

April 11, 2011

Information Collection
Comments, Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

Re: Cost of Funds Indices – Notice of Intent to Discontinue and Request for Comment, February 8, 2011

Dear Sir or Madame:

The American Bankers Association is pleased to submit comments regarding the stated intention of the Office of Thrift Supervision (OTS) to eliminate Cost of Funds (COF) indices.

OTS proposes to cease collection of data used to calculate cost of funds indices, and to end publication of the indices on January 31, 2012. This would include the Monthly Median Cost of Funds Index, the Quarterly Cost of Funds Index, the Semiannual Cost of Funds Index, and other related cost of funds ratios currently published monthly in the OTS's Cost of Funds (COF) Report. These indices have been used by certain mortgage lenders as benchmarks for adjustable rate mortgages.

ABA does not object to the termination of these indices.

The OTS states that the volume of ARMs using COF indices has declined significantly and reports from our member institutions confirm this. Since elimination of these indices was last proposed in 1994, the number of OTS-regulated institutions reporting data has declined by more than half, diminishing the statistical reliability of the index. In addition, the portion of ARM loans based on COF indices has declined from about 20 percent of savings association assets to just 1 percent as of September 30, 2010. Our members generally agree with the OTS assertion that readily available alternative indices with more stable statistical characteristics are available.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 requires the OTS to designate acceptable substitute indices should it discontinue publication of indices used for ARM rate adjustments. OTS evaluated 17 publicly available indices as potential substitutes for the COF indices, and found four to be highly correlated. These are:

1. 11th District Cost of Funds (*Source:* The Federal Home Loan Bank of San Francisco (FHLB–SF))
2. Federal Cost of Funds (*Source:* Freddie Mac (FHLMC))
3. National Average Contract Mortgage Rate (*Source:* The Federal Housing Finance Agency (FHFA))
4. Monthly Treasury Average (MTA) (*Source:* Federal Reserve Board—H.15 FRSD)

ABA members agree that each of the indices identified have adequately high correlations with COF indices, and expressed no overwhelming preference for one substitute over the other. ABA members agree that MTA is less suitable as a direct substitute based in index levels because of recent changes in interest rate relationships resulting from monetary policy actions. Otherwise, each index might have particular advantages that an institution would prefer, such as transparency for consumers, investors or

both. The 11th District Cost of Funds has the strongest correlation to COF indices, but is not as well known outside the 11th FHLB District. The Federal Cost of Funds is well known and highly correlated, but its future may depend on the outcome of GSE reform. The National Average Contract Mortgage Rate has a strong correlation, and may have a greater degree of permanence since it is published by a federal agency. The Monthly Treasury Average presumably would have the greatest degree of expected permanence.

If the COF indices are to be discontinued, we would ask that OTS provide guidance regarding converting ARM loans to an alternative index. We ask that this guidance recognize situations where loan contracts might address circumstances where use of an alternative index may be necessary, as well as certain legacy ARM contracts that we understand may be silent or non-specific regarding such circumstances.

ABA appreciates this opportunity to comment and we stand ready to provide further information or assistance to ensure a smooth transition from the OTS indices to the alternatives. Please do not hesitate to contact me if ABA can be of assistance.

Sincerely,

A handwritten signature in black ink that reads "Robert R. Davis". The signature is written in a cursive, flowing style.

Robert R. Davis
Executive Vice President