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MORTGAGE BANKERS ASSOCIATION

August 9, 2021

Michael R. Drayne  
Acting Executive Vice President  
Ginnie Mae  
425 3<sup>rd</sup> Street, SW, Suite 500  
Washington, DC 20024

**Re: Request for Input on Eligibility Requirements for Single-Family MBS Issuers**

Dear Acting Executive Vice President Drayne:

The Mortgage Bankers Association (MBA)<sup>1</sup> thanks Ginnie Mae for the opportunity to provide our observations and recommendations on its Request for Input (RFI) regarding eligibility requirements for single-family mortgage-backed security (MBS) issuers.<sup>2,3</sup> MBA appreciates the proactive engagement by Ginnie Mae in soliciting industry feedback on a variety of policy issues, including capital, liquidity, and net worth requirements for program participants.

MBA consistently has supported robust financial eligibility requirements that help ensure Ginnie Mae issuers are able to withstand idiosyncratic market dislocations or periods of broader economic stress. A well-calibrated set of requirements should promote safety and soundness while not unduly restricting issuer participation and growth or raising the cost of credit for consumers.

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<sup>1</sup> The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 330,000 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 1,900 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](http://www.mba.org).

<sup>2</sup> Ginnie Mae, "Request for Input: Eligibility Requirements for Single-Family MBS Issuers," July 9, 2021. Available at: [https://www.ginniemae.gov/newsroom/publications/Documents/Financial%20Requirements%20RFI\\_v2.pdf](https://www.ginniemae.gov/newsroom/publications/Documents/Financial%20Requirements%20RFI_v2.pdf).

<sup>3</sup> Voluntary response provided to HUD in response to an RFI. This is not a required submission for participation in a federal program.

The Ginnie Mae proposals related to liquidity and net worth, though in need of targeted adjustments, are constructed in a manner that could achieve this balance. MBA has significant concerns, however, regarding the Ginnie Mae proposal related to a risk-based capital ratio requirement. This proposed requirement – a novel approach in the context of Ginnie Mae financial eligibility requirements – is unnecessarily punitive in its treatment of mortgage servicing rights (MSRs), inappropriately calibrated for the business models of the issuers to which it would apply, and insufficiently tested for a thorough understanding of its potential impact. As such, MBA fears that its implementation, as proposed, could reduce issuer participation and diversity, severely undermine market demand for Ginnie Mae MSRs, reduce aggregator demand for government-insured or -guaranteed loans, and lead to higher interest rates and diminished access to credit for consumers. This outcome would be particularly problematic given the low- to moderate-income, veteran, and rural homebuyers predominantly served by the loans backing Ginnie Mae securities.

In light of these concerns, MBA recommends that Ginnie Mae withdraw the proposed risk-based capital ratio requirement and pause any efforts to implement it. To the extent Ginnie Mae feels that such a requirement is necessary, it first should (i) assess the key business risks and market conditions that have driven historic issuer defaults; (ii) follow a thorough analytical framework to identify and understand the intrinsic risks associated with various assets held by issuers; (iii) engage with issuers to observe how they monitor, manage, and mitigate these risks; (iv) undertake significant impact analysis and backtesting to more fully understand the effects of the requirement on individual issuers, various categories of issuers, the MSR market, and consumers; (v) develop risk weightings that reflect the relevant risks and risk mitigants; (vi) allow issuers further opportunities to analyze and comment on these risk weightings; (vii) recalibrate the parameters of the requirement as necessary; and (viii) allow a reasonable implementation period to prevent shocks to the market.

More broadly, MBA has engaged with the Federal Housing Finance Agency (FHFA), Fannie Mae and Freddie Mac (the government-sponsored enterprises, or GSEs), and the Conference of State Bank Supervisors (CSBS), as well as Ginnie Mae, as these organizations simultaneously have considered changes to capital, liquidity, and net worth requirements primarily directed at independent mortgage bank (IMB) servicers. MBA frequently has called for alignment between the requirements adopted or recommended by these organizations – and continues to do so.<sup>4</sup>

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<sup>4</sup> MBA, “Industry Views on Updated Eligibility Requirements for Enterprise Single-Family Seller/Servicers,” April 30, 2020, Available at: [https://www.mba.org/Documents/MBA\\_FHFA\\_IMB\\_Financial\\_Requirements\\_April2020.pdf](https://www.mba.org/Documents/MBA_FHFA_IMB_Financial_Requirements_April2020.pdf). MBA, “RE: Proposed Regulatory Prudential Standards for Nonbank Mortgage Servicers,” December 28, 2020, Available at: [https://www.mba.org/Documents/MBA\\_CSBS\\_IMB\\_Prudential\\_Standards\\_December2020\(0\).pdf](https://www.mba.org/Documents/MBA_CSBS_IMB_Prudential_Standards_December2020(0).pdf).

The case for aligned requirements is compelling. Many IMB servicers are subject to the requirements put in place by FHFA (because they are GSE seller/servicers), Ginnie Mae (because they are Ginnie Mae issuers), and state regulators (in the states in which they do business). The most stringent among these requirements at any given time becomes binding for the servicer, and the other requirements therefore provide little benefit with respect to safety and soundness. Misaligned requirements also lead to higher compliance costs for servicers, which represent wasted resources given the lack of incremental safety and soundness that they produce. For these same reasons, the federal banking regulators have gone to great lengths to align the capital and liquidity requirements in place for the institutions they oversee.

