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July 29, 2021

Mr. Michael R. Drayne
Acting Executive Vice President
Government National Mortgage Association
425 3rd Street SW
Washington, DC. 20024

Dear Mr. Drayne:

The Community Home Lenders Association (CHLA) is pleased to provide comments in response to your Request for Input (RFI) on Eligibility Requirements for Single Family MBS Issuers. This RFI proposes substantial financial requirement increases – but only for independent mortgage bank (IMB) issuers. As the only national organization that exclusively represents IMBs, we are disappointed both in the short 30-day comment and the lack of industry consultation.

This RFI proposal would reduce access to mortgage credit, disproportionately affect smaller issuers, and increase issuer concentration. Thus, CHLA requests that Ginnie Mae withdraw the proposal - or rework it to focus on larger issuers, where most of Ginnie Mae's risk is.

CHLA believes the proposal as drafted ultimately fails Ginnie Mae's statutory requirement to balance access to credit and minimizing losses**.** Ginnie Mae's statutory charter requires it to *"establish a secondary market"* with four *"access to credit"* prongs and *only* one financial prong (managing portfolios with *"minimum loss to the Federal Government").*

The RFI does not explain why Ginnie Mae developed these proposed increased financial requirements based on a standard of **"minimizing risks"** [page 3 of RFI] - instead of the less stringent actual statutory standard of **"minimum loss."**

There is only a cursory discussion and justification why significant new IMB financial requirements are deemed necessary at this time, in light of the continued strong financial performance of GInnie Mae. Ginnie Mae has virtually no credit risk on the already government insured mortgages that it in turn re-insures. Ginnie Mae consistently makes a profit (even in the aftermath of the 2008 housing crisis) and is currently making a record profit in the midst of COVID - a real-world stress test where IMB issuers showed financial resilience in the face of a Congressionally mandated forbearance option and a huge spike in advance responsibilities.

Finally, there is no discussion in the RFI regarding: (1) the expected negative impact on consumer access to mortgage credit, (2) why PLS and portfolio loans are excluded, (3) why differences in GSE servicer advance responsibilities are ignored, and (4) why a new bank-like risk-based capital standard is applied to non-banks in an unduly short compliance timetable.

In support of our recommendation to rework the proposal to focus scrutiny and financial requirements on Ginnie Mae's largest issuers, CHLA makes the following points, some of which are drawn from or build on our January 2019 **"Report on Ginnie Mae":**

- **Reworking the RFI to focus scrutiny and increases in financial requirements on Ginnie Mae's largest issuers is appropriate, since smaller issuers pose a much smaller risk than larger issuers. This is due to lower resolution costs and diversification of issuers. Moreover, Ginnie Mae itself has acknowledged that its primary risk is systemic risk from larger issuers.**

- **Reworking the RFI to protect smaller IMB issuers is needed to avoid reducing access to mortgage credit, due to increased issuer concentration and fewer loan securitization choices.**

- **Reworking the RFI to protect smaller IMB issuers will reduce Ginnie Mae's financial and systemic risk that would otherwise result from increased Ginnie Mae issuer concentration.**

- **The RFI disproportionately impacts smaller IMB issuers, because of its inclusion of GSE loans - but exclusion of PLS and portfolio loans - from net worth and liquidity requirements.**

- **The RFI disproportionately impacts smaller IMB issuers, because of identical treatment of GSE loans regardless of whether P & I remittances (advances) are scheduled or actual.**

- **The new risk-based capital requirement inappropriately applies a bank-like capital standard to non-banks, forcing IMBs to come into compliance within an unduly short compliance period. It would increase mortgage costs due to a reduction in the value of Mortgage Servicing Rights (MSRs), discourage origination of small balance mortgage loans, and encourage churning of refi loans (which increases prepay speeds). It fails to reflect hedging on pipeline loans, and it appears inconsistent with prior Ginnie Mae warnings about issuers with insufficient I/O strips.**

- **Instead of actions to contract access to credit, Ginnie Mae should expand it – by reinstating its Targeted Lending Initiative, which provides a price break for loans to lower income borrowers.**

Proposal Fails Statutory Balancing of Access to Credit and Minimum Losses

CHLA is very appreciative that Ginnie Mae has over the last decade accommodated the growth in IMB issuance of Ginnie Mae securities. As noted in our 2021 CHLA Report on IMBs, the percentage of Ginnie Mae issuance by IMBs has increased from 12% in 2010 to 90% in 2020.

