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American Bankers Association

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The Honorable Timothy F. Geithner
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

The Honorable Ben S. Bernanke
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551-0001

The Honorable Shaun Donovan
Secretary
U.S. Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410

The Honorable Sheila C. Bair
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW, Room MB-6028
Washington, DC 20429

The Honorable Mary L. Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Mr. John Walsh
Acting Comptroller of the Currency
Office of the Comptroller of the Currency
250 E Street, NW
Washington, DC 20219

Mr. Edward J. DeMarco
Acting Director
Federal Housing Finance Agency
1700 G Street, NW, 4th Floor
Washington, DC 20552

Mr. John E. Bowman
Acting Director
Office of Thrift Supervision
1700 G Street, NW
Washington, D.C. 20552

Dear Sir or Madam:

I am writing to share with you the perspectives of the American Bankers Association regarding the "risk retention" provisions of Section 941 of the Dodd Frank Act which were intended to address underwriting deficiencies in securitization transactions. Our specific concerns are with the exemption from those risk retention provisions for "qualified residential mortgages "(QRMs).

INTRODUCTION

The housing and mortgage markets have been battered in recent years and are still struggling to recover from the impact of the financial crisis. It is therefore imperative that we correct systemic problems which led to the crisis, but also avoid taking actions not necessary to address systemic issues and which could further destabilize the fragile recovery now underway. The overwhelming majority of ABA members in every asset category and of every charter type and organizational structure have concerns about detrimental market and economic effects which could be triggered by those new risk retention requirements. Our members believe strongly that imposing too broad a risk retention requirement – or imposing risk retention to achieve policy goals beyond improved underwriting - is likely to cause lenders to leave the marketplace and result in a constriction of credit to otherwise eligible borrowers. We urge you to consider these impacts and exercise the discretion explicitly provided under Section 941 to avoid such ill effects when risk retention requirements are imposed.

CONSIDER QRM IN CONCERT WITH OTHER LEGISLATIVE AND REGULATORY CHANGES

Section 941 of the Dodd/Frank Act was passed in part to correct systemic problems in the securitization market which contributed to the crisis. Congress determined that some form of risk retention was desirable to ensure that participants in a mortgage securitization transaction had so-called "skin in the game." The goal was to prevent (or at least discourage) the origination of loans both without regard for a borrower's ability to repay, and without regard to default risk or the ultimate losses posed if originators or others in the securitization process had no risk beyond the origination stage. Importantly, however, Congress also recognized that some mortgage loans – those with lower risk characteristics – could and should be exempted from the risk retention requirements. Exempting such "qualified residential mortgage" loans is important to ensure the stability and recovery of the mortgage market and to avoid risk retention and capital requirements not necessary to address systemic issues.

Requiring risk retention broadly on all – or nearly all – mortgage loans would certainly serve as a strong deterrent to many of the now discredited market and business practices that led to the housing crisis. However, risk retention requirements cannot be considered in isolation from the many other mandates of Dodd/Frank intended to deter or eliminate these same practices. Even before enactment of Dodd/Frank, there have been ongoing dramatic changes to the regulations governing mortgages under the Real Estate Settlement Procedures Act (RESPA), the Truth in Lending Act (TILA), and the Secure and Fair Enforcement for Mortgage Licensing (SAFE) Act. Moreover the federal bank agencies have just announced significant changes to appraisal standards. Failure to consider the joint impact of these new requirements, which are intended to work in concert with other legislative and regulatory changes, will defeat the purpose of Dodd/Frank by imposing significant and unintended costs on borrowers and lenders far beyond what is contemplated by the legislation, thereby unnecessarily constraining credit markets.

Simply stated, using every new regulatory tool in isolation to correct every problem identified during the crisis will result in an over-regulated market that is unable to address the nation's credit needs. An unintended and additional risk is that many fewer lenders will remain committed to mortgage lending, particularly at the community bank level. Such a course would make it much more difficult for borrowers to obtain credit and inflict another blow on our economy. Importantly, driving community banks from the mortgage marketplace would be counterproductive as these lenders have been shown to be the most responsible underwriters and the best able to serve their borrowers and communities.

