revised TILA Statement Version C1**
- **Revised TILA Statement Version C2**
- **Revised TILA Statement Version C3**
- **Revised TILA Statement Version D1**
- **Revised TILA Statement Version D2**
- **Revised TILA Statement Version D3**
- **Proposed Language for Required Disclosures**

## STATEMENT OF LOAN TERMS

DATE: January 23, 2009  
 LENDER: ABC Bank  
 BORROWER: Joe Smith & Jane Doe  
 PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied, and to compare this loan to other offers. For information about your rights, see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

**Loan Amount:** \$200,000.00  
**Down Payment:** \$57,000.00  
**Loan Term:** 30 years  
**Loan Type:** 3/1 Adjustable Rate Mortgage (ARM); your interest rate adjusts in 3 years and once a year after that  
**Amt. Financed:** \$195,250.00 (loan amount minus prepaid closing costs, such as points)

#### ESTIMATED CLOSING COSTS

**Paid Before Closing:** \$ 350.00  
**Included in Loan Amount:** \$2,000.00  
**Due at Closing:** + \$4,292.00  
**TOTAL** \$6,642.00

### This Loan's Price Tag

## 7.41 % APR

*The interest rate when some closing costs are factored in.*

## \$ 303,767.47

**Finance Charge**

*Total interest and fees over the life of the loan.*

### PAYMENT SUMMARY

	INTRODUCTORY Rate & Est. Payment (for first 3 years)	MAXIMUM at FIRST ADJUSTMENT (Jan. 2012)	MAXIMUM EVER (as early as 2014)
Interest Rate	<b>5.625%</b>	<b>7.625%</b>	<b>11.625%</b>
Principal + Interest	\$1,151.31	\$ 1,397.15	\$ 1,924.97
Taxes + Insurance (Escrow)	+ \$ 241.00	+ \$ 241.00	+ \$ 241.00
<b>Total Est. Monthly Payment</b>	<b>\$1,392.31</b>	<b>\$ 1,638.15</b>	<b>\$ 2,165.97</b>

**Rate Change** You have a discounted interest rate of 5.625% for the first three years. After that, your rate will be based on the one year LIBOR index (the market rate) + 2.125%. This interest rate can increase no more than 2.00% yearly, and no more than 6.00% total for the life of the loan.

**Escrow** An escrow account **is required** for this loan, and will be used to pay your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates**; they can change at any time.

### KEY QUESTIONS ABOUT THIS LOAN

Can my interest rate increase?	<b>YES.</b>
Can my monthly payment increase?	<b>YES.</b>
Can my balance stay the same even after I've made payments?	No.
Can my balance increase even after I've made payments?	No.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell this property within <b>3 years</b> you could pay a penalty of up to <b>\$4,000.00</b> .
Will I owe a balloon payment?	No.
Will I owe a fee if I make a late payment?	<b>YES.</b> If you make a payment more than 15 days late, you may be charged a penalty of <b>18%</b> of your monthly payment.

### OPTIONAL FEATURES

The following optional features increase the cost of this loan:

- Credit Life Insurance, which is adding \$50.00 to your monthly payment for 15 years.
- Reduced Documentation (No Doc or Low Doc), which makes you ineligible for our lowest interest rate.
- Owner's Title Insurance, which has added \$325 to the closing costs you will pay separately at closing.

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

\_\_\_\_\_  
 Borrower Signature

\_\_\_\_\_  
 Date



## STATEMENT OF LOAN TERMS

DATE: January 23, 2009  
LENDER: ABC Bank  
BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.**  
Use this statement to confirm that these are the loan terms for which you applied, and to compare this loan to other offers. For information about your rights, see:  
[www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

**Loan Amount:** \$303,234  
**Down Payment:** --  
**Loan Term:** 15 years  
**Loan Type:** Fixed Rate Conventional  
**Amt. Financed:** \$287,764.00 (loan amount minus prepaid closing costs, such as points)

#### ESTIMATED CLOSING COSTS

<b>Paid Before Closing:</b>	\$0
<b>Included in Loan Amount:</b>	\$15,470.00
<b>Due at Closing:</b>	\$0
<b>TOTAL</b>	<b>\$15,470.00</b>

### This Loan's Price Tag

**7.08% APR**

*The interest rate when some closing costs are factored in.*

**\$ 180,235.26**

**Finance Charge**

*Total interest and fees over the life of the loan.*

### PAYMENT SUMMARY

	Estimated Payment
Interest Rate	6.250%
Principal + Interest	\$2,600.00
Taxes + Insurance (Escrow)	+ \$ 459.00
<b>Total Est. Monthly Payment</b>	<b>\$3,059.00</b>

**An escrow account is required for this loan**, and will be used to pay your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates**; they can change at any time.

### KEY QUESTIONS ABOUT THIS LOAN

Can my interest rate increase?	No.
Can my monthly payment increase?	<b>YES</b> , but only to cover increases in your property taxes or insurance.
Can my balance stay the same even after I've made payments?	No.
Can my balance increase even after I've made payments?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Will I owe a fee if I make a late payment?	<b>YES</b> . If you make a payment more than 15 days late, you may be charged a penalty of <b>18%</b> of your monthly payment.

### OPTIONAL FEATURES

The following optional features increase the cost of this loan:

- Credit Life Insurance, which is adding \$50.00 to your monthly payment for 15 years.
- Owner's Title Insurance, which has added \$325 to the closing costs you will pay separately at closing.

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

\_\_\_\_\_  
Borrower Signature

\_\_\_\_\_  
Date

## STATEMENT OF LOAN TERMS

DATE: January 23, 2009  
LENDER: ABC Bank  
BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.**  
Use this statement to confirm that these are the loan terms for which you applied, and to compare this loan to other offers. For information about your rights, see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

**Loan Amount:** \$300,000.00  
**Down Payment:** --  
**Loan Term:** 15 years  
**Loan Type:** Fixed Rate Conventional  
**Amt. Financed:** \$300,000.00 (loan amount minus prepaid closing costs, such as points)

#### ESTIMATED CLOSING COSTS

<b>Paid Before Closing:</b>	\$0
<b>Included in Loan Amount:</b>	\$0
<b>Due at Closing:</b>	+ \$0
<b>TOTAL</b>	\$0

### This Loan's Price Tag

**6.50% APR**

*The interest rate when some closing costs are factored in.*

**\$ 170,398.28**

**Finance Charge**

*Total interest and fees over the life of the loan.*

### PAYMENT SUMMARY

	Estimated Payment
Interest Rate	6.500%
Principal + Interest	\$2,613.32
Taxes + Insurance (Escrow)	+ \$ 458.00
<b>Total Est. Monthly Payment</b>	<b>\$3,071.32</b>

**An escrow account is required for this loan**, and will be used to pay your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates**; they can change at any time.

### KEY QUESTIONS ABOUT THIS LOAN

Can my interest rate increase?	No.
Can my monthly payment increase?	<b>YES</b> , but only to cover increases in your property taxes or insurance.
Can my balance stay the same even after I've made payments?	No.
Can my balance increase even after I've made payments?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Will I owe a fee if I make a late payment?	<b>YES</b> . If you make a payment more than 15 days late, you may be charged a penalty of <b>15%</b> of your monthly payment.

### OPTIONAL FEATURES

The following optional features increase the cost of this loan:

- Credit Life Insurance, which is adding \$50.00 to your monthly payment for 15 years.
- Owner's Title Insurance, which has added \$350 to the closing costs you will pay separately at closing.

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

\_\_\_\_\_  
Borrower Signature

\_\_\_\_\_  
Date

## STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: January 23, 2009

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

### LOAN SUMMARY

**Loan Amount:** \$210,000.00  
**Down Payment:** \$70,000.00  
**Loan Term:** 30 years  
**Loan Type:** 5/1 Adjustable Rate Mortgage (ARM); your interest rate adjusts in 5 years and once a year after that  
**Amt. Financed:** \$201,560.00 (loan amount minus prepaid closing costs, such as points)

#### ESTIMATED CLOSING COSTS

**Paid Before Closing:** \$ 445.00  
**Included in Loan Amount:** \$0  
**Due at Closing:** + \$9,720.00  
**TOTAL** \$10,165.00

<b>TOTAL COST</b>	<b>5.875%</b>	+	<b>\$10,165.00</b>	=	<b>Finance Charges of</b>	<b>An APR of</b>
	Introductory Interest Rate		Estimated Closing Costs		<b>\$ 291,352.68</b>	
					<i>Total interest and fees over the life of the loan.</i>	<i>&amp; The interest rate when some closing costs are factored in.</i>

### PAYMENT SUMMARY

	INTRODUCTORY Rate & Est. Payment (for first 5 years)	MAXIMUM EVER (as early as 2017)
Interest Rate	<b>5.875%</b>	<b>11.875%</b>
Principal + Interest	\$1,242.23	\$ 2,017.68
Taxes + Insurance (Escrow)	+ \$ 336.00	+ \$ 336.00
<b>Total Est. Monthly Payment</b>	<b>\$1,578.23</b>	<b>\$ 2,353.68</b>

**An escrow account is required for this loan**, and will be used to pay your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates**; they can change at any time.

### KEY QUESTIONS ABOUT THIS LOAN

Can my interest rate increase?	<b>YES.</b>
Can my monthly payment increase?	<b>YES.</b>
Can my balance stay the same even after I've made payments?	No.
Can my balance increase even after I've made payments?	No.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell this property within <b>3 years</b> you could pay a penalty of up to <b>\$4,000.00</b> .
Will I owe a balloon payment?	No.
Will I owe a fee if I make a late payment?	<b>YES.</b> If you make a payment more than 15 days late, you may be charged a penalty of <b>18%</b> of your monthly payment.

**HOW CAN I COMPARE THIS LOAN TO OTHER LOAN OFFERS?**

The APR tells you which loan costs you more, depending on how long you keep the loan. Estimate how long you plan to keep this loan before you pay it off, refinance or sell your property to determine your approximate APR. Use that APR to compare any loan offers you are considering.

<b>If market rates did not change, and you kept this loan for:</b>	<b>The Finance Charge would be:</b>	<b>The APR would be:</b>
3 years	\$ 44,753.95	7.40%
5 years	\$ 68,083.58	6.86%
30 years	\$ 291,352.68	7.02%

**WHAT DETERMINES HOW MY PAYMENT CAN CHANGE?**

**Rate Change** You have a discounted interest rate of 5.875% for the first five years. After that, your rate will be based on the one year LIBOR index (the market rate) + 1.50%. This interest rate can increase no more than 2.00% yearly, and no more than 6.00% total for the life of the loan.

