Veterans United Home Loans

Veterans United Home Loans
Veteransunited.com

800-884-5560 (p)
NMLS 1907

December 31, 2020

John Ryan
President and Chief Executive Officer
Conference of State Bank Supervisors
1129 20th St, NW, 9th Floor
Washington, DC 20036

Re: COMMENTS ON PROPOSED REGULATORY PRUDENTIAL STANDARDS FOR NON-BANK MORTGAGE SERVICERS 2020

Dear Mr. Ryan:

Veterans United Home Loans appreciates the opportunity to comment on proposed regulatory baseline and enhanced state prudential standards for non-bank mortgage servicers. As the nation's largest VA purchase lender, we take pride in our servicing of Ginnie Mae-backed loans as an extension of our customer service and service to our nation's military Veterans.

You will find these comments are very similar to our comments on the 2015 proposed regulatory baseline and enhanced prudential standards. Generally, the standards set forth by the Conference of State Bank Supervisors ("CSBS") Non-Depository Supervisory Committee ("NDSC") are repetitive of standards put forth by federal regulators with jurisdiction, particularly in the context of servicers with the vast majority of their portfolios with Ginnie Mae ("GNMA"); Fannie Mae and Freddie Mac ("GSEs"). As we noted in those comments, duplication of existing federal standards or implementation of differing or even higher standards will inevitably and unnecessarily increase costs and complexity for non-bank servicers, which will affect the affordability of and access to credit for lower and middle-income consumers and ultimately may have the opposite of the intended effect by increasing the instability and systemic risk in the financial system.

As a servicer, Veterans United primarily services loans in GNMA portfolios. Loans with GNMA are insured or guaranteed by a U.S. agency and maintain an explicit U.S. government guaranty to bond holders. Each of the relevant agencies exerts regulatory and oversight authority, including by monitoring loan performance, in order to ensure originators and servicers are meeting its specific standards. GNMA is ultimately liable for any servicer defaults, and accordingly should be responsible for regulating the health of its non-bank servicers. In the event of a failure or default, GNMA simply takes over the entire portfolio, moves it to a different, healthy servicer, and the original servicer no longer has any rights to the portfolio. For purposes of loans in these portfolios, an additional layer of prudential state regulations and examinations add no meaningful protection against systemic risk. This is a similar scenario for the GSEs.

It is Veterans United's position that loans in GNMA and GSE portfolios should be entirely exempted from the prudential standards such that they, alone, would not cause any company to

A VA approved lender; Not endorsed or sponsored by the
Dept. of Veterans Affairs or any government agency.
Equal Opportunity Lender.
1400 Veterans United Dr., Columbia, MO 65203

be subject to the baseline standards and also do not count toward qualifying a company as subject to the enhanced standards. This responsibility should rest with the relevant investor (GNMA or GSE). At minimum, Veterans United would recommend some threshold percentage of loans or unpaid principal balance ("UPB") in GNMA and GSE portfolios at which point servicers would not be subject to either the baseline or enhanced standards at the state level. This threshold should be set such that most servicers – the vast majority of which do not pose any systemic risk to the financial system – would be exempt. Such a threshold would properly reflect the importance of the standards, while avoiding unnecessary, duplicative, and potentially conflicting application to servicers already subject to the federal standards that could raise costs on consumers.

While we appreciate the effort of CSBS to align various requirements to existing federal standards, we remain concerned that state regulations and examinations will not be consistently adopted or enforced in all jurisdictions, and may end up disconnected from federal standards as those are adapted over time by GNMA, the GSEs, or other actors like the FDIC, FHFA, or Congress, resulting in a patchwork regulatory environment in this area among the states and between the state and federal levels. While this can work in some areas, such as origination, the adoption of prudential standards, for servicers specifically, is qualitatively different in that it could increase instability and systemic risk in an extreme market environment, potentially resulting in harm to consumers.

A significant cause of the speed and severity of the financial crisis was the dangerous combination of: (a) the poorly-understood risks inherent in private-label mortgage servicing and securitizations leading up to the crisis, and (b) the knock-on effect, once those risks became apparent, on banks' capital requirements.

This first factor is not relevant to loans in GNMA or GSE portfolios. Ability-to-repay rules and agency and GSE underwriting requirements, including monitoring of loan performance, now ensure the continued quality and marketability of those loans and MSRs. Specifically with regard to VA Loans, the safety and soundness of the product is well documented, along with the servicing efforts the Department of Veterans Affairs Loan Guaranty Service employs. There are also now rules in place for issues such as loss mitigation and servicing transfers, which protect consumers by setting consistent standards in the event of servicer stress.

