DEPARTMENT OF THE TREASURY

Office of Thrift Supervision

AGENCY: Office of Thrift Supervision (OTS).

ACTION: Notice of Intent to Discontinue and Request for Comment.

SUMMARY: The OTS is requesting public comment on its proposal to cease collection of data used to calculate and publish the Monthly Median Cost of Funds Index (MMCOF), the Quarterly Cost of Funds Index (QCOF), the Semiannual Cost of Funds Index (SCOF), and other related cost of funds ratios currently published monthly in the OTS's Cost of Funds (COF) Report.[1] At the end of the comment period, the comments and recommendations received will be analyzed to determine the extent to which the OTS should modify the proposal prior to giving final approval. The OTS will then submit the revisions to OMB for review and approval.

DATES: Comments must be submitted on or before [INSERT DATE 60 DAYS FROM DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: Interested parties are invited to submit written comments to the OTS.

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[1] Link to published COF reports: http://www.ots.treas.gov/?p=StatisticalReleases

You may submit comments, identified by "Cost of Funds Indices," by any of the following methods:

- Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.
- E-mail address: infocollection.comments@ots.treas.gov. Please include "Cost of Funds Indices" in the subject line of the message and include your name and telephone number in the message.
- Fax: (202) 906-6518.
- Mail: Information Collection Comments, Chief Counsel's Office, Office of Thrift Supervision, 1700 G Street, NW., Washington, DC 20552, Attention: "Cost of Funds Indices."
- Hand Delivery/Courier: Guard's Desk, East Lobby Entrance, 1700 G Street, NW., from 9:00 a.m. to 4:00 p.m. on business days, Attention: Information Collection Comments, Chief Counsel's Office, Attention: "Cost of Funds Indices."

Instructions: All submissions received must include the agency name. All comments received will be posted without change to the OTS Internet Site at http://www.ots.treas.gov/pagehtml.cfm?catNumber=67&an=1, including any personal information provided.

Docket: For access to the docket to read background documents or comments received, go to http://www.ots.treas.gov/pagehtml.cfm?catNumber=67&an=1.

In addition, you may inspect comments at the Public Reading Room, 1700 G Street, NW., by appointment. To make an appointment for access, call (202) 906-5922, send an e-mail to public.info@ots.treas.gov, or send a facsimile transmission to (202) 906-7755. (Prior notice

identifying the materials you will be requesting will assist us in serving you.) The OTS schedules appointments on business days between 10:00 a.m. and 4:00 p.m. In most cases, appointments will be available the next business day following the date we receive a request.

FOR FURTHER INFORMATION CONTACT: For further information about the revisions discussed in this notice, please contact Jim Caton, Managing Director – Economic and Industry Analysis, at (202) 906-5680.

In addition, copies of the reporting forms and instructions for cost of funds reporting requirements can be obtained at the OTS web site through the following link: http://www.ots.treas.gov/?p=StatisticalReleases.

SUPPLEMENTARY INFORMATION: The OTS is proposing to cease collection of data used to calculate and publish the MMCOF and to cease publication of the MMCOF, QCOF, SCOF, and other related COF indices.

Abstract

Some institutions submit MMCOF data to the OTS monthly for the OTS's use in calculating a monthly median cost of funds index. Additionally, the OTS publishes two indices based on calculations from data included in the Thrift Financial Report (TFR):[2]

1. A quarterly average cost of funds index, and
2. A semiannual average cost of funds index.

[2] Copies of the reporting forms and instructions for the TFR can be obtained at the OTS Web site (http://www.ots.treas.gov/?p=ThriftFinancialReports).

These indices are used by certain mortgage lenders as benchmarks from which to base rate adjustments for adjustable rate mortgages (ARMs).

Effect of Recent Legislation

The Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203 (the Dodd-Frank Act), was enacted into law on July 21, 2010. Title III of the Dodd-Frank Act abolishes the OTS, provides for its integration with the Office of the Comptroller of the Currency (OCC) effective as of July 21, 2011 (the "transfer date"), and transfers the OTS's functions to the OCC, the Board of Governors of the Federal Reserve System (Board), and the Federal Deposit Insurance Corporation (FDIC).