**Escrow** The escrow amounts shown are estimates; they can change at any time based on, for example, property values or insurance premiums.

<b>Payment Change Scenarios</b>			<b>SCENARIO A: If Market Rates Stayed the Same as Today</b>		<b>SCENARIO B: Maximum Possible Rate Increases</b>	
<b>Year of Loan</b>	<b># of Payments</b>	<b>Taxes + Insurance</b>	<b>Interest Rate</b>	<b>Monthly Payment</b>	<b>Interest Rate</b>	<b>Monthly Payment</b>
1 to 5	60	\$336	5.875%	\$1,578.23	5.875%	\$1,578.23
6	12	\$336	7.125%	\$1,730.59	7.875%	\$1,825.77
7	12	\$336	7.125%	\$1,730.59	9.875%	\$2,085.27
8 to 30	276	\$336	7.125%	\$1,730.59	11.875%	\$2,353.68
<b>TOTAL of Payments at Loan End</b> (including interest, principal and all fees)				<b>\$613,873.37</b>	<b>\$791,238.63</b>	

**ARE THERE ANY FEATURES THAT I COULD ELIMINATE TO SAVE MONEY ON THIS LOAN?**

The following optional features increase the cost of this loan:

- Credit Life Insurance, which is adding \$50.00 to your monthly payment for 15 years.
- Reduced Documentation (No Doc or Low Doc), which makes you ineligible for our lowest interest rate.
- Owner’s Title Insurance, which has added \$325 to the closing costs you will pay separately at closing.

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

**Borrower Signature**

**Date**

## STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: January 23, 2009

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

### LOAN SUMMARY

**Loan Amount:** \$303,234.00  
**Down Payment:** --  
**Loan Term:** 15 years  
**Loan Type:** Fixed Rate Conventional  
**Amt. Financed:** \$287,764 (loan amount minus prepaid closing costs, such as points)

#### ESTIMATED CLOSING COSTS

**Paid Before Closing:** \$ 0  
**Included in Loan Amount:** \$15,470.00  
**Due at Closing:** \$ 0  
**TOTAL** \$15,470.00

<b>TOTAL COST</b>	<b>6.250%</b>	+	<b>\$15,470.00</b>	=	<b>Finance Charges of</b>	&	<b>An APR of</b>
	Interest Rate		Estimated Closing Costs		<b>\$ 180,235.26</b>		The interest rate when some closing costs are factored in.
					<i>Total interest and fees over the life of the loan.</i>		<b>7.08%</b>

### PAYMENT SUMMARY

	Estimated Payment
Interest Rate	<b>6.250%</b>
Principal + Interest	\$2,600.00
Taxes + Insurance (Escrow)	+ \$ 459.00
<b>Total Est. Monthly Payment</b>	<b>\$3,059.00</b>

**An escrow account is required for this loan**, and will be used to pay your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates**; they can change at any time.

### KEY QUESTIONS ABOUT THIS LOAN

<i>Can my interest rate increase?</i>	No.
<i>Can my monthly payment increase?</i>	<b>YES</b> , but only to cover increases in your property taxes or insurance.
<i>Can my balance stay the same even after I've made payments?</i>	No.
<i>Can my balance increase even after I've made payments?</i>	No.
<i>Could I owe a prepayment penalty?</i>	No.
<i>Will I owe a balloon payment?</i>	No.
<i>Will I owe a fee if I make a late payment?</i>	<b>YES</b> . If you make a payment more than 15 days late, you may be charged a penalty of <b>18%</b> of your monthly payment.

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**HOW CAN I COMPARE THIS LOAN TO OTHER LOAN OFFERS?**

The APR tells you which loan costs you more, depending on how long you keep the loan. Estimate how long you plan to keep this loan before you pay it off, refinance or sell your property to determine your approximate APR. Use that APR to compare any loan offers you are considering.

<b>If you kept this loan for:</b>	<b>The Finance Charge</b> would be:	<b>The APR</b> would be:
3 years	\$ 68,770.87	8.09%
5 years	\$ 99,799.37	7.62%
30 years	\$ 180,235.26	7.08%

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**ARE THERE ANY FEATURES THAT I COULD ELIMINATE TO SAVE MONEY ON THIS LOAN?**

The following optional features increase the cost of this loan:

- Credit Life Insurance, which is adding \$50.00 to your monthly payment for 15 years.
- Owner's Title Insurance, which has added \$325 to the closing costs you will pay separately at closing.

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

---

**Borrower Signature**

**Date**

## STATEMENT OF LOAN TERMS

LENDER: ABC Bank  
DATE: January 23, 2009

BORROWER: Joe Smith & Jane Doe  
PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. Use this statement to shop and compare these loan terms to other loan offers. For more information about what the terms of this loan mean, and your rights as a borrower, visit [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

### LOAN SUMMARY

<p><b>Loan Amount:</b> \$300,000.00</p> <p><b>Down Payment:</b> \$ --</p> <p><b>Loan Term:</b> 15 years</p> <p><b>Loan Type:</b> Fixed Rate Conventional</p> <p><b>Amt. Financed:</b> \$300,000.00 (loan amount minus prepaid closing costs, such as points)</p>	<p>ESTIMATED CLOSING COSTS</p> <p><b>Paid Before Closing:</b> \$0</p> <p><b>Included in Loan Amount:</b> \$0</p> <p><b>Due at Closing:</b> + \$0</p> <hr/> <p><b>TOTAL</b> \$0</p>
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<b>TOTAL COST</b>	<p><b>6.500%</b></p> <p>Interest Rate</p>	+	<p><b>\$ 0</b></p> <p>Estimated Closing Costs</p>	=	<p>Finance Charges of</p> <p><b>\$ 170,398.28</b></p> <p><i>Total interest and fees over the life of the loan.</i></p>	&	<p>An APR of</p> <p><b>6.50%</b></p> <p><i>The interest rate when some closing costs are factored in.</i></p>
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### PAYMENT SUMMARY

	Estimated Payment
Interest Rate	<b>6.500%</b>
Principal + Interest	\$2,613.32
Taxes + Insurance (Escrow)	+ \$ 458.00
<b>Total Est. Monthly Payment</b>	<b>\$3,071.32</b>

**An escrow account is required for this loan**, and will be used to pay your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates**; they can change at any time.

### KEY QUESTIONS ABOUT THIS LOAN

<i>Can my interest rate increase?</i>	No.
<i>Can my monthly payment increase?</i>	<b>YES</b> , but only to cover increases in your property taxes or insurance.
<i>Can my balance stay the same even after I've made payments?</i>	No.
<i>Can my balance increase even after I've made payments?</i>	No.
<i>Could I owe a prepayment penalty?</i>	No.
<i>Will I owe a balloon payment?</i>	No.
<i>Will I owe a fee if I make a late payment?</i>	<b>YES</b> . If you make a payment more than 15 days late, you may be charged a penalty of <b>15%</b> of your monthly payment.

---

**HOW CAN I COMPARE THIS LOAN TO OTHER LOAN OFFERS?**

The APR tells you which loan costs you more, depending on how long you keep the loan. Estimate how long you plan to keep this loan before you pay it off, refinance or sell your property to determine your approximate APR. Use that APR to compare any loan offers you are considering.

<b>If you kept this loan for:</b>	<b>The Finance Charge</b> would be:	<b>The APR</b> would be:
3 years	\$ 54,910.73	6.50%
5 years	\$ 86,950.70	6.50%
30 years	\$ 170,398.28	6.50%

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**ARE THERE ANY FEATURES THAT I COULD ELIMINATE TO SAVE MONEY ON THIS LOAN?**

The following optional features increase the cost of this loan:

- Credit Life Insurance, which is adding \$50.00 to your monthly payment for 15 years.
- Owner's Title Insurance, which has added \$350 to the closing costs you will pay separately at closing.

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

---

**Borrower Signature**

**Date**



A:

Read your loan contract to learn what happens if you stop making payments, default, pay or refinance the loan early, or if the lender demands early repayment of the entire loan balance.

B:

If you sell your home after you take out this loan, your lender has the option to permit the buyer to take over your mortgage.

C:

You can obtain property insurance from anyone that is also acceptable to your lender.

D:

The lender can require that you pay off the full amount of your loan at any time. All disclosures are based on the assumed maturity of one year.

E:

If pay, refinance, or sell this property early, you are entitled to a refund of some of the interest and fees you have paid on your loan.

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# **Round 10: Dallas, TX February 24-25 2009**

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- **Revised TILA Statement Version E1**
- **Revised TILA Statement Version E2**
- **Revised TILA Statement Version F1**
- **Revised TILA Statement Version F2**
- **Alternate Presentations of APR**
- **Proposed Early Disclosure: “Key Questions to Ask About Your Mortgage”**
- **Proposed Language for Required Disclosures**

## STATEMENT OF LOAN TERMS

DATE: February 23, 2009  
 LENDER: ABC Bank  
 BORROWER: Joe Smith & Jane Doe  
 PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. For information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b> , of which <b>\$2,000.00</b> goes toward your total settlement charges.
Loan Term:	<b>30 years</b>
Loan Type:	<b>3/1 Adjustable Rate Mortgage (ARM)</b>
Total Settlement Charges:	<b>\$6,642.00<sup>1</sup></b> (see your Good Faith Estimate for details)

**TRUE COST FACTOR (TCF)**

# 7.41

When comparing loans of the same type and term, a higher TCF means a more expensive loan.

### PAYMENT SUMMARY

	INTRODUCTORY Rate & Est. Payment (for first 3 years)	MAXIMUM at FIRST ADJUSTMENT (Feb. 2012)	MAXIMUM EVER (as early as 2014)
Interest Rate	<b>5.625%</b>	<b>7.625%</b>	<b>11.625%</b>
Principal + Interest	\$1,151.31	\$ 1,397.15	\$ 1,924.97
Taxes + Insurance (Escrow)	+ \$ 241.00	+ \$ 241.00	+ \$ 241.00
<b>Total Est. Monthly Payment</b>	<b>\$1,392.31</b>	<b>\$ 1,638.15</b>	<b>\$ 2,165.97</b>

**Introductory Rate** You have a discounted introductory rate of 5.625% for the first three years. If the market rate does not change, at the end of this period your interest rate will increase by 2.00%, adding approximately \$250.00 to your monthly payment.

**Rate Changes** After the first three years, your rate adjusts annually based on the one-year LIBOR index (the market rate) + 2.125%. Your interest rate can increase no more than 2.00% in any one year, and no more than 6.00% total for the life of the loan.

**Escrow** An escrow account **is required** for your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates** and can change at any time.

**Total Payments** If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$585,778.09, including escrow. Of this amount, \$303,767.47 would go to interest and fees.