Second, adding the states as prudential regulators could multiply the severity of that crisis, if or when it occurs. Having additional regulators with responsibility for oversight of servicers' capital, liquidity, or the like, some of which may have differing regulatory schemes, standards, and sensitivities, will increase complexity and limit the speed and flexibility of government responses. Instead of having to communicate and coordinate with a smaller set of federal regulators, servicers might now be faced with multiple different state requirements and have to seek individual relief from various individual state authorities. This could have unforeseen effects on consumers downstream.

This issue would be magnified in the event any state standard differs from the financial ratios and covenants imposed by servicers' funding sources. One of the primary concerns often expressed about non-bank servicers is the risk that they lose access to funding in a crisis. This funding is generally provided by banks and other sophisticated entities that have deep experience in the industry, a nuanced understanding of credit risks, and most importantly, their own skin in the game. They are in the best position to evaluate the safety and soundness of the non-bank servicers to which they lend money, and to determine whether to trigger a default or continue to work with their borrowers. If the states were to impose their own prudential standards, including capital and liquidity requirements, they risk causing the exact outcome they are attempting to avoid – if a non-bank servicer is working with its lender to continue funding but is unable to procure a waiver from even one state, it could leave the lender with no choice but to declare a default and accelerate the loan.

It is easy to conceive of how the above situations might force servicers to take drastic actions like liquidating MSR portfolios at reduced prices in an attempt to comply with state mandates, which would then have the same knock-on effect, through declining MSR values, on other servicers' capital requirements.

The discussion above highlights another difference between banks and non-bank servicers. One of the primary benefits of state prudential regulation of banks is to protect depositors who may not be fully covered by deposit insurance and ensure the ongoing stability of the banking system. On the other hand, those with the most to lose in the event of a failure of a non-bank servicer are the federal agencies and investors and private lenders, which are on the hook financially and in the best position to judge the adequacy of a servicers' capital and liquidity position. Further, mechanisms already exist to protect the stability of the servicing system in the event of an isolated failure of one or more non-bank servicers, such as GNMA's ability to force a servicing transfer. There are risks to consumers from a failure of a servicer, but those are largely mitigated by ongoing oversight of servicers' compliance with existing servicing rules.

Last, we have a general concern about broad overlap of jurisdiction between state and federal regulators, particularly with regard to issues of consumer protection versus the stability of the regulated entities. The COVID-19 pandemic provided a real example of how state and federal regulators' rightful focus on different aspects of the marketplace reached a positive result for stakeholders. During the COVID crisis, many states adopted their own forbearance policies, foreclosure moratoriums, and other consumer protection measures, in addition to the federal CARES Act and resulting regulations. It was then on the servicers, their lenders, and the relevant federal regulators to communicate and address the potential adverse impacts on servicers. Some examples of this include mechanisms such as GNMA's PTAP facility and FHA and VA partial claims, each of which provided additional protections to servicers and their customers in the event of significant liquidity issues. We believe this approach –where states focused on the needs of their citizens and allowed servicers and their relevant federal regulators to address potential solvency and stability issues – worked well for stakeholders and consumers.

Following are additional comments on specific proposed standards proposed by CSBS.

Capital and Liquidity
Veterans United appreciates the effort to align the CSBS capital and liquidity standards with federal standards. While Veterans United considers these federal standards as generally reasonable, it also sees these state standards as duplicative given that they are already set forth by federal entities with jurisdiction. GNMA, for example, already requires single-family issuers to maintain a minimum net worth of $2,500,000 plus 35 basis points of the issuer's total single-family outstanding obligations.

Either state standards are the same, and therefore unnecessary for servicers with large GNMA or GSE portfolios, or they are different, in which case they will add costs and complexity for everyone as well as increasing systemic risk in a crisis. Veterans United offers for CSBS consideration that these standards simply refer to applicable federal standards, including as the same may be amended from time to time.

If, however, CSBS determines to propose capital and liquidity standards which differ from federal standards, we offer for consideration that all: (a) financial terms be defined by reference either to some other authoritative source like generally accepted accounting principles or to non-bank servicers' credit agreements, or (b) if that is not possible, definitions should be clear enough to avoid potential differences of interpretation, and/or for there to be a process for requesting private rulings or the like to avoid an automatic default in the event there is a difference of interpretation.

