

December 3, 2007

The Honorable Ben S. Bernanke, Chairman
The Honorable Randall Kroszner, Governor
Jennifer J. Jackson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue
Washington, DC 20551

Dear Chairman Bernanke, Governor Kroszner, and Members of the Board:

We, the undersigned organizations and advocates, write to thank you for planning to use your rulemaking authority under HOEPA and to renew our request that you ban prepayment penalties in subprime mortgage loans, require escrows for taxes and insurance, require appropriate documentation for loans, and ensure that borrowers have the ability to repay their loans.

In particular, a rule prohibiting prepayment penalties would demonstrate that the Federal Reserve Board is serious about combating predatory lending and assisting families who have been steered into higher cost loans than those for which they qualify. While prepayment penalties are often defended as a tradeoff for borrowers who agree to the penalty in exchange for a lower interest rate, empirical evidence shows that in the subprime market there are no resulting rate discounts. Indeed, in many subprime loans, interest rates are *higher* on loans with prepayment penalties. This alarming fact is largely due to the relationship between prepayment penalties and yield-spread premiums; the prepayment penalty serves to lock borrowers into the higher-rate loans that result when lenders pay brokers additional compensation for placing borrowers into more expensive loans than those for which they qualify.

It is also extremely troubling that brokers disproportionately steer minority borrowers to subprime loans and especially subprime loans with prepayment penalties, which means that the increased risk of foreclosure associated with prepayment penalties falls most heavily on neighborhoods of color. Furthermore, while subprime mortgages are typically marketed as a way for borrowers with blemished credit to improve their credit scores and refinance into a loan with more favorable terms, the prepayment penalties prevent borrowers from doing so.

For these reasons, prepayment penalties in the subprime market create precisely the kind of structural market imperfection that meets the FTC's unfairness test. They are

inherently deceptive, and they cause significant and unavoidable harm to consumers that is not outweighed by any benefit either to consumers or to market competition.

Again, we thank you for the time and energy that you have put into exploring how to prevent predatory mortgage lending, and we look forward to a comprehensive and effective set of rules.

Sincerely,

American Federation of Labor and Congress of Industrial Organizations
Association of Community Organizations for Reform Now (ACORN)
Black Leadership Forum
Center for Responsible Lending
Central Illinois Organizing Project (CIOP)
Consumer Action
Consumer Federation of America
International Union, United Auto Workers
Lawyers' Committee for Civil Rights Under Law
Leadership Conference on Civil Rights
National Association of Consumer Advocates
National Consumer Law Center (on behalf of its low-income clients)
National Fair Housing
Opportunity Finance Network