

Office of Thrift Supervision

TB 53 was rescinded 1/13/95. Incorporated into Thrift Activities 212.

Handbook: Thrift Activities
Subject: Real Estate Mortgage Lending

Section: 212
TB 53

April 20, 1992

Qualification of Borrowers at Below Market Rates

RESCINDED

Summary: The OTS will generally treat as an unsafe and unsound practice the qualification of borrowers at below market rates (such as "teaser" or buydown rates) if the rates are significantly below the fully indexed mortgage rate as of the date of the commitment.

For Further Information Contact: Your Regional Office or Supervision Policy (Credit Risk), OTS, Washington, D.C.

Thrift Bulletin 53

Background

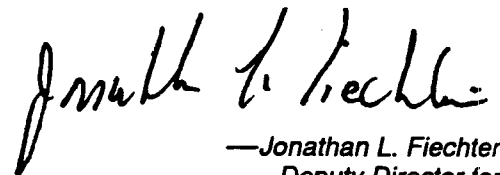
Some savings associations have qualified borrowers for home mortgage loans based on below market rates, such as initial "teaser" rates. "Teaser" rates are interest rates that are significantly below the fully indexed rates and that are effective for a short period of time. This includes situations where borrowers receive a short-term subsidy or "buy down"

of interest rates. Qualifying borrowers at these low temporary rates when it is expected that the interest rate on the mortgage loan (and monthly payments) will increase over the life of the loan is inconsistent with sound underwriting standards.

OTS is concerned about this use of a short-term, below market interest rate to qualify borrowers because of the potential for increased credit risk, particularly when the loan-to-value ratio exceeds 80%. Use of a below market rate for this purpose implicitly assumes that a borrower's ability to pay will rise at a rate at least equal to the annual increase in the loan payment.

General Policy

Qualification of borrowers at below market rates is an unsafe and unsound practice. Institutions should generally qualify borrowers at the fully indexed mortgage rate as of the date of commitment. An exception to this policy is when a thrift institution engages in a program of immediately selling such loans, without recourse, to non-thrift third parties, thereby removing the credit risk from its own portfolio.



—Jonathan L. Fiechter
Deputy Director for
Washington Operations