Risk Management
Having specific state requirements around a formal risk management program may not be the most practical or best approach to ensuring that firms are addressing risk appropriately. Companies can address risk most effectively by having the flexibility to set up their own individualized risk management approach and program that is best for their own organizational structure and circumstances. The relevant measure is whether a company is able to demonstrate the ability to monitor, measure, and mitigate or address risk. If implemented by the states, any framework for regulation of risk management programs should include significant flexibility in how such programs are structured and implemented. Such flexibility would properly reflect the different business models, structures, and needs of independent mortgage banks.

Data Standards and Protection
These standards are duplicative because, as recognized by CSBS, data protection is already regulated at the federal level by the CFPB. Also, as we noted in 2015, CSBS should specifically consider the role and responsibilities of subservicers in this area.

Corporate Governance
Veterans United follows this proposed standard as required by GNMA and federal regulations, and appreciates CSBS's effort to mirror GNMA standards, although it may be duplicative.

Servicing Transfer Requirements
As noted in the proposal, these standards mirror existing requirements by the CFPB and FHFA, which creates unnecessary redundancies. Veterans United remains concerned that the proposed standards will be worded in such a way that additional requirements will be placed on servicers or create unnecessary conflicts among state and federal regulators, which can negatively affect consumers.

Change of Control Requirements
The company sees 10 percent ownership change as being reasonable for purposes of notification only. Many states already require mortgage lenders to provide such notification.

Veterans United Comments on the Enhanced Set of Prudential Standards for Non-Bank Mortgage Servicers

In general, Veterans United is concerned with how the enhanced standards will be applied, and the varying laws and regulations that will set them forth. While understanding that the primary factor for identifying complex servicers would be UPB, broad additional factors listed for inclusion as a complex servicer could lead to companies being subject to different standards among the states. Further clarity of these factors would be helpful, as would a timeline for when designation as a complex servicer is made and the application of the enhanced standards to the entity after such designation.

Capital and liquidity
Veterans United sees some cause for concern in how "more complex" entities will have different capital and liquidity requirements than those outlined in baseline standards. As noted above, conflicting requirements among various regulators could unnecessarily increase risk as well as costs. This concern is particularly significant with regard to the individualized minimum operating liquidity requirements for complex servicers described in the proposal. As drafted, this could subject a servicer to 51 different standards and requirements for minimum operating liquidity, based on a number of subjective factors considered by examiners.

We appreciate the recognition of differing risk based on the size of each portfolio segment owned. As noted above, loans in GNMA portfolios represent significantly less risk to both servicers and consumers than many other products.

Stress Testing
We are supportive of stress testing as a tool to ensure financial stability of the market, and believe expectations must be put forward clearly. If implemented, any state stress testing should align with existing and future GNMA stress testing models. Any separate policies implemented by the states should be uniform across all states, while flexible enough to appropriately tailor the stress testing to varying sizes and business models. Further, CSBS and the states should

carefully consider the limitations of the data sources used, the modeling and calculation methodologies, and the potentially incomplete outputs created by those differing factors.

Inflexible stress testing standards will often not apply consistently across business models based on various data sources and performance criteria, and outputs could be skewed relative to the actual financial soundness of a company. Finally, if the states implement stress testing, we would recommend a phased implementation over a period of years that would allow for an initial focus on data integrity, adjustments to the modeling, observation, testing, and feedback from servicers.

Living Will and Recovery Resolution Plans
Veterans United understands the reasoning behind CSBS wanting companies to have plans in place in the event of significant financial stress. We look forward to seeing more specifics regarding CSBS's proposal.

Request for Public Comment—Specific Feedback areas

General
1. Is the need for state prudential standards sufficiently established?

Veterans United recognizes the importance of reasonable prudential standards to protect consumers from the risk of a financial downturn, and we appreciate that these standards may be properly applied to non-GSE/GNMA loans. However, such standards already exist at the federal level for the GSEs and GNMA, and it is unclear what, if anything, would be the benefit of another layer of regulation at the state level for companies already subject to federal regulation for the vast majority of their portfolios. For these federally-backed and regulated loans, we do not believe that the need for state prudential standards has been established. In fact, with respect to these loans, we believe it will not reduce the likelihood of a crisis occurring but may increase the likelihood and severity of servicer losses and failures in a crisis should one occur, leading to additional harm to consumers. Finally, because non-bank servicers are reliant on external funding, their lenders are in the best position to establish, evaluate, and monitor their risk management standards and efforts.

