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December, 22, 2001

Mr. Edward DeMarco
Acting Director
Federal Housing Finance Agency
1700 G Street, NW, 4th Floor
Washington, DC 20552

Dear Director DeMarco:

On behalf of the California Mortgage Bankers Association ("CMBA"), we want to thank you for the opportunity to voice our opinion concerning the *Alternative Mortgage Servicing Discussion Paper* (Discussion Paper), released on September 27, 2011.

The CMBA is the only statewide association solely dedicated to representing the residential and commercial mortgage banking industry in California. We represent approximately 200 member companies and the thousands of individuals employed at those entities. CMBA membership is largely comprised of small to mid-size mortgage banks that produce quality loans and enjoy relatively low delinquencies compared to national and state averages. Our members know their customers well through mortgage servicing and/or other business and community relationships, and take great pride in the services they provide. We do not advocate legislative or regulatory change that would establish barriers to entry or expansion for the industry, thus maintaining access to affordable credit for borrowers.

We understand that, in light of the recent financial crises, the Federal Housing Finance Agency (FHFA) is interested in examining ways to ensure acceptable servicing standards for borrowers, reduce financial risks to all parties involved in the servicing and guaranteeing of mortgages, provide investors more control over non-performing loan management, and maintain a competitive marketplace for the servicing and origination of residential mortgages.

Unfortunately, we---like every other statewide association of mortgage bankers we know of in the United States---have grave concerns over the proposals outlined in the Discussion Paper and, for the reasons set forth below, we must OPPOSE any changes to the current structure at the present time.

In submitting the Discussion Paper for comment, the FHFA notes that its primary goals are to improve service for borrowers, reduce financial risk to servicers and provide flexibility for guarantors to better manage non-performing loans, while promoting liquidity in the mortgage securities marketplace. The CMBA believes that no change to the current servicing compensation model is necessary to accomplish these goals and could, in fact, significantly undermine them, for the following reasons:

- It is currently impossible for servicers to know their real and ultimate cost to service loans in light of pending Fannie Mae, Freddie Mac, attorney's general, regulators, consumer groups, and certain consent decrees, calling for more robust national servicing standards. In view of this dramatic uncertainty, it is simply not possible to construct a rational servicing compensation structure at this time that would not have substantial unintended consequences, including but not limited to those involving tax and accounting issues.
- A dramatic service fee reduction could impair the value of the existing mortgage servicing rights now capitalized on servicers or lenders financial statements. *((Many of our members state they would not be willing to pay current multiples for servicing rights because – when experiencing possible excessive refinancing of the mortgages- the servicing compensation would be dramatically curtailed. This could lead to impairment concerns for every servicer and possible solvency issues as servicers mark the servicing rights to market.))*
- Currently, servicing costs are approximately 4 bps on the Unpaid Principal Loan Balances. Using the United State average of \$250k loan balance this is \$100. The fee for service model pays \$120 / loan annually. The proposed “half way” idea of .125% for servicing does nothing to improve the current system and, in fact, would create more consolidation as it would enable the larger banks to add more servicing to their books. The larger servicers would handle even more servicing than today. This does not bode well for diversity. It is interesting to note that the lower MSR helps larger banks aggregate more servicing even under the new Basel 3 requirements.
- With capital requirements and income opportunities being diminished, if not eliminated, under these proposals we might expect to see further consolidation in the servicing arena. Our conclusion is that capital efficiency and economies of scale will still benefit the large servicers resulting in small and regional servicers having less incentive to enter or sustain the servicing business. This could certainly exacerbate the potential “too big to fail” argument and pose additional risk on the financial system.
- The fee for service proposal is also almost certain to force borrower contact into automated, non-human methods to meet the economy of scale demands to achieve reasonable returns on investment. This inevitable outcome is the exact *opposite* of what consumers need and that servicers will most likely be required to provide under more difficult national standards still being discussed.
- The proposals in the Discussion Paper also diminish the incentive of using best practices when collecting accounts in the early stages of delinquency as servicers of performing loans will be forced to reduce collection staffs or reallocate them to non-performing loans. Over time this will only lead to higher delinquencies.
- The proposed fee-for-service model also has a component that would pay higher fees for non performing loans. The stated reason is to help these servicers maintain the same level of quality of service. But there is a “moral hazard” issue here: If someone is paid to originate and service loans that go into default, economic incentives are created for bad practices and bad lending.

- In addition, the proposed fee-for-service model also does not have an IRS Safe Harbor component. This would be a deterrent for the smaller servicers because currently they can add servicing and grow their balance sheets while deferring taxes but under the new proposal it is not clear that the "safe harbor" would be amended to allow for this same tax treatment. The proposal would thus be a huge tax "hit."
- This also holds true for the IO strip proposed to be sold separately. The proposal is that the IO be sold and thus would not come with the same onerous reps and warrants. However, the IO strip is treated as a taxable asset and therefore does not have the safe harbor.
- We have grave concern over the price disparity already evident in the marketplace between Fannie and Freddie Mortgage Backed Securities. If your proposal were implemented, the forward securities for Fannie and Freddie would have to be bifurcated even further leaving an even greater price disparity between Fannie and Freddie Securities and also potentially remove Freddie as a functioning Secondary Market option.
- Like many other state associations, we find it completely unacceptable that Fannie Mae, as an actual owner of mortgage servicing through its recent acquisitions, and also while still in conservatorship, could be dictating or driving the proposed servicing compensation options for the private sector.
- Borrowers will no doubt experience a greater cost of financing as rates will go up as a result of rising costs and reduced servicing fees. This also seems counterproductive to the measures the government has employed in an attempt to reinvigorate the economy.
- The economy needs no more shocks. This new proposal will not help the industry regain itself. Nor will it help make more credit available to needy borrowers. Instead it would lead to fewer players helping fewer Americans get home loans, with lower levels of service. This, in turn, would further slow down economic growth and lead to even fewer jobs.

For these reasons, we strongly urge the FHFA to leave the existing servicing fee structure in place.

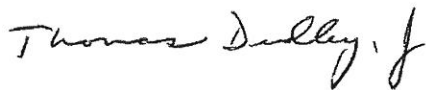
If, at a later time, changes to the servicing compensation structure are deemed unavoidable and absolutely necessary, then we believe some kind of reserve account structure would certainly be superior to a fee-for-service model. Such a structure might include, for example, a 5 bps reserve account, where 5 bps of the Servicer's MSR would be held a separate custodial account for 12 -24 months, after which it would be released to the servicer as income. The servicing reserve could remain on the balance sheet of the servicing entity, but reside in a bankruptcy remove account held jointly by the servicer and the applicable GSE. Upon expiration of the holding period, or prepayment of the loan, the proceeds of the account would automatically be paid to the servicer. The amount withheld for such reserve could even be lowered for qualified mortgages with holistic attributes that together would make the loan less likely to default.

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But these characteristics of a so-called "reserve account" system are not offered as recommendations for change. As stated above, we do not believe any change to the current servicing compensation system is necessary or desirable at the present time and would, in all likelihood, result in major damage to the industry and contraction of mortgage credit availability to borrowers most in need.

Thank you for your consideration of our comments. If you have any questions, please contact CMBA Executive Director Susan Milazzo.

Respectfully,



G. Thomas Dudley, Jr.
Chair, Board of Directors



Michael R. Pfeifer, Esq.
Chair, National Policy Committee



Susan Milazzo
Executive Director

Cc: Members, House Financial Services Committee
Members, Senate Banking, Housing & Urban Affairs