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Committee on Financial Services
Subcommittee on Financial Institutions and Consumer Credit

"The State of Bank Lending in America"

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Chairman Luetkemeyer, Ranking Member Clay, thank you for the opportunity to testify on behalf of the Mortgage Bankers Association (MBA)[1] on the current lending environment and the impediments to credit availability for the American homebuyer in today's market. I am J. David Motley, President of Colonial Savings, F.A. in Fort Worth, Texas, a Certified Mortgage Banker, and Chair-Elect of the Mortgage Bankers Association.

In accordance with the subcommittee's request, my testimony addresses the impact of federal regulation on mortgage lending, the constricted availability of credit in recent years, and how these factors have affected the ability of the mortgage industry to provide financial products or services to consumers and smaller lenders.

The Mortgage Bankers Association represents mortgage lenders of all sizes and business models: from small independent mortgage bankers, community banks, and credit unions to the nation's largest financial institutions. All of MBA's members play their own unique role in helping families all across the country achieve the American dream of homeownership.

Similarly, my community bank, Colonial Savings, serves consumers in all 50 states, originating $1.8 billion in mortgages in 2016 through its retail branches for both the bank's portfolio and for sale to the secondary market, and buying loans from smaller institutions that no longer maintain the capacity or have the desire to engage in mortgage servicing themselves. We are also a servicing outlet under the Federal Home Loan Bank Mortgage Partnership Finance Program and participate as a servicing buyer of the Fannie Mae/Freddie Mac Co-issue execution. Today Colonial services more than $27 billion in residential mortgages.

MBA has consistently supported reasonable requirements that will prevent a reemergence of housing and market disruptions. We believe some aspects of the Dodd-Frank Wall Street Reform and Consumer Protection Act and other statutes have made the mortgage market safer; however, in many other respects the Dodd-Frank rules have reduced the availability and affordability of mortgage credit for many American families.

Today, credit availability is substantially more constrained than it has been historically. Regulatory uncertainty combined with heightened enforcement risk have forced many responsible lenders to reconsider their ability to lend to the full extent of the credit box. These decisions ultimately impact the consumer, and often disproportionately impact low-to-moderate income borrowers, minorities, and first-time homebuyers.

While we believe some of these new regulations were needed, the pendulum has swung too far and certain aspects of the current regulatory regime warrant review and adjustment. These changes need to be considered judiciously to balance the need for appropriate consumer protections while ensuring access to safe, sustainable mortgage credit. In this regard, we strongly urge that particular attention be given to simplifying rules, providing greater clarity and certainty, and mitigating supervisory burdens. These goals are particularly important for smaller, community lenders that may not be able to sustain excessive compliance and legal infrastructures.

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[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 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 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 over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

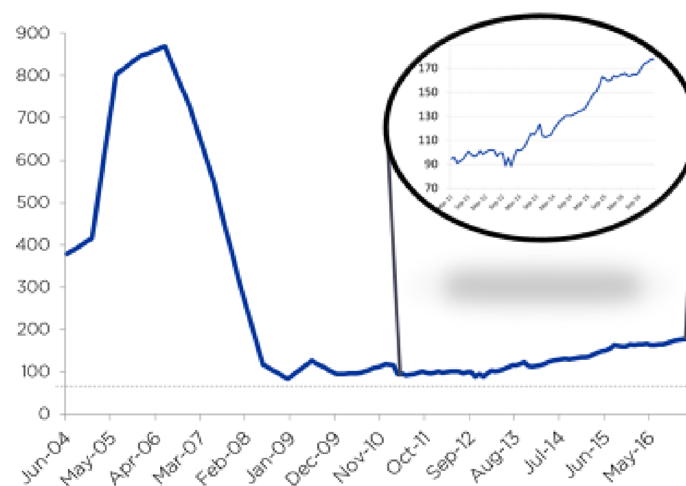
Background

According to MBA's Mortgage Credit Availability Index (MCAI) the availability of affordable mortgage credit is limited for many American homebuyers. The MCAI measures the quantity and quality of mortgage credit over time and for different segments of the market. A decline in the MCAI indicates credit is tightening, while increases in the index are indicative of greater credit availability.

Recent data show that mortgage credit availability increased 0.4 percent in February 2017 and reached its highest level since 2007.[2] However, recent increases in the index are deceptive, and a more detailed analysis shows that while the index reached a high of 869 in mid-2006, today it stands at 177. While no one would suggest a return to the unsustainable lending of the 2006 period, today's index remains less than half the level it was in 2004 (see Chart 1).

Chart 1

Mortgage Credit Availability In Historic Context



Source: MBA's Mortgage Credit Availability Index Powered by Ellie Mae's AllRegs Market Clarit 4 MBA.