2. Do any of the standards threaten the viability of a servicer or a specific subsector within the industry?

The level of duplication and increased costs could adversely affect certain servicers or subsectors of the industry and could, in a crisis, affect their viability. Conflicting regulations across the states could exacerbate the costs and risks, representing a potential threat to servicers and consumer options, particularly where each state could implement unique requirements within the framework.

3. What is a reasonable transition period to implement the standards?

Two years is likely a reasonable transition period to implement most of these standards, however, additional transition time should be allowed for entities determined to be subject to enhanced standards or standards that do not align with existing federal requirements. Additionally, other regulators should be given time to adequately address conflicting regulations.

4. Are there specific standards that would require additional time to implement?

Any application of enhanced standards to a servicer based on additional complex servicer factors would likely necessitate additional time to implement. Further, a clear timeline for application of enhanced standards following designation as a complex servicer would be extremely helpful.

5. What effect will the enhanced standards have on the warehouse and advance facility borrowing contracts/capacity of large servicers?

The standards will cause due diligence and oversight to be more extensive and may reduce the availability or increase the costs of facilities.

Coverage

6. Do you agree with a scaled approach for coverage where all servicers are subject to Baseline Standards and Complex Servicers only are subject to Enhanced Standards?

We believe a large percentage of GNMA and GSE portfolios should be exempted from even the Baseline Standards, as those portfolios can be expected to remain reasonably liquid, and the failure of a discrete number of those servicers does not pose a systemic risk. Only the largest servicers pose a risk to the financial system and borrowers, simply because of their size and scale. In addition, Veterans United is concerned with how the enhanced standards will be applied, and the varying laws that will set them forth. Additionally, the caveat for individualized determinations for particular Complex Servicers is vague and ambiguous. This catch-all could create wide disparities in how “Complex Servicers” are designated and treated state by state.

7. Nonbank servicer coverage in this proposal is intentionally unspecific. We seek comment to assist in the appropriate coverage triggers. In this proposal, we have not established a de minimis threshold for baseline coverage. Further, we have limited coverage of Subservicers Only and have excluded companies that only perform servicing for reverse mortgages. Finally, we have proposed a triggering level for Complex Servicers that would be subject to the Enhanced Standards. We request comment on the following:

> a. Should there be a de minimis threshold (a minimum volume or size threshold that triggers coverage)? Please identify any threshold and explain your reasoning.
>
> Yes, and this should be set high enough to exempt a large percentage of GNMA and GSE

portfolios. As noted above, the vast majority of these standards are based on existing federal standards. Any de minimis threshold should take into consideration the loans or UPB in GNMA and GSE portfolios versus other loans not already subject to these federal standards. Such a threshold would properly reflect the importance of the standards, while avoiding unnecessary and duplicative application to servicers already subject to the federal standards mostly mirrored in this proposal.

b. What risk factors besides size of servicing portfolio are appropriate to consider for those servicers that have no agency servicing volume and therefore are not covered by either FHFA or Ginnie Mae requirements?

As noted above, Veterans United primarily services federally-backed loans in GNMA portfolios and believes servicers with a significant percentage of such loans should be excluded from the standards. We have no additional commentary with regard to non-agency servicing.

c. Have we struck the correct balance for Subservicer Only coverage as well as exclusion of portfolios serviced for others? Please explain any disagreement with our inclusion/exclusion of subservicing activity.

As outlined above, Veterans United believes a greater share of companies should be considered for exclusion, specifically those with portfolios predominantly with GNMA and the GSEs.

d. Do you agree or disagree on whether servicers performing only servicing for reverse mortgages should be excluded from this proposal? If you disagree, please explain your reasoning.

Veterans United does not originate or service reverse mortgage loans.

e. What size or volume of servicing do you believe is the appropriate threshold for a Complex Servicer? Please explain.

CSBS should consider applying the enhanced standards to the 10 largest servicers in a given state. Any alternative factors should capture only the truly massive industry leaders who are better equipped to address the enhanced standards.

f. Are there specific risk factors that should be considered in the evaluation for inclusion or exclusion as a Complex Servicer? Please provide detail.

As noted previously, the type of servicing being performed is a key indicator, and some threshold percentage of loans in GNMA and GSE portfolios should be considered for exclusion as a Complex Servicer.