Perhaps most importantly, there is no logical reason for significant differences to exist among the requirements applicable to IMB servicers. FHFA, the GSEs, Ginnie Mae, and CSBS seek to promote stable operations and financial resiliency at IMB servicers, and these common goals should be achieved through a common regulatory and supervisory approach.

Finally, there are several additional enhancements to the Ginnie Mae program and the broader housing finance system that would reduce risks and bolster safety and soundness – particularly with respect to IMB servicers. In the Ginnie Mae program, these enhancements include policies that:

- re-balance advancing obligations,
- make emergency liquidity more consistently available,
- promote enhanced access to third-party financing of MSR advances separate from MSRs,
- diversify the sources of MSR ownership, and
- allow for loan-level capabilities.

For the broader housing finance system, these policy recommendations include:

- better aligning Federal Housing Administration (FHA) servicing policies with those of the GSEs and eliminating unnecessary risk related to the improper use of the False Claims Act,
- reducing the punitive treatment of MSRs in capital rules applicable to depository institutions,
- expanding eligibility for Federal Home Loan Bank (FHLB) membership, and
- re-calibrating agency MBS margining practices and requirements.

Ginnie Mae and other federal and state agencies should pursue these policies in tandem with any changes to capital, liquidity, and net worth requirements. Together, these policies will strengthen the housing finance system while increasing access to responsible and sustainable credit for consumers.

### ***Risk-Based Capital***

In the RFI, Ginnie Mae proposes to introduce a risk-based capital ratio requirement for all IMB and credit union issuers. This proposed requirement follows the statement from Ginnie Mae that it “observe[s] significant differences in mortgage bank balance sheets, but current program requirements are unable to address these differences.”<sup>5</sup> Ginnie Mae defines this risk-based capital calculation as the ratio of an issuer’s adjusted net worth, less any “excess MSR,” divided by risk-based assets. Issuers would be required to maintain a ratio of no less than 10 percent.

While the observations and recommendations below discuss granular issues related to this proposed requirement, MBA’s overarching concern is that the highly punitive treatment of MSRs does not accurately reflect the economic and financial risks of this asset class. Excessively harsh treatment would severely constrict demand and liquidity in the market for MSRs and in third-party purchases of government-insured or -guaranteed loans, which in turn would make mortgage servicing less attractive, raise costs associated with financing and hedging MSRs, and ultimately make mortgage credit more expensive for consumers.

MBA therefore believes these unintended consequences of this proposed requirement necessitate its withdrawal and an indefinite pause on efforts to implement it. Ginnie Mae should more thoroughly evaluate whether such a risk-based capital ratio requirement is needed to ensure financial resiliency and explore alternative approaches. If Ginnie Mae does decide to proceed, it should follow the process outlined above, including steps to conduct backtesting, impact analysis, and recalibration to eliminate the potential for any harmful effects on issuers, the MSR market, and consumers.

### Conceptual Issues

In many contexts, the use of a risk-based capital ratio requirement in financial regulation is preferable to that of a risk-insensitive leverage ratio requirement. When leverage ratios serve as binding constraints for financial institutions, the institutions typically maintain incentives to increase their holdings of higher-risk assets, in an effort to generate higher returns without increasing their required levels of minimum capital.

The use of binding risk-based capital ratio requirements generally works well in situations in which financial institutions hold a variety of assets that feature different levels of risk and return, as typically is the case for larger, diversified banks. Many IMB servicers, however, hold only a few types of assets – primarily MSRs and GSE- or

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<sup>5</sup> Ginnie Mae, “Request for Input: Eligibility Requirements for Single-Family MBS Issuers,” July 9, 2021. Available at: [https://www.ginniemae.gov/newsroom/publications/Documents/Financial%20Requirements%20RFI\\_v2.pdf](https://www.ginniemae.gov/newsroom/publications/Documents/Financial%20Requirements%20RFI_v2.pdf).

government-backed loans, as well as cash, cash equivalents, and government securities. This limited set of assets reflects the business models and monoline nature of many IMB servicers. Because they do not hold a wide variety of loans, securities, and other financial instruments with differing levels of risk, it is not feasible for them to meaningfully change the risk profile of their portfolios, unless they move a greater portion of their assets into cash, cash equivalents, or government securities. Properly calibrated net worth and liquidity requirements therefore are more effective than risk-based capital requirements.

As such, it is not immediately clear how a risk-based capital framework would translate into improved financial resiliency for IMB servicers. If Ginnie Mae's objective is to increase the cash positions of its issuers, this objective can be accomplished using existing liquidity requirements. The proposed risk-based capital ratio requirement instead penalizes the most common asset on IMB servicers' balance sheets and serves as an inefficient method of raising minimum thresholds for cash holdings.

Ginnie Mae also does not articulate the specific concerns that it seeks to address with respect to issuers' MSR holdings. While MSRs are an interest rate-sensitive asset class, they typically serve as a "natural hedge" for issuers' origination businesses (if held under a fair value accounting treatment), with rising valuations as interest rates increase. These higher valuations offset the reduced origination volumes and revenues expected when interest rates increase. (This negative correlation was displayed in reverse in the period immediately following the onset of the COVID-19 pandemic, as rising origination volumes and revenues offset declines in MSR valuations.)

Several larger issuers also engage in derivative-based hedging strategies to further reduce exposure to asset value and cash flow volatility caused by changes in interest rates. Issuers across the industry have developed a strong understanding of the financial management of MSRs, including more accurate valuation modeling and greater ability to hedge volatility. Together, these developments have improved risk analysis and assessment and have led to a more transparent MSR market than existed even a decade ago.

