RESCINDED

Office of Thrift Supervision **October 2, 2002**

Department of the Treasury

Transmittal

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This rescission does not change the applicability of the conveyed document. To determine the applicability of the conveyed document, refer to the original issuer of the document.

The attached final rule regarding the Alternative Mortgage Transaction Parity Act; Preemption was published in the Federal Register on September 26, 2002.

conjunction with ISTC 4.3, 1995 Edition with the 1996 and 1997 Addenda, or ISTC–3600, 1998 Edition through the latest edition and addenda incorporated by reference in paragraph (b)(3) of this section. Licensees choosing to apply the Code Case shall apply all of its provisions.

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(iv) *Appendix II.* Licensees applying Appendix II, ''Check Valve Condition Monitoring Program,'' of the OM Code, 1995 Edition with the 1996 and 1997 Addenda, shall satisfy the requirements of paragraphs (b)(3)(iv)(A), (b)(3)(iv)(B), and (b)(3)(iv)(C) of this section. Licensees applying Appendix II, 1998 Edition through the latest edition and addenda incorporated by reference in paragraph (b)(3) of this section, shall satisfy the requirements of paragraphs (b)(3)(iv)(A), (b)(3)(iv)(B), and (b)(3)(iv)(D) of this section.

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(D) The provisions of ISTC–3510, ISTC–3520, and ISTC–3540 in addition to ISTC–5221 must be implemented if the Appendix II condition monitoring program is discontinued.

(v) *Subsection ISTD.* Article IWF–5000, ''Inservice Inspection Requirements for Snubbers,'' of the ASME BPV Code, Section XI, provides inservice inspection requirements for examinations and tests of snubbers at nuclear power plants. Licensees may use Subsection ISTD, ''Inservice Testing of Dynamic Restraints (Snubbers) in Light-Water Reactor Power Plants,'' ASME OM Code, 1995 Edition through the latest edition and addenda incorporated by reference in paragraph (b)(3) of this section, in place of the requirements for snubbers in Section XI, IWF–5200(a) and (b) and IWF–5300(a) and (b), by making appropriate changes to their technical specifications or licensee-controlled documents. Preservice and inservice examinations must be performed using the VT–3 visual examination method described in IWA–2213.

(vi) *Exercise interval for manual valves.* Manual valves must be exercised on a 2-year interval rather that the 5-year interval specified in paragraph ISTC–3540 of the 1999 Addenda through the latest edition and addenda incorporated by reference in paragraph (b)(3) of this section, provided that adverse conditions do not require more frequent testing.

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(g) * * *

(6) * * *

(ii) * * *

(B) Licensees do not have to submit to the NRC staff for approval of their containment inservice inspection programs which were developed to satisfy the requirements of Subsection IWE and Subsection IWL with specified modifications and limitations. The program elements and the required documentation must be maintained on site for audit.

(C) * * *

(*1*) Appendix VIII and the supplements to Appendix VIII to Section XI, Division 1, 1995 Edition with the 1996 Addenda of the ASME Boiler and Pressure Vessel Code must be implemented in accordance with the following schedule: Appendix VIII and Supplements 1, 2, 3, and 8—May 22, 2000; Supplements 4 and 6—November 22, 2000; Supplement 11—November 22, 2001; and Supplements 5, 7, and 10—November 22, 2002.

(*2*) Licensees implementing the 1989 Edition and earlier editions and addenda of IWA–2232 of Section XI, Division 1, of the ASME Boiler and Pressure Vessel Code must implement the 1995 Edition with the 1996 Addenda of Appendix VIII and the supplements to Appendix VIII of Section XI, Division 1, of the ASME Boiler and Pressure Vessel Code.

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Dated at Rockville, Maryland this 9th day of September 2002.

For the U.S. Nuclear Regulatory Commission.

William D. Travers,

Executive Director For Operations.

[FR Doc. 02–23811 Filed 9–25–02; 8:45 am]

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DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

12 CFR Parts 560, 590, and 591

[No. 2002–43]

RIN 1550–AB51

Alternative Mortgage Transaction Parity Act; Preemption

AGENCY: Office of Thrift Supervision, Treasury.

ACTION: Final rule.

SUMMARY: The Alternative Mortgage Transaction Parity Act (AMTPA) authorizes state chartered housing creditors to make, purchase, and enforce alternative mortgage transactions without regard to any state constitution, law, or regulation. To rely on AMTPA, certain state chartered housing creditors must comply with regulations on alternative mortgage transactions issued by the Office of Thrift Supervision (OTS). In today's rulemaking, OTS revises its rules identifying the OTS regulations that apply under AMTPA. OTS will no longer identify its regulations on prepayments and late charges for state chartered housing creditors.

OTS is also revising its limits on the amount of late charges that may be assessed on loans secured by first liens on residential manufactured homes under part 590, which addresses the preemption of state usury laws. In addition, OTS is making a minor technical change to the definition of reverse mortgage in part 591, which addresses the preemption of state due-on-sale laws.

EFFECTIVE DATE: January 1, 2003.

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SUPPLEMENTARY INFORMATION:

I. Alternative Mortgage Transaction Parity Act Regulations (§ 560.220)

The Alternative Mortgage Transaction Parity Act (AMTPA) [1] permits state chartered housing creditors [2] to make, purchase, and enforce alternative mortgage transactions if the creditors comply with regulations governing such transactions issued by federal regulators. AMTPA applies to loans with any alternative payment features that vary from conventional fixed-rate, fixed-term mortgage loans, such as variable rates, balloon payments, or call features. It allows state chartered housing creditors to engage in alternative mortgage transactions notwithstanding ''any State constitution, law, or regulation,'' provided the transactions are made in conformity with regulations issued by one of three federal regulators.[3] Housing creditors, other than state chartered commercial banks and state chartered

[1] 12 U.S.C. 3801 *et seq.*

[2] A ''housing creditor'' is a depository institution, a lender approved by the Secretary of Housing and Urban Development for participation in certain mortgage insurance programs, ''any person who regularly makes loans, credit sales or advances secured by interests in properties referred to in [AMTPA]; or * * * any transferee of any of them.'' To qualify as a state housing creditor and take advantage of preemption, AMTPA specifically provides that the creditor must be ''licensed under applicable State law and [remain or become] subject to the applicable regulatory requirements and enforcement mechanisms provided by State law.'' 12 U.S.C. 3802(2).

[3] 12 U.S.C. 3803(c).

credit unions, that wish to make an alternative mortgage transaction under the authority of AMTPA, must comply with OTS regulations. State chartered commercial banks and state chartered credit unions must comply with regulations of the Office of the Comptroller of the Currency (OCC) and the National Credit Union Administration (NCUA), respectively.[4]

AMTPA directed the Federal Home Loan Bank Board (Bank Board), OTS's predecessor agency, OCC, and NCUA to identify, describe, and publish those portions of their regulations that are inappropriate for, and thus inapplicable to, their respective state chartered housing creditors.[5] The identified regulations are enforced by each state housing creditor's applicable state regulator.

Currently, OTS's regulation at § 560.220 identifies the following regulations as appropriate for, and applicable to, state housing creditors:

- § 560.33. This reference permits state housing creditors to impose late charges for any delinquent periodic payment and sets out certain limitations on the assessment of such late charges.
- § 560.34. This reference permits state housing creditors to impose a prepayment penalty and indicates how prepayments must be applied.
- § 560.35. This section addresses adjustments to interest rate, adjustments to the payment and loan balance, and the use of indices.
- § 560.210. This reference requires state housing creditors to provide initial disclosures and adjustment notices for variable rate transactions.

Housing creditors must comply with these requirements to obtain the benefit of AMTPA's preemption of state laws. All other OTS regulations are inappropriate and inapplicable to state housing creditors.

On April 5, 2000, OTS published an advance notice of proposed rulemaking (ANPR) entitled ''Responsible Alternative Mortgage Lending.''[6] The ANPR sought public comment on various questions in connection with a review of mortgage lending regulations, including comments on possible amendments to § 560.220.

On April 25, 2002, OTS issued a notice of proposed rulemaking (NPRM).[7] OTS proposed to delete the late charge and prepayment rules (§§ 560.33 and 560.34) from the list of regulations that apply to state housing creditors under AMTPA. OTS proposed to continue to identify the other two rules (§§ 560.35 and 560.210) as appropriate and applicable for state housing creditors.

OTS received 298 comments on the proposed rule and 293 of these commenters addressed changes to AMTPA provisions. The commenters were equally divided between support and opposition for the rule. About three-quarters of the commenters filed one of five form letters.

A. OTS Authority Under AMTPA

1. Background

Congress enacted AMTPA in 1982 to stimulate credit in an unusually high interest rate environment by encouraging variable rate mortgages and other creative financing. In hearings before the Senate in 1981, mortgage bankers testified that statutes in 26 states barred state chartered mortgage bankers and lending institutions from originating alternative mortgage loans, or imposed significantly higher restrictions on such loans than applied to federally chartered lenders operating under federal regulations.

Congress incorporated this factual background at 12 U.S.C. 3801(a). Congress found that increasingly volatile and dynamic changes in interest rates had seriously impaired the ability of housing creditors to provide consumers with fixed-term, fixed-rate credit secured by interests in real property, and that alternative mortgage transactions were essential to an adequate supply of credit. AMTPA also noted that OCC, NCUA, and OTS had recognized the importance of alternative mortgage transactions and had adopted ''regulations authorizing federally chartered depository institutions to engage in alternative mortgage financing.'' AMTPA indicated that:

> It is the purpose of this chapter to eliminate the discriminatory impact that those regulations have upon nonfederally chartered housing creditors and provide them with parity with federally chartered institutions by authorizing all housing creditors to make, purchase, and enforce alternative mortgage transactions so long as the transactions are in conformity with the regulations issued by the Federal agencies. 12 U.S.C. 3801(b).

Section 3803(a) states that state housing creditors may comply with regulations governing alternative mortgage transactions issued by NCUA, OCC, or OTS. Section 807(b) of AMTPA directs the three federal regulators to identify, describe, and publish those portions or provisions of their respective regulations that are ''inappropriate for (and thus inapplicable to)'' nonfederally chartered housing creditors.

Apart from references to federal regulations governing alternative mortgage transactions and regulations authorizing federally chartered lenders to engage in alternative mortgage transactions, neither the statute nor the legislative history details how the three federal agencies are to exercise their authority under section 807(b). For example, AMTPA and the legislative history do not reference or provide examples of specific types of regulations that the agencies should identify for state housing creditors.