### KEY QUESTIONS ABOUT RISKS

Can my interest rate increase?	<b>YES.</b>
Can my monthly payment increase?	<b>YES.</b>
Can my lender demand full repayment at anytime?	<b>YES.</b> We can demand that you pay off the <b>full</b> amount of your loan at any time, for any reason. We are required to give you at least 30 days notice.
Do I have to share any equity I gain?	<b>YES.</b> We are entitled to 50% of any gain you make when you sell or refinance this property. In exchange, we are giving you a lower interest rate.

The following features are **not** included in this loan: interest-only payments, negative amortization, a balloon payment, and a prepayment penalty.

### OPTIONS WITH ADDITIONAL COSTS

Credit Life Insurance is available for an additional cost of \$50.00 per month for the first 15 years. It is not required for this or any loan. Initial below to add Credit Life Insurance to your loan.

YES, add Credit Life Insurance to my loan. \_\_\_\_\_  
 (Initial here)

**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

\_\_\_\_\_  
 Borrower Signature Date

<sup>1</sup> Pursuant to Regulation 226.2(23), which implements the Truth in Lending Act, \$4,750.00 of this is considered "pre-paid finance charges."

## STATEMENT OF LOAN TERMS

DATE: February 23, 2009  
 LENDER: ABC Bank  
 BORROWER: Joe Smith & Jane Doe  
 PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. For information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

Loan Amount:	<b>\$201,000.00</b> , of which <b>\$3,000.00</b> goes toward your total settlement charges.
Loan Term:	<b>30 years</b>
Loan Type:	<b>3/1 Adjustable Rate Mortgage (ARM)</b>
Total Settlement Charges:	<b>\$10,797.00<sup>1</sup></b> (see your Good Faith Estimate for details)

**TRUE COST FACTOR (TCF)**

7.50

When comparing loans of the same type and term, a higher TCF means a more expensive loan.

### PAYMENT SUMMARY

	INTRODUCTORY Rate & Est. Payment (for first 3 years)	MAXIMUM at FIRST ADJUSTMENT (Feb. 2012)	MAXIMUM EVER (as early as 2014)
Interest Rate	<b>5.125%</b>	<b>7.125%</b>	<b>11.125%</b>
Principal + Interest	\$1,094.42	\$ 1,335.16	\$ 1,855.02
Taxes + Insurance (Escrow)	+ \$ 233.00	+ \$ 233.00	+ \$ 233.00
<b>Total Est. Monthly Payment</b>	<b>\$1,327.42</b>	<b>\$ 1,568.16</b>	<b>\$ 2,088.02</b>

**Introductory Rate** You have a discounted introductory rate of 5.125% for the first three years. If the market rate does not change, at the end of this period your interest rate will increase by 2.00%, adding approximately \$250.00 to your monthly payment.

**Rate Changes** After the first three years, your rate adjusts annually based on the one-year LIBOR index (the market rate) + 2.125%. Your interest rate can increase no more than 2.00% in any one year, and no more than 6.00% total for the life of the loan.

**Escrow** An escrow account **is required** for your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates** and can change at any time.

**Total Payments** If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$580,104.61, including escrow. Of this amount, \$305,019.52 would go to interest and fees.

### KEY QUESTIONS ABOUT RISKS

Can my interest rate increase?	<b>YES.</b>
Can my monthly payment increase?	<b>YES.</b>
Can my lender demand full repayment at anytime?	<b>YES.</b> We can demand that you pay off the <b>full</b> amount of your loan at any time, for any reason. We are required to give you at least 30 days notice.
Do I have to share any equity I gain?	<b>YES.</b> We are entitled to 50% of any gain you make when you sell or refinance this property. In exchange, we are giving you a lower interest rate.

The following features are **not** included in this loan: interest-only payments, negative amortization, a balloon payment, and a prepayment penalty.

### OPTIONS WITH ADDITIONAL COSTS

Credit Life Insurance is available for an additional cost of \$50.00 per month for the first 15 years. It is not required for this or any loan. Initial below to add Credit Life Insurance to your loan.

YES, add Credit Life Insurance to my loan. \_\_\_\_\_  
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**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments.**

**Do not sign this form if there is any part of it that you do not understand.**

Borrower Signature \_\_\_\_\_

Date \_\_\_\_\_

<sup>1</sup> Pursuant to Regulation 226.2(23), which implements the Truth in Lending Act, \$9,795.00 of this is considered "pre-paid finance charges."

## STATEMENT OF LOAN TERMS

DATE: February 23, 2009  
 LENDER: ABC Bank  
 BORROWER: Joe Smith & Jane Doe  
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**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. For information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b> , of which <b>\$2,000.00</b> goes toward your total settlement charges
Loan Term:	<b>30 years</b>
Loan Type:	<b>3/1 Adjustable Rate Mortgage (ARM)</b>
Total Settlement Charges:	<b>\$6,642.00<sup>1</sup></b> (see your Good Faith Estimate for details)

### Overall Rate of Fees + Interest

# 7.41%

*Your interest rate when your closing costs are included.*

### PAYMENT SUMMARY

	INTRODUCTORY Rate & Est. Payment (for first 3 years)	MAXIMUM at FIRST ADJUSTMENT (Feb. 2012)	MAXIMUM EVER (as early as 2014)
Interest Rate	<b>5.625%</b>	<b>7.625%</b>	<b>11.625%</b>
Principal + Interest	\$1,151.31	\$ 1,397.15	\$ 1,924.97
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**Rate Changes** You have a discounted introductory rate of 5.625% for the first three years. After that, your rate will adjust annually based on the one-year LIBOR index (the market rate) + 2.125%. Your interest rate can increase no more than 2.00% in any one year, and no more than 6.00% total for the life of the loan.

**Escrow** An escrow account **is required** for your property taxes and homeowners and other insurance. The amounts shown for taxes and insurance are **estimates** and can change at any time.

**Total Payments** If your interest rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$585,778.09, including escrow. Of this amount, \$303,767.47 would go to interest and fees.

### KEY QUESTIONS ABOUT RISKS

Can my interest rate increase?	<b>YES.</b>
Can my monthly payment increase?	<b>YES.</b>
Will my monthly payments reduce my loan balance?	Yes.
Even if I make monthly payments, can my loan balance increase over time?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Can my lender demand full repayment at anytime?	<b>YES.</b> We can demand that you pay off the <b>full</b> amount of your loan at any time, for any reason. We are required to give you at least 30 days notice.
Do I have to share any equity I gain?	<b>YES.</b> We are entitled to 50% of any gain you make when you sell or refinance this property. In exchange, we are giving you a lower interest rate.

### OPTIONS WITH ADDITIONAL COSTS

Credit Life Insurance is available for an additional cost of \$50.00 per month for the first 15 years. It is not required for this or any loan. Initial below to add Credit Life Insurance to your loan.

YES, add Credit Life Insurance to my loan. \_\_\_\_\_  
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Borrower Signature \_\_\_\_\_

Date \_\_\_\_\_

<sup>1</sup> Pursuant to Regulation 226.2(23), which implements the Truth in Lending Act, \$4,750.00 of this is considered "pre-paid finance charges."

## STATEMENT OF LOAN TERMS

DATE: February 23, 2009  
 LENDER: ABC Bank  
 BORROWER: Joe Smith & Jane Doe  
 PROPERTY: 1234 Main Street, Anytown, ST 12345

**You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied. For information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm)

### LOAN SUMMARY

Loan Amount:	<b>\$201,000.00</b> , of which <b>\$3,000.00</b> goes toward your total settlement charges
Loan Term:	<b>30 years</b>
Loan Type:	<b>3/1 Adjustable Rate Mortgage (ARM)</b>
Total Settlement Charges:	<b>\$10,797.00<sup>1</sup></b> (see your Good Faith Estimate for details)

### Overall Rate of Fees + Interest

# 7.50%

Your interest rate when your closing costs are included.

### PAYMENT SUMMARY

	INTRODUCTORY Rate & Est. Payment (for first 3 years)	MAXIMUM at FIRST ADJUSTMENT (Feb. 2012)	MAXIMUM EVER (as early as 2014)
Interest Rate	<b>5.125%</b>	<b>7.125%</b>	<b>11.125%</b>
Principal + Interest	\$1,094.42	\$ 1,335.156	\$ 1,855.02
Taxes + Insurance (Escrow)	+ \$ 233.00	+ \$ 233.00	+ \$ 233.00
<b>Total Est. Monthly Payment</b>	<b>\$1,327.42</b>	<b>\$ 1,568.16</b>	<b>\$ 2,088.02</b>

**Rate Changes** You have a discounted introductory rate of 5.125% for the first three years. After that, your rate will adjust annually based on the one-year LIBOR index (the market rate) + 2.125%. Your interest rate can increase no more than 2.00% in any one year, and no more than 6.00% total for the life of the loan.

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**Total Payments** If your interest rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$580,104.61, including escrow. Of this amount, \$305,019.52 would go to interest and fees.

### KEY QUESTIONS ABOUT RISKS

Can my interest rate increase?	<b>YES.</b>
Can my monthly payment increase?	<b>YES.</b>
Will my monthly payments reduce my loan balance?	Yes.
Even if I make monthly payments, can my loan balance increase over time?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Can my lender demand full repayment at anytime?	<b>YES.</b> We can demand that you pay off the <b>full</b> amount of your loan at any time, for any reason. We are required to give you at least 30 days notice.
Do I have to share any equity I gain?	<b>YES.</b> We are entitled to 50% of any gain you make when you sell or refinance this property. In exchange, we are giving you a lower interest rate.

### OPTIONS WITH ADDITIONAL COSTS

Credit Life Insurance is available for an additional cost of \$50.00 per month for the first 15 years. It is not required for this or any loan. Initial below to add Credit Life Insurance to your loan.

