

Press Releases

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OTS 00-38 - OTS Begins Formal Inquiry Into Subprime Lending Practices

Office of Thrift Supervision

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OTS Begins Formal Inquiry Into Subprime Lending Practices

WASHINGTON, D.C., April 4, 2000 -The Office of Thrift Supervision (OTS) announced today it has begun a full-scale review of its mortgage lending regulations to determine how they impact the subprime market and issued an official appeal to the public for comment on how it should approach the issue. OTS is the first federal banking agency to formally address rising concern over predatory lending.

While OTS has regulatory jurisdiction and examination authority only over federally and state-chartered savings associations, under the 1982 Alternative Mortgage Transaction Parity Act certain lenders that OTS neither supervises nor examines may rely on OTS regulations rather than state law. OTS is concerned that market developments since 1982 may be inadvertently creating a situation in which OTS regulations, applied through the Parity Act, have encouraged predatory practices.

"Our basic regulatory interest is to further responsible lending, and we encourage thrifts to make safe and sound loans, both prime and sub-prime, in all markets including those suffering from credit drought," OTS Director Ellen Seidman said. "We also recognize that sub-prime loans entail higher risk and often necessitate higher cost or non-traditional terms, but we cannot condone egregious lending practices. If helping to curb such tactics means changing the agency's lending regulations, then we need to ascertain how best to do that without handicapping responsible lending, including safe and sound lending programs reaching out to under-served populations and communities."

Officially, OTS is issuing an advance notice of proposed rulemaking (ANPR) posing a series of questions about lending practices and seeking public input. Key issues include how extensive predatory lending in the home mortgage market may be and who exactly is doing it. OTS also is seeking suggestions as to whether it should reevaluate its approach to implementing the 1982 Parity Act. The ANPR will be published in the Federal Register Wednesday, and the comment period runs through July 5, 2000.

What concerns OTS and other federal and state regulators are lending practices such as pressuring borrowers into loan agreements they can't afford; convincing borrowers to consolidate their debts into a loan that is less advantageous; refinancing a low-interest mortgage loan to a loan with higher rates; charging borrowers excessive fees and then rolling the fees into the loan so the borrower, in effect, can't pay off the loan; and inducing borrowers

to sign up for unnecessary credit insurance. All are considered by regulators to be potentially predatory.

Although the agency's primary function is to safeguard the safety and soundness of thrifts, OTS's lending rules have an impact on the broader lending market through the Parity Act. The statute was enacted at a time of high interest rates to encourage variable rate mortgages and other creative financing to stimulate credit. It allows state-licensed and regulated housing creditors to engage in alternative mortgage transactions in conformity with certain federal lending regulations without regard to conflicting state law or regulation.

Ms. Seidman noted that North Carolina has recently enacted legislation addressing predatory lending, and New York has proposed regulations to impose certain limitations on high-cost loans. She added that OTS will continue to work with other federal regulators on a possible joint policy statement and other action to curb predatory lending. The agency also is interested in working with state regulators, as well.

In its public request for comments, OTS wants to find out, among other facts:

- how much activity involves onerous terms and targets under-served and financially unsophisticated markets;
- how widespread is the use of rates significantly above and terms substantially less favorable to borrowers than those of conventional prime mortgages to persons with good or excellent credit records;
- how much do housing creditors vary among themselves or from insured depository institutions in using prepayment penalties, financing prepaid credit life insurance or loan fees or the frequency of partial amortizing, non-amortizing or negative amortizing loans, and do variations relate to characteristics of the borrower that would be suspect under the Equal Credit Opportunity Act -such as race or age - or the neighborhood where the borrower lives; and
- do creditors refinance their own borrowers' mortgage loans at rates at or above those on the existing loan, and does this practice exist at insured depository institutions?

From a regulatory standpoint, OTS is asking if it should impose limits on fees, on refinancings and rollovers, prepayment penalties, balloon payments and other features of high-cost loans? Also, should OTS require some federal savings associations to notify it before making high-cost loans and how would such a requirement apply to state housing creditors?

Advance Notice Proposed Rulemaking Responsible Alternative Mortgage Lending - <http://www.occ.gov/static/news-issuances/ots/press-releases/ots-pr-2000-38a.pdf>

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The Office of Thrift Supervision (OTS), an office of the U.S. Treasury, regulates and supervises the nation's thrift industry. OTS's mission is to ensure the safety and soundness of thrift institutions and to support their role as home mortgage lenders and providers of other community credit and financial services. For copies of news releases or other documents visit the OTS web page at www.ots.treas.gov.