As a result of this inconclusive direction, OTS and the Bank Board have wrestled with the proper scope of the identification of regulations for state housing creditors under AMTPA. At times, the agency has taken a narrow view of AMTPA and its legislative history. For example, the Bank Board initially identified as appropriate and applicable only those regulations that ''describe and define'' alternative mortgage transactions and did not identify regulations intended for the general supervision of federal savings associations. As a result, the Bank Board declined to identify rules that applied to loans generally (as distinguished from rules that bear directly on the unique features of alternative mortgage loans).[8]

In 1996, however, OTS reviewed its AMTPA authority and identified two general lending rules—the prepayment and late charge provisions at issue in this rulemaking.[9] The apparent rationale, contained in a contemporaneous legal opinion, but not in the rulemaking, was the conclusion that state housing creditors would be ''disadvantaged vis-à-vis federal thrifts'' if they were required to comply with state laws restricting prepayment penalties and late charges.[10] Even the contemporaneous legal opinion, however, conceded that the state laws on these subjects fell somewhere between laws clearly preempted by AMTPA (state laws barring variable rate mortgage loan transactions) and laws clearly not preempted (state laws governing liens and foreclosures).

NCUA and OCC regulations also reflect various interpretations of the scope of section 807(b) of AMTPA. NCUA has interpreted section 807(b) to permit the identification of all of its lending regulations as applicable to alternative mortgage transactions by state chartered credit unions. These mortgage regulations address such matters as the term of the loan;

[4] 12 U.S.C. 3803(a).

[5] Section 807(b) of Pub. L. 97–320 (1982).

[6] 65 FR 17811 (Apr. 5, 2000).

[7] 67 FR 20468 (Apr. 25, 2002).

[8] 47 FR 51732 (Nov. 17, 1982) and 48 FR 23032, 23053 (May 23, 1983).

[9] 61 FR 50951 (Sept. 30, 1996).

[10] OTS Op. Chief Counsel (Apr. 30, 1996).

requirements governing security instruments, notes, and liens; due-on-sale provisions; and assumptions. NCUA rules specifically preempt state laws addressing certain areas. 12 CFR 701.21. OCC, on the other hand, has identified as applicable for state commercial banks a narrow band of rules. These rules: define adjustable rate mortgages (ARMs); state that ARMS may be made, sold, purchased, participated in, or otherwise dealt in without regard to any state law limitation on those activities; authorize certain indices; and specifically allow prepayment fees. 12 CFR part 34, subpart B.

As these various approaches illustrate, section 807(b) is susceptible to a number of interpretations. Each of the agencies has exercised broad discretion in its identification of appropriate regulations under AMTPA and has struck a different balance depending on its applicable statutory and regulatory scheme. Under the current rules, each of the three agencies has advanced a different interpretation of its responsibilities under section 807(b) of AMTPA.

2. OTS's Approach

In the NPRM, OTS reexamined its 1996 interpretation. OTS noted that the purpose of AMTPA was to enable all housing creditors to provide credit through alternative mortgages and to preempt state laws that would prevent that type of credit. OTS found that its regulations governing adjustments to the interest rate, adjustments to the payment and loan balance, the use of indices, initial disclosures, and adjustment notices were essential or intrinsic to the ability of state housing creditors to continue to provide alternative mortgage transactions. To provide parity with federal thrifts, OTS proposed to continue to identify §§ 560.35 and 560.210 for state housing creditors.

On the other hand, OTS tentatively noted, upon further reflection, that the prepayment and late fee provisions were not essential or intrinsic to the ability to offer alternative mortgages. Rather, these regulations apply to real estate lending in general and are part of the broader regulatory scheme governing the lending operations of thrifts. OTS noted that one of the congressional findings underlying AMTPA was that the various federal regulators had adopted regulations authorizing federal institutions to offer alternative mortgages, and that the purpose of AMTPA was to eliminate the discriminatory impact of those regulations. OTS tentatively found that its regulations on prepayments and late fees were not adopted to enable federal thrifts to engage in alternative mortgage financing, but rather to permit federal thrifts to operate safely and soundly under a uniform federal scheme. *See* 12 CFR 560.2(a). Therefore, OTS tentatively concluded that these regulations did not offer a basis for claiming discriminatory treatment or were not needed to provide parity with federally chartered institutions. Accordingly, OTS tentatively concluded that there was no basis to distinguish prepayment and late charge provisions from other general lending rules and proposed to delete the two provisions from the list of identified rules for state housing creditors. As we explain in this statement of supplementary information, after reviewing the comments and further considering the issues, OTS adopts these findings and conclusions.

3. Comments on OTS's Approach

Several commenters argued that if AMTPA is to be given its proper effect, state housing creditors should be governed by the same regulations that address alternative mortgage transactions by federal savings associations. According to commenters, these rules include § 560.2(a), which states OTS's intent to occupy the entire field of lending regulation for federal savings associations in preemption of state law, and § 560.2(b), which expressly preempts state laws that address such matters as private mortgage insurance requirements, loan-to-value ratios, terms of credit, loan-related fees (including late charges and prepayment penalties), access to credit reports, disclosures, and advertising laws.

OTS has never identified its preemption rules as applicable to state housing creditors under AMTPA. While commenters argued that the failure to apply these preemptive regulations would disadvantage state housing creditors vis-à-vis federal thrifts, OTS believes that this position would lead to an inappropriate result under its regulatory framework.

To enhance safety and soundness and to enable federal savings associations to conduct their operations in accordance with best practices, OTS has occupied the entire field of lending regulation for federal thrifts and has given federal savings associations the maximum flexibility to exercise their lending powers in accordance with a uniform federal scheme. *See* 12 CFR 560.2(a). This complex uniform regulatory scheme benefits federal thrifts by preempting most state laws that otherwise would impose on federal savings associations different regulatory requirements from state-to-state. The system, however, also imposes various obligations on federal savings associations. For example, thrifts must comply with an array of regulatory limitations designed to ensure that their mortgage lending operations are conducted in a safe and sound manner. These limitations include appraisal requirements, real estate lending standards, underwriting guidelines, limits on loans to one borrower, and documentation requirements. Thrifts are also subject to regular examination, supervision, and enforcement of their lending activities.

OTS does not believe that it may impose these concomitant obligations on state housing creditors in this rulemaking given the instructions in the legislative history that it was not Congress' intent to place state housing creditors under the supervision of the federal agencies.[11] However, preemption under § 560.2, without the application of the related duties, would lead to an unreasonable regulatory result, *i.e.*, the perverse situation where state housing creditors could engage in mortgage lending—an area that is traditionally highly regulated—unfettered by most state or federal restrictions, thereby creating a regulatory vacuum. Accordingly, OTS declines to identify its preemption rules as applicable to state housing creditors.

Other general lending rules, such as §§ 560.33 and 560.34, are also a part of the broader regulatory scheme governing OTS supervision of the lending operations of federal thrifts. The states have, to a greater or lesser degree, adopted laws and regulations similarly designed to supervise the lending operations of state housing creditors. States that restrict prepayment penalties and late charges usually apply those restrictions to all real estate loans, not just to alternative mortgage transactions. As a result, the state laws in these areas are not directed at restricting alternative mortgage transactions, but in regulating mortgage transactions in general. OTS is reluctant to encroach upon this state authority, given the cited statutory direction and the statements of legislative intent.

For these reasons, OTS declines to identify its rules preempting state lending regulations or any other rule

[11] Sen. Rep. 97–463, at 55 (1982). This interpretation is also contrary to other expressions of congressional intent, which left room for state action by specifically reserving specific areas to the states. 12 U.S.C. 3802(2), for example, indicates that state housing creditors must comply with applicable state licensing requirements and must remain or become subject to the applicable regulatory requirements and enforcement mechanisms provided by state law.

that applies to real estate lending in general. Rather, OTS will identify only those regulations that OTS deems to be intrinsic to the ability to offer alternative loans.[12]

A number of commenters alleged that this interpretation of AMTPA would subject state housing creditors to state laws on prepayments and late charges while federal thrifts would remain subject to more permissive OTS regulations in these areas. As a result, these commenters argued that the proposed rule is inconsistent with the twin purposes of AMTPA—the elimination of discriminatory impact that federal regulations have on state housing creditors and the promotion of parity for state housing creditors. Specifically, commenters speculated that the proposed rule would discriminate against state housing creditors vis-à-vis federal savings associations in the following ways:

- Limit the range of products offered by state housing creditors. Some state housing creditors would no longer be able to offer lower rates to consumers who agree to take a loan with a prepayment penalty. In addition, restrictions on late charges would deny lenders flexibility in loan pricing and prohibit lenders from placing the cost of late payments on delinquent borrowers.
- Increase compliance costs, risk of document error, and litigation risk. Rather than complying with uniform OTS rules, creditors with multi-state operations would have to comply with inconsistent state and local laws.
- Reduce the ability to minimize prepayment risk. Prepayment penalties protect state housing creditors (and secondary market purchasers) from extreme changes in their portfolios.
- Reduce the value of their loans in the secondary market. Investors will be less able to protect against prepayment risk, and will incur additional due diligence costs (and risks) to review pools against widely varying state law. These costs will be passed on to state housing creditors. The secondary market also may have to create separate pools for federally chartered lenders and state chartered lenders to accommodate these differences.

Commenters also speculated that some lenders may choose not to offer alternative mortgage transactions in jurisdictions with restrictive laws, may cease all lending operations within those jurisdictions, or exit the industry entirely. This reduced competition, they argue, would reduce the availability of affordable credit to consumers contrary to the goals of AMTPA.

Contrary to commenters' speculation, historical evidence indicates that the final rule should not have a significant detrimental effect on state housing creditors' ability to compete against federal thrifts in the alternative mortgage market. State housing creditors functioned for 14 years (1982–1996) without applying OTS regulations on late charges and prepayments. While various prepayment regulations were applicable during this period, federal thrifts were relatively free to impose prepayment penalties since 1983.[13] Additionally, the regulations on late charges have not changed substantially during this period, other than to eliminate limitations on the amount of the late charge.[14] Accordingly, OTS has concluded that these provisions are not essential for parity.

OTS also notes that state housing creditors were vigorous competitors in mortgage lending throughout this time period. While relative market share in the alternative mortgage market is not available, OTS does have information regarding the relative participation in the one- to four-family mortgage market. In 1982, commercial banks and thrifts dominated this market by originating approximately 66.0 percent of one- to four-family mortgages. Mortgage companies' market share was significantly smaller at 28.9 percent of the market. By 1996, when OTS changed its AMTPA rules, these positions had reversed with mortgage companies originating 56.8 percent and commercial banks and thrifts originating 42.5 percent of all one- to four-family mortgages.[15]

Moreover, it is not clear that Congress viewed prepayment penalties and late charges as essential to parity. Neither AMTPA nor its legislative history provides any useful guidance concerning this issue. However, if Congress had viewed these provisions as essential to parity, it is unlikely that Congress would have adopted the statutory scheme found in AMTPA. As noted above, AMTPA does not place all state housing creditors within the jurisdiction of one federal regulator, but assigns state housing creditors to three federal agencies in a way that "recogniz[es] traditional industry lines."[16] When AMTPA was enacted, however, NCUA, OCC, and the Bank Board had different requirements regarding prepayment penalties. Congress banned federal credit unions from imposing prepayment penalties, which suggests that, at least for credit unions, Congress recognized that prepayment penalties were not essential to the ability to make, purchase, or enforce alternative mortgage transactions.[17] OCC regulations, on the other hand, permitted national banks to impose prepayment penalties on ARMs until 30 days prior to the first scheduled interest rate adjustment date.[18] Bank Board regulations permitted federal savings associations to impose prepayment penalties on alternative mortgage transactions under other limited circumstances.[19] If Congress had

[12] One commenter warned that this focus could undermine the broad preemption available for federal thrifts, *i.e.*, that state law may be preempted for federal thrifts only when preemption is "intrinsic" to the effectuation of a federal policy or goal. Other commenters sought assurance that the final rule would not erode or impair the scope of preemption available to, or the lending powers of, federal savings associations under the Home Owners' Loan Act (HOLA). This rule addresses OTS authority to identify rules for state housing creditors under AMTPA and has no impact on preemption available to, or the lending powers of, federal thrifts under the HOLA. The preemption principles under the HOLA are well settled. *See e.g.*, 12 CFR 545.2, 557.11, and 560.2; and OTS Op. Chief Counsel (Nov. 22, 1999).

[13] Until May 23, 1983, federal savings associations were permitted to impose prepayment penalties under limited circumstances. *See* 12 CFR 545.8–5(b) (1983) summarized below at note 19. On May 23, 1983, the Bank Board changed this rule to permit a federal savings association to impose prepayment penalties as provided in the loan contract. Penalties on loans secured by owner-occupied homes, however, were prohibited for a 90-day period following the issuance of a notice of adjustment of interest rate, payment balance, or term to maturity. 12 CFR 545.34(c) (1984). In 1993, OTS removed even these limited restrictions and allowed federal thrifts to impose prepayment penalties at any time and in any amount authorized in the loan contract for both adjustable rate and fixed rate loans. 58 FR 4308 (Jan. 14, 1993). This rule is now codified at 12 CFR 560.34 (2002).

[14] *Compare* 12 CFR 545.8–3(e) (1983) with 12 CFR 560.33 (2002).

[15] This information was obtained on the Mortgage Bankers' Association's Web site, which indicates that its source was a HUD Survey of Mortgage Lending Activity discontinued in 1998. OTS notes that at least one commenter asserts that state housing creditors now originate approximately 80 percent of all mortgages.

[16] Sen. Rep. 97–463, at 55 (1982).

[17] 12 U.S.C. 1757(5)(A)(viii) (1982).

[18] 12 CFR 29.6 (1983). Shortly after AMTPA was enacted, OCC revised this rule to permit prepayment fees without regard to the first scheduled interest rate adjustment. 48 FR 28970 (June 24, 1983).

[19] 12 CFR 545.8–5(b) (1983) provided: "a borrower on a loan secured by a home or combination of home and business property may prepay the loan without penalty unless the loan contract expressly provides for all of the following: (1) A prepayment penalty, (2) an interest rate that, after loan closing and after any interest-rate adjustment, remains fixed for a period of at least five years, and (3) only such increases in the loan balance as result from the deferral and capitalization of interest pursuant to § 545.6–2(a)(2)(iv) of this part. The prepayment penalty for a loan secured by a home or combination of home and business property shall not be more than six months' advance interest on that part of the aggregate amount of all prepayments made on such loan in any 12-month period which exceeds 20

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viewed the regulation of prepayment penalties as essential to parity, it is unlikely that Congress would have imposed a regulatory scheme that, at the time of enactment, ensured different treatment among the various state creditors.

The agencies also took different approaches to the regulation of late charges in 1982. The Bank Board limited the amount of late charges, prescribed a minimum grace period, and set other restrictions for loans made on the security of a home occupied or to be occupied by the borrower.[20] By contrast, NCUA rules on alternative mortgage lending did not specifically address late fees, although a federal credit union was permitted by statute to levy late charges in accordance with its by-laws for failure of a member to meet promptly its obligations.[21] OCC's ARM rule also did not specifically address late charges.

The federal regulators continue to have divergent policies regarding prepayment penalties and late charges under AMTPA. For example, OCC has promulgated a prepayment provision that applies only to ARM lending. This rule permits national banks to impose prepayment fees in connection with ARM loans notwithstanding contrary state laws. OCC applies this rule to state chartered commercial banks under AMTPA.[22] NCUA's statute, on the other hand, continues to bar federal credit unions from imposing prepayment fees on any loan. 12 U.S.C. 1757(5)(A)(viii). NCUA identifies its regulation implementing this ban and its regulation preempting state laws on prepayment limits for state chartered credit unions under AMTPA.[23]

OTS notes that absolute competitive equality is simply not attainable through any unilateral OTS action in this rulemaking. While commenters argued that this rule would have a detrimental impact on the ability of state housing creditors to compete, state housing creditors have had, and will continue to have, a competitive advantage over federal depository institutions in other areas. Unlike national banks, federal credit unions, and federal savings associations, state housing creditors are not required to follow federal regulations for any particular transaction. If a state housing creditor makes an alternative mortgage transaction in a state that has a more favorable regulatory environment, it may elect to ignore the federal regulations and comply with appropriate state laws. Federally chartered institutions have only one choice of law.

OTS also notes that the 1996 rulemaking may have introduced other new inequalities into the alternative mortgage market by giving state housing creditors within OTS's jurisdiction a competitive advantage over depository institution competitors. For example, these state housing creditors may have gained an edge over state credit unions using AMTPA and federal credit unions, which are precluded from imposing prepayment fees. Moreover, while the 1996 rule permitted these state housing creditors to impose prepayment penalties to the same extent as national banks and federal savings associations, these depository institutions may have been disadvantaged since they remained subject to various federal restrictions on their ability to compete freely in the alternative mortgage market.[24] These same restrictions do not apply to non-depository institution state housing creditors.

Thus, given the statutory scheme underlying AMTPA, complete competitive parity is impossible. Within this imperfect system, however, OTS has attempted to appropriately identify those regulations necessary for making alternative mortgages.

Commenters also speculated that the final rule would have a significant negative impact on the availability of affordable credit to borrowers. In AMTPA, Congress found that "alternative mortgage transactions are essential to the provision of an adequate supply of credit secured by residential property necessary to meet the [expected] demand * * *" 12 U.S.C. 3801(a)(2). This goal has been accomplished through AMTPA and other innovations in the mortgage market. In 1982, the mortgage industry relied on fixed-rate, fixed-term mortgage instruments that lenders, primarily depository institutions, funded through relatively short-term deposits. AMTPA addressed one side of this equation by increasing the availability of alternative mortgage transactions from state housing creditors.[25] the other side of the equation—the liquidity of the mortgage market " has been enhanced through the government sponsored entities that fostered the creation of government-guaranteed mortgage-backed securities and through the emergence of private mortgage-backed securitization channels. Widespread securitization began in the 1980's and lenders now routinely originate loans for sale in the secondary market. The constant flow of money into the home mortgage market has dramatically altered the business of mortgage lending, significantly reducing liquidity issues for banks, thrifts, and other lenders. Securitization has also created opportunities for non-depository institutions. Lenders no longer need to be financial institutions with significant deposits and capitalization. Instead, thinly capitalized creditors can originate loans for sale on the secondary market.[26] As a result of these innovations, mortgage credit of all types is widely available and should not be significantly affected by this final rule.

Commenters also claimed that the proposed rule conflicts with the decisions in *National Home Equity Mortgage Ass'n* v. *Face,* 239 F.3d 633 (4th Cir. 2001); and *Shinn* v. *Encore Mortgage Services Inc.,* 96 F.Supp.2d 419 (D.N.J. 2000). Commenters noted that *Face* and *Shinn* held that state housing creditors within OTS jurisdiction may charge prepayment fees under § 560.34, notwithstanding any restrictions in state law.

OTS's analysis is consistent with these two decisions. In the *Face* case, the United States Court of Appeals for the Fourth Circuit held that non-federally chartered housing creditors could elect to have alternative mortgage transactions governed by OTS regulations on prepayment fees because OTS had identified its prepayment fee regulation as applicable to alternative mortgage transactions. The court explained as follows:

> The particular issue presented in this case is whether a non-federally chartered institution in Virginia may require and enforce a prepayment fee in a mortgage agreement notwithstanding Virginia's limitation on prepayment penalties as contained in Virginia Code §§ 6.1–330.83 and 6.1–330.85. *The resolution of this issue depends on whether the OTS has issued regulations authorizing prepayment fees as part of its regulations for alternative mortgage transactions,* because if it has authorized the collection of prepayment fees

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percent of the original principal amount of the loan."

[20] 12 CFR 545.8–3(d) and (e) (1983).

[21] 12 CFR 701.21–6 and 701.21–6B, 12 U.S.C. 1757(10) (1982).

[22] 12 CFR 34.23 and 34.24.

[23] 12 CFR 701.21(a) and (b).

[24] These restrictions include restrictions on loans to one borrower, real estate lending standards governing such matters as loans-to-value ratios and underwriting standards, and appraisal requirements.

[25] The Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) also facilitated new mortgage products by extending the variable rate ceiling for national banks to all federally insured banks and thrifts (12 U.S.C. 85, 1463(g), 1785(g), 1831d(a)), and by providing for the preemption of state usury ceilings on "interest, discount points, finance charges and other charges" for loans secured by first mortgages on borrowers' homes. 12 U.S.C. 1735f-7a. *See* Kathleen C. Engel & Patricia A. McCoy, A Tale of Three Markets: The Law and Economics of Predatory Lending, 80 Tex. L. Rev. 1255, 1275 (May 2002).

[26] *Id.* at 1273–74.

in alternative mortgage transactions, then Virginia may not apply its law proscribing such prepayment fees if the non-federally chartered housing creditor has otherwise complied with the requirements of the Parity Act.

239 F.3d at 638 (emphasis added). In short, the Court's ruling correctly rested on whether OTS had designated its prepayment fee regulation as applicable to alternative mortgage transactions. Under this analysis, if OTS did not so designate the prepayment fee regulation, then that regulation would not apply to alternative mortgage transactions, and non-federally chartered housing lenders would be subjected to state laws concerning prepayment fees.