#### Calculation Methodology

The RFI does not provide details regarding the rationale for the calculation methodology, including how Ginnie Mae determined that 10 percent was the appropriate minimum threshold for this ratio. It is unclear how the proposed risk weights relate to identified risks or whether any modeling or assessment of historical fluctuations in MSR values (or projected changes in future MSR values under different economic scenarios) was used.

The proposed calculation methodology features unnecessarily harsh constraints on MSRs in both the numerator and the denominator. The subtraction of "excess MSRs"

in the numerator serves as a dollar-for-dollar cap on the contribution of MSR to issuers' ability to satisfy this requirement, despite MSR representing one of the most important assets held by many servicers. In effect, the subtraction of excess MSR penalizes large MSR portfolios in ways that are counterintuitive for institutions that are designed to hold, and manage the risks associated with, MSR. It also is unclear whether the proposed requirement defines excess MSR as net of deferred tax liabilities, as is the case in the Basel framework in place for banking institutions.

Similarly, a 250 percent risk weighting in the denominator of this calculation is grossly inconsistent with the underlying risks of MSR. While Ginnie Mae does not provide a clear rationale for this risk weight in the RFI, presumably the objective was to align with the Basel framework. Doing so, however, simply would import the demonstrably flawed Basel methodology – which has contributed to a significant decline in bank participation in the mortgage servicing market – to other types of servicers. Indeed, the punitive Basel risk weight is likely driven in part by the lack of familiarity with MSR by European regulators rather than by a sound understanding of the inherent risks associated with the asset class.

MBA has long advocated for a more sensible risk weight for MSR in the Basel context and therefore believes it would be a mistake for Ginnie Mae or other U.S. agencies to mirror this misguided policy choice. The use of a 250 percent risk weight in the Ginnie Mae proposal is even more problematic when viewed in the context of the other specified risk weights. With the exception of MSR, no asset class is assigned a risk weight greater than 100 percent. This construct implies that Ginnie Mae views MSR as a far riskier asset than any other asset that an issuer conceivably could hold. This view is inconsistent with prior Ginnie Mae supervision, the business models of IMB servicers, and the realities of the MSR market.

The proposed calculation methodology also does not distinguish between hedged MSR portfolios and unhedged MSR portfolios. This blunt view of MSR holdings fails to accurately differentiate between the risks of hedged and unhedged portfolios and represents a missed opportunity to encourage greater use of hedging. Further, the proposed methodology would penalize issuers that use cash to purchase MSR hedges by increasing their required capital relative to issuers that do not hedge. As was noted earlier, issuers have developed more efficient and effective means of hedging MSR, and a capital regime that both ignores the benefits of hedging and penalizes those issuers that do so will exhibit serious deficiencies.

The proposal also includes a particularly broad category of "Other Assets" that features a 100 percent risk weight. The presence of such a broad category would capture certain assets, such as prepaid expenses, that do not warrant this relatively high risk weight. To address this problem, Ginnie Mae should provide more granular categories

of assets in the proposal's risk weighting to reflect the fact that other types of low-risk assets may be held on issuers' balance sheets.

MBA also requests further clarity on the treatment of securitized assets that are held in structures such as variable interest entities. Without specific guidance from Ginnie Mae, these assets could be consolidated into an issuer's total assets for purposes of the risk-based capital ratio requirement because they do not receive sale treatment. This outcome could unnecessarily inflate the denominator in the calculation, making it more difficult for certain issuers to meet this requirement.

### Backtesting

It is not apparent that Ginnie Mae performed backtesting of this requirement to determine how many issuers would have been in violation of the minimum threshold at varying points in the credit cycle. While the number of issuers in violation appears to be modest in 2020, a year in which industry profits were quite high, MBA's preliminary analysis of nearly 200 issuers suggests that a much larger set of issuers would have been in violation in 2018 and 2019 (more than 10 percent of issuers in the fourth quarters of these years). Because several of these issuers have large MSR portfolios, the issuers that would have been in violation of the risk-based capital ratio requirement hold an outsized share of Ginnie Mae MSRs.

If Ginnie Mae's justification for the fast implementation timeline proposed in the RFI is in part attributable to the belief that few issuers would fail to meet this new requirement, this argument needs to be tested against several different historical scenarios. If, as MBA's preliminary analysis suggests, an elevated number of issuers would have been in violation of this requirement had it been in place in recent years, this serves as further evidence that the requirement is in need of re-calibration or, at a minimum, warrants a much longer implementation period. Such backtesting should be conducted over several years and a full credit cycle, including periods of varying margins and origination volumes, to determine whether the proposed risk-based capital ratio requirement is designed properly.

### Potential Impacts

The punitive treatment of MSRs in this proposal is likely to lead to severe negative impacts on the demand for government-insured or -guaranteed loans and the broader MSR market. Issuers will find MSRs to be less attractive investments, and providers of MSR financing may pull back from the market or offer far more costly terms – perhaps decreasing financing levels from the roughly 60-70 percent observed in the current market to dramatically lower advance rates.