YES, add Credit Life Insurance to my loan. \_\_\_\_\_  
 (Initial here)

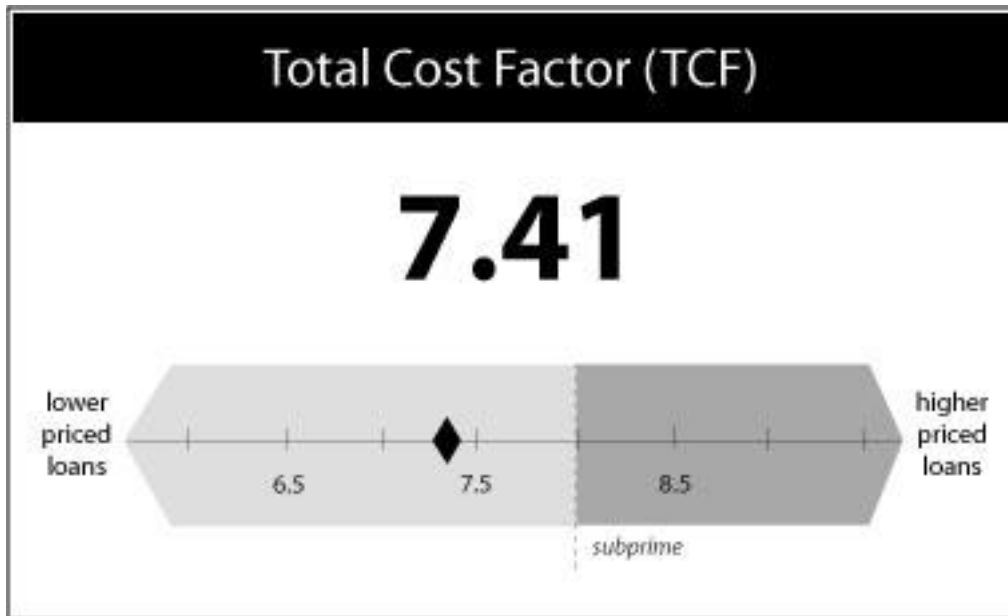
**If you are unable to make payments on this loan, you could lose your home. There is no guarantee that you will be able to refinance to lower your rate and payments. Do not sign this form if there is any part of it that you do not understand.**

\_\_\_\_\_  
 Borrower Signature

\_\_\_\_\_  
 Date

<sup>1</sup> Pursuant to Regulation 226.2(23), which implements the Truth in Lending Act, \$9,795.00 of this is considered "pre-paid finance charges."

A1, no percentage sign



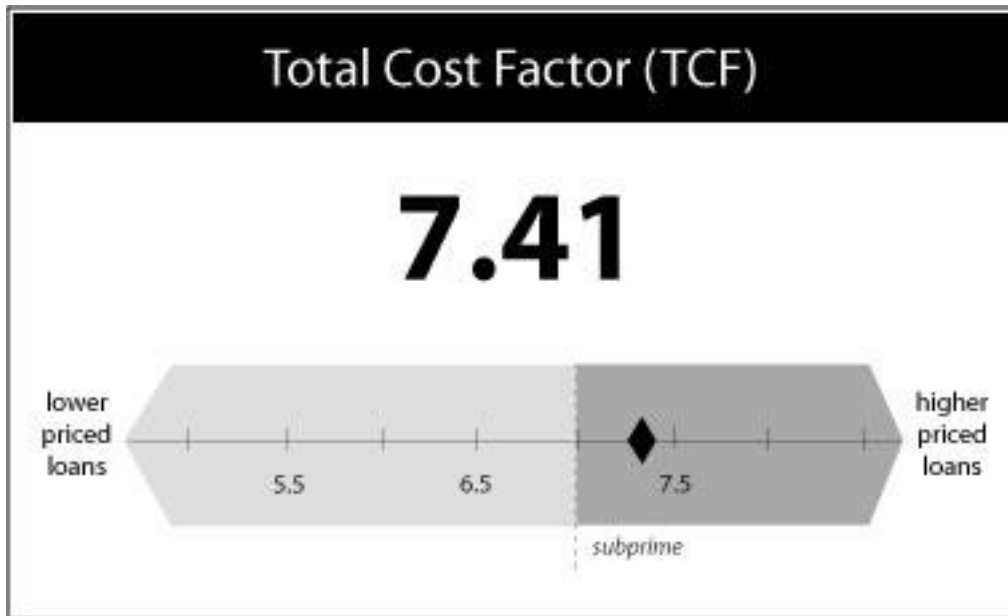
This illustration is based on loans of comparable type and term recently offered to borrowers with excellent credit.

A1, with percentage sign



This illustration is based on loans of comparable type and term recently offered to borrowers with excellent credit.

A2, no percentage sign



This illustration is based on loans of comparable type and term recently offered to borrowers with excellent credit.

A2, with percentage sign



This illustration is based on loans of comparable type and term recently offered to borrowers with excellent credit.



B1, no percentage sign

**Total Cost Factor (TCF)**

**7.41**

**How does this loan compare?**  
The average TCF on comparable loans recently offered to borrowers with excellent credit was **6.50**. A loan with a TCF of **8.00** or above is considered subprime.

B1, with percentage sign

**Total Cost Factor (TCF)**

**7.41%**

**How does this loan compare?**  
The average TCF on comparable loans recently offered to borrowers with excellent credit was **6.50%**. A loan with a TCF of **8.00%** or above is considered subprime.

B2, no percentage sign

**Total Cost Factor (TCF)**

**7.41**

**How does this loan compare?**  
The average TCF on comparable loans recently offered to borrowers with excellent credit was **5.50**. A loan with a TCF of **7.00** or above is considered subprime.

B2, with percentage sign

**Total Cost Factor (TCF)**

**7.41%**

**How does this loan compare?**  
The average TCF on comparable loans recently offered to borrowers with excellent credit was **5.50%**. A loan with a TCF of **7.00%** or above is considered subprime.



# Key Questions to Ask About Your Mortgage

When you are shopping for a loan, ask each lender the questions below. Some loans have risky features that could make it difficult for you to make payments in the future. Make sure you understand the terms of your loan. If you are not comfortable with the risks, ask your lender about other loan products. **The only way to make sure you get the best possible loan terms is to get offers from several lenders.**

## Shop. Compare. Negotiate.

For more information about risky loan features, read *Shop Wisely: Understanding Your Mortgage Choices*, available at: [www.federalreserveconsumerhelp.gov/shopwisely](http://www.federalreserveconsumerhelp.gov/shopwisely).

**1****Can my interest rate increase?**

If you have an adjustable rate mortgage (ARM), your interest rate can go up or down after a short period. This means that your monthly payments could increase.

**2****Can my monthly payment increase?**

With some loans, your monthly payment could increase after a period of time, often by hundreds of dollars. This increase could be because you have a lower introductory interest rate, your property taxes or insurance premiums increase, or because in the beginning your monthly payment only covers the interest on the loan, and not the principal owed.

**3****Will my monthly payments reduce my loan balance?**

Some loans let you pay only the interest on your loan each month. These payments do not pay down the amount you borrowed. As a result, if you have this type of loan, you may not build any equity in your home.

**4****Even if I make my monthly payments, can my loan balance increase?**

Some loans let you choose to pay even less than the interest owed each month. The unpaid interest is added to your loan balance and increases the total amount that you owe. This could cause you to lose equity in your home over time.

**5****Could I owe a prepayment penalty?**

Some loans charge you a large fee if you pay off your loan, refinance it, or sell your home within the first few years of the loan. This penalty fee could be thousands of dollars.

**6****Will I owe a balloon payment?**

Some loans require a very large payment at the end of the loan—sometimes tens of thousands of dollars. If interest rates go up or if the value of your property drops, you may not be able to refinance your loan before you have to make this large payment.

**7****Could I be required to repay this loan before the end of the term?**

With some loans, lenders can demand that you pay off the full amount of the loan at any time.

**8****Will I have to document my employment, income, and assets to get this loan?**

Sometimes a lender will make a loan without requiring you to show that you are employed and have the income or assets to repay the loan. These no-documentation ("no-doc") or low-documentation ("low-doc") loans usually have higher interest rates or higher fees than other loans.

**9****Will I have to share part of the equity in my home with the lender?**

Some lenders will offer you a low interest rate in exchange for a percentage of your home's increased value at a later date, such as when you refinance or sell your home. This percentage can represent a large amount of money if your home's value increases significantly.

1. Read your loan contract to find out what happens if you stop making payments, default, pay off or refinance your loan early.
2. If you sell your home after you take out this loan, we have the option to permit the buyer to take over your mortgage.
3. You may get property insurance from any insurer that is acceptable to us.
4. If you pay off or refinance your loan, or sell this property early, you will receive a refund of some of the interest and fees you have paid on your loan.
5. If you make a payment more than 15 days late, you may be charged a penalty equal to 15% of your monthly payment.

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# **Round 11: Providence, RI March 31–April 1, 2009**

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- **Revised TILA Statement Version G1**
- **Revised TILA Statement Version G2**
- **Revised TILA Statement Version H1**
- **Revised TILA Statement Version H2**
- **Revised ARM Loan Program Disclosure**
- **Proposed Early Disclosure: “Fixed vs. Adjustable Rate Mortgages”**
- **Proposed ARM Adjustment Notice**

# STATEMENT OF LOAN TERMS

**Joe Smith & Jane Doe**  
 1234 Main Street, Anytown, ST 12345

**ABC Bank**  
 January 28, 2009

*You have no obligation to accept this loan. Use this statement to confirm that these are the loan terms for which you applied. For more information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).*

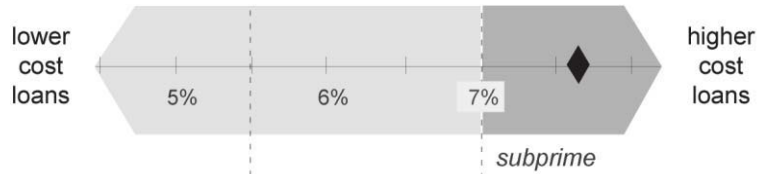
## LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b> of which: \$198,000.00 goes toward the home purchase \$2,000.00 goes toward settlement charges
Loan Term:	<b>30 years</b>
Loan Type:	<b>Adjustable Rate Mortgage (ARM)</b>
Total Estimated Settlement Charges:	<b>\$8,625.00</b> This does not include your down payment. See your Good Faith Estimate or HUD-1 for details.
Prepayment Penalty:	Up to <b>\$4,000.00</b> if you pay off your loan, refinance, or sell this property within 2 years.

## ANNUAL PERCENTAGE RATE (APR)

Your interest rate with settlement charges included:

7.59%



**How does this loan compare?** The average APR on comparable loans recently offered to borrowers with excellent credit was **5.49%**. In today's market, an APR of **6.99%** or above is considered subprime (high cost).