Shinn addressed the limited issue of whether OTS acted reasonably and within the scope of its authority when it identified the prepayment provisions for alternative mortgage transactions under AMTPA. The *Shinn* case held that OTS rules reflected ''a permissible interpretation of the congressional authority vested in OTS'' under AMTPA.[27] The *Shinn* ruling does not preclude a different interpretation by the agency under AMTPA.

Accordingly, the removal of the prepayment and late charge rules from its list of identified regulations for state housing creditors is consistent with OTS's authority under AMTPA.

B. Impact on Predatory Lending

Commenters opposing the rule asserted that OTS initiated the proposed rule to respond to allegations that state housing creditors use the AMTPA regulations to avoid state consumer protection laws governing prepayments and late charges and to engage in abusive lending practices. These commenters argued that the proposed rule would do little to address predatory lending. They noted that no single loan term or practice is the hallmark of a predatory loan and that prepayment penalties and late fees are not inherently predatory. These commenters observed that non-predatory loans often provide for prepayment penalties or late fees and that, under certain circumstances, these terms can make it more difficult for lenders to engage in certain types of predatory lending, such as loan flipping.

Other commenters, however, indicate that two key indicia of predatory lending are prepayment penalties and late charges.[28] Prepayment penalties may inhibit the borrower's ability to refinance his or her loan at a lower rate. Prepayment penalties in sub-prime loans also function as deferred fees. Commenters indicated that over one-half of all sub-prime loans with prepayment penalties are eventually paid off with a penalty. These penalties typically are 5–7 percent of the loan amount.

Lenders may also impose excessive charges for untimely payments. Some alternative mortgage transactions regularly call for late fees of up to 10 percent of the monthly payment. Many states limit late fees to 4–5 percent of the payment amount.

Commenters opposing the proposed rule also argued that OTS cited no hard evidence indicating that prepayment penalties or late fees are subject to abuse under AMTPA regulations. Indeed, one commenter, a trade association representing a substantial segment of the real estate financing community, including national and regional lenders, mortgage brokers, mortgage conduits, and service providers, reported that it is unaware of any comprehensive report demonstrating that AMTPA rules are used to defraud or abuse customers. These commenters asserted that the anecdotal information provided in support of the ANPR is inadequate and that OTS should not proceed with this rule until it gains a more thorough understanding.

Because OTS does not directly regulate state housing creditors, it cannot collect information on state housing creditors that take advantage of AMTPA. OTS has found no comprehensive data available addressing this issue. However, as discussed below, the data sources cited and additional data submitted by commenters suggest that unregulated prepayment penalties and late charges may be subject to abuse.

1. A joint report issued by the Department of Housing and Urban Development (HUD) and the Department of the Treasury found that prepayment penalties in high cost loans can inhibit borrowers from refinancing at lower rates when their credit improves.[29]

2. Prepayment penalties are becoming more common in sub-prime loans. One commenter estimated that the frequency of prepayment penalties in sub-prime loans was 10 percent in 1995. Yet the HUD/Treasury Report indicates that four years later approximately 70 to 76 percent of sub-prime mortgage originations carried prepayment penalties.[30] Several commenters cited data from nationally recognized statistical rating agencies confirming the HUD/Treasury Report estimate. By contrast, between 1 and 2 percent of prime borrowers currently are subject to such penalties.[31]

3. Various commenters provided data to demonstrate the extent to which prepayment penalties and late charges are used in predatory lending. Although OTS has not independently verified the accuracy of this information, commenters included the following data. One commenter, a national representative of community reinvestment groups, sampled 30 loans drawn from its rescue fund files. The commenter found that the vast majority of the loans were high cost loans with burdensome monthly payments that consumed unreasonable portions of borrower income and included prepayment penalties. The commenter observed that a significant portion of the loans also had high late fees of 10 percent of the overdue payment. To expand their sample, the commenter reviewed two prospectus statements for loan securitizations by major sub-prime lenders available on the SEC's Web site and concluded that over 80 percent of the loans in the pools had prepayment penalties. In addition, the commenter suggested that high delinquency rates showed a failure to adequately document borrower income levels and pricing inefficiencies. Numerous commenters offered anecdotal information of predatory lending in their communities, including practices directed at minorities and the elderly. For example, one fair housing center indicated that it had 417 predatory lending cases in 2001 and that all of the loans in these cases included a prepayment penalty for a period of at least five years. Ninety-seven percent of these cases involved ARMs.

The above information leads to the reasonable conclusion that sub-prime

[27] 96 F. Supp. 2d at 425.

[28] A national representative of community reinvestment groups provided this information based on data obtained from its consumer rescue fund. The fund provides prime rate refinance loans for victims of predatory lending.

[29] The Joint HUD/Treasury Report on Recommendations to Curb Predatory Home Mortgage Lending (Apr. 20, 2000) (HUD/Treasury Report) at 94.

[30] *Id.* at 93.

[31] *Id.* As noted elsewhere in this document, some commenters argued that creditors often offer lower rates in return for prepayment penalties. Other commenters disputed the notion that sub-prime borrowers freely accept prepayment penalties as a means to lower their interest rates. These commenters noted that the vast majority of sub-prime applicants are never offered one rate without a prepayment penalty and a lower rate with a penalty. Even if these offers were made, commenters alleged that interest rates on sub-prime loans are not standardized and it is extremely difficult to comparison shop. Commenters further argued that it is implausible that sub-prime borrowers choose prepayment penalties such a high percentage of the time and prime borrowers do so only 2 percent of the time, particularly if one is describing a market that is driven by price competition.

lenders often include prepayment penalties in sub-prime loans. OTS recognizes that there is some disagreement as to the extent that prepayment penalties may affect a borrower's ability or willingness to refinance. It is reported that one unidentified study found that sub-prime loans with prepayment penalties are prepaid at about 90 percent of the rate of sub-prime loans without prepayment penalties.[32] Nevertheless, common sense dictates that the existence of a prepayment penalty may well inhibit a borrower from refinancing his or her loan, which can be problematic where a good payment history may allow the borrower to graduate to a lower cost loan.[33] Equally important, prepayment penalties may also be problematic in the sub-prime market where a borrower may be forced to refinance on less favorable terms in order to avoid default.[34] Indeed, those circumstances may account for the prepayment of many sub-prime loans. Additionally, the cost of the prepayment penalty may be refinanced in the new loan balance, which drives up the overall price of the loan to the borrower. High penalties that are repeatedly financed into the cost of successive loans may be used by lenders to strip borrowers' equity in the home.[35]

In short, OTS can properly conclude that the wide-spread use of prepayment penalties not only may deter consumers from seeking to refinance high cost loans that have burdensome provisions, but also may have other adverse consequences for sub-prime borrowers, such as increasing the overall lending cost for a consumer who refinances to avoid default.

OTS believes that laws on prepayment penalties and late charges are a key component in states' regulation of predatory lending. Because these laws reflect each state legislature's judgment, after due consideration, about appropriate consumer protections applicable to state chartered lenders, OTS will not construe its authority under AMTPA to frustrate these state efforts where another less intrusive construction of AMTPA is permissible.

C. Scope of Preemption Under AMTPA

One commenter requested OTS to specifically state that creditors offering mortgages under AMTPA must comply with *all* state laws relating to alternative mortgages, except those that expressly conflict with regulations identified by OTS.

AMTPA provides little explicit guidance regarding the types of state laws that Congress intended to preempt. A few conclusions, however, may be drawn. AMTPA preempts state laws that would ban a state housing creditor from entering into an alternative mortgage (*e.g.*, a law that bars variable rate loans). Similarly, state laws that conflict, or are inconsistent, with identified OTS regulations would be preempted. Because OTS is no longer identifying its regulations on prepayment penalties and late charges, state laws addressing prepayments or late charges generally would not be preempted by AMTPA.[36]

D. Alternatives, Modifications, and Clarifications

Commenters addressed the following alternatives, modifications, and clarifications of the proposed rule.

1. Modify Regulations Applicable to Federal Thrifts

As an alternative to the proposed rule, a number of commenters urged OTS to revise §§ 560.33 and 560.34. Commenters urged OTS to impose reasonable limitations on prepayment penalties and late charges by federal thrifts and apply these limitations to state housing creditors under AMTPA. Commenters suggested: (1) Banning prepayment penalties and late charges on all mortgage transactions or on high-cost alternative mortgage transactions; (2) Permitting prepayment penalties only during the first two years after origination of the alternative mortgage transaction; (3) Restricting the amount of prepayment penalties; and (4) Requiring a lender that wishes to impose a prepayment penalty to demonstrate that it has offered the customer a loan with a prepayment penalty and an identical loan (at a lower rate) without a prepayment penalty.

OTS declines to adopt any of these alternatives. OTS oversight and review of federal savings associations have not revealed a level of abusive practices that would warrant industry-wide regulation. Rather, OTS believes that the current prepayment and late charge regulations, when combined with the OTS comprehensive regime of regular examination and supervision of the lending activities of federal savings associations and its related enforcement activities, are adequate to address the operations of federal thrifts and to discourage their participation in predatory practices. In light of these factors, OTS is disinclined to impose new regulatory burdens on the federal savings associations within its jurisdiction.

Additionally, OTS notes that the suggested changes, to the extent they would regulate the operations of federal savings associations, fall beyond the scope of the proposed rule and would require additional public comment under the Administrative Procedure Act. 5 U.S.C. 553.

2. Apply §§ 560.33 and 560.34 to State Savings Associations

AMTPA requires OTS to identify regulations for state housing creditors, which includes both depository institutions and non-depository institutions. By contrast, OCC and NCUA regulations apply only to depository institutions (*i.e.*, state chartered commercial banks and credit unions). The NPRM noted that state savings associations are subject to a safety and soundness regulatory scheme that is similar to the regulation of federal thrifts and substantially different from other state housing creditors. On this basis, OTS asked whether it should treat state chartered savings associations differently under AMTPA. OTS also asked whether AMTPA authorizes the agency to differentiate between state housing creditors on this basis.

The NPRM also noted that §§ 560.33 and 560.34 could be viewed as safety and soundness-based regulations. For example, § 560.34 permits federal thrifts to moderate prepayment risk through the assessment of prepayment penalties. Similarly, § 560.33 allows federal savings associations to encourage the timely payment of loans and to recover costs associated with late payment. Accordingly, OTS asked whether it was appropriate to apply these rules to some or all mortgage transactions by state chartered housing lenders that are depository institutions.

[32] HUD/Treasury Report *supra* note 29, at 94.

[33] *Id.*

[34] Engel & McCoy, *supra* note 25, at 1285.