The experience of banks subject to excessive risk weights and tight caps on MSRs under the Basel framework is instructive. This capital treatment is one of the primary drivers of the widespread retreat of banks from mortgage servicing, particularly for

loans backing Ginnie Mae securities. There is little reason to think that IMB or credit union servicers will react any differently when subject to similar constraints. If the capital required to hold MSR's leads to severely diminished returns on these assets, it will drive institutions away from servicing, regardless of their business model. Application of the misguided Basel framework for IMB or credit union servicers, moreover, will do nothing to encourage banks to become more engaged in mortgage servicing, thus undermining Ginnie Mae's objective of ensuring a deep and liquid market for Ginnie Mae MSR's.

Together, these policies will bring lower demand and reduced liquidity for both government-insured and -guaranteed loans and MSR's. Downward price volatility is likely to be sharp in the early stages of the implementation of this requirement, as the negative shock to the valuation of loans in issuers' pipelines represents an immediate impact that cannot be hedged. Similarly, forced sellers of Ginnie Mae MSR's could flood the market and overwhelm the demand from potential buyers, leading to amplified price declines. These price declines would impact all holders of MSR's – not just those that are active sellers – as institutions borrowing against these assets would be forced to meet additional margin calls or have difficulty hedging. These negative impacts could be felt in the GSE MSR market, as well, due to the inclusion of all MSR's (and the lack of differentiation across various types of MSR's) in the proposal.

These negative impacts are likely to manifest in different ways – and with different severities – based on the different business models employed by issuers. It is not clear, however, that Ginnie Mae has considered the disparity in potential impacts, particularly for issuers with unique business models or funding structures. While MSR holdings and the use of leverage certainly are factors that would influence the severity of the proposal for a given issuer, other important factors include whether the issuer maintains whole loans in its portfolio, whether the issuer primarily originates or serves as an aggregator, and whether the issuer services loans in-house or contracts primarily with a servicer.

Over the longer run, many institutions may exit the market for originating and servicing government-insured or -guaranteed loans, leading to consolidation in the industry and within the Ginnie Mae issuer base. This result would increase concentration risk for Ginnie Mae – a perverse outcome with respect to the safety and soundness of the broader system.

While this series of events would be quite damaging to a large swath of Ginnie Mae issuers, the negative impacts would be felt most acutely by consumers seeking government-insured or -guaranteed loans. Soft demand for these loans and the resulting MSR's flows through to higher interest rates, and therefore higher costs and fewer choices, for consumers. Increased costs would make mortgage credit less accessible in the loans that disproportionately serve low- to moderate-income and

minority borrowers, a result that is at odds with ongoing efforts by government, private sector, and non-profit entities to reduce disparities in access to affordable mortgage credit.

### Other Issues

The proposed system of risk weighting constructed by Ginnie Mae does not include any potential for consideration of risk transfer mechanisms employed by issuers. Without the possibility for bona fide transfers of risk to be recognized, it is unlikely that issuers will pursue or develop such mechanisms. This construct would inhibit efforts by issuers to de-risk their portfolios and, as a result, would serve as a missed opportunity to reduce counterparty risk for Ginnie Mae. While issuers currently are not employing such risk transfer mechanisms on a consistent basis, the proposal should recognize the potential for these mechanisms to develop further and become more commonly used.

Separately, while naming conventions may be considered a matter of semantics, the use of the term “excess MSR” is likely to generate confusion among issuers and other market participants given the existing, widely-accepted use of the term “excess servicing.” If this concept remains in any finalized requirements and Ginnie Mae seeks to define the MSR exceeding an issuer’s adjusted net worth, it should refer to them as “incremental MSR above adjusted net worth” or a term to this effect.

### ***Liquidity***

Ginnie Mae further proposes to amend its minimum liquidity thresholds by requiring single-family issuers to hold liquid assets in proportion to their outstanding GSE obligations (5 basis points) and their Held for Sale (HFS) loans (20 basis points). In the RFI, Ginnie Mae notes that “the current requirement does not address liquidity demands from sources other than Ginnie Mae obligations and does not address interest rate risk of loans in the origination pipeline.”<sup>6</sup>

### GSE Obligations

It is not unreasonable for minimum liquidity requirements to reflect the multiple business lines in which issuers engage, so as to prevent “double counting” of the same resources for the purposes of meeting separate requirements put in place by Ginnie Mae and by FHFA and the GSEs. The references to GSE obligations in the Ginnie Mae requirements, as well as expected references to Ginnie Mae obligations in forthcoming FHFA/GSE requirements, therefore have a clear conceptual basis.

In order for these updated requirements to achieve their intended purpose, however, it is critical that Ginnie Mae and FHFA and the GSEs align the multipliers that are used

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<sup>6</sup> Id.

in their calculations. The proposed Ginnie Mae requirements of 10 basis points on Ginnie Mae obligations and 5 basis points on GSE obligations are similar – but not identical – to those proposed by FHFA in January 2020 (10 basis points on Ginnie Mae obligations and 4 basis points on GSE obligations).<sup>7</sup>

In particular, it would make little sense for Ginnie Mae to impose a higher liquidity requirement on GSE obligations than one that FHFA puts in place, given FHFA's role as the primary regulator of the GSEs. Indeed, if Ginnie Mae were to implement its proposed requirements on the timeline suggested in the RFI, its liquidity requirement on GSE obligations would be higher than that of FHFA, at least for some period of time. This is a paradoxical outcome that should be avoided. Further recommendations regarding both the need for alignment across the agencies and the benefits of a more measured implementation period appear below.