## PAYMENT SUMMARY

	<b>INTRODUCTORY Rate &amp; Monthly Payment (for first 5 years)</b>	<b>MAXIMUM at FIRST ADJUSTMENT (Mar. 2014)</b>	<b>MAXIMUM EVER (as early as 2016)</b>
Interest Rate	<b>6.875%</b>	<b>8.875%</b>	<b>12.875%</b>
Principal	\$0	\$182.14	\$116.64
Interest	\$1,145.83	\$1,479.17	\$2,101.91
Est. Taxes + Insurance (Escrow)	\$332.00	\$332.00	\$297.00
<b>Total Est. Monthly Payment</b>	<b>\$1,477.83</b>	<b>\$1,993.31</b>	<b>\$2,515.55</b>

## STATEMENT OF LOAN TERMS

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### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase beginning in March 2014. For more information, see the Payment Summary table on page 1.
Can my monthly payment increase?	<b>YES.</b> Your payment can increase beginning in March 2014. For more information, see the Payment Summary table on page 1.
Will any of my monthly payments be interest-only?	<b>YES.</b> Your monthly payments for the first 5 years of the loan (until March 2014) only cover interest and do not include any principal. Making these monthly payments will not reduce your loan balance during this period.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell your home within <b>2 years</b> you could pay a penalty of up to <b>\$4,000</b> .
Will I owe a balloon payment?	No.

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### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Change</b>	As shown in the Payment Summary table above, you have a discounted introductory rate that is fixed at 6.875% for the first five years. After this five year period, and each year after that, your rate will be based on the one-year LIBOR index (the market rate) plus 5.00%.
<b>Rate Change Limits</b>	After the first five years, your interest rate can increase no more than 2.00% from one year to the next, and no more than 6.00% total for the life of the loan, which would result in the maximum ever rate of 12.875%.
<b>Escrow</b>	An escrow account is required for property taxes, and for homeowner's, private mortgage, and other insurance. Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$589,385.69, including estimated escrow. Of this amount, \$307,935.69 would go to interest and settlement charges. This amount and your amount financed of \$193,250.00 are used to calculate your APR.

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### Ask questions if you do not understand any part of this form.

- If you are unable to make payments on this loan, you could lose your home.
- There is no guarantee that you will be able to refinance to lower your rate and payments.

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I acknowledge receipt of this form

Date

## STATEMENT OF LOAN TERMS

Joe Smith & Jane Doe  
1234 Main Street, Anytown, ST 12345

ABC Bank  
January 28, 2009

*You have no obligation to accept this loan. Use this statement to confirm that these are the loan terms for which you applied. For more information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).*

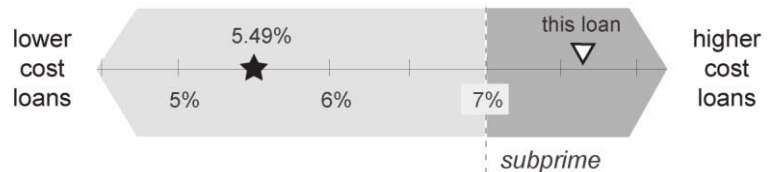
### LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b> of which: \$198,000.00 goes toward the home purchase, and \$2,000.00 goes toward settlement charges.
Loan Term:	<b>30 years</b>
Loan Type:	<b>Adjustable Rate Mortgage (ARM)</b>
Total Estimated Settlement Charges:	<b>\$8,625.00</b> This does not include your down payment. See your Good Faith Estimate or HUD-1 for details.
Prepayment Penalty:	Up to <b>\$4,000.00</b> if you pay off your loan, refinance, or sell this property within 2 years.

### ANNUAL PERCENTAGE RATE (APR)

Your interest rate with settlement charges included:

7.59%



**How does this loan compare?** The average APR on comparable loans recently offered to borrowers with excellent credit was **5.49%**. In today's market, an APR of **6.99%** or above is considered subprime (high cost).

### PAYMENT SUMMARY

	<b>INTRODUCTORY Rate &amp; Monthly Payment (for first 5 years)</b>	<b>MAXIMUM at FIRST ADJUSTMENT (Mar. 2014)</b>	<b>MAXIMUM EVER (as early as 2016)</b>
Interest Rate	<b>6.875%</b>	<b>8.875%</b>	<b>12.875%</b>
Principal	\$0	\$182.14	\$116.64
Interest	\$1,145.83	\$1,479.17	\$2,101.91
Est. Taxes + Insurance (Escrow)	\$332.00	\$332.00	\$297.00
<b>Total Est. Monthly Payment</b>	<b>\$1,477.83</b>	<b>\$1,993.31</b>	<b>\$2,515.55</b>



## STATEMENT OF LOAN TERMS

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### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase beginning in March 2014. For more information, see the Payment Summary table on page 1.
Can my monthly payment increase?	<b>YES.</b> Your payment can increase beginning in March 2014. For more information, see the Payment Summary table on page 1.
Will any of my monthly payments be interest-only?	<b>YES.</b> Your monthly payments for the first 5 years of the loan (until March 2014) only cover interest and do not include any principal. Making these monthly payments will not reduce your loan balance during this period.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell your home within <b>2 years</b> you could pay a penalty of up to <b>\$4,000</b> .
Will I owe a balloon payment?	No.

---

### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Introductory Rate</b>	As shown in the Payment Summary table above, you have a discounted introductory rate that is fixed at 6.875% for the first five years. After this five year period, and each year after that, your rate can increase.
<b>Escrow</b>	An escrow account is required for property taxes, and for homeowner's, private mortgage, and other insurance. Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$589,385.69, including estimated escrow. Of this amount, \$307,935.69 would go to interest and settlement charges. This amount and your amount financed of \$193,250.00 are used to calculate your APR.

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### Ask questions if you do not understand any part of this form.

- If you are unable to make payments on this loan, you could lose your home.
- There is no guarantee that you will be able to refinance to lower your rate and payments.

---

I acknowledge receipt of this form

Date

# STATEMENT OF LOAN TERMS

Joe Smith & Jane Doe  
1234 Main Street, Anytown, ST 12345

ABC Bank  
January 28, 2009

*You have no obligation to accept this loan. Use this statement to confirm that these are the loan terms for which you applied. For more information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).*

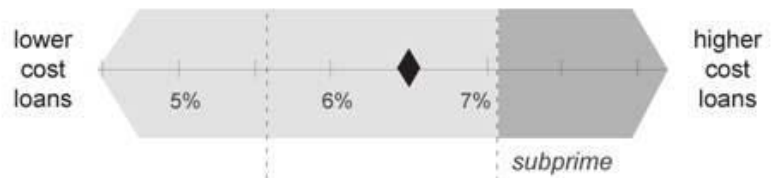
## LOAN SUMMARY

Loan Amount:	<b>\$210,000.00</b> of which: \$207,000.00 goes toward the home purchase \$3,000.00 goes toward settlement charges
Loan Term:	<b>3 years</b>
Loan Type:	<b>Fixed Rate</b>
Total Estimated Settlement Charges:	<b>\$7,472.00</b> <i>This does not include your down payment. See your Good Faith Estimate or HUD-1 for details.</i>

## ANNUAL PERCENTAGE RATE (APR)

Your interest rate with settlement charges included:

**6.50%**



**How does this loan compare?** The average APR on comparable loans recently offered to borrowers with excellent credit was **5.66%**. In today's market, an APR of **7.16%** or above is considered subprime (high cost).

## PAYMENT SUMMARY

	Rate and Monthly Payment	Final Balloon Payment (due Mar. 2012)
Interest Rate	<b>5.50%</b>	
Principal + Interest	\$ 1,192.36	
Est. Taxes + Insurance (Escrow)	not included	
<b>Total Est. Monthly Payment</b>	<b>\$ 1,192.36</b>	<b>\$202,217.84</b>

## STATEMENT OF LOAN TERMS

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### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	No.
Will any of my monthly payments be interest-only?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	<b>YES.</b> You will owe a balloon payment of <b>\$202,217.84</b> , due in March 2012.
Do I have to share any equity I gain?	<b>YES.</b> In exchange for giving you a lower interest rate on this loan, we are entitled to 50% of any gain you make when you sell or refinance this property.

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### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Escrow</b>	An escrow account is not required on this loan. You must pay your property taxes, homeowner's, and other insurance on your own.
<b>Total Payments</b>	If you made all payments as scheduled, you would make 36 payments totaling \$243,950.33. Of this amount, \$39,530.44 would go to interest and settlement charges. This amount and your amount financed of \$204,420.00 are used to calculate your APR.

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### Ask questions if you do not understand any part of this form.

- If you are unable to make payments on this loan, you could lose your home.
- There is no guarantee that you will be able to refinance to lower your rate and payments.

---

I acknowledge receipt of this form

Date

## STATEMENT OF LOAN TERMS

Joe Smith & Jane Doe  
1234 Main Street, Anytown, ST 12345

ABC Bank  
January 28, 2009

*You have no obligation to accept this loan. Use this statement to confirm that these are the loan terms for which you applied. For more information see: [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).*

### LOAN SUMMARY

Loan Amount:	<b>\$210,000.00</b> , of which: \$207,000.00 goes toward your home purchase, and \$3,000.00 goes toward settlement charges.
Loan Term:	<b>3 years</b>
Loan Type:	<b>Fixed Rate</b>
Total Estimated Settlement Charges:	<b>\$7,472.00</b> <i>This does not include your down payment. See your Good Faith Estimate or HUD-1 for details.</i>

### ANNUAL PERCENTAGE RATE (APR)

Your interest rate with settlement charges included:

6.50%



**How does this loan compare?** The average APR on comparable loans recently offered to borrowers with excellent credit was **5.66%**. In today's market, an APR of **7.16%** or above is considered subprime (high cost).

### PAYMENT SUMMARY

	Rate and Monthly Payment
Interest Rate	<b>5.50%</b>
Principal + Interest	\$ 1,192.36
Est. Taxes + Insurance (Escrow)	not included
<b>Total Est. Monthly Payment</b>	<b>\$ 1,192.36</b>

**Final Balloon Payment due March 2012: \$202,217.84**

## STATEMENT OF LOAN TERMS

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### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	No.
Will any of my monthly payments be interest-only?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	<b>YES.</b> You will owe a balloon payment of <b>\$202,217.84</b> , due in March 2012.
Do I have to share any equity I gain?	<b>YES.</b> In exchange for giving you a lower interest rate on this loan, we are entitled to 50% of any gain you make when you sell or refinance this property.

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### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Escrow</b>	An escrow account is not required on this loan. You must pay your property taxes, homeowner's, and other insurance on your own.
<b>Total Payments</b>	If you made all payments as scheduled, you would make 36 payments totaling \$243,950.33. Of this amount, \$39,530.44 would go to interest and settlement charges. This amount and your amount financed of \$204,420.00 are used to calculate your APR.

---

### Ask questions if you do not understand any part of this form.

- If you are unable to make payments on this loan, you could lose your home.
- There is no guarantee that you will be able to refinance to lower your rate and payments.