Under Title III of the Dodd-Frank Act, all functions of the OTS relating to federal savings associations and rulemaking authority for all savings associations are transferred to the OCC. All functions of the OTS relating to state-chartered savings associations (other than rulemaking) are transferred to the FDIC. All functions of the OTS relating to supervision of savings and loan holding companies (including rulemaking) are transferred to the Board.

Current Actions

After careful review, the OTS believes the volume of ARMs using COF indices the OTS publishes as benchmarks for ARM rate adjustments has declined significantly. In addition, the COF indices published by the OTS are being derived from data of fewer savings associations than they were in prior years as discussed in more detail later in this notice. Hence, these indices are subject to greater skewing from data outliers and extraneous data movements. For these

reasons, the OTS is proposing to eliminate the data collection used to calculate and publish the MMCOF index, as well as the publications of the QCOF, SCOF, and other related COF indices.

The OTS is proposing to implement changes to savings associations' data reporting requirements effective January 31, 2012. The proposed changes would require savings associations currently regulated by the OTS to cease filing data used to calculate the MMCOF index. Further publication of the MMCOF, the QCOF, the SCOF, and other related cost of funds ratios currently published monthly in the COF Report would cease as of January 31, 2012. The final COF Report would be for the month of December 2011. Until the effective date of these changes, savings associations would continue to file MMCOF data in the current manner using existing processes.

In making this proposal, the OTS reviewed its proposal made in 1994[3] to eliminate the MMCOF and the comments received regarding that proposal. The OTS also closely reviewed the changes in savings associations' aggregate asset composition and mortgage portfolio since the 1994 proposal, as well as recent changes in the overall mortgage markets.

As noted in the 1994 proposal, mortgage lending survey data from the then Federal Housing Finance Board (FHFB) indicated the indices published by the OTS were not widely used. For loans closed in March 1994, only 1.8 percent of ARMs were adjusted with indices included in the "Other Cost of Funds Indexes" – the category that included the MMCOF as well as the QCOF and SCOF.[4]

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[3] Link to 1994 proposal: http://www.ots.treas.gov/_files/4830057.pdf

[4] Comparable mortgage lending survey data is no longer published by the successor agency to the FHFB – the Federal Housing Finance Agency (FHFA).

Despite the low usage of these indices by lenders, the OTS decided not to pursue eliminating the MMCOF at that time. The primary reasons for this decision were comments regarding potential customer confusion and concern if the MMCOF index were discontinued.

The OTS notes that much has changed regarding the volume of ARMs held by savings associations and the number of institutions whose data comprise the MMCOF, QCOF, and SCOF indices. At the end of 1994, there were 1,526 OTS-regulated savings associations that participated in providing information to calculate the MMCOF. That number declined 52 percent to 733 at the end of the third quarter 2010. This decline has made the MMCOF index more susceptible to outlier and extraneous data movements.

The QCOF and SCOF are weighted averages of the cost of funds from all applicable OTS-regulated savings associations. Like the MMCOF, the decline in the number of OTS-regulated savings associations has made these indices more susceptible to outlier and extraneous data movements. This is especially true of these indices since weighted averages subject them to more skewing by large institutions and data outliers.

Additionally, the amount of adjustable rate residential mortgages and mortgage-backed securities held by savings associations has also declined since 1994 despite an increase in aggregate thrift industry assets. At the end of 1994, OTS-regulated savings associations held $774 billion in aggregate assets. Of that total, $304 billion, or 39.6 percent, were held in residential ARM loans and related securities. Though third quarter 2010 industry assets of $928 billion were higher than at the end of 1994, ARM holdings declined to $130 billion, or 14.0 percent of assets.

The decline in ARM loans and related securities with lagging market indices (LMI) – which include the MMCOF, QCOF, and SCOF among other LMIs – was more stark over this

period. At the end of 1994, savings associations' LMI ARMs totaled $152 billion, or 19.8 percent of assets. LMI ARMs held by savings associations declined 93 percent to just $10 billion, or 1.1 percent of assets as of September 30, 2010.