Additionally, because the Dodd/Frank Act requires that the QRM exclusion must not be broader than the safe harbor established by the Bureau of Consumer Financial Protection under Title XIV of the bill, it will be important to correctly calibrate the interaction of these two safe harbors. The safe harbor to be established by the Bureau will focus not on risk of loss associated with the loan, but on risks to the consumer. Both provisions will need to use underwriting criteria (which protect both borrower and lender) and loan product type as benchmarks. It is vitally important both for lender and servicer compliance and for borrower comprehension of eligibility criteria that these safe harbors are well crafted and that they interact in a rational manner. Therefore, we urge you to consult with the Bureau (and vice versa) as you and the Bureau begin crafting these regulations.

TOO NARROW A QRM DEFINITION IS INAPPROPRIATE FOR ENSUING PROPER UNDERWRITING AND SHOULD NOT BE IMPOSED TO ACHIEVE OTHER POLICY GOALS

ABA believes it is imperative that the QRM exclusion should provide a safe harbor for properly underwritten loans with a low risk of default – and that this includes the majority of loans being made by depository institutions today.

Isolated suggestions have come from some in the industry for a very narrow definition of QRM. ABA strongly believes that creating a narrow definition of QRM is an inappropriate method for achieving the desired underwriting reforms intended by Dodd/Frank. Similarly, narrowly defining QRM to achieve goals unrelated to the intended statutory purpose is equally inappropriate.

Those arguing for a narrow definition of QRM have proposed basing the definition on a very low loan-to-value (LTV) ratio. Certainly loans with lower LTVs are likely to have lower default rates, and we concur that this may be *one* of a number of characteristics to be considered. However, the LTV should not be the *only* characteristic for eligibility as a QRM, and it should not be considered in isolation. Setting the QRM cutoff at a specific LTV without regard to other loan characteristics or features, including documentation and ability-to-pay requirements, is likely to result in an overly broad restriction of credit. In addition, we believe the regulators should also consider risk retention features already in existence and that these features are currently being enhanced by changes in regulation and market practice.

Further, some of the arguments that QRM should be defined narrowly are *misdirected* because they appear to be motivated by concerns that the secondary mortgage market GSEs currently operating under conservatorship, or any successor, might somehow be able to manage the QRM to expand their market share. ABA believes this to be a legitimate concern, especially based on the past history of the GSEs. However, we note that Dodd-Frank explicitly excluded loans with FHA and VA guarantees from the requirements of Section 914, but did not include loans with GSE guarantees. Thus, it is clear that Congress did not intend the QRM exclusion to provide an exception from risk retention for loans based upon their eligibility for sale to the GSEs. ABA strongly believes that defining the QRM exclusion narrowly to severely restrict loans from purchase by the GSE and thereby reduce their activities is an inappropriate use of the QRM exclusion. Rather, GSE policy *must* be considered separately from the improved underwriting goals of risk retention.

The Administration is expected to propose a course of action for dealing with the on-going conservatorship of Fannie Mae and Freddie Mac in the near future. We expect proposals from the Administration and from Congress to share a common goal of shrinking the role of GSEs in supporting housing finance, replacing that function over time with largely private market alternatives. ABA supports such goals, and perhaps risk retention requirements now being debated will need to be reviewed in response to any changes brought about by reform of the GSEs. As stated above, however, ABA does not regard the QRM definition as an appropriate means to direct or influence the GSE debate.

CONCLUSION

The imposition of risk retention requirements to improve underwriting of mortgage loans is a significant change to the operation of the mortgage markets and must not be undertaken lightly. It is important that policymakers consider the intent of the statute, and not stray from that intent when implementing these requirements. Nor should the regulators disregard the impact that risk retention requirements will have on the housing market and the potential for constricting credit to homebuyers.

ABA stands ready to assist with any data or other assistance you may need in furthering this endeavor. Should you have any questions, please contact Robert R. Davis at 202-663-5588 or rdavis@aba.com, or Joseph Pigg at 202-663-5480 or jpigg@aba.com.

Sincerely,

Frank Keating