[35] HUD/Treasury Report *supra* note 29, at 73–75, 94. The practice of repeated refinancing of a mortgage loan within a short time period with little or no benefit to the borrower is referred to as loan flipping. Loan flipping typically occurs when a borrower is unable to meet scheduled payments or repeatedly consolidates other unsecured debts into a new home-secured loan at the urging of a lender. In addition to the origination fees, each refinancing may trigger prepayment fees. Such fees may be refinanced as a part of the total loan amount and ultimately strip borrowers' equity out of the borrower's home. *Id.*

[36] The OTS April 30, 1996 legal opinion stated that AMTPA would preempt a state law *even in the absence of a designated OTS regulation,* if state housing creditors would be disadvantaged. Based on these statements, the commenter asserted that state laws addressing prepayment penalties would continue to be preempted even if OTS no longer designated §§ 560.33 and 560.34 as applicable. As noted above, OTS reviewed its prior position and, after further consideration, concluded that prepayment penalties and late charges are not essential to parity; that state housing creditors would not be disadvantaged within the meaning of AMTPA if state laws on these subjects applied to their loans; and that state laws on these subjects are not preempted.

Commenters supporting this alternative observed that federal laws governing state and federal savings associations have become more similar since 1989 and that OTS has increasingly applied many federal thrift operational and supervisory regulations to state savings associations. Commenters also remarked that state and federal savings associations pursue similar strategies within a similar corporate and regulatory structure. As a result, the lending authority of these two types of depository institutions should be similar. Commenters also asserted that state savings associations were less likely to engage in predatory practices than unregulated lenders and mortgage brokers.

OTS is authorized under the HOLA to provide for the examination, safe and sound operation, and regulation of federal and state savings associations, and to issue appropriate regulations addressing these subjects. 12 U.S.C. 1462a(b)(2), 1463(a) and 1464(a).[37] However, state savings associations are also creatures of state law. States have responsibility for addressing safety and soundness, as well as legislating consumer protection for their citizens. OTS rules must strike a reasonable regulatory balance to permit the dual banking system to operate. Many state laws permit state chartered institutions to comply with laws and regulations governing federally chartered institutions as an alternative to state regulation. OTS believes that this choice should remain within state discretion and that state thrifts should be required to comply with state law, except where federal regulation is necessary.[38]

At this point, OTS has concluded that AMTPA does not permit it to distinguish between state chartered savings associations and other state housing creditors. AMTPA states that transactions by all state housing creditors, other than banks and credit unions, must be made in accordance with regulations governing alternative mortgage transactions issued by OTS. 12 U.S.C. 3803(a). While the statute indicates that state housing creditors include savings and loan associations, mutual savings banks, and savings banks, nothing in AMTPA or its legislative history permits OTS to identify different regulations for state housing creditors that are depository institutions. Accordingly, OTS has concluded that AMTPA does not permit the proposed distinction.

OTS, however, will continue to review the impact of these changes on state chartered savings associations and will consider suggestions from interested persons as to whether additional changes are permissible and necessary. If appropriate, OTS may address this matter in a separate rulemaking at some future date.

3. Definition of Alternative Mortgage Transaction

AMTPA defines an alternative mortgage transaction as a loan or credit sale secured by an interest in residential real property—

(A) in which the interest rate or finance charge may be adjusted or renegotiated;
(B) involving a fixed-rate, but which implicitly permits rate adjustments by having the debt mature at the end of an interval shorter than the term of the amortization schedule; or
(C) involving any similar type of rate, method of determining return, term, repayment, or other variation not common to traditional fixed-rate, fixed-term transactions, including without limitation, transactions that involve the sharing of equity or appreciation;
described and defined by applicable regulation * * * .[39]

Thus, AMTPA applies to all manner of mortgage instruments that do not conform to the traditional fully-amortized, fixed-interest rate mortgage loan. OTS rules adopt this statutory definition without elaboration.[40]

Several commenters requested OTS to clarify whether loans with certain terms are alternative mortgage transactions under OTS rules. Specifically, commenters seek clarification regarding the following loan terms:

- Interest rates that reduce if the borrower pays on time. OTS has opined that loans that permit rate adjustments to reflect a borrowers' actual payment performance can be alternative mortgage transactions under paragraph (A) or (C) of the definition.[41]
- Balloon payments. To the extent that a loan has a fixed rate, but permits rate adjustments by having the debt mature at the end of an interval shorter than the term of the amortization schedule (*e.g.*, a balloon loan), a loan may be an alternative mortgage transaction under paragraph (B).[42]
- Shared appreciation. Shared appreciation loans are specifically included in the definition at paragraph (C) and can be an alternative mortgage transaction.
- Prepayment penalties and late charges. While prepayment penalties and late fees may affect a creditor's rate of return on a loan, conventional prepayment penalties and late charges are ''common to traditional fixed-rate, fixed-term transactions'' and do not transform a fixed-rate, fixed-term loan into an alternative mortgage transaction.
- Negative amortization. Some mortgages, such as ARMs and graduated payment loans, are designed to negatively amortize or have the potential to negatively amortize, in the absence of delinquency or default. OTS believes that these transactions are alternative mortgages under AMTPA.

Several commenters asked whether loans with interest rates that adjust insignificantly or within a very narrow range would fall within the definition of an alternative mortgage transaction. The AMTPA definition does not expressly require a loan to adjust by a minimum amount before it may be considered to be an alternative mortgage transaction. However, creditors issuing loans that are alternative in form, but not substance, solely to obtain the benefits of preemption, assume the risk that the loans may not be found to be alternative mortgage transactions within the AMTPA definition.

4. Definition of State Housing Creditor

One commenter cautioned that certain statements in the NPRM were misleading to the extent they indicated that a housing creditor must hold a state license to be eligible to make a loan under AMTPA. The commenter observed that state laws exempt certain creditors from state licensing obligations. AMTPA does not unconditionally require a housing

[37] While OTS has authority to apply these two regulations to state chartered savings associations, it has no authority under the HOLA over state savings banks. Therefore, OTS's application of these rules to state chartered savings associations would still result in disparate treatment for one type of depository institution, state chartered savings banks.

[38] Most states addressing the area have restricted the imposition of prepayment penalties, rather than imposed outright prohibitions against all such penalties for alternative mortgages. OTS is not aware of any state that prohibits all late charges. This illustrates that each state has weighed and struck its own balance regarding the regulation of state housing creditors and the protection of state consumers.

[39] 12 U.S.C. 3802(1).

[40] The current regulation at 12 CFR 560.220 includes a specific cross-reference to the statutory definition, but the proposed rule text did not. To clarify this point, OTS has revised the final rule to include the statutory reference.

[41] *See* OTS Op. Chief Counsel (Nov. 27, 1996) (A loan that explicitly provides for a specified increase in the interest rate if the borrower becomes delinquent for more than 30 days twice in a revolving twelve month period is an alternative mortgage transaction under paragraph (A) or (C) of the definition).

[42] *See* OTS Op. Chief Counsel (Feb. 10, 1997). *But see Hays* v. *Bankers Trust Co.,* 46 F. Supp. 2d 490, 499 (S.D.W.V. 1999) (footnote 17 states that AMTPA applies only to ARMs and does not cover the loan at issue, which was a balloon loan. This footnote appears to be erroneous in light of paragraph (B) of the definition).

creditor to hold a state license.[43] Rather, it merely requires a creditor to hold a state license where the underlying state law imposes a licensing requirement.

5. Preemption for Operating Subsidiaries

Two commenters asked OTS to confirm that operating subsidiaries of federal thrifts have the same lending authority and benefits of federal preemption as federal thrifts and, thus, do not need to use AMTPA to preempt state law. Another commenter, however, hinted that operating subsidiaries of federal thrifts should be treated like other state housing creditors under AMTPA.

Under OTS rules, operating subsidiaries of federal thrifts are subject to the same requirements as federal thrifts. For example, an operating subsidiary is permitted to engage in any activity that the federal savings association may conduct directly. 12 CFR 559.3(e)(1). Unless specifically provided by statute, regulation, or OTS policy, all federal statutes and regulations apply to operating subsidiaries in the same manner as they apply to federal savings associations. 12 CFR 559.3(h)(1). In addition, state laws apply to operating subsidiaries only to the extent that they apply to a federal savings association. 12 CFR 559.3(n)(1). OTS has taken these positions because operating subsidiaries, which may only engage in activities permissible for its parent federal savings association and must be controlled by the thrift, are treated as the equivalent of the parent thrift for regulatory and reporting purposes.[44] Because operating subsidiaries of federal savings associations have the same lending authority and benefits of federal preemption, they do not need to use AMTPA to preempt state law.

6. Retroactive Application

One commenter asked whether the final rule will apply to loans consummated before the effective date. The commenter warned that borrowers would argue that the new rule must apply retroactively to existing transactions because OTS was ''incorrect'' when it revised the rules in 1996. In this final rule, OTS has selected between two permissible interpretations of AMTPA based upon a reevaluation of the statute. OTS has, in no way, concluded that the 1996 rule changes reflected an impermissible construction of its statute. Accordingly, there is no basis for arguing that the final rule applies retroactively to transactions consummated before the effective date.

Even if OTS were to assume that it had the ability to apply this rule retroactively, such a position would seriously disrupt the mortgage markets. Borrowers and originating lenders have made pricing decisions regarding the interest rates and conditions and terms of mortgages based on the inclusion or exclusion of prepayment penalties. Similar pricing decisions have been made regarding secondary sales of these mortgages, either on a whole loan basis or as a part of mortgage pools backing securities. OTS does not believe that it may take away or impair vested rights acquired under a lawfully issued and effective regulation.

E. Legislative Recommendations

Numerous commenters on the NPRM urged OTS to recommend that Congress repeal AMTPA. These commenters noted that AMTPA was passed in a high interest rate environment and was designed to permit state chartered institutions to offer alternative mortgage transactions that were otherwise prohibited under state law. Because all states, except one, permit alternative mortgage transactions, these commenters asserted that AMTPA has outlived its usefulness and may be repealed. Other commenters, however, supported the retention of AMTPA. These commenters noted that state laws continue to restrict or prohibit alternative mortgage transactions and that local governments are beginning to regulate this area.

Legislative actions affecting AMTPA are beyond the scope of this rulemaking. In OTS's view, however, piecemeal legislative and regulatory solutions aimed at the various complex issues raised under AMTPA—predatory lending, the availability of credit, and parity among housing creditors—are not the best way to approach this problematic area. Accordingly, OTS and a substantial number of commenters on the NPRM believe that that Congress should revisit AMTPA, in the context of broader mortgage reform legislation involving the Real Estate Settlement Procedures Act,[45] the Truth In Lending Act,[46] and predatory lending. Only comprehensive reform can guarantee that borrowers receive meaningful information in a comprehensive and comprehensible form, that healthy competition between housing creditors is stimulated so that affordable housing credit continues to be available to consumers, and that statutory and regulatory burdens are minimized. OTS continues to advocate broad-based reform in this area as well as a review of existing laws that have inconsistencies and duplications that make the mortgage process more complicated and expensive for consumers than is needed.