In order to understand whether the proposed 5-basis-point multiplier on GSE obligations is appropriately calibrated, it is necessary to understand the risks that Ginnie Mae is attempting to address. If one of the main liquidity risks stems from advancing obligations on delinquent loans, for example, these risks differ materially for loans that feature actual servicing remittances relative to scheduled servicing remittances (which in turn implies differences across the two GSEs and the use of the cash window relative to MBS swaps). In its pursuit of alignment with the requirements put in place by FHFA and the GSEs, Ginnie Mae should ensure that any recognition of the lower advancing risk associated with actual servicing remittances is reflected in its requirements, as well.

Ginnie Mae also should provide clarity regarding the measurement of the GSE obligations within the final calculation of the minimum liquidity requirement. The final calculation in the RFI references GSE *single-family* obligations (emphasis added), while the description of this requirement in the RFI references GSE outstanding obligations. Any language incorporated into the MBS Guide should specify that the additional GSE component of this requirement relates only to single-family obligations.

#### Held For Sale Loans

The second proposed add-on to the Ginnie Mae liquidity requirements relates to issuers' HFS loans. This is a new concept that appears to target the liquidity risks associated with loans not yet delivered into Ginnie Mae pools. While Ginnie Mae does not provide details in the RFI, the proposal seems to stem from the potential for pipelines of closed loans to decrease in value prior to their securitization due to a rise in interest rates in this intervening period. Alternatively, in rare and extraordinary situations such as the market conditions observed in March 2020, lenders that hedge

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<sup>7</sup> FHFA, "Updated Eligibility Requirements for Enterprise Single-Family Seller/Serviceers," January 31, 2020. Available at: <https://www.fhfa.gov/Media/PublicAffairs/Documents/Serviceer-Eligibility-FAQs-1302020.pdf>.

these pipelines using short positions in the To-Be-Announced (TBA) market could face short-term losses on their hedges due to sharp upward movements in agency MBS valuations.

Large-scale, mark-to-market losses on pipeline hedges in March 2020 were not due to purely market-based events; they were caused by unprecedented policy interventions by the Federal Reserve. While these interventions were necessary to stabilize the economy following the severe shock brought about by the onset of the COVID-19 pandemic, they resulted in unintended negative consequences for many mortgage originators.

When considering the liquidity risks associated with margin calls on pipeline hedges, Ginnie Mae should recognize that severe risks are unlikely to arise from normal or even outlier market movements. Minimum Ginnie Mae liquidity thresholds should not be calibrated to account for the risks emanating from truly extraordinary government policy interventions caused by an extraordinarily rare global public health emergency. Such a standard is far too conservative and ignores better ways to manage these rare occurrences. The most productive policy response to this risk would be to address the manner in which margin calls on pipeline hedges are calculated and executed in times of stress. Further details on this issue appear below.

The 20-basis-point liquidity multiplier on HFS loans also may be set at a higher-than-necessary level because the proposal does not recognize differences in seasoning or dwell times for these loans – that is, the amount of time that the loans have been held on an issuer's balance sheet. Many loans in issuers' HFS portfolios are government-insured or -guaranteed loans that will be securitized (and effectively turned into cash) within 30 days. These loans therefore are highly-liquid assets and should not be subject to the same liquidity requirements as loans classified as HFS which are held on an issuer's balance sheet for longer periods of time. While differentiating between HFS loans based on seasoning or dwell times would add complexity to the proposal (for example, by necessitating exemptions for loans originated through programs offered by housing finance agencies that may take longer to securitize), Ginnie Mae should explore this option to understand how it could better reflect the true liquidity risks associated with these assets.

Ginnie Mae should provide additional details regarding the calculations underpinning the liquidity requirement on HFS loans, as well. It is not clear, for example, whether HFS loans are meant to capture only single-family loans or a broader set of loans. It also appears that HFS loans are calculated following a series of adjustments (deferred fees and costs, basis adjustments from hedging, etc.), though this is not specified in the RFI. Further, if HFS loans are calculated post-adjustments, it appears that this calculation is being applied to all HFS – not only to government-insured or -guaranteed loans. Finally, it is not clear whether early buyouts (EBOs) are classified as HFS loans

for purposes of this calculation. If they are classified as HFS loans, this proposed requirement would serve to penalize EBOs given the additional liquidity that would have to be held against them, as well as the higher risk weight associated with HFS loans relative to Ginnie Mae loans eligible for repurchase.

#### Committed Servicing Advance Lines of Credit

The proposed liquidity requirements in the RFI continue to rely on Ginnie Mae's existing classification of liquid assets, which permits the use of cash, cash equivalents, and AAA-rated U.S. government securities to meet the requirements. This narrow set of allowable liquid assets ignores a readily-available source of liquidity for many issuers – the unused portions of committed servicing advance lines of credit.

Such lines feature committed funding from reliable counterparties that typically can be withdrawn only in response to one or more specific covenant violations. Many issuers use these committed lines of credit to address liquidity needs that arise from advancing obligations with respect to delinquent loans in their servicing portfolios. Issuers would be borrowing against pristine collateral: servicing advance receivables on loans that primarily are government-insured or -guaranteed (or GSE-guaranteed).

By excluding the unused portions of committed servicing advance lines of credit, Ginnie Mae fails to provide an important incentive for issuers to obtain and pay for these committed lines of credit. Many issuers may determine that, absent the ability to help satisfy liquidity requirements, the costs of obtaining committed lines of credit (in contrast to uncommitted lines of credit) are too great and forgo them altogether. This outcome diminishes, rather than strengthens, aggregate issuer liquidity.

