MORTGAGE BANKERS ASSOCIATION

November 22, 2019

Mr. Jeffrey F. London
Executive Director
Loan Guaranty Service
U.S. Department of Veterans Affairs
810 Vermont Avenue, NW
Washington, DC 20420

Industry Views on Enforcement of VA Refinance Requirements

Dear Mr. London:

The Mortgage Bankers Association (MBA)[1] writes to share our views regarding implementation of section 309 of the *Economic Growth, Regulatory Relief, and Consumer Protection Act* (the Act)[2] by the U.S. Department of Veterans Affairs (VA). In recent weeks, VA has informed hundreds of mortgage lenders throughout the country that thousands of VA-guaranteed refinance loans originated in 2018 and 2019 may not be fully compliant with the requirements of the Act.

As a result of the highly irregular process by which lenders have received guidance to implement the requirements of the Act, including numerous documented instances of conflicting or inaccurate guidance provided by VA staff, the magnitude of impacted loans is sizable. MBA therefore requests that VA use its discretion to accept cures that will satisfy the requirements of the Act while also recognizing the unique challenges faced by lenders offering these cures. MBA is seeking reasonable solutions that work for borrowers, lenders, and investors.

VA is well aware of MBA's long-standing commitment to ending the practice of serial refinancing, or "churning," of VA-guaranteed loans. MBA has called on policymakers to address these concerns well before Congress began to legislate in this area. For

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, DC, the association works to ensure the continued strength of the nation's residential and commercial real estate markets, to expand homeownership, and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,300 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, credit unions, thrifts, REITs, Wall Street conduits, life insurance companies, and others in the mortgage lending field. For additional information, visit MBA's website: www.mba.org.

[2] Public Law 115-174.

example, in January 2018, then-MBA Chairman Dave Motley provided testimony to a House of Representatives subcommittee in which he stated that "MBA fully supports supervisory efforts to improve the policing of the market, as well as appropriate regulatory and legislative efforts to remove the ability or incentive for lenders to engage in churning."[3] In that testimony, Motley went on to comment that "such conduct is unacceptable and should be put to an end."[4]

MBA has also submitted several comment letters to both VA and the Government National Mortgage Association (Ginnie Mae) that featured detailed recommendations to deter churning in the VA-guaranteed market. These recommendations include support for the types of requirements put in place by the Act, such as maximum fee recoupment periods, minimum loan seasoning periods, and net tangible benefit tests. In many instances, MBA recommended bright-line standards and more stringent requirements than those put in place through recent reforms.

While the Act strengthened requirements related to VA-guaranteed refinances, its immediate effective date created severe challenges for both market participants and regulators.[5] One day after enactment of the Act, VA published Circular 26-18-13 to provide guidance to market participants on the implementation of section 309 of the Act with respect to Interest Rate Reduction Refinance Loans (IRRRLs). Unfortunately, ambiguous language in paragraph 3(a) sowed confusion among many lenders regarding proper application of the fee recoupment requirements established by the Act.

Specifically, paragraph 3(a) contains multiple references to an earlier guidance document – Circular 26-18-1 – that also addressed requirements for IRRRLs. Circular 26-18-1 requires lenders to provide borrowers with information regarding the fee recoupment periods associated with their loans. Paragraph 3(f) of that circular, however, expressly states that "in the case of an increased principal and interest payment due to a lower term, or from changing from an adjustable rate to a fixed rate, <u>it is not necessary to show the recoupment</u>…" (emphasis added).

The language found in the later guidance document – Circular 26-18-13 – requires lenders to "provide recoupment statements to VA in accordance with VA Circular 26-

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[3] Motley, J. David, "Home Loan Churning Practices and How Veteran Homebuyers are Being Affected." Testimony before the U.S. House Committee on Veterans' Affairs, Subcommittee on Economic Opportunity. January 10, 2018. Available at: https://www.mba.org/Documents/1%202018%20MBA_Testimony_Motley.pdf.

[4] Id.

[5] For example, the enactment of the Act led to the "orphaning" of thousands of VA-guaranteed refinances, by which these loans were denied eligibility for Ginnie Mae pooling. This problem required corrective legislation (the *Protecting Affordable Mortgages for Veterans Act of 2019*; Public Law 116-33), which was enacted in July 2019.