OTS also indicated that it would make two recommendations if Congress decides to retain AMTPA. First, OTS suggested that Congress should give states a new opportunity to opt out from AMTPA preemption. Congress originally gave the states three years to opt out of AMTPA preemption. If a state opted out, state housing creditors would continue to be bound by the state's regulations on alternative mortgage transactions.[47] Only a handful of states decided to reject preemption.

Commenters opposing a new opt out period argued that this change would increase costs to consumers, raise new compliance issues, reduce certainty in the markets, and raise the possibility that Congress would add new opt out periods to other statutes including DIDMCA. One commenter feared that many states would opt out, which would gut the application of what was intended as a uniform law.

The mortgage loan market has seen dramatic and fundamental changes since the original opt out period closed in 1985. Certain changes, such as the general acceptance of alternative mortgage transactions under state law and the increased availability of housing credit, may have been anticipated. The states, however, could not have anticipated other changes, such as the explosion in sub-prime lending, increases in predatory practices by lenders, and the breadth of preemption of state law permitted under AMTPA. Given these changes, OTS believes that the states should have a new opportunity to opt out of AMTPA.

OTS also indicated that it would recommend that Congress require state housing creditors making loans under AMTPA to identify themselves to the states. Several commenters observed that this disclosure would enhance enforcement and monitoring activities by state supervisory agencies, fair housing organizations, and others. One commenter, however, argued that this revision is unnecessary because AMTPA

[43] 12 U.S.C. 3802(2) states: ''A person is not a 'housing creditor' with respect to a specific alternative mortgage transaction if, except for this chapter, in order to enter into that transaction, the person would be required to comply with licensing requirements imposed under State law, unless that person is licensed under applicable State law and such person remains, or becomes, subject to the applicable regulatory requirements and enforcement mechanisms provided by State law.''

[44] *See* 61 FR 66561, 66563 (Dec. 18, 1996).

[45] 12 U.S.C. 2601 *et seq.*

[46] 15 U.S.C. 1601 *et seq.*

[47] 12 U.S.C. 3804(a).

requires state housing creditors to comply with state licensing requirements and states have the authority to require these creditors to identify themselves to the state regulator.

OTS continues to believe that enforcement is difficult unless states have a reliable means of identifying AMTPA creditors. OTS will continue to make this recommendation to ensure that all states have the ability to utilize their applicable enforcement mechanisms.

II. Preemption of State Usury Laws (12 CFR Part 590)—Late Fees on Federally-Related Residential Manufactured Housing Loans

Part 590 implements section 501 of DIDMCA.[48] Section 501 provides for the permanent preemption of state laws that expressly limit the rate or amount of interest, discount points, finance charges, or other charges assessed in connection with certain federally-related residential loans. This preemption does not apply to loans secured by a first lien on a residential manufactured home unless the loan complies with consumer protections in § 590.4. This regulation addresses such matters as balloon payments, prepayment penalties, late charges, deferral fees, notice before repossession or foreclosure, and the refund of prepaid interest. Section 590.4(f) specifically addresses late charges. Paragraph (f)(4) states: ''To the extent that applicable state law does not provide for a lower charge * * * a late charge on any installment * * * may not exceed the lesser of $5.00 or five percent of the unpaid amount of the installment.''

OTS proposed to eliminate the $5.00 limit. Two commenters opposed this change. They noted that this change would permit lenders to increase allowable late fees several times over the current levels and would facilitate predatory lending. Commenters also observed that low-income borrowers, including limited-income seniors, are more likely to live in manufactured homes and would be adversely affected by the rule change. Four commenters supported the proposed change because it would: (1) Ensure that lenders are adequately compensated; (2) provide a stronger self-adjusting incentive for consumers to pay on time; and (3) provide parity with late charges permitted under state laws.

OTS has not adjusted the $5 limit on late fees in 20 years. As a result, the limit has not kept pace with lenders' costs and is too small to serve as an effective deterrent to late payment. According to commenters, the $5 limit is an effective percentage rate of only 1.3 percent of the average manufactured home loan payment. This amount is well below the prevailing state late fee for manufactured housing, which commenters assert is 5 percent of the loan installment payment. By contrast, the proposed limit is within the mix of late fee structures established under state law.

While some commenters feared that the proposed rule would facilitate predatory lending, the revised regulation continues to impose effective limitations on such practices. As revised, § 590.4 limits the late charge to 5 percent of the unpaid amount of the installment unless the state provides for a lower amount. In addition, the rule would continue to provide that:

- No late charge may be assessed, imposed, or collected unless the written contract between the borrower and the lender provides for the charge (§ 590.4(f)(1)).
- No late charge may be collected if an installment is paid in full on or before the 15th day after its scheduled or deferred due date, unless state law permits a longer period (§ 590.4(f)(2)).
- A late charge may be imposed only once on an installment, and may not be collected if an installment has been deferred § 590.4(f)(3).

The NPRM asked whether OTS should also eliminate the 5 percent limit on the amount of the late fee and permit state law to govern the amount of late charges. One commenter supported and one commenter opposed this change. A third noted that this alternative would not have a significant impact since few states allow late charges in excess of 5 percent.

OTS has retained the 5 percent late fee limitation. While few states permit a lower charge, OTS believes that the 5 percent fee serves as an effective consumer safeguard to the extent that states permit late fees in excess of 5 percent of the unpaid amount.

III. Preemption of State Due-on-Sale Laws (12 CFR Part 591)—Definition of Reverse Mortgage

OTS proposed a minor technical change to part 591, which implements section 341 of the Garn St. Germain Depository Institutions Act of 1982 (12 U.S.C. 1701j–3).[49] Part 591 governs due-on-sale clauses in real estate loans and the preemption of state prohibitions on such clauses. OTS proposed to revise the definition of reverse mortgage at § 591.2(n) to clarify that a reverse mortgage is not limited to a loan that provides for periodic payments, but also includes a loan that provides for a lump sum payment. This change is consistent with OTS legal opinions,[50] and no commenter addressed the issue. The proposed rule is adopted without change.

IV. Regulatory Certifications

A. Executive Order 12866

The Director of OTS has determined that the final rule does not constitute a ''significant regulatory action'' for purposes of Executive Order 12866.

B. Unfunded Mandates Reform Act of 1995

Section 202 of the Unfunded Mandates Reform Act of 1995, Public Law 104–4 (Unfunded Mandates Act), requires an agency to prepare a budgetary impact statement before promulgating a rule that includes a federal mandate that may result in expenditure by state, local, and tribal governments, or by the private sector, of $100 million or more in any one year. If a budgetary impact statement is required, section 205 of the Unfunded Mandates Act also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. OTS has determined that the rule will not result in expenditures by state, local, or tribal governments or by the private sector of $100 million or more. Accordingly, a budgetary impact statement is not required under section 202 of the Unfunded Mandates Act of 1995.

C. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) (5 U.S.C. 601–612) requires federal agencies to prepare a final regulatory flexibility analysis with a final rule that was subject to notice and comment, unless the agency certifies that the rule will not have a significant impact on a substantial number of small entities.

Parts 590 and 591. OTS did not prepare an initial or final regulatory flexibility analysis for the revisions to parts 590 and 591. The change to part 590 affects creditors making federally-related loans secured by first liens on residential manufactured housing. The final rule provides these creditors with greater flexibility in charging late fees, while retaining the benefits of preemption of state usury laws under section 501 of DIDMCA. The current rule limits late fees to $5, which has proven to be too small to deter late

[48] 12 U.S.C. 1735f–7a.

[49] Pub. L. 97–320, 96 Stat. 1469 (1982).

[50] OTS Op. Chief Counsel (June 2, 2000) (reverse mortgage loans include an instrument providing for a lump sum payment).

payments. The final rule permits the imposition of a more tangible penalty and will benefit all creditors making such loans, including small businesses. Part 591 permits all lenders, whether federally- or state chartered, to exercise due-on-sale clauses in real property loans without regard to state law. The final rule makes a clarifying change that broadens the definition of reverse mortgage and codifies an existing OTS interpretation. OTS believes that the impact of the final rule on lenders should be beneficial. Thus, OTS certifies to the Chief Counsel of Advocacy of the Small Business Administration that the changes to parts 590 and 591 will not have a significant economic impact on a substantial number of small entities.

Section 560.220. OTS has performed a final regulatory flexibility act analysis for the changes to § 560.220. A description of the reasons why OTS is adopting the final rule, a statement of the objectives of, and legal basis for, this aspect of the final rule are included in the supplementary material above. In addition, OTS has addressed the following topics.

1. Small Entities to Which the Rule Applies

Section 560.220 applies to state housing creditors other than credit unions or commercial banks. OTS does not compile data on the total number of state housing creditors that may utilize § 560.220. Moreover, except for state chartered savings associations, OTS does not have any authority to require state housing creditors to identify themselves or submit other data to OTS. Similarly, AMTPA does not require state housing creditors to notify the states that they are taking advantage of it. As a result, OTS has little information regarding how many state housing creditors may use § 560.220 or how many of these creditors are small businesses.

Nonetheless, OTS estimates that 6,757 small state housing creditors may be affected by this regulation. United States Census data indicates that 7,257 firms (excluding depository institutions) engage in real estate credit. OTS estimates approximately 6,457 of these firms are small businesses.[51] Based on the most recent TFR and Call Report data, OTS estimates that an additional 300 state chartered savings associations and state savings banks are small businesses.[52] For purposes of this analysis, we have assumed that all 6,757 of these small businesses engage in alternative mortgage transactions.

OTS believes that this number may overstate the number of small businesses that may be affected by the changes to the final rule for several reasons. First, the use of AMTPA is solely at the election of the state housing creditor. State housing creditors may, for whatever reason, decline to use AMTPA for their alternative mortgage transactions. Moreover, many small state housing creditors will conduct alternative mortgage transactions that are governed by laws in states that either:

- Opted out of AMTPA. State housing creditors conducting alternative mortgage transactions governed by these laws currently cannot use § 560.220 to preempt state law; or
- Enacted statutes that do not impose any substantive prohibitions and restrictions on prepayments or late charges for the loans. State housing creditors may continue to charge penalties and fees on alternative mortgage transactions in these states, notwithstanding the final rule.

OTS's original estimate of small businesses was based on the best information available to it. OTS encouraged commenters with access to more complete and more accurate data to submit information regarding the number of state housing creditors (other than credit unions or commercial banks) that may be affected by this rule. OTS also requested information regarding how many of these creditors may be small businesses.