If the proposal does not provide recognition for committed lines of credit, issuers will have a perverse incentive to draw these lines down at the end of each reporting period to strengthen their liquidity positions, only to reverse these actions shortly thereafter. These steps would do nothing to improve the actual resiliency of issuers, but rather would lead to a substitution of available liquidity sources for reporting purposes.

Ginnie Mae also should reconsider this exclusion in light of the industry's recent experience during the COVID-19-induced market downturn. Despite widespread concerns regarding liquidity and potential advancing obligations in March 2020, committed lines of credit to issuers remained in place and were available without interruption. If these lines of credit were durable enough to withstand a sharp and unanticipated global recession and a severe macroeconomic shock, it is not clear what type of scenario would lead to their widespread withdrawal.

### ***Net Worth***

The RFI also proposes a change to the Ginnie Mae minimum net worth requirement, adding an amount equal to 25 basis points of an issuer's outstanding GSE obligations. This potential addition is similar in substance to the change in minimum net worth requirements for GSE seller/servicers proposed by FHFA in January 2020.<sup>8</sup> Again, Ginnie Mae notes in the RFI that it seeks to "address all lines of mortgage banking activity...and the entirety of the issuer's financial profile."<sup>9</sup>

As was noted above with respect to the proposed liquidity requirements, it is not unreasonable for minimum net worth requirements to reflect the multiple business lines in which issuers engage, so as to prevent "double counting" of the same resources for the purposes of meeting separate requirements put in place by Ginnie Mae and FHFA and the GSEs. MBA did not object to this general construct when proposed by FHFA in January 2020 and does not do so with respect to this RFI.

### Additional Clarity

MBA requests additional information from Ginnie Mae regarding the "total single-family pools funded" component of the outstanding Ginnie Mae obligations contained within the minimum net worth calculation. It is not clear what this component is intended to capture, nor is it clear how it differs from the component related to outstanding Ginnie Mae securities.

As was noted with respect to the proposed liquidity requirements, Ginnie Mae should be as precise as possible when defining total Ginnie Mae or GSE obligations relative to single-family Ginnie Mae or GSE obligations. The RFI describes the proposed net worth requirement by noting that the components of the Ginnie Mae obligations are specific to the single-family market, but the final calculation does not label the Ginnie Mae portion as "single-family." Similarly, the final calculation references GSE outstanding obligations, in contrast to the final calculation for the liquidity requirement, which references GSE *single-family* obligations (emphasis added). The final net worth calculation should address only single-family obligations, and therefore the language that is incorporated into the MBS Guide should specify that this is the case.

To provide further clarity to issuers, Ginnie Mae also should specify how the calculation of available commitment authority may be impacted by an issuer's participation in the Pools Issued for Immediate Transfer (PIIT) program. Several issuers who are PIIT sellers have inquired as to whether agreed-upon co-issue arrangements for a specified

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<sup>8</sup> Id.

<sup>9</sup> Ginnie Mae, "Request for Input: Eligibility Requirements for Single-Family MBS Issuers," July 9, 2021. Available at: [https://www.ginniemae.gov/newsroom/publications/Documents/Financial%20Requirements%20RFI\\_v2.pdf](https://www.ginniemae.gov/newsroom/publications/Documents/Financial%20Requirements%20RFI_v2.pdf).

volume result in a commensurate decrease in their available commitment authority, as the servicing is issued in the name of the PIIT buyer at the time of issuance.

## ***Implementation***

### Alignment

As is noted above, success in implementing any new financial eligibility requirements rests on the ability of Ginnie Mae, FHFA, the GSEs, and state regulators through CSBS to align their respective frameworks. Alignment across these entities would provide a unified approach to the financial resiliency of covered servicers. Such a unified approach would reduce burdens on regulators and examiners as well as on servicers.

Regulators and examiners would have a clearer understanding of the risk management processes of servicers, better engage in information sharing, and be able to better coordinate any supervisory actions. These process improvements would enhance the agencies' capacity to identify material risks at earlier stages, thereby reducing the likelihood of more serious problems developing that could threaten a servicer's solvency. In the absence of aligned requirements, one agency could take a supervisory action against a servicer in a manner that would be unexpected by the other agencies (e.g., because a servicer was approaching a minimal threshold set by that agency, but remained well above the minimum requirements set by the other agencies). This scenario likely would lead to confusion and additional uncoordinated actions that could trigger warehouse covenant violations, jeopardize counterparty relationships, or otherwise interrupt business operations.

Aligned requirements also benefit servicers by reducing compliance costs without sacrificing safety and soundness. Many IMB servicers are subject to requirements set by Ginnie Mae, FHFA, the GSEs, and several state regulators, as well as warehouse lenders that actively manage counterparty risk through financing limits and an array of covenants. The costs of ongoing compliance with these varying sets of requirements are substantial, and are difficult to justify when the variations across federal and state agencies do not provide incremental benefits in terms of financial resiliency. Reduced compliance costs lead to more efficient operations and greater demand for MSRs, which in turn leads to lower interest rates for consumers. Significant deviations across agency requirements, on the other hand, represent "deadweight" costs that burden servicers and increase interest rates (and thereby reduce access to credit) for consumers.

### Timing

In the RFI, Ginnie Mae notes that the proposed revisions would take effect for calendar year 2021 audited financial statements. For most servicers, compliance with these new requirements would be evaluated using audited financial statements as of December 31, 2021, which typically would be submitted to Ginnie Mae by March 31, 2022.