In addition to the overall tightening of credit availability, both production and servicing expenses have substantially increased over the past 10 years. MBA's Quarterly Performance Report data – which compiles financial statistics from more than 300 independent mortgage bankers – show that the costs to originate a mortgage loan for a consumer has increased from approximately $4,376 in the third quarter of 2009 to approximately $7,562 by the fourth quarter of 2016 (see Chart 2). Similarly, MBA's servicing data show the fully loaded cost to service a performing loan has gone from $58 in 2008 to $228 by the first half of 2016. For a non-performing loan this increase is even more dramatic, as costs have gone from $482 in 2008 to $2,522 by the first half of 2016 (see Chart 3).

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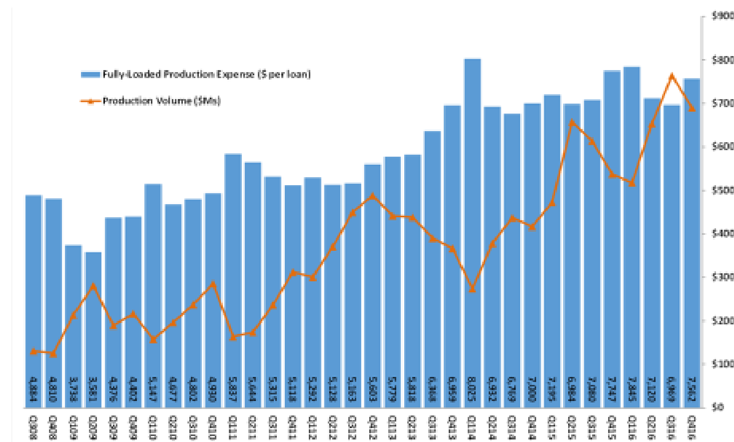
[2] The increase in February was the net result of two countervailing movements. There was an increase in the supply of credit, as more investors offered affordable low down payment mortgages and streamlined documentation for loans guaranteed by the Federal Housing Administration and the Veterans Administration. This increase was partially offset by the first downturn in the availability of jumbo credit in a year, due to the consolidation of some jumbo programs.

Chart 2

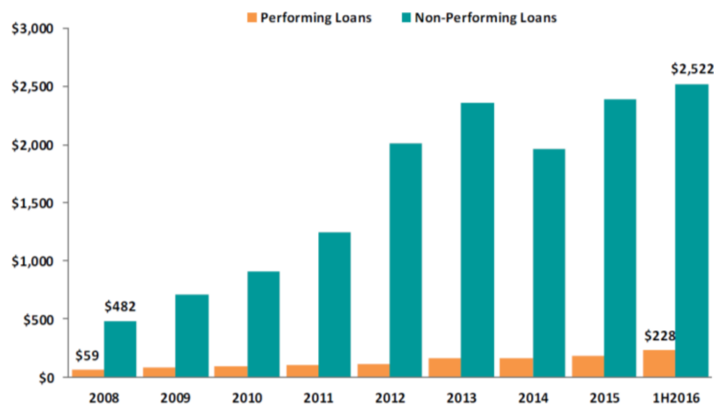
IMB Fully-Loaded Production Expenses ($ per loan):



Source: MBA's Quarterly Mortgage Bankers Performance Report, www.mba.org/performancereport

Chart 3

Fully-Loaded Servicing Operating Costs of Performing and Non-Performing Loans*



*Includes direct cost to service, unreimbursed foreclosure and REO costs (less lookbacks,) compensatory fees, and corporate allocation

Source: MBA's Servicing Operations Study and Forum (Prime Servicers): www.mba.org/sosf; PGR 1H2016

These soaring production and servicing costs are, to a large degree, a consequence of a new legal and regulatory landscape for mortgage lending. The Dodd-Frank Act charged several key regulators with drafting a number of significant and complex rules that impacted almost every facet of the mortgage industry. Most of these rules have already been implemented or are in the process of being implemented. Unfortunately, many of these rules were also drafted and implemented unevenly creating the need for additional clarifying rules and guidance or even considerable revision.

The Dodd-Frank Act also created a new regulator, the Consumer Financial Protection Bureau (CFPB). Although the CFPB is empowered with significant rulemaking authority, the CFPB's approach to redirecting behavior in the marketplace has relied heavily on enforcement actions.

For most financial institutions these actions have resulted in tremendous uncertainty about where and to what extent legal and reputational risks exist. Too often it is unclear how the CFPB interprets a particular statute until an enforcement action, or even multiple enforcement actions, have occurred.[3] Rather than responding proactively to a rule or guidance, financial institutions can only pay for considerably more counsel and compliance advice and hope they are not used to exemplify non-compliant behavior.[4] These costs are particularly burdensome to smaller lenders.

In response to these trends, MBA offers the following views and recommendations that we believe will remove, or at least diminish many of the regulatory impediments that are stifling today's mortgage market and lessening the availability of credit for American consumers.

Many Regulations Are Too Restrictive or Complex

While MBA recognizes the need for clear and reasonable regulations to ensure a safe and transparent mortgage market, we recommend that certain regulations be revisited and revised to encourage lenders to offer a greater degree of sustainable and affordable mortgage credit to consumers.

Ability to Repay and Qