MORTGAGE BANKERS ASSOCIATION

February 12, 2024

The Honorable Janet L. Yellen
Secretary of the Treasury
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

RE: FSOC Concerns About Nonbank Mortgage Servicers

Dear Secretary Yellen,

The Mortgage Bankers Association[1] writes today in response to certain comments you made regarding independent mortgage bankers (IMBs) during last week's hearings on the Financial Stability Oversight Council (FSOC)'s Annual Report to Congress.

In response to a question during your Senate testimony, you asserted that the gradual shift in mortgage market share away from banks and toward IMBs represents a risk to the stability of the global financial system. Further, you stated that IMBs "tend to have very little capital and loss absorbing capacity" and that "in stressful times their credit lines can be pulled." We believe each of these assertions exaggerates the actual risk of the business model while minimizing the crucial role IMBs play in facilitating credit access.

As MBA noted in its statement last Thursday in response to your testimony, IMBs play an indispensable role providing sustainable mortgage credit to, and servicing loans for, first-time and low- and moderate-income homebuyers. IMBs already face robust requirements related to capital, net worth, and liquidity – requirements that have increased sharply over the past 15 years at the direction of the Federal Housing Finance Agency (FHFA) and the

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 300,000 people in virtually every community in the country. Headquartered in Washington, D.C., 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 more than 2,000 companies includes all elements of real estate finance: independent mortgage banks, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies, credit unions, and others in the mortgage lending field. For additional information, visit MBA's website: www.mba.org

government-sponsored enterprises (Fannie Mae and Freddie Mac), the Government National Mortgage Association (Ginnie Mae), and the Federal Housing Administration (FHA). Furthermore, they face additional risk-management requirements from their warehouse lenders, state regulatory exams for capital, liquidity and governance standards, and consumer compliance supervision and enforcement by the CFPB.

The recent strengthening of these requirements has been done in response to FSOC's recommendations in its annual reports. The industry has worked constructively with the FHFA, Ginnie Mae, and state regulators to ensure these enhanced capital and liquidity requirements are aligned and properly calibrated to the risks of the IMB business model. We are concerned, however, that FSOC appears to presuppose[2] that IMBs pose systemic risks and is preparing to impose a solution – SIFI designation of IMBs or IMB activities -- where no problem exists.

Among MBA's 2,000 member companies are hundreds of non-bank mortgage servicers that engage in a core banking activity that is widely understood, easily transferrable, and decentralized. Today, even the largest IMB servicer comprises no more than a small fraction – less than 8% -- of the market for servicing outstanding single family mortgage debt. Of note, even today's largest non-bank mortgage servicers have balance sheet assets of less than $25 billion, well below the original SIFI asset threshold Congress established for banks in 2010, at least eight times smaller than the current bank asset threshold established by Congress in 2018, at least twenty times smaller than any of the non-bank entities FSOC has previously attempted to designate, and at least one hundred times smaller than the balance sheet assets of their largest counterparties, Fannie Mae and Freddie Mac. The concern that IMB servicers could pose a systemic risk to the entire U.S. financial system appears very remote and unfounded.

We recognize and support FSOC's mission of monitoring nonbank risks in the financial system, but as we noted in our comment letter[3] to the recently revised designation guidance, any assessment by FSOC must first look at the tools of existing regulatory entities to address any concerns they have identified. Federal regulators, under existing statutes and programmatic authorities, have ample ability to understand, closely monitor, and make programmatic adjustments to ensure the mortgage servicing business remains healthy.

For example, Ginnie Mae and FHFA can already mitigate the perceived risks of mortgage servicers to the broader financial marketplace by tweaking capital and liquidity standards, modifying mortgage servicing advance obligations, making programmatic changes, and taking steps to encourage new, smaller issuers to enter the market. As we saw during the

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[2] Chopra: Nonbanks, Mortgage Servicers May Also Pose Systemic Risk – NMP (nationalmortgageprofessional.com): "No one really believes that there is no nonbank that could offer the same type of contagion or same type of systemic effect" as SVB, he [Chopra] said.
[3] mba-fsoc-response-final.pdf

COVID pandemic, Fannie Mae and Freddie Mac acted at FHFA's direction to modify servicer agreements using the authority that already exists.