CHLA believes this is consistent with Ginnie Mae's statutory mandate to promote "*access to credit"* and to meet the other related prongs of its statutory mandate, which include *"increasing the liquidity of mortgage investments and improving the distribution of investment capital available for residential mortgage financing."*

CHLA appreciates the fact that Ginnie Mae has a supervisory responsibility to continue to monitor its risks, establish appropriate issuer financial requirements, and conduct supervisory oversight, taking into account the increasing IMB market share of Ginnie Mae issuance.

However, the RFI includes no reference to the impact of issuer financial requirements (particularly for smaller issuers) on Ginnie Mae's statutory requirement to promote access to mortgage credit and meet the other three statutory access to credit prongs.

This is compounded by the fact that the RFI explicitly refers to an objective of *"minimizing risk"* to justify the increased requirements. This is a much stricter financial standard than the statutory requirement that Ginnie Mae is required to follow, of "minimum losses."

From our perspective, it appears that Ginnie Mae's policies are guided by an objective of creating a very high probability that Ginnie Mae will never incur a loss in any year – or even more stringently that it will not incur any losses on any individual issuer, no matter how small. **As noted, this is inconsistent with Ginnie Mae's statutory directives on the subject.**

As noted in our 2019 Report, Ginnie Mae consistently makes a net profit, year in and year out, not even losing money in the aftermath of the 2008 housing crisis, even though virtually every other major entity or program involved in mortgages suffered significant losses.

Moreover, Ginnie Mae is currently making record profits in the midst of the COVID crisis – a projected net profit of $2.453 billion in the current fiscal year ending this September 30 and $2.34 billion in the following fiscal year ending September 30, 2022 [source: OMB HUD Budget Appendix for FY 2022].

There is a very simple reason for this, which is explained in our 2019 Ginnie Mae Report. **Ginnie Mae has virtually no credit risk, since the pools of mortgages it insures (FHA, VA, and RHS) are in themselves either 100% insured or mostly insured by the federal government.**

The only financial risk Ginnie Mae incurs is if it is forced to sell portfolios of issuers that are in financial distress. As explained in the following section, this risk is negligible for smaller issues.

We understand that if a number of smaller issuers were to go under at the same time, there would be an increased administrative burden on Ginnie Mae. However, we believe administrative convenience is not a valid basis for ratcheting up financial requirements for smaller issuers, with an apparent goal of never having a smaller issuer fail. Moreover, if this is a concern, Ginnie Mae could simply use a tiny portion of some of the billions of dollars in annual profits it churns out to cover the administrative costs of resolving smaller IMBs.

Most importantly, such a strict supervisory approach for smaller issuers does not meet the statutory requirement to balance the goals of access to credit and "minimum losses" – because it would foster increased concentration that hurts access to credit and increases risk.

Smaller IMBs Pose Much Less Risk to Ginnie Mae than Larger Issuers

This point was laid out in detail in CHLA's 2019 Report on Ginnie Mae, in the following excerpt:

> The section *"Risk Disclosures"* in GNMA's 2018 Annual Report highlights Ginnie Mae's greatest risksas *"Counterparty Credit Risk"* and *"Issuer Concentration Risk."* The priority that Ginnie Mae puts onmonitoring issuer concentration risk is shown by its recent action to send letters to its 15 largest issuers (see page 14).
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> Similarly, an October 2018 HUD Inspector General report cited the risks of larger issuers, referring to thechallenge of Ginnie Mae servicing mortgages absorbed in a default, saying this *"might require additionalfunds from the U.S. Treasury to pay investors if a large issuer default occurs."*

There are a number of reasons why larger issuers are riskier to Ginnie Mae than smaller ones:

(1) Large issuers constitute the bulk of Ginnie Mae's risk exposure. Ginnie Mae's largest 15 issuers constitute 75% of GNMA securities – while its smallest 144 issuers (almost half of the number of total issuers) constitute only .49% [less than ½ of one percent]

(2) In the same way that it is much easier for the FDIC to resolve a smaller failed bank than a larger one, it is generally easier for Ginnie Mae to arrange the transfer of a failed portfolio of a smaller issuer than a large issuer. This is because the universe of servicers capable of absorbing a small servicing portfolio is much larger than for a large portfolio.

(3) The possibility that a single, fast growing issuer is going to engage in fraud or otherwise place FHA loans without proper insurance in Ginnie Mae pools is much higher for one large servicer than for a number of smaller issuers with the same total issuance exposure.

