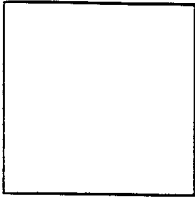


P-97-3



Office of Thrift Supervision
Department of the Treasury

Chief Counsel

1700 G Street, N.W., Washington, DC 20552 • (202) 906-6251

June 12, 1997

[

]

Re: Adjustments to Home Loans Indexed to LIBOR

Dear []:

This responds to your inquiry on behalf of [_____] (the "Company"), to the Office of Thrift Supervision ("OTS") regarding the permissibility of a London InterBank Offered Rate ("LIBOR") as an index for adjustable rate mortgage ("ARM") loans. You request confirmation that the LIBOR index described in your letter of May 15, 1997, would be considered a "national or regional index" for purposes of 12 C.F.R. § 560.35(d) ("Adjustments to home loans"). In brief, we confirm that an index based on the six-month LIBOR rate for U.S. dollar- denominated deposits and published in the Wall Street Journal as of a specified date would qualify as a national index pursuant to § 560.35(d).

You represent that the Company is an FHA-approved mortgage lender and a "housing creditor" as defined in § 803 of the Alternative Mortgage Transaction Parity Act of 1982 ("Parity Act").¹ The Company proposes to offer ARM loan products.² The Parity Act authorizes "housing creditors" to engage in "alternative mortgage transactions" without regard to State law, provided the transactions are in conformity with certain federal lending regulations.³ Non-

¹ 12 U.S.C.A. §§ 3801, 3802(2) (West 1989).

² You have not asked and we do not address whether the ARM loan products the Company proposes to offer constitute "alternative mortgage transactions" under the Parity Act.

³ 12 U.S.C.A. §§ 3801, 3802, and 3803 (West 1989). We note that the Parity Act gave states three years to override or "opt out" of its federal preemption, 12 U.S.C.A. §3804(a), and that the Parity Act does not override the Texas homestead laws, which prohibit foreclosure on borrower-occupied homes except in connection with purchase money mortgages. See 12 U.S.C.A. § 1462a(f) (West Supp. 1997).

federally chartered housing creditors, other than banks and credit unions, lending in reliance on the Parity Act must comply with OTS regulatory requirements for alternative mortgage transactions including, inter alia, requirements pertaining to ARM loan adjustments and disclosures for ARM loans.⁴

OTS regulations, at 12 C.F.R. § 560.35, set forth the requirements for adjustments to the interest rates of ARM loans.⁵ Section 560.35(d)(1) provides, inter alia, that any index used to adjust the interest rate of ARM loans “must be readily available and independently verifiable.” Section 560.35(d)(2) requires, inter alia, that adjustments to the loan balance of ARM loans reflect a change in an index that “must be a national or regional index,” unless a thrift meets certain regulatory exceptions.

You have described the index upon which the interest rate adjustments for the Company’s ARM loans would be based as “the six (6) month LIBOR rate for [U.S.] dollar denominated deposits as published in the Wall Street Journal” on the forty-fifth day prior to the interest rate change date. You further indicate that the ARM disclosure document would describe that rate as follows:

the index upon which your interest rate will be based is the six (6) month London InterBank Offered Rate (“LIBOR”) as published on the forty-fifth (45) day prior to your interest rate change date (or if the forty-fifth (45) day is not a business day, the last preceding day that is a business day) in the “Wall Street Journal.”

OTS’s Glossary of Selected Terms⁶ describes LIBOR as “the interest rate offered by a specific group of London banks for U.S. dollar deposits of a stated maturity,” and goes on to state that LIBOR is used as a base index for setting rates of some adjustable rate financial instruments.⁷ Thus, although LIBOR is

⁴ 12 U.S.C.A. § 3803; 12 C.F.R. § 560.220 (1997).

⁵ 12 C.F.R. § 560.35 (1997).

⁶ OTS Glossary of Selected Terms (April 1996), p. 79.

⁷ Your May 15 letter also cites a definition of LIBOR as “[t]he rate of *interest* offered on *loans* to first-class banks in the London *Interbank Market* for a specified period (usually three or six months). Owing to the heavy volume of interbank dealing, the three-month and six-month rates have come to be widely used as a basis of reference for the setting of many other interest rates. . . .” Graham Bannock and William Manser, *The Penguin International Dictionary of Finance*, p. 126 (1990).

composed of several international interest rates, LIBOR is an index used nationally by U.S. financial institutions and investors.⁸

Accordingly, we confirm that an index based on the six month LIBOR rate for U.S. dollar-denominated deposits and published in the Wall Street Journal as of a specified date would qualify as a national index pursuant to § 560.35(d)(2). We also find that the proposed index's regular publication in the Wall Street Journal, a major newspaper, satisfies the requirement in § 560.35(d)(1) that any index used be "readily available and independently verifiable." The Company's disclosure statement must comply with OTS regulation § 560.210,⁹ which imposes disclosure requirements for ARM loans.¹⁰

In reaching the foregoing conclusions, we have relied upon the representations made in the materials you submitted and in conversations with staff. Our conclusions depend upon the accuracy and completeness of those representations. Any material difference in facts or circumstances from those described herein could result in different conclusions.

⁸ See, for example, the attached description of six-month LIBOR indexed ARMS being offered by Fannie Mae. See also interagency Supervisory Statement of Policy on Securities Activities approved by the Federal Financial Institutions Examination Council and adopted by the federal banking agencies, which describes LIBOR as a conventional, widely-used market interest rate index. OTS Thrift Bulletin 52, Attachment 1, p. 11 (January 10, 1992); Office of the Comptroller of the Currency Supervisory Policy Statement on Securities Activities, Banking Circular BC 228 (Rev.) (January 10, 1992); Federal Reserve Board Supervisory Policy Statement on Securities Activities, SR 92-1 (January 10, 1992); Federal Deposit Insurance Corporation Supervisory Policy Statement on Securities Activities, 57 Fed. Reg. 4029 (February 3, 1992). See also National Credit Union Administration regulations, 12 C.F.R. § 703.5(j)(3)(1996).

⁹ 12 C.F.R. § 560.210 (1997).

¹⁰ In this regard, the disclosure statement should indicate that the LIBOR rate proposed for use is to be denominated in U.S. dollar deposits. You have not asked for, and we do not express any opinion on, the adequacy of the Company's proposed disclosure statement.

If you have any questions, please feel free to contact Ellen Sazzman, Counsel (Banking and Finance), at (202) 906-7133 or Evelyne Bonhomme, Counsel (Banking and Finance), at (202) 906-7052.

Very truly yours,

/s/

Carolyn J. Buck
Chief Counsel

Attachment

cc: All Regional Directors
All Regional Counsel