One commenter argued that OTS underestimated the number of small businesses affected by the rule. The commenter asserted that OTS excluded 40,000 to 50,000 mortgage brokers who originate the majority of residential loans in the United States. The commenter also asserted that thousands of appraisers and title companies would also see diminished revenues.

OTS used United States Census data to determine the number of non-depository institutions that would be effected by the rule. Specifically, OTS used the Census classification—NAICS 522292—Real Estate Credit, which is a subcategory within NAICS 5222—Non-Depository Credit Intermediation. NAICS 5222 includes establishments that are primarily engaged in extending credit or lending funds raised by credit market borrowing. Within this group, industries are broken out based on the type of credit extended. The selected classification—NAICS 522292—comprises non-depository institutions that are engaged in lending funds with real estate as collateral and includes mortgage bankers and loan correspondents.

The Regulatory Flexibility Act requires an agency to consider direct effects that a regulation may have on small businesses that it regulates. OTS is not, however, required to analyze the effects of its rule on entities that it does not regulate. Arguably, OTS regulates state housing creditors that make loans, credit sales, or advances secured by interests in real property.[53] However, it does not directly impose any regulation on those entities that garner fees through brokerage services or through other services that facilitate the credit intermediation process. Accordingly,

[51] OTS based this figure on firms reported under NAICS 522292 and the special tabulation of the 1997 economic census from the United States Bureau of the Census. The initial regulatory flexibility analysis estimated that 6,300 of the 7,257 firms were small businesses. OTS has revised this figure to reflect recent increases to SBA's thresholds defining small businesses. A firm engaged in real estate credit is now considered small if it has total receipts of $6 million or less per year. 67 FR 3041 (Jan. 23, 2002) *to be codified* at 13 CFR 121.201. The threshold previously was $5 million. 13 CFR 121.201 (2002). While the 1997 special tabulation does not indicate the number of real estate credit firms that had less than $6 million in receipts, it indicates that an additional 157 firms had less than $7.5 million in receipts. Recognizing that this number will overstate the number of small businesses satisfying the $6 million threshold, OTS has estimated that there are 6,457 small firms engaged in real estate credit.

[52] OTS originally estimated that an additional 86 depository institutions were small state chartered housing creditors. This number has been revised to 300. The number used in the initial regulatory flexibility analysis did not include state savings banks, and must be recalculated to reflect recent changes to the SBA's thresholds defining small depository institutions. Until recently, small depository institutions were defined, for RFA purposes, as depository institutions with assets under $100 million. 13 CFR 121.201 (2002). The threshold amount, however, was increased to $150 million. *See* 67 FR 3041 (Jan. 23, 2002) *to be codified* at 13 CFR 121.201. Based on March 2002 TFR data, OTS regulates 135 state savings associations. Of these savings associations, 93 have assets of $150 million or less. Based on March 2002 Call Report data, the FDIC regulates 508 state savings banks. Of these state savings banks, 207 have assets of $150 million or less.

[53] OTS questions whether a regulatory flexibility analysis is required for the rule. Revised 12 CFR 560.220 imposes no restriction or limitation on any small entity's ability to impose prepayment penalties or late charges. Rather, the rule leaves the regulation of these matters entirely to the discretion of the individual states. As a result, OTS believes that it may certify that the rule will not have a significant impact on a substantial number of small entities. *See American Trucking Ass'n, Inc.* v. *EPA,* 175 F.3d 1027 (D.C. Cir. 1999) (The D.C. Circuit held that EPA was not required to perform a regulatory flexibility analysis for its national ambient air quality standards (NAAQS). The NAAQS imposed no regulations on small entities. Instead, each state regulated small entities through the state implementation plans that they were required to develop under the Clean Air Act. Because the NAAQS regulated small entities only indirectly—that is, insofar as they affected the planning decisions of the states—the EPA concluded, and the D.C. Circuit agreed, that small entities were not subject to the rule).

OTS has not included within its tabulation entities that appear within the classification NAICS 5223—Activities Related to Credit Intermediation. This classification includes establishments that are primarily engaged in facilitating credit intermediation by performing activities, such as arranging loans by bringing borrowers and lenders together on a commission or fee basis.[54]

2. Requirements of the Rule

AMTPA permits certain state housing creditors to make, purchase, and enforce alternative mortgage transactions without regard to any state constitution, law, or regulation, provided that they comply with regulations identified by OTS. As described more fully in the supplementary information section, the final rule no longer identifies rules on prepayment and late charges for state housing creditors under AMTPA. As a result, these state housing creditors will likely be subject to state laws addressing prepayment and restricting late charges.

OTS is unable to quantify the impact of the final rule on small state housing creditors for several reasons. Based on available data, it is difficult to determine how many alternative mortgage transactions were made under OTS AMTPA regulations. Industry-wide data is available only for one type of alternative mortgage transaction—ARMs. Other types of mortgages with alternative features are generally reported as fixed-rate mortgages. The available data, however, indicates that all housing lenders originated $243.6 billion and $256 billion in ARMs in 2001 and 2000, respectively.[55] The most recent data available indicates that state housing creditors (excluding commercial banks and thrifts) account for approximately 56.3 percent of all lending or $137.1 billion and $144.1 billion of ARMs in 2001 and 2000.[56] OTS estimates that $17.0 billion and $17.9 billion of these ARM loans were originated by small state housing creditors in 2001 and 2000.[57] This available data, however, does not distinguish between transactions that are made under AMTPA, and those that are not. As noted above, OTS has no authority to require state housing creditors that use § 560.220 to provide this information.[58]

In the ANPR and NPRM, OTS attempted to obtain more complete and accurate information regarding the extent to which state housing creditors and small state housing creditors engage in alternative mortgage transactions under AMTPA. OTS also requested information concerning the amount of late fees and prepayment penalties generated by these alternative mortgage transactions. Commenters, however, provided no reliable additional information on this subject.[59]

Even if reliable estimates were available, these amounts would not accurately reflect the impact of the deletion of the preemption of prepayment charge provisions and late charge provisions. The 6,757 small state housing creditors that may be affected by the final rule will become subject to a broad range of state laws. For example, some of these laws may continue to permit the imposition of prepayment penalties. Others may prohibit or restrict prepayment charges. Still other laws would subject prepayment penalties to a range of restrictions, such as prohibiting penalties for a set period after execution of the note or mortgage or limiting the amount of the prepayment penalty. Based on this wide variety of restrictions and the fact that state laws will change over time, OTS cannot determine how much income would be lost by small state housing creditors under the rule.[60]

Moreover, the impact of the loss of prepayment penalties may be ameliorated somewhat through other techniques. For example, lenders often impose a higher overall interest rate where prepayment penalties are excluded from the loan agreement.[61] In addition, some commentators assert that the payment of points upon origination and the imposition of a prepayment penalty are economically equivalent transactions. Since a mortgage with points includes an implicit and easily calculable prepayment penalty, state housing creditors may substitute points where prepayment penalties are prohibited.[62]

Some commenters indicated that OTS did not fully consider all impacts on small businesses, such as increased compliance costs to conform to newly applicable states laws, and the negative economic effects on small entities' ability to offer a competitive product, to address prepayment risk, or to access the secondary loan markets. Commenters, however, did not provide any reliable estimates or sources of information regarding the magnitude of these impacts on small entities.

3. Significant Alternatives

Section 603(c) of the RFA requires OTS to describe any significant alternatives that accomplish the stated objectives of the rule while minimizing any significant economic impact of the rule on small entities. Section 603(c) lists several examples of significant alternatives, including: (1) Establishing different compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) clarifying, consolidating, or simplifying compliance and reporting requirements for small entities; (3) using performance standards rather than design standards; and (4) excepting small entities from coverage of the rule or a part of the rule.

[54] Mortgage and non-mortgage loan brokers are included within a subcategory of this classification—NAICS 52231.

[55] The Mortgage Bankers Association's Web site at *www.mbaa.org* indicates that the industry originated $2,030 billion in 1- to 4-family mortgages in 2001, and $1,024 billion of these loans in 2000, and that 12 percent and 25 percent of these loans were ARMs in 2001 and 2000, respectively.

[56] This information was also obtained on the Mortgage Bankers Association's Web site, which indicates that its source was a HUD Survey of Mortgage Lending Activity discontinued in 1998.

[57] OTS computed this figure using receipts by real estate creditors as proxy for originations. Based on these figures, OTS estimates that small creditors accounted for 12.4 percent of all ARM originations by real estate creditors.

[58] OTS does not currently collect data on the ARM originations by the small state savings associations. However, March 2002 CMR data indicates that these 93 thrifts hold approximately $1.04 billion of ARMs in their portfolios. Again, this data does not distinguish transactions subject to AMTPA regulations.

[59] One of the commenters on the ANPR, a trade association representing a substantial segment of the real estate financing community, including national and regional lenders, mortgage brokers, mortgage conduits, and service providers, stated that it "does not have specific numbers regarding the extent to which lenders are using AMTPA to craft alternative mortgage products that would otherwise be affected by state law. Furthermore [it] knows of no reliable and comprehensive industry data from any source."

[60] *See* "The Handbook of Mortgage-Backed Securities," 88–101 (Frank J. Fabozzi, ed. (5th ed. 2001)), which contains a compilation of current state laws on prepayment penalties.

[61] In April 2000, one large sub-prime lender indicated that it lowered the interest rate on a loan by 75 basis points for those borrowers who accepted a prepayment penalty. See Joint HUD/Treasury Report supra note 29, at 93, citing information from the New Century Mortgage Corporation Web site, *www.newcentury.com.*

[62] Alan L. Feld & Stephan G. Marks, Legal Differences Without Economic Distinctions: Points, Penalties, and the Market for Mortgages, 77 B.U. L. Rev. 405 (1997). Some commenters objected to OTS's suggestion that state housing creditors can "ameliorate loss of income by substituting points or simply raising rates." They argued that a point is an immediate, out-of-pocket cost to a borrower. That cost is fixed regardless of whether the borrower keeps the loan for its full term, or chooses to repay or refinance the loan at some earlier date. By contrast, a prepayment penalty does not necessarily cost the borrower anything if the loan is retained through the prepayment penalty period. Commenters asserted that state housing creditors would be at a distinct disadvantage because they must charge higher rates and points. Even if one assumes that the average loan will prepay and cost a penalty, such costs in the aggregate will be less than if lenders are forced to ameliorate. Even if competitive equality were not the issue, state housing creditors would still be limited by state caps on rates.