(4) Ginnie Mae proactively encourages smaller issuers starting to encounter financial problems to sell their servicing portfolio before financial problems worsen – thus eliminating or reducing Ginnie Mae financial exposure before it occurs. This is more difficult to do with larger issuers.

In fact, there is an argument that the greatest risk that smaller IMBs pose to Ginnie Mae (and Fannie Mae and Freddie Mac) is regulatory overreach – encouraged by large banks that seek to regain dominance in servicing by pressing for artificial regulatory advantages in the face of their inability or unwillingness to compete on pricing and service to consumers.

Again, quoting from the 2019 CHLA Report on Ginnie Mae:

> "Moreover, excessive Ginnie Mae focus on the risk of non-bank issuers could increase its risk by becoming a self-fulfilling prophecy. Ginnie Mae should of course be prudent in its supervision and transparent about the risks it perceives. **But, if warehouse lenders become overly concerned that Ginnie Mae will make it hard for smaller issuers to remain in the program or will reduce the valueof Ginnie Mae issuance authority, warehouse lenders could clamp down on or stop lending to smaller IMBs. This could increase Ginnie Mae's risk in this sector of the market."**

We would also point out that smaller IMBs also just recently passed a real- life stress test – COVID. Congress granted FHA, RHS, VA, Fannie Mae, and Freddie Mac borrowers a relatively easy option to invoke forbearance (and not make mortgage penalties without penalty) – and the economic shutdown that resulted from COVID resulted in a huge increase in Ginnie Mae servicer advance responsibilities. Yet the number of failed Ginnie Mae IMB issuers appears to be miniscule or non-existent.

CHLA does greatly appreciate that Ginnie Mae provided a standby COVD-related advance authority for potentially distressed issuers. However, the fact that this was not extensively used proves our point: IMBs – particularly smaller IMB issuers – are well placed financially to weather economic storms – and the main risk is lack of confidence by warehouse banks that the rules of the game will not suddenly change.

Financial & Systemic Risk will Increase without an Exemption for Smaller Issuers

Again, citing from the CHLA's 2019 Report on Ginnie Mae:

> "Tightened supervision of small lenders disproportionate to their risk could even **increase Ginnie Mae risk**. To some extent, driving smaller issuers out of the program will result in fewer Ginnie Mae securities issued and fewer mortgage loans originated. **However, to the extent such loans are made and securitized instead by larger issuers or correspondent lenders, the result is an increase in the concentration of Ginnie Mae securities among the largest Ginnie Mae issuers – precisely the typesof issuers with higher level of risk."**

Access to Credit will be Reduced Without Protecting Smaller Issuers

Without access to Ginnie Mae's internal black box calculations, it is difficult to predict the shrinkage in the number of smaller IMB issuers because of the increased requirements. Moreover, there is no discussion of this issue in the RFP. We believe there will be a meaningful impact, particularly with the new risk-based capital requirement. Some smaller IMBs may not meet the increased requirements; more commonly, consolidation with larger issuers.

The impact of a shrinking of the base of smaller IMB issuers would be heightened issuer concentration. Fewer issuers translates into less consumer choice, less consumer access to the secondary market, and higher mortgage rates and fees on FHA, VA, and RHS loans.

The proposal increases financial requirements for IMBs – but not banks. Since IMBs account for 90% of new Ginnie Mae issuance, if the proposal reduces the number and breadth of smaller IMB issuers, borrowers would lose mortgage options or be forced to turn to banks, which have a demonstrably poorer record on access to credit than IMBs.

CHLA documented this difference in their recent IMB Report. To cite from the report:

"A Greenlighting Institute report **"Home Lending to Communities of Color in California** concluded:

- ***"Women of color . . . are more likely to access a loan from a non-bank lender than from a mainstream bank."***
- ***"When Black, Asian and Latino low-income households do access home purchase loans, it is more likely to be from a non-bank lender"***
- ***"Non-bank lenders make twice as many home purchase loans to low-income borrowers as mainstream banks."***

URBAN INSTITUTE MORTGAGE REPORTS

- An August 2017 Urban Institute Report *("Housing Finance at a Glance") found* that ***". . . the median FICO score for nonbank originations has been consistently less than the median FICO for bank originations for all three agencies"*** (Fannie, Freddie and GNMA].
- The report also noted that ***"the median DTIs of non-bank loans are higher, indicating the nonbanks are more accommodating in the DTI dimension as well as the FICO dimension."***
- Urban Institute Monthly Chartbook statistics consistently show IMBs do a better job than banks of serving underserved borrowers, as measured by metrics like FICO scores and DTI.