Your response in the Senate Banking Committee hearing noted that IMBs rely on the market to fund originations and advances. It is important to understand the context and historical record of how IMBs borrow and perform in times of stress. IMBs generally borrow from warehouse lenders by pledging secured collateral, and their warehouse lending partners have a long and strong track record of standing by their borrowers in times of stress—such as at the onset of the recent pandemic. While it may be prudent to explore a liquidity backstop in times of extreme distress for all market participants or changes to the reimbursement timing requirements for Ginnie Mae securities, IMBs have sound and well-tested lending relationships in a diverse and competitive credit market. Indeed, the larger threat to mortgage market stability may be existing regulations and ill-considered regulatory proposals that impose stress on other aspects of the system.

In the 15 years since the financial crisis, banks' share of mortgage origination and servicing volume has steadily declined. This decline undoubtedly reflects a reassessment of the economic returns available in mortgage lending and a shifting of resources into business lines that provide better returns on equity. It clearly also reflects regulations specific to banks which reduce the returns on capital from mortgage lending, as noted in report-outs from FSOC's own nonbank servicer task force.[4]

For example, the Basel capital framework's punitively high 250% risk weight on mortgage servicing rights (MSRs), coupled with a strict cap on the ratio of MSRs to Tier 1 capital, have significantly altered the economic incentives for banks to service mortgage loans for others. In a mortgage market dominated by securitization, MSRs are critically important. An excessively high risk weighting has discouraged banks from originating mortgages for securitization and retaining the servicing asset.

This highlights the critical question for FSOC: if bank regulations are so punitive that they discourage banks from effectively competing in markets for core banking services, shouldn't FSOC first re-examine the regulatory regime that caused this change? As we noted in our comment letter, the FSOC designation framework should require this analysis before "extending the regulatory perimeter" to nonbank entities that are serving a market for which banks have pulled back. This is particularly important in the mortgage market, where banks should be able to leverage their lower cost of funds, preemption of many state laws, and access to the payments system and liquidity backstops. If policymakers are concerned about the growth of nonbank market shares for traditional banking services, they should first examine whether existing rules are impeding banks' ability or desire to serve those markets.

Notably, the recent Basel III "Endgame" proposal would only exacerbate this issue. By reducing the MSR cap as a percentage of CET1 from 25 percent to 10 percent for certain

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[4] FSOC_20230421_Minutes.pdf (treasury.gov); page 7.

banks, certain market participants will have no choice but to further retreat from participation in the mortgage market.

The Basel III "Endgame" proposal would also negatively impact the availability and cost of warehouse lending for IMBs. Specifically, the proposed increase in the Credit Conversion Factor (CCF) for warehouse commitments, including the undrawn portion of the commitment, risks making warehouse lending an unattractive line of business for many banks. MBA is concerned that if warehouse lenders are required to hold more capital – against the undrawn portion of their lines -- they could either decide to exit this line of business or charge IMBs more. Regardless of the outcome, it would mean a higher cost of credit for all borrowers. Retaining the current CCF and lowering the risk weight on warehouse lines to reflect the risk weight of the underlying collateral will increase the capacity of banks to fund more loans, thereby providing much-needed support to the real estate finance market and ensuring the continued flow of mortgage credit.

Ultimately, the real estate finance system is the most healthy and stable, and consumers win, when a greater number of actors utilizing a range of business models and strategies compete on a level playing field. Simply imposing higher costs across the system will only burden prospective homeowners with higher prices and fewer choices at a time of constrained housing affordability.

We have articulated these concerns to the FSOC staff and shared our in-depth data on the IMB sector. We request the opportunity to meet with you to discuss the current state of the mortgage market and the concerns you expressed about the strength and resilience of the IMB business model, the crucial role IMBs play in the market today to expand credit access to underserved communities, as well as actions that can and should be undertaken to bring depository institutions back into the mortgage market. Please reach out to me directly (bob@mba.org) or to Pete Mills, Senior Vice President of Residential Policy (pmills@mba.org). Thank you in advance for your consideration.

Sincerely,

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

CC: Sandra Lee, Deputy Assistant Secretary, Financial Stability Oversight Council
Daniel Hornung, Deputy Director, National Economic Council