18-1" and to "certify that all fees and incurred costs, referenced in Circular 26-18-1, shall be recouped on or before the date that is 36 months after the date of the loan…"

The ambiguity regarding whether the exceptions provided in Circular 26-18-1 (increased monthly principal and interest payment due to a reduced term or change to a fixed rate) were incorporated by reference in Circular 26-18-13 led many lenders to seek further guidance from staff at VA Regional Loan Centers (RLCs). MBA has been made aware of many instances in which these VA staff explicitly instructed lenders that term reductions or adjustable-to-fixed refinances were exempt from the fee recoupment requirements described in Circular 26-18-13. This inaccurate guidance was not isolated to a single RLC employee or even to a single RLC; it was widespread and communicated to a substantial number of lenders over a lengthy period of time.

It is therefore unsurprising that the set of impacted loans and lenders grew so large. In many cases, lenders that initially interpreted Circular 26-18-13 to require fee recoupment without exception for all IRRRLs only began waiving fee recoupment requirements for term reductions or adjustable-to-fixed refinances in response to guidance from VA staff. In other words, these lenders changed their initial compliance policy in response to the erroneous guidance from VA staff.

Put simply, many responsible lenders made what they believed to be prudent decisions regarding their IRRRL originations based on direct input from VA staff. Those lenders will now incur significant costs to remediate these loans or face enforcement actions for violations of VA refinance requirements because they followed VA staff guidance.

The scale of the problem will lead to severe financial consequences for some of these lenders. The exact magnitude of the consequences, including whether some lenders' entire operations are jeopardized, will be dictated by the cures deemed acceptable by VA. As such, and because of the extenuating circumstances described above, MBA strongly recommends that VA provide significant flexibility to lenders that are engaging in good-faith efforts to ensure compliance with the requirements of the Act.

In determining whether to accept any particular cure, VA should recognize that a significant share of impacted loans already conferred benefits on borrowers. Meaningful term reductions or conversions to fixed rates provide important financial benefits for borrowers. Lenders should not be unduly penalized for originating such loans, and it would be inappropriate for VA to ignore existing borrower benefits when evaluating potential cures.

For example, if lenders are required to reimburse borrowers for fees collected as a result of the refinance, VA should count toward the recoupment any reduced interest payments made by borrowers due to the refinance (*e.g.*, from reducing the term) when determining the size of the necessary reimbursement.

In addition, for situations in which an impacted loan was already refinanced, VA should allow the prior lender to reimburse the fees incurred on the impacted loan, prorated for the number of months that loan was in existence (rather than the entirety of the fees). Such a cure would "make the borrower whole" for the period of time in which the loan was in place, while also reducing the cost burden on the lender. See below for an illustrative example.

Example	
Prior Monthly P&I:	$3,000
New Monthly P&I:	$3,100
Origination Fees:	$4,000
P&I Needed to Satisfy 36-Month Recoupment:	$3,000 – ($4,000/36) = $2,888
Monthly Reimbursement:	$3,100 – $2,888 = $212
Number of Months Loan in Existence:	10 Months
Reimbursement to Borrower:	**$212 x 10 Months = $2,120**

Some lenders have also indicated a desire to buy loans out of Ginnie Mae pools, modify them so as to lower the interest rate, and then re-pool these loans. This option adheres to the spirit of the existing requirements, and MBA urges VA to work closely with Ginnie Mae to facilitate its implementation.

Similarly, VA should provide flexibility with respect to the timelines associated with any potential cures. Because of the severe financial consequences for some lenders, it may not be feasible for them to cure all impacted loans immediately. Cures may need to be spread over a longer time horizon to ensure that lenders have the financial and operational capacity to implement them. VA should not object to lender plans to cure impacted loans simply because of the timing associated with these cures.

Finally, MBA is concerned about the processes and procedures that allowed VA staff to provide inaccurate guidance to lenders for such an extended period of time. It is encouraging that VA has recognized this problem and is instituting a structural reorganization with respect to Loan Guaranty Service staff and the RLCs. It is our hope that this reorganization will lead to an improved system that produces guidance that is clear, timely, consistent, and accurate. In the absence of these improvements, borrowers and lenders alike will continue to be adversely impacted, and some market participants may reconsider their participation in the VA home loan program.

MBA is committed to working with VA and other stakeholders to ensure that the issues arising from the market confusion regarding refinance requirements are resolved in an appropriate manner, and that the market for VA-guaranteed loans remains robust for borrowers, lenders, and investors. To that end, we would appreciate any opportunities to meet with you or other VA Loan Guaranty Service staff to discuss these issues and potential solutions.

Thank you in advance for your consideration of these comments. Should you have questions or wish to discuss further, please contact Dan Fichtler, Associate Vice President of Housing Finance Policy, at (202) 557-2780 and dfichtler@mba.org.

Sincerely,

Robert D. Broeksmit, CMB
President and Chief Executive Officer
Mortgage Bankers Association