Capital and Liquidity
8. The capital and liquidity components of this proposal align with existing and future FHFA Seller/Servicer requirements where possible. Do you support such alignment?

Yes, if such components continue to be included, we support aligning them with federal requirements, preferably by reference such that they continue to change whenever federal requirements change.

9. Do you agree with the components included in the calculation of net worth? Is there an alternative calculation that would be more effective?

We believe there should be no specific net worth requirement and, if there is, that it not have a stated calculation but rather exist only by reference to FHFA standards.

10. State supervisors hold jurisdiction over a nonbank servicer's entire portfolio. Do you feel that applying the FHFA calculations to all owned servicing is an appropriate approach for these standards?

As noted above, Veterans United appreciates the CSBS proposal's alignment with existing federal standards, but remains concerned about the potential for different state regulators implementing differing standards that do not precisely align with FHFA calculations. This still could lead to extensive differences between states, enhanced burdens on servicers, and increased costs to consumers.

11. These standards define two types of liquidity need: Servicing Liquidity for the direct performance of servicing and Operating Liquidity for general operations of the organization. Do you agree with these definitions? What alternative definitions would you propose?

We believe that any liquidity requirements should be by reference to FHFA standards only. Veterans United takes liquidity very seriously and has sophisticated means for estimating and managing it, which change over time with business circumstances. Injecting additional concepts and definitions will not improve transparency, stability, or at the end of the day liquidity itself. Any artificial distinctions between liquidity buckets will only increase the complexity and difficultly of management efforts and increase the risk of technical violations.

12. Allowable Assets for Liquidity is intended to align with FHFA's 2019 Servicer Eligibility 2.0 Proposal. Do you agree with this alignment?

We appreciate the effort to align with federal standards, although we remain concerned about the implementation of differing liquidity standards among the various states. Additionally, the complete exclusion of unused or available portions of lines of credit from allowable assets for liquidity (an important source of liquidity for many servicers) is of concern, both at the state and federal level.

Corporate Controls

13. Do the Risk Management standards appropriately capture the risks faced by nonbank mortgage servicers?

As noted above, any framework for regulation of risk management should include sufficient flexibility for how such programs are structured and implemented, allowing for appropriate application to nonbank servicers with varying business models, structures, and needs.

14. Is it a reasonable expectation that all covered servicers establish a risk management program under a board of directors scaled to the complexity of the organization?

We would note that many servicers do not operate in this manner. For example, at Veterans United, we are a limited liability company without a board of directors. Any framework for regulation of risk management programs should include significant flexibility in how such programs are structured and implemented. Such flexibility would properly reflect the different business models, structures, and needs of independent mortgage banks, and permit efforts to be more effective precisely because they can be tailored to each servicer's individual situation.

15. Is it appropriate for the Data Standards to incorporate the CFPB's Mortgage Servicing Rules standards? What alternative standards should we consider?

While we appreciate the effort to align with existing federal standards, these standards are duplicative because data protection is already regulated at the federal level by the CFPB.

16. Are the Data Protection standards appropriate for the data risks inherent in nonbank mortgage servicers?

As we noted in 2015, CSBS should specifically consider the role and responsibilities of subservicers in this area, as subservicers are often looked to for expertise in this area.

17. Is it appropriate to rely on the Ginnie Mae audit standards for Corporate Governance?

Veterans United appreciates CSBS's effort to mirror GNMA standards, although this may be duplicative, particularly for servicers whose loans are largely with GNMA.

18. Should all covered nonbank mortgage servicers be required to have a full financial statement audit conducted by an independent certified public accountant?

We believe that this is a reasonable requirement.

19. Is it appropriate for the Servicing Transfer Requirements to rely on existing CFPB and FHFA transfer requirements?

While Veterans United appreciates the effort to align with existing standards, this creates unnecessary redundancies. Veterans United remains concerned that the proposed standards will be structured in such a way that additional requirements will be placed on servicers or create unnecessary conflicts among state and federal regulators.

20. For Change of Ownership and Control, do you believe we have chosen the correct number of days for notification and the appropriate ownership percent trigger?

Veterans United sees the time and ownership percent triggers as reasonable for purposes of notification.

Again, Veterans United greatly appreciates the opportunity to provide comments on these proposed prudential standards and looks forward to continued discussions.

Sincerely,

Eric Wilson
External Affairs Manger
Veterans United Home Loans
eric.wilson@veteransunited.com
(573) 876-2600 ext 3463