While the proposed revisions to the liquidity and net worth requirements are unlikely to cause many issuers to fall out of compliance, MBA believes it is more appropriate for these new requirements to take effect with financial reporting in calendar year 2022. The finalization of these new requirements is unlikely to occur prior to October 2021 (assuming at least 60 days for Ginnie Mae to review public responses to the RFI and adjust the proposals as needed). That timeframe simply does not allow adequate opportunity for issuers to make changes to their operations or financial profiles prior to year end.

MBA recognizes that Ginnie Mae maintains the capacity to issue waivers for those companies that do fall out of compliance in 2021 due to the updated requirements, but this is an inefficient and unnecessary process. Ginnie Mae should not penalize issuers that fall out of compliance with standards finalized so late in a reporting period, and if Ginnie Mae simply plans to provide waivers for each of those companies, there is no reason to make the new requirements effective for calendar year 2021.

With respect to the proposed risk-based capital ratio requirement, the numerous concerns described above should eliminate any potential for implementation in calendar year 2021. Indeed, implementation of this requirement should be delayed indefinitely until Ginnie Mae completes further work to determine whether it is necessary. If Ginnie Mae does decide to move forward, adequate time should be provided for backtesting, impact analysis, and re-calibration. Such a process would better correspond with the well-understood process by which risk-based capital requirements are developed and refined for banks and bank holding companies subject to the Basel framework. Under the Basel framework, changes to risk-based capital requirements are implemented through an iterative process that often involves several proposals and re-proposals over periods measured in years, as well as a lengthy period between finalization and effective dates. While the risk-based capital ratio requirement proposed by Ginnie Mae is not nearly as complex as many of the updates to the Basel framework, the Basel process in this case should serve as a guide for Ginnie Mae – particularly given that this proposal represents an entirely new and untested approach to Ginnie Mae's oversight of issuers.

#### Monitoring Tools

For many issuers, Ginnie Mae's monitoring tools are important components of their compliance processes. The data and scorecards provided by Ginnie Mae allow issuers to understand how their data on delinquencies, prepayment rates, and other metrics compare to those of other institutions, ensure issuers can reconcile their internal calculations with those of Ginnie Mae, and alert issuers when they are approaching key thresholds. As such, Ginnie Mae should update its monitoring tools well in advance of the implementation of any changes to the capital, liquidity, or net worth requirements. During a transition period, it will be important for issuers to understand how their financial profiles are positioned relative to the new Ginnie Mae minimum requirements

so as to manage their businesses towards compliance, as well as to confirm that their internal calculations of these new requirements align with the calculations maintained by Ginnie Mae.

### ***Other Structural Reforms to Enhance Resiliency***

Capital, liquidity, and net worth requirements are important components of prudent risk management and agency oversight, but they are not the only mechanisms by which Ginnie Mae and other agencies can strengthen the resiliency of the residential mortgage servicing market. Several structural reforms to the Ginnie Mae program and the broader housing finance system can further enhance stability, attract more diverse sources of capital, and increase the capacity of policymakers to respond to market stress.

#### **Actions That Should Be Taken By Ginnie Mae**

The most significant strain on Ginnie Mae issuers takes the form of advancing obligations on delinquent loans that are far more onerous than the comparable system in place at the GSEs. Whereas GSE servicers generally are limited to advancing missed borrower payments to MBS investors for four months, Ginnie Mae issuers must do so until the loan re-performs or is liquidated (including through loan buyouts, which require additional issuer resources) – a period that often takes much longer than four months. Because the loans backing Ginnie Mae securities typically have higher risk factors than the loans backing GSE securities, Ginnie Mae issuers are exposed to a greater likelihood of being called upon to advance delinquent payments. This feature of the Ginnie Mae program was particularly problematic in the midst of the COVID-19 pandemic, as Congress legislated broad availability of payment forbearance for borrowers without providing corresponding liquidity support for servicers.

While these different advancing structures often are viewed as “accepted facts” among housing finance professionals, it is not clear why these structures exist in their current forms. If one were to design a housing finance system anew, it is difficult to imagine one making the conscious decision to assign lengthy advancing obligations – in essence, credit risk exposure – on higher-risk (yet ultimately government-insured or -guaranteed) loans to institutions whose role is to administer payments and other servicing functions.

Ginnie Mae should take active steps to explore a fundamental re-balancing of its program structure to mitigate these risks. Such a re-balancing could entail Ginnie Mae reimbursing issuers in a manner similar to that of the GSEs after short periods of issuers advancing delinquent borrower payments – likely in conjunction with an increase in the guarantee fees charged by Ginnie Mae to enable it to carry out these reimbursements. While such reforms would require action on the part of Congress, they neither will be practical nor possible without Ginnie Mae analyzing how this

structure could work and identifying the necessary actions to be taken by various parties. Ginnie Mae should lead such an effort and begin this work immediately.

In the absence of these broader reforms, Ginnie Mae should consider ways to better ensure issuers have access to reliable sources of liquidity in the event they face temporary liquidity shortfalls. One such option would be for Ginnie Mae to make the Pass-Through Assistance Program (PTAP) available for situations beyond natural disasters or pandemics. PTAP allows issuers to obtain assistance from Ginnie Mae in meeting their advancing obligations, with the program set up as a “last resort” that carries an above-market interest rate on funds provided to the issuer. These conditions are reasonable and appropriate to avoid imprudent reliance on PTAP by issuers.