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I acknowledge receipt of this form

Date

## ABC Bank 3/1 Adjustable Rate Mortgage (ARM) Product Description

Interest Rate	
Introductory Period	<p><b>3 Years</b></p> <p>The interest rate is discounted and will stay the same for a 3-year introductory period. After this initial period, the interest rate could increase.</p>
Frequency of Rate Change	<p><b>Annually</b></p> <p>The interest rate will adjust once each year after the introductory period.</p>
Index	<p><b>LIBOR Index</b></p> <p>After the initial 3-year period, your interest rate will be based on the 1-year LIBOR Index plus a margin that is determined at application. The LIBOR is published daily in the Wall Street Journal.</p>
Limits on Rate Changes	<p><b>2% Annual Cap; 6% Lifetime Cap</b></p> <p>Your interest rate can increase <b>no more than 2%</b> in any one year, and <b>no more than 6%</b> over the life of the loan.</p>

Risk Factors	
Can my interest rate increase?	<b>YES.</b> Your interest rate could increase at the end of the 3-year introductory period, and annually after that.
Can my monthly payment increase?	<b>YES.</b> If your interest rate increases, your monthly payment will increase.
Will any of my monthly payments be interest-only?	No.
Can my lender demand full repayment at anytime?	<b>YES.</b> We can demand that you pay off the <b>full</b> amount of your loan at any time, for any reason. We are required to give you at least 30 days notice.
Could I owe a prepayment penalty?	No.
Do I have to share any equity I gain?	<b>YES.</b> We will give you a lower interest rate on this loan, but in exchange we are entitled to 50% of any gain you make when you sell or refinance this property.

For more information about ARMs, or for a list of licensed housing counselors in your area that can help you understand the risks and benefits of this loan, visit [www.frb.gov](http://www.frb.gov).



# Fixed vs. Adjustable Rate Mortgages

## What Type of Mortgage is Right for You?

A traditional fixed rate mortgage is a safe choice for many borrowers, but in some circumstances an adjustable rate mortgage (ARM) might make sense for you. If you are considering an ARM, be sure you understand the tradeoffs.

Fixed Rate Mortgages	ARMs
<p>With a fixed rate mortgage, the interest rate and monthly payment stay the same for the entire loan term.</p> <p><b>Consider a Fixed Rate Mortgage if:</b></p> <ul style="list-style-type: none"><li>• You would prefer predictable payments or have difficulty managing monthly payments that increase; or</li><li>• You plan to stay in your home for a long period of time.</li></ul>	<p>With an ARM, the interest rate and monthly payment often start out lower than with a fixed rate mortgage. However, both the rate and payment can increase very quickly.</p> <p><b>Consider an ARM if:</b></p> <ul style="list-style-type: none"><li>• You are confident that you could afford increases in your monthly payment, even at the maximum amount (sometimes as much as double your initial payment amount); or</li><li>• You plan to sell your home within a short period of time.</li></ul>

**If you are considering an ARM, don't count on being able to refinance before your interest rate and monthly payments increase.** You might not qualify for refinancing if the market value of your home goes down, or your financial situation changes due to job loss, illness, or other large debts.

## Where to Find Help

For more information about how to choose the right loan for you, or for a list of licensed housing counselors in your area that could help you make this decision, visit [www.frb.gov](http://www.frb.gov).

## Important Changes to Your Loan Terms

The following is a summary of changes that are being made to your loan terms, effective 4/10/09. For more detailed information, please refer to your loan agreement(s).

These changes will impact your loan terms as follows:

	<b>Current Rate and Monthly Payment</b>	<b>New Rate and Monthly Payment</b>
Interest Rate	<b>5.75%</b>	<b>7.75%</b>
Principal	\$0	\$195.56
Interest	\$1,166.55	\$1,471.35
Taxes + Insurance (Escrow)	\$345.00	\$400.00
<b>Total Monthly Payment</b>	<b>\$ 1,511.55</b>	<b>\$2,066.91</b> (due on May 1, 2009)

**Interest Rate:** Your interest rate will change from 5.75% to 7.75%, due to an increase in the 1-year LIBOR index.

**Rate Change:** Your rate can change each year, by no more than 2.00%. Your rate can never go higher than 11.00% over the life of the loan.

**New Payment:** Your new payment includes some of your loan's principal, and will therefore reduce your loan balance.

**Prepayment Penalty:** If you pay off your loan, refinance or sell your home before 5/10/13 you may be subject to a pre-payment penalty of up to **\$4,000**.

If you are unable to pay your mortgage, contact us at (555) 555-5555 or [www.creditor.com/assistance](http://www.creditor.com/assistance) as soon as possible.

If you would like to talk with a licensed housing counselor, you can find a list of counselors in your area:

- On the Neighborworks website, at <http://www.nw.org/network/home.asp>.
- On the U.S. Department of Housing and Urban Development's (HUD) website, at <http://www.hud.gov/offices/hsg/sfh/hcc/hccprof14.cfm>.
- By calling (800) 569-4287.



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# **Round 12: Denver, CO April 21-22, 2009**

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- **Revised TILA Statement Version J-IO**
- **Revised TILA Statement Version J-PO**
- **Revised TILA Statement Version K-IO**
- **Revised TILA Statement Version K-PO**
- **Proposed Payment Option Monthly  
Payment Disclosure**
- **Proposed Credit Life Insurance Disclosure**



## STATEMENT OF LOAN TERMS

### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase <b>annually</b> beginning in April 2014. For more information, see the Payment Summary table on page 1.
Can my monthly payment increase?	<b>YES.</b> Your payment can increase beginning in April 2014. For more information, see the Payment Summary table on page 1.
Will any of my monthly payments be interest-only?	<b>YES.</b> Your monthly payments for the first 5 years of the loan (until April 2014), shown in the Payment Summary table on page 1, only cover interest and do not include any principal. Making these monthly payments will not reduce your loan balance during this period.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell your home within <b>2 years</b> you could pay a penalty of up to <b>\$4,000</b> .
Will I owe a balloon payment?	No.

### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Calculation</b>	When the 5-year introductory period ends, your rate will be determined annually based on the one-year LIBOR index (the market rate) plus 5.00%.
<b>Rate Change Limits</b>	When the 5-year introductory period ends, your interest rate can increase no more than 2.00% from one year to the next, and no more than 6.00% total for the life of the loan, which would result in the maximum ever rate of 12.875%.
<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's and private mortgage insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$589,385.69, including estimated escrow. Of this amount, \$307,935.69 would go to interest and settlement charges. This amount, and your amount financed of \$193,250.00, are used to calculate your APR.

- **You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied.
- **Ask questions if you do not understand any part of this form.** If you are unable to make payments on this loan, you could lose your home. There is also no guarantee that you will be able to refinance to lower your rate and payments.
- **For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).**

By signing below, I acknowledge receipt of this form.

Borrower's Signature

Date



## STATEMENT OF LOAN TERMS

### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase <b>monthly</b> beginning in April 2009.
Can my monthly payment increase?	<b>YES.</b> Your full payment can increase beginning in April 2009. Your minimum payment can increase beginning in March 2010. For more information, see the Payment Summary table on page 1.
Will any of my monthly payments be interest-only?	<b>YES.</b> This loan gives you the choice to make monthly payments that only cover interest and do not include any principal. Making these monthly payments will not reduce your loan balance.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Even if I make my monthly payments, could my loan balance increase?	<b>YES.</b> Your minimum payment does not cover all the interest that you owe each month. The unpaid interest will be added to your loan balance, which over time will increase the total amount you owe and cause you to lose equity in your home.

### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Calculation</b>	When the 1-month introductory period ends, your rate will be determined monthly based on the one-year LIBOR index (the market rate) plus 3.75%.
<b>Rate and Payment Change Limits</b>	When the 1-month introductory period ends, your interest rate can increase up to a maximum of 10.5% for the life of the loan. Your minimum payments due cannot increase more than 7.5% each year until the total loan balance has increased by 15%. When this happens, you must make full monthly payments that cover all principal and interest owed on the loan.
<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's and private mortgage insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$545,943.65, including estimated escrow. Of this amount, \$251,893.65 would go to interest and settlement charges. This amount, and your amount financed of \$193,250.00, are used to calculate your APR.

- **You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied.
- **Ask questions if you do not understand any part of this form.** If you are unable to make payments on this loan, you could lose your home. There is also no guarantee that you will be able to refinance to lower your rate and payments.
- **For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).**

By signing below, I acknowledge receipt of this form.

Borrower's Signature

Date

# STATEMENT OF LOAN TERMS

Joe Smith & Jane Doe  
1234 Main Street, Anytown, ST 12345

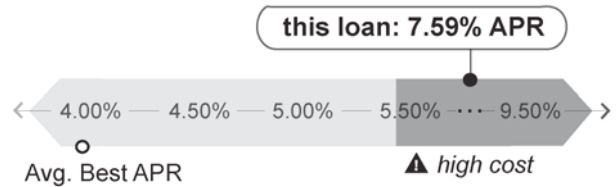
ABC Bank  
February 26, 2009

## LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b>
Loan Term:	<b>30 years</b>
Loan Type:	<b>Adjustable Rate Mortgage (ARM), Interest-Only Payments</b>
Total Estimated Settlement Charges:	<b>\$8,625.00</b> \$2,000.00 of these charges are rolled into your loan amount above. This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.
Prepayment Penalty:	Up to <b>\$4,000.00</b> if you pay off your loan, refinance, or sell this property within 2 years.

## ANNUAL PERCENTAGE RATE (APR)

Your interest rate with settlement charges included: **7.59% APR**



**How does this loan compare?** During the week of February 23, 2009, the average APR on similar loans offered to borrowers with excellent credit was **4.00%**.

**What does this mean in dollars?** For this loan, a 1% reduction in APR could reduce your monthly payment by **\$167/month** for the first 5 years.

## PAYMENT SUMMARY

	<b>INTRODUCTORY Rate &amp; Monthly Payment (for first 5 years)</b>	<b>MAXIMUM at FIRST ADJUSTMENT (April 2014)</b>	<b>MAXIMUM EVER (as early as 2016)</b>
Interest Rate	<b>6.875%</b>	<b>8.875%</b>	<b>12.875%</b>
Principal	\$0	\$182.14	\$116.64
Interest	\$1,145.83	\$1,479.17	\$2,101.91
Est. Taxes + Insurance (Escrow) <i>including private mortgage insurance</i>	\$332.00	\$332.00	\$297.00
<b>Total Est. Monthly Payment</b>	<b>\$1,477.83</b>	<b>\$1,993.31</b>	<b>\$2,515.55</b>

### Teaser Rate Notice

As shown in the table above, you have a discounted introductory rate that is **6.875%** which ends after five years. In the sixth year, even if market rates **do not** change, this rate will increase by .125% to **7.00%**, bringing your monthly payment up to \$1,745.56.

see page 2

## STATEMENT OF LOAN TERMS

### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase <b>annually</b> beginning in April 2014. For more information, see the Payment Summary table on page 1.
Can my monthly payment increase?	<b>YES.</b> Your payment can increase beginning in April 2014. For more information, see the Payment Summary table on page 1.
Will any of my monthly payments be interest-only?	<b>YES.</b> Your monthly payments for the first 5 years of the loan (until April 2014), shown in the Payment Summary table on page 1, only cover interest and do not include any principal. Making these monthly payments will not reduce your loan balance during this period.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell your home within <b>2 years</b> you could pay a penalty of up to <b>\$4,000</b> .
Will I owe a balloon payment?	No.

### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Calculation</b>	When the 5-year introductory period ends, your rate will be determined annually based on the one-year LIBOR index (the market rate) plus 5.00%.
<b>Rate Change Limits</b>	When the 5-year introductory period ends, your interest rate can increase no more than 2.00% from one year to the next, and no more than 6.00% total for the life of the loan, which would result in the maximum ever rate of 12.875%.
<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's and private mortgage insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$589,385.69, including estimated escrow. Of this amount, \$307,935.69 would go to interest and settlement charges. This amount, and your amount financed of \$193,250.00, are used to calculate your APR.

- **You have no obligation to accept this loan.** Use this statement to confirm that these are the loan terms for which you applied.
- **Ask questions if you do not understand any part of this form.** If you are unable to make payments on this loan, you could lose your home. There is also no guarantee that you will be able to refinance to lower your rate and payments.
- **For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).**

By signing below, I acknowledge receipt of this form.

Borrower's Signature

Date

# STATEMENT OF LOAN TERMS

Joe Smith & Jane Doe  
1234 Main Street, Anytown, ST 12345

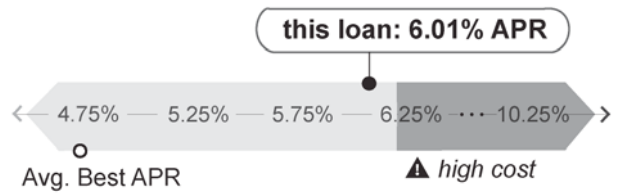
ABC Bank  
February 4, 2009

## LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b>
Loan Term:	<b>30 years</b>
Loan Type:	<b>Adjustable Rate Mortgage (ARM), Payment Options</b>
Total Estimated Settlement Charges:	<b>\$7,426.00</b> \$1,000.00 of these charges are rolled into your loan amount above. This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.

## ANNUAL PERCENTAGE RATE (APR)

Your interest rate with settlement charges included: **6.01% APR**



**How does this loan compare?** During the week of February 2, 2009, the average APR on similar loans offered to borrowers with excellent credit was **4.75%**.

**What does this mean in dollars?** For this loan, a 1% reduction in APR could reduce your full monthly payment by **\$125/month**.

## PAYMENT SUMMARY

This loan offers you several monthly payment options. The table below shows you what your payments would be under two of these options **if the interest rate reached its maximum of 10.5%** in the second month of this loan. All payments shown include \$280 for estimated taxes and insurance.

	March 2009 (1 month teaser)	April 2009 (1st adjustment)	March 2010 (2nd adjustment)	June 2011 + every month after
Maximum Interest Rate	<b>1.5%</b> (intro rate)	<b>10.5%</b>	<b>10.5%</b>	<b>10.5%</b> (max. ever)
<b>Full Payment Option</b> <i>Monthly payments cover all principal and interest.</i>	<b>\$970.24</b>	<b>\$2,016.18</b>	<b>\$2,016.18</b>	<b>\$2,016.18</b>
<b>Minimum Payment Option</b> <i>Initial payments do not cover principal and interest and increase the amount you are borrowing.</i>	\$970.24	\$970.24	\$1022.00	\$2402.54

You will borrow an additional **\$29,943.00** by June 2011 if you make only minimum payments on this loan.

see page 2



## STATEMENT OF LOAN TERMS

### KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase <b>monthly</b> beginning in April 2009.
Can my monthly payment increase?	<b>YES.</b> Your full payment can increase beginning in April 2009. Your minimum payment can increase beginning in March 2010. For more information, see the Payment Summary table on page 1.
Will any of my monthly payments be interest-only?	<b>YES.</b> This loan gives you the choice to make monthly payments that only cover interest and do not include any principal. Making these monthly payments will not reduce your loan balance.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Even if I make my monthly payments, could my loan balance increase?	<b>YES.</b> Your minimum payment does not cover all the interest that you owe each month. The unpaid interest will be added to your loan balance, which over time will increase the total amount you owe and cause you to lose equity in your home.

### MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Calculation</b>	When the 1-month introductory period ends, your rate will be determined monthly based on the one-year LIBOR index (the market rate) plus 3.75%.
<b>Rate and Payment Change Limits</b>	When the 1-month introductory period ends, your interest rate can increase up to a maximum of 10.5% for the life of the loan. Your minimum payments due cannot increase more than 7.5% each year until the total loan balance has increased by 15%. When this happens, you must make full monthly payments that cover all principal and interest owed on the loan.
<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's and private mortgage insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$545,943.65, including estimated escrow. Of this amount, \$251,893.65 would go to interest and settlement charges. This amount, and your amount financed of \$193,250.00, are used to calculate your APR.

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- **Ask questions if you do not understand any part of this form.** If you are unable to make payments on this loan, you could lose your home. There is also no guarantee that you will be able to refinance to lower your rate and payments.
- **For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).**

**By signing below, I acknowledge receipt of this form.**

Borrower's Signature

Date

## Your Payment Options This Month

Payment Option	This Payment Covers	If you make this payment <i>this</i> month	If you make this payment <i>every</i> month
<input type="checkbox"/> <b>\$500.00</b> <b>Full Payment</b> <i>(recommended)</i>	All the interest that you owe this month, plus some principal.	Your balance will decrease. You will be closer to having it paid off.	Your balance will steadily decrease and you will pay off your loan on schedule.
<input type="checkbox"/> <b>\$250.00</b> Interest-Only Payment	All the interest that you owe this month, but none of the principal.	Your balance will stay the same. You will be no closer to having it paid off.	As early as June 2011, you will have to make monthly payments much larger than today's "Full Payment" amount.
<input type="checkbox"/> <b>\$100.00</b> Minimum Payment	Just part of the interest that you owe this month.	<b>\$150.00 in unpaid interest will be added to your loan balance.</b> You are borrowing more money, and you will be losing equity in your home.	As early as June 2011, you will have to make payments more than double today's "Full Payment" amount to pay off your loan.

## OPTIONAL COSTS

**STOP.** You do **not** have to buy this insurance to get this loan. If you have insurance already, this policy may not provide you with any additional benefits. To learn more about credit life insurance, or to find a licensed housing counselor who can help you evaluate your options, go to [www.frb.gov](http://www.frb.gov).

- Yes, I want to purchase optional credit life insurance at an additional cost of \$72 per month for a loan of \$100,000 for a term of 10 years.

\_\_\_\_\_  
Signature of Borrower(s)

\_\_\_\_\_  
Date

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**Round 13**  
**Bethesda, MD**  
**May 6-7, 2009**

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- **Revised TILA Statement Version L1**
- **Revised TILA Statement Version L2**
- **Revised TILA Statement Version M**
- **Revised TILA Statement Version N**
- **Proposed Credit Life Insurance Disclosure**

# TRUTH IN LENDING STATEMENT

Joe Smith & Jane Doe  
1234 Main Street,  
Anytown, ST 12345

March 26, 2009  
ABC Bank  
Loan Officer No. 12345 1234

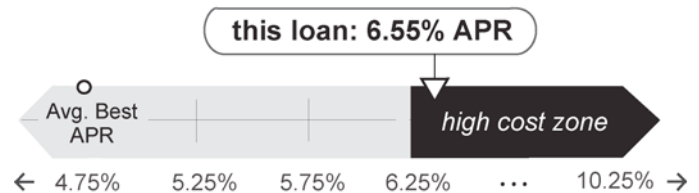
## LOAN SUMMARY

Loan Amount:	<b>\$306,000.00</b>
Loan Term:	<b>30 years</b>
Loan Type:	<b>Fixed Rate</b>
Total Estimated Settlement Charges:	<b>\$10,893.00</b> <ul style="list-style-type: none"><li>• \$3,000.00 of these charges are already included in your loan amount above.</li><li>• This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.</li></ul>

## ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan,  
including interest and  
settlement charges:

**6.55% APR**



**How does this loan compare?** For the week of March 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **4.75%**. Today, an APR of **6.25%** or above is considered high cost and is usually offered to applicants with poor credit.

**How much could I save by lowering my APR?** For this loan, a 1% reduction in the APR could save you **\$194 each month**.

## PAYMENT SUMMARY

	Rate & Monthly Payment
Interest Rate	<b>6.250%</b>
Principal + Interest Payment	\$1,884.09
Est. Taxes + Insurance (Escrow)	\$410.00
<b>Total Est. Monthly Payment</b>	<b>\$2,294.09</b>

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## KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	<b>YES.</b> If your property taxes or insurance premiums increase, your monthly payment will increase to cover them.
Will any of my monthly payments be interest-only?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.

---

## MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	You will make 360 payments totaling \$825,877.51, including estimated escrow. Of this amount, \$381,595.51 will go to interest and settlement charges. This amount, and your amount financed of \$296,682.00, are used to calculate your APR.

- 
- ➔ **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.
  - ➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.
  - ➔ **If you do not understand any part of this form, ask questions.** For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

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Applicant's Signature

Date

# TRUTH IN LENDING STATEMENT

Joe Smith & Jane Doe  
1234 Main Street,  
Anytown, ST 12345

March 26, 2009  
ABC Bank  
Loan Officer No. 12345 1234

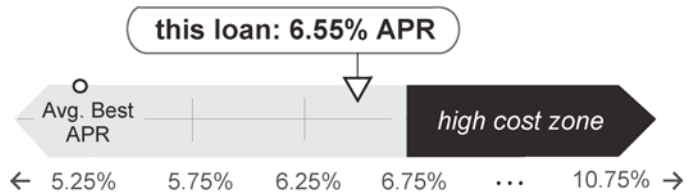
## LOAN SUMMARY

Loan Amount:	<b>\$306,000.00</b>
Loan Term:	<b>30 years</b>
Loan Type:	<b>Fixed Rate</b>
Total Estimated Settlement Charges:	<b>\$10,893.00</b> <ul style="list-style-type: none"><li>• \$3,000.00 of these charges are already included in your loan amount above.</li><li>• This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.</li></ul>

## ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan,  
including interest and  
settlement charges:

**6.55% APR**



**How does this loan compare?** For the week of March 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **5.25%**. Today, an APR of **6.75%** or above is considered high cost and is usually offered to applicants with poor credit.