The general decline in savings associations' ARMs was attributable to low prevailing interest rates for fixed-rate loans during the past three years. These low rates have resulted in strong refinancing activity out of ARMs and into fixed-rate loans.

Due to the decline in savings associations' ARMs outstanding, especially for LMI ARMs, savings associations' reporting costs and burden associated with reporting for the MMCOF, agency costs and burden associated with the publication of these indices, and the declining number of institutions comprising these indices, the OTS is proposing to discontinue the publication of, and special data collections for all the OTS's COF indices.

Index Substitution

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Public Law 101-73 (FIRREA), was enacted into law on August 9, 1989. Section 402(e)(4) of FIRREA requires the OTS to designate acceptable substitute indices should it discontinue publication of indices used for ARM rate adjustments. To help designate acceptable substitute indices for the MMCOF, QCOF, and SCOF indices, the OTS analyzed the values and changes of 17 publicly available indices on a monthly basis from January 1990 through August 2010. The OTS compared the values and changes of the publicly available indices to those of the MMCOF,

QCOF, and SCOF. Correlation coefficients[5] were calculated for each publicly available index value to the MMCOF, QCOF, and SCOF.

Based on this analysis, the following indices were the most highly correlated to the MMCOF:

1. 11th District Cost of Funds (Source: The Federal Home Loan Bank of San Francisco (FHLB-SF)): Correlation 0.98
2. Federal Cost of Funds (Source: Freddie Mac (FHLMC)): Correlation 0.96
3. National Average Contract Mortgage Rate (Source: The Federal Housing Finance Agency (FHFA): Correlation 0.96
4. Monthly Treasury Average (MTA) (Source: Federal Reserve Board - H.15 FRSD): Correlation 0.93

The following were the most highly correlated to the QCOF:

1. 11th District Cost of Funds: Correlation 1.00
2. Federal Cost of Funds: Correlation 0.98
3. National Average Contract Mortgage Rate: Correlation 0.96
4. Monthly Treasury Average (MTA): Correlation 0.96

Quarterly averages were calculated from the monthly indices and used for calculating the correlation to the QCOF.

The following were the most highly correlated to the SCOF:

1. 11th District Cost of Funds: Correlation 1.00

[5] The correlation coefficient is a single number that describes the degree of relationship between two variables. A perfect positive correlation (a correlation co-efficient of +1) implies that as one index moves, either up or down, the other index will move in lockstep, in the same direction.

2. Federal Cost of Funds: Correlation 0.98
3. National Average Contract Mortgage Rate: Correlation 0.97
4. Monthly Treasury Average (MTA): Correlation 0.96

Semi-annual averages were calculated from the monthly indices and used for calculating the correlation to the SCOF.

As set out above, the same four publicly available indices had the highest correlation coefficients when compared to each of the OTS's COF indices. Though the correlation coefficients differed slightly, all were highly correlated to the OTS's COF indices.

It should be noted that due to the significant monetary actions taken to help the U.S. economy stabilize and fully recover from the most recent recession, some of the publicly available indices based on U.S. Treasury security rates – such as the MTA – have declined to levels below the OTS's COF indices. However, as indicated by the correlation coefficients, the movements of these indices track the OTS's COF movements well. Hence, the movements in these indices could possibly be used for future rate adjustments rather than the index value itself.

Request for Comment

Comments are requested on the proposed requirement that OTS-regulated savings associations cease filing data used to calculate the MMCOF index. Comments are also requested on what should be considered an appropriate substitute index for each of the OTS's COF indices

or alternatively, what should be considered an appropriate index to benchmark periodic changes to ARM rates based currently on the OTS's COF indices.

Comments submitted in response to this notice will become a matter of public record.

[THIS SIGNATURE PAGE PERTAINS TO THE NOTICE OF INTENT AND REQUEST FOR COMMENT; COMMENT REQUEST, FOR THE TERMINATION OF MONTHLY MEDIAN COST OF FUNDS REPORTING AND PUBLICATION OF COST OF FUNDS INDICES.]

Dated: FEB - 3 2011

By the Office of Thrift Supervision.

John E. Bowman
Acting Director.

Billing Code
OTS: 6720-01-P