OTS considered retaining its current identification of regulations for all state housing creditors. For the reasons discussed above, OTS believes that this course is inappropriate. OTS also considered whether it should continue to identify the existing regulations for small state housing creditors, but not for other state housing creditors. However, given its analysis of the purposes and goals of AMTPA, OTS has concluded that it is inappropriate to distinguish between small and large state housing creditors.

OTS solicited comments on other alternatives that would minimize the burdens on small state housing creditors. The commenters did not suggest any alternatives aimed at small housing creditors. Other alternatives, however, are discussed in the supplementary information section above.

4. Other Matters

Various federal rules or statutes duplicate or overlap with the final rule. NCUA has identified all of its lending regulations as applicable to alternative mortgage transactions by state chartered credit unions. 12 CFR 701.21(a). These regulations address such matters as the term of the loan, requirements governing security instruments, notes, liens, due-on-sale provisions, and assumptions. These rules specifically prohibit prepayment penalties and preempt state laws on prepayment limits and late charges. OCC, on the other hand, has identified as applicable to state chartered commercial banks, its rules that directly relate to ARMs. OCC's identified regulations define ARM loans; state that ARMs may be made, sold, purchased, participated in, or dealt in without regard to any state law limitation on those activities; authorize certain indexes; and allow prepayment fees. 12 CFR 34.24.

In addition, the Home Ownership and Equity Protection Act (HOEPA) [63] imposes limits on certain high cost mortgage loans by state housing creditors. These limits include restrictions on balloon payments, prepayment penalties, and other matters. Other federal statutes and rules may also preempt the application of state laws on prepayments and late fees for alternative mortgage transactions by state housing creditors. *See e.g.*, 12 CFR 590.4 (preemption of state usury laws under section 501 of DIDMCA—first liens on residential mobile homes) and 12 CFR part 591 (preemption of state due-on-sale clauses under section 341 of Garn St. Germain Depository Institutions Act of 1982).[64]

OTS is aware of no federal rules or statutes that conflict with the final rule.

D. Federalism

Executive Order 13132 imposes certain requirements on an agency when formulating and implementing policies that have federalism implications or taking actions that preempt state law. In accordance with those requirements, OTS has consulted with the Conference of State Bank Supervisors and the National Association of Attorneys General concerning this change.

List of Subjects

12 CFR Part 560

Consumer protection, Investments, Manufactured homes, Mortgages, Reporting and recordkeeping requirements, Savings associations, Securities.

12 CFR Part 590

Banks, banking, Loan programs—housing and community development, Manufactured homes, Mortgages, Savings associations.

12 CFR Part 591

Banks, banking, Loan programs—housing and community development, Mortgages, Savings associations.

Accordingly, the Office of Thrift Supervision amends 12 CFR parts 560, 590, and 591 as set forth below:

PART 560—LENDING AND INVESTMENT

1. The authority citation for part 560 continues to read as follows:

Authority: 12 U.S.C. 1462, 1462a, 1463, 1464, 1467a, 1701j–3, 1828, 3803, 3806; 42 U.S.C. 4106.

2. Revise § 560.220 to read as follows:

§ 560.220 Alternative Mortgage Transaction Parity Act.

(a) *Applicable housing creditors.* A housing creditor that is not a commercial bank, a credit union, or a federal savings association, may make an alternative mortgage transaction as defined at 12 U.S.C. 3802(1), by following the regulations identified in paragraph (b) of this section, notwithstanding any state constitution, law, or regulation. *See* 12 U.S.C. 3803.

(b) *Applicable regulations.* OTS identifies §§ 560.35 and 560.210 as appropriate and applicable for state housing creditors. All other OTS regulations are not identified, and are inappropriate and inapplicable for state housing creditors. State housing creditors engaged in credit sales should read the term ''loan'' as ''credit sale'' wherever applicable in applying these regulations.

PART 590—PREEMPTION OF STATE USURY LAWS

3. The authority citation for part 590 continues to read as follows:

Authority: 12 U.S.C. 1735f–7a.

4. Revise the section heading and paragraph (f)(4) in § 590.4 to read as follows:

§ 590.4 Federally-related residential manufactured housing loans—consumer protection provisions.

* * * * *

(f) * * *

(4) To the extent that applicable state law does not provide for a lower charge or a longer grace period, a late charge on any installment not paid in full on or before the 15th day after its scheduled or deferred due date may not exceed five percent of the unpaid amount of the installment.

* * * * *

PART 591—PREEMPTION OF STATE DUE-ON-SALE LAWS

5. The authority citation for part 591 is revised to read as follows:

Authority: 12 U.S.C. 1464 and 1701j–3.

6. Revise § 591.2(n) to read as follows:

§ 591.2 Definitions.

* * * * *

(n) *Reverse mortgage* means an instrument that provides for one or more payments to a homeowner based on accumulated equity. The lender may make payment directly, through the purchase of an annuity through an insurance company, or in any other manner. The loan may be due either on a specific date or when a specified event occurs, such as the sale of the property or the death of the borrower.

* * * * *

Dated: September 20, 2002.

[63] Pub. L. No. 103–325 (1994), 108 Stat. 2160, amending the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* The reference to HOEPA was not included in the initial regulatory flexibility analysis.

[64] One commenter argued that the initial regulatory flexibility analysis incorrectly listed part 590 as an overlapping or duplicative provision because 12 U.S.C. 3805 states that the consumer protections in section 501(c)(1) of DIDMCA do not apply to alternative mortgage transactions under AMTPA. State housing creditors, however, may rely on state law rather than AMTPA for authority to make alternative mortgage transactions. If they do, they may assert preemption under section 501 under DIDMCA.

By the Office of Thrift Supervision.

James E. Gilleran,

Director.

[FR Doc. 02–24407 Filed 9–25–02; 8:45 am]

BILLING CODE 6720–01–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 23

[Docket No. CE171; Special Conditions No. 23–128–SC

Special Conditions: Eclipse Aviation Corporation, Model 500; Fire Extinguishing System for Aft Mounted Engine Installations.

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Final special conditions.

SUMMARY: These special conditions are issued for the Eclipse Aviation Corporation, Model 500 airplane. This airplane will have a novel or unusual design feature(s) associated with aft mounted turbine engines. The applicable airworthiness regulations do not contain adequate or appropriate safety standards for this design feature. These special conditions contain the additional safety standards that the Administrator considers necessary to establish a level of safety equivalent to that established by the existing airworthiness standards.

EFFECTIVE DATE: October 28, 2002.

FOR FURTHER INFORMATION CONTACT: Lowell Foster, FAA, Aircraft Certification Service, Small Airplane Directorate, ACE–111, 901 Locust Street, Kansas City, Missouri 64106, 816–329–4111.

SUPPLEMENTARY INFORMATION:

Background

On July 12, 2001, Eclipse Aviation Corporation applied for a type certificate for their new Model 500 airplane.

The Model 500 design includes turbine engines mounted aft on the fuselage, which means early visual detection of engine fire is precluded. The applicable existing regulations do not require fire extinguishing systems for engines. Aft mounted turbine engine installations, along with the need to protect such installed engines from fires, were not envisioned in the development of part 23; therefore, a special condition regarding fire protection for the engines of the Model 500 is required.

Type Certification Basis

Under the provisions of 14 CFR 21.17, Eclipse Aviation Corporation must show that the Eclipse Model 500 meets the following:

(1) Applicable provisions of 14 CFR part 23, effective December 18, 1964, as amended by Amendments 23–1 through 23–54 (September 14, 2000).

(2) Part 34 of the Federal Aviation Regulations effective September 10, 1990, plus any amendments in effect on the date of type certification.

(3) Part 36 of the Federal Aviation Regulations effective December 1, 1969, as amended by Amendment 36–1 through the amendment in effect on the date of type certification.

(4) Noise Control Act of 1972.

(5) Special conditions that are not relevant to these special conditions;

(6) Exemptions, if any;

(7) Equivalent level of safety findings, if any; and

(8) Special conditions adopted by this rulemaking action.

In addition to the applicable airworthiness regulations and special conditions, the Model 500 must comply with the part 23 fuel vent and exhaust emission requirements of 14 CFR part 36, and the FAA must issue a finding of regulatory adequacy pursuant to § 611 of Public Law 92–574, the ''Noise Control Act of 1972.''

Special conditions, as appropriate, as defined in § 11.19, are issued in accordance with § 11.38 after public notice and become part of the type certifications basis in accordance with § 21.17(a)(2).

Special conditions are initially applicable to the model for which they are issued. Should the type certificate for that model be amended later to include any other model that incorporates the same novel or unusual design feature, the special conditions would also apply to the other model under the provisions of § 21.101.

Novel or Unusual Design Features

The Model 500 will incorporate the following novel or unusual design features:

Turbine engines mounted on the aft of the fuselage. Aft mounted turbine engine installations need to be protected from fire since early visual detection of engine fires is not possible. This special condition covers a fire extinguishing system for the engines of the Model 500.

Discussion of Comments

Notice of proposed special conditions No. 23–01–04–SC–A for the Eclipse Model 500 airplanes was published on January 29, 2002 (67 FR 4215). On June 17, 2002, we published an amended notice of proposed special conditions (67 FR 46927). No comments were received, and the special conditions are adopted as proposed.

Applicability

As discussed above, these special conditions are applicable to the Eclipse Model 500 airplane. The engine installation used in the Model 500 does not utilize additional engine compartments other than those addressed in the special conditions. Should Eclipse Aviation Corporation apply at a later date for a change to the type certificate to include another model incorporating the same novel or unusual design feature, the special conditions would apply to that model as well under the provisions of § 21.101.

Conclusion

This action affects only certain novel or unusual design features on one model of airplane. It is not a rule of general applicability, and it affects only the applicant who applied to the FAA for approval of these features on the Eclipse Model 500 airplane.

List of Subjects in 14 CFR Part 23

Aircraft, Aviation safety, Signs and symbols.

Citation

The authority citation for these special conditions is as follows:

Authority: 49 U.S.C. 106(g), 40113 and 44701; 14 CFR 21.16 and 21.17; and 14 CFR 11.38 and 11.19.

The Special Conditions

Accordingly, pursuant to the authority delegated to me by the Administrator, the following special conditions are issued as part of the type certification basis for the Eclipse Aviation Model 500 airplane.

Engine Fire Extinguishing System

(a) Fires originating in combustor, turbine, and tailpipe sections of the engine installation which contain lines or components carrying flammable fluids must either:

(1) Be demonstrated at critical conditions to be controllable by test or a combination of test or analysis; or

(2) a fire extinguishing system must serve each engine compartment.

(b) If a fire extinguishing system is installed, the system must comply with the following requirements:

(1) The system must serve each engine compartment;

(2) The system, the quantity of the extinguishing agent, the rate of discharge, and the discharge