**How much could I save by lowering my APR?** For this loan, a 1% reduction in the APR could save you **\$194 each month**.

## PAYMENT SUMMARY

	Rate & Monthly Payment
Interest Rate	<b>6.250%</b>
Principal + Interest Payment	\$1,884.09
Est. Taxes + Insurance (Escrow)	\$410.00
<b>Total Est. Monthly Payment</b>	<b>\$2,294.09</b>

---

## KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	No.
Can my monthly payment increase?	<b>YES.</b> If your property taxes or insurance premiums increase, your monthly payment will increase to cover them.
Will any of my monthly payments be interest-only?	No.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.

---

## MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	You will make 360 payments totaling \$825,877.51, including estimated escrow. Of this amount, \$381,595.51 will go to interest and settlement charges. This amount, and your amount financed of \$296,682.00, are used to calculate your APR.

- 
- ➔ **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.
  - ➔ **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.
  - ➔ **If you do not understand any part of this form, ask questions.** For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

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Applicant's Signature

Date



# TRUTH IN LENDING STATEMENT

Joe Smith & Jane Doe  
1234 Main Street  
Anytown, ST 12345

February 26, 2009  
ABC Bank  
Loan Officer No. 12345-1234

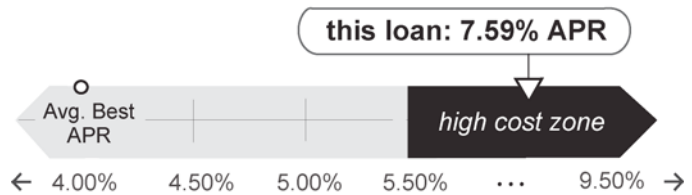
## LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b>
Loan Term:	<b>30 years</b>
Loan Type:	<b>Adjustable Rate Mortgage (ARM):</b> rate is fixed for first 5 years, then adjusts every year • Includes interest-only payments
Total Estimated Settlement Charges:	<b>\$8,625.00</b> • \$2,000.00 of these charges are already included in your loan amount above. • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.
Prepayment Penalty:	Up to <b>\$4,000.00</b> if you pay off your loan, refinance, or sell this property within 2 years.

## ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges:

7.59% APR



**How does this loan compare?** For the week of February 23, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **4.00%**. Today, an APR of **5.50%** or above is considered high cost and is usually offered to applicants with poor credit.

**How much could I save by lowering my APR?** For this loan, a 1% reduction in the APR could save you **\$167 each month** for the first 5 years.

## PAYMENT SUMMARY

	<b>INTRODUCTORY Rate &amp; Monthly Payment (for first 5 years)</b>	<b>MAXIMUM at FIRST ADJUSTMENT (April 2014)</b>	<b>MAXIMUM EVER (as early as 2016)</b>
Interest Rate	<b>6.875%</b>	<b>8.875%</b>	<b>12.875%</b>
Principal Payment	<b>- none -</b>	\$182.14	\$116.64
Interest Payment	\$1,145.83	\$1,479.17	\$2,101.91
Est. Taxes + Insurance (Escrow) • Includes Private Mortgage Insurance	\$332.00	\$332.00	\$297.00
<b>Total Est. Monthly Payment</b>	<b>\$1,477.83</b>	<b>\$1,993.31</b>	<b>\$2,515.55</b>

### Introductory Rate Notice

You have a discounted introductory rate of **6.875%** that ends after five years. In the sixth year, even if market rates **do not** change, this rate will increase to **7.00%**.

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## KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase <b>annually</b> beginning in April 2014.
Can my monthly payment increase?	<b>YES.</b> Your payment can increase beginning in April 2014.
Will any of my monthly payments be interest-only?	<b>YES.</b> Your monthly payments for the first 5 years of the loan cover the interest you owe each month, but <b>none</b> of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Could I owe a prepayment penalty?	<b>YES.</b> If you pay off your loan, refinance, or sell your home within <b>2 years</b> you could pay a penalty of up to <b>\$4,000</b> .
Will I owe a balloon payment?	No.

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## MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Calculation</b>	When the 5-year introductory period ends, your rate will be determined annually based on the one-year LIBOR index (the market rate) plus 5.00%.
<b>Rate Change Limits</b>	When the 5-year introductory period ends, your interest rate can increase no more than 2.00% from one year to the next, and no more than 6.00% total for the life of the loan, which would result in a maximum ever rate of 12.875%.
<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Private Mortgage Insurance</b>	Private Mortgage Insurance (PMI) <b>is</b> required for this loan. It is included in your escrow.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$589,385.69, including estimated escrow. Of this amount, \$307,935.69 would go to interest and settlement charges. This amount, and your amount financed of \$193,250.00, are used to calculate your APR.

- 
- **You have no obligation to accept this loan.** Your signature below only confirms that you have received this form.
  - **If you are unable to make the payments on this loan, you could lose your home.** There is no guarantee that you will be able to refinance to lower your rate and payments.
  - **If you do not understand any part of this form, ask questions.** For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

---

Applicant's Signature

Date

# TRUTH IN LENDING STATEMENT

Joe Smith & Jane Doe  
1234 Main Street,  
Anytown, ST 12345

February 4, 2009  
ABC Bank  
Loan Officer No. 12345 1234

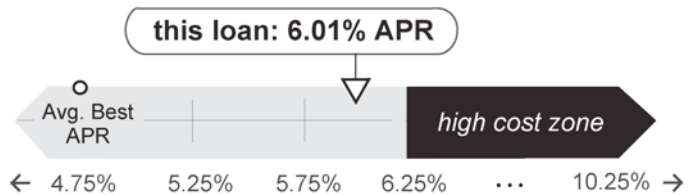
## LOAN SUMMARY

Loan Amount:	<b>\$200,000.00</b>
Loan Term:	<b>30 years</b>
Loan Type:	<b>Adjustable Rate Mortgage (ARM):</b> rate adjusts monthly • Includes Payment Options
Total Estimated Settlement Charges:	<b>\$7,426.00</b> • \$1,000.00 of these charges are already included in your loan amount above. • This total does not include a down payment. See your Good Faith Estimate or HUD-1 for details.

## ANNUAL PERCENTAGE RATE (APR)

Overall cost of this loan, including interest and settlement charges:

6.01% APR



**How does this loan compare?** For the week of February 2, 2009, the average APR on similar conforming loans offered to applicants with excellent credit was **4.75%**. Today, an APR of **6.25%** or above is considered high cost and is usually offered to applicants with poor credit.

**How much could I save by lowering my APR?** For this loan, a 1% reduction in the APR could save you **\$125 each month** on the full payment option.

## PAYMENT SUMMARY

This loan offers you several monthly payment options. The table below shows you what your payments would be under two of these options **if the interest rate reached its maximum of 10.5%** in the second month of this loan.

All payments shown in the table include **\$280** for estimated taxes and insurance (escrow).

	March 2009 (1 month intro)	April 2009 (1st adjustment)	March 2010 (2nd adjustment)	June 2011 + every month after
Maximum Interest Rate	1.5% (intro rate)	10.5%	10.5%	10.5% (max. ever)
<b>Full Payment Option</b> <i>Monthly payments cover all principal and interest.</i>	<b>\$970.24</b>	<b>\$2,016.18</b>	<b>\$2,016.18</b>	<b>\$2,016.18</b>
<b>Minimum Payment Option</b> <i>Initial monthly payments cover no principal and only some interest and increase your loan amount.</i>	\$970.24	\$970.24	\$1,022.00	\$2,402.54

You will borrow an additional **\$29,943.00** by June 2011 if you make only minimum payments on this loan.

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## KEY QUESTIONS ABOUT RISK

Can my interest rate increase?	<b>YES.</b> Your interest rate can increase <b>monthly</b> beginning in April 2009.
Can my monthly payment increase?	<b>YES.</b> Your full payment can increase beginning in April 2009. Your minimum payment can increase beginning in March 2010.
Will any of my monthly payments be interest-only?	<b>YES.</b> This loan gives you the choice to make monthly payments that cover the interest you owe each month, but <b>none</b> of the principal. Making these monthly payments means your loan amount will stay the same and you will be no closer to having it paid off.
Could I owe a prepayment penalty?	No.
Will I owe a balloon payment?	No.
Even if I make my monthly payments, could my loan balance increase?	<b>YES.</b> Your minimum payment covers only part of the interest you owe each month and <b>none</b> of the principal. The unpaid interest will be added to your loan amount, which over time will increase the total amount you are borrowing and cause you to lose equity in your home.

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## MORE INFORMATION ABOUT YOUR PAYMENTS

<b>Rate Calculation</b>	When the 1-month introductory period ends, your rate will be determined monthly based on the one-year LIBOR index (the market rate) plus 3.75%.
<b>Rate Change Limits</b>	When the 1-month introductory period ends, your interest rate can increase up to a maximum of 10.5% for the life of the loan.
<b>Payment Change Limits</b>	Your minimum payments due cannot increase more than 7.5% each year until the total loan amount has increased by 15%. When this happens, you must make full monthly payments that cover all principal and interest owed on the loan.
<b>Escrow</b>	An escrow account is required for property taxes and insurance (such as homeowner's insurance). Your escrow payment is an estimate and can change at any time. See your Good Faith Estimate or HUD-1 form for more details.
<b>Total Payments</b>	If the market rate did not change and you made all payments as scheduled, you would make 360 payments totaling \$545,943.65, including estimated escrow. Of this amount, \$251,893.65 would go to interest and settlement charges. This amount, and your amount financed of \$193,250.00, are used to calculate your APR.

- 
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  - ➔ **If you do not understand any part of this form, ask questions.** For more information, go to [www.frb.gov/mortgage/tilahelp.htm](http://www.frb.gov/mortgage/tilahelp.htm).

---

Applicant's Signature

Date

## OPTIONAL COSTS

### Credit Life Insurance

**STOP.** You do not have to buy this insurance to get this loan.

- If you have insurance already, this policy may not provide you with any additional benefits.
- Other types of insurance can give you similar benefits and are often less expensive.
- Even if you pay for this insurance, you may not qualify to receive any benefits in the future.

To learn more about credit life insurance go to [www.frb.gov](http://www.frb.gov).

- Yes, I want to purchase optional credit life insurance at an additional cost of \$72 per month for a loan of \$100,000 for a term of 10 years.

\_\_\_\_\_  
Signature of Applicant(s)

\_\_\_\_\_  
Date



an ICF International Company

ICF Macro  
11785 Beltsville Drive  
Calverton, Maryland 20705  
[icfmacro.com](http://icfmacro.com)