FEDERAL HOUSING ADMINISTRATION (FHA) LOANS

- **Nonbanks (IMBs) now originate 90% of FHA loans**, the program focused on "***first-time homebuyers, minorities, lower-income families, and residents of under-served areas."***

Smaller IMBs are Disproportionately Affected by Exclusion of PLS Loans

It is mystifying that the proposal adds a percentage of GSE serviced loans to the Net Worth and Liquidity requirements – but excludes non-agency Private Label Securities (PLS) and portfolio loans. There is no explanation for this discrepancy.

This disparate treatment disproportionately and negatively affects smaller issuers. Smaller issuers overwhelmingly service federal agency loans (Ginnie Mae [FHA/VA/RHS)] and GSE loans), 100% of which are included in the RPF's Net Worth and Liquidity requirements.

However, the proposal **exempts** PLS and portfolio loans, which constitute a higher percentage of larger issuers' servicing business. We do not understand the rationale for this, since the IMB's liabilities are likely to be equal or greater than in a federal agency loan.

This also encourages more mortgage loans that lack consumer and loss mitigation protections. PLS loans have historically been the source of the great majority of problem loans for consumers (as exemplified in the 2008 subprime housing crisis) and lack the vigorous loss mitigation requirements of federal agency loans. Exempting PLS loans from the Net Worth and Liquidity requirements only encourages origination of more mortgage loans that lack distressed borrower protections and rigorous loss mitigation requirements.

Therefore, any proposal to add non-Ginnie Mae loans to Net Worth and Liquidity requirements should include ALL loans serviced by an issuer.

Smaller IMBs Disproportionately Affected By Actual/Scheduled Treatment

It is also mystifying that the proposal appears to treat all GSE loans the same regardless of whether required remittances are scheduled or actual – and does not provide an explanation for this treatment.

Failure to provide for a distinction between loans that are scheduled and actual disproportionately and negatively affects smaller issuers. This is because smaller issuers are much more likely to select the servicing option which bases advances on "actual" borrower payments.

Therefore, at a minimum the proposal should be revised to create an appropriate distinction based on whether required remittances are actual or scheduled.

A New Risk-based Capital Requirement Will Reduce Access to Credit

We understand that banks are upset about Basel 2 treatment of Mortgage Servicing Rights (MSRs). However, that is not a reason to impose a similar bank-like risk-based capital standard on non-banks (IMBs).

Further, regardless of the merits of this proposal, it is not appropriate to rush this completely new Ginnie Mae issuer requirement, to have it take effect in less than six months – especially since early indications are that the required MSR haircuts are significant.

There is a developing consensus that the risk based capital requirement will reduce the value of MSRs – which will inevitably translate into higher mortgage costs and rates for consumers.

Another likely impact of the new risk-based capital standard will be to discourage small balance loans, which Congress has already identified as a problem area. Use of higher I/O strips is necessary to cover the costs of originating small balance loans. Therefore, penalizing such loans through a risk-based capital standard will make it much harder to profitably originate and securitize these loans.

Additionally, by creating financial incentives for loan originators to reduce the level of I/O strips, Ginnie Mae will make it more attractive to refinance loans In its pools. This encourages refinancing – and refinance churning – a problem that Ginnie Mae expressed significant concerns about just a few years ago.

We would also note that Ginnie Mae has previously warned issuers about loans with insufficient I/O strips – which seems inconsistent with the clear intent of the risk-based capital rule. Reducing the level of I/O strips makes these loans worth less on the open market, and thus modestly increases the main risk Ginnie Mae faces, which is liquidating portfolios of distressed or bankrupt issuers.

Finally, the risk-based capital rule treats loans in the pipeline the same whether or not they are hedged. We understand the complexity of making adjustments for hedging in the calculations, but we make this point to accentuate the potential flaws in this new capital requirement.

In closing, instead of actions to contract access to credit, Ginnie Mae should expand it – by reinstating its Targeted Lending Initiative, which provides a price break for loans to lower income borrowers.

Thank you for consideration of our comments.

Sincerely yours,

COMMUNITY HOME LENDERS ASSOCIATION