To make PTAP a more effective option for liquidity support in exigent circumstances, however, Ginnie Mae should follow the example it set with respect to the COVID-19 amendments to PTAP and confirm that use of this assistance does not, on its own, constitute a basis for default. This provision would decrease the likelihood that use of PTAP would trigger other adverse actions, such as the loss of warehouse funding or supervisory actions by state regulators. Ginnie Mae also should amend its MBS Guide to enable the use of PTAP in situations beyond natural disasters or pandemics, which would allow it to address other instances of temporary issuer liquidity shortfalls. Again, if Ginnie Mae believes that additional authority from Congress is required for such actions, it should begin this outreach as soon as possible.

Another long-running flaw in the current Ginnie Mae structure is the difficulty and complexity associated with issuers obtaining third-party financing for Ginnie Mae MSR, particularly in contrast to GSE MSR. Important changes to the Ginnie Mae acknowledgement agreement are needed to facilitate bifurcation of MSR and advance receivables. This bifurcation would allow third-party MSR lenders to be compensated in the event of an issuer default without being required to take on the obligations associated with servicing the loans. With this greater flexibility, there likely would be a larger pool of MSR lenders offering financing on more attractive terms.

Further, issuers are the only institutions permitted to own Ginnie Mae MSR, despite demand from other types of investors. Reforms to the Ginnie Mae structure that allow “passive” MSR ownership by additional parties would increase bids for MSR and improve pricing, which would flow through to lower interest rates for consumers. Related reforms would allow the “splitting” of Ginnie Mae pools in order to increase the demand for, and liquidity of, Ginnie Mae MSR, as well. It is incongruous that Ginnie Mae would adopt more stringent treatment of issuers that are large MSR holders in its proposed risk-based capital ratio requirement while at the same time operating a program that makes it difficult for interested third parties to obtain MSR. Together, these reforms should reduce any risks that could result from increasing levels of concentration in MSR ownership, as well.

### Actions That Should Be Taken By Other Agencies

Misalignment in servicing requirements across various federal agencies and the GSEs raises costs for servicers while also producing varied outcomes for borrowers. Standardization of these requirements – particularly the adaptation of FHA requirements to better align with those of the GSEs – would increase the value of Ginnie Mae MSR portfolios and the overall health and strength of servicers with Ginnie Mae portfolios. FHA should implement several servicing improvements, including adoption of a single foreclosure timeline, use of proportional curtailment of advances, and elimination of costly anachronisms like the face-to-face meeting requirement for delinquent borrowers. To attract as many institutions as possible to FHA lending and servicing, FHA also should ensure that litigation risks related to the use of the False Claims Act to penalize minor underwriting defects are eliminated.

As was noted above, the federal banking regulators have implemented a Basel framework for bank capital requirements that includes punitive treatment of MSRs – a problematic approach that clearly served as the basis for the treatment of MSRs in Ginnie Mae's proposed risk-based capital ratio requirement. MBA has advocated forcefully in favor of critical revisions to this approach, such as an increase in the limit on MSRs as a percentage of capital and a decrease in the risk weight associated with MSRs. The existing requirements are far too conservative relative to the actual risks posed by MSRs – for the same reasons provided above with respect to IMBs – and have played an important role in discouraging many banks from more active participation in mortgage servicing. Both depository and nondepository institutions instead should be encouraged to participate in this market, which would boost MSR liquidity and reduce concentration risk.

FHFA should consider mechanisms by which well-managed IMBs that meet appropriate financial benchmarks can gain eligibility for FHLB membership. Such eligibility could come directly through legislative actions permitting IMB membership or through expanded use of captive insurance affiliates, as has been permitted previously. Membership for IMBs could entail FHLBs offering advances that are collateralized by MSRs or servicing advances. This expansion of FHLB membership eligibility, if exercised responsibly, would diversify and strengthen IMB liquidity sources while further promoting the housing finance mission of the FHLB System.

Finally, the industry's March 2020 experience with margin calls on TBA positions used as loan pipeline hedges is a clear indication that margining practices and requirements related to the single-family mortgage market are in need of re-evaluation. Loan originators typically work with broker-dealers to obtain their pipeline hedges, though at least one GSE provides this service, as well. In exigent circumstances that necessitate extraordinary government policy interventions, loan originators can face pressure due to a timing mismatch between daily mark-to-market losses on hedges and corresponding gains in pipeline valuations that may not be recognized for several

weeks. Margin calls on the near-term fluctuations in the hedges should not reach destabilizing levels when the loan originator maintains high-quality, liquid assets that can offset these losses fairly quickly. The Securities and Exchange Commission, the Financial Industry Regulatory Authority, the Federal Reserve Bank of New York, FHFA, and the Treasury Market Practices Group should examine agency MBS margining practices and requirements to ensure broker-dealers and other providers of financing have the ability to exercise flexibility with their clients under these extreme circumstances. Without important changes to existing procedures, margin calls have the potential to add to, rather than alleviate, stress in the mortgage market.

These reforms undertaken by Ginnie Mae and other federal and state housing agencies would address significant structural flaws in the housing finance system. Together, they would strengthen the financial profiles of servicers, improve aggregate demand for MSRs, and diversify the sources of capital contributing to housing finance – all of which would serve to lower costs and expand access to credit for consumers.

\* \* \*

Thank you in advance for your consideration of these recommendations. Should you have questions or wish to discuss further, please contact Pete Mills, Senior Vice President of Residential Policy and Member Engagement, at (202) 557-2878 or [pmills@mba.org](mailto:pmills@mba.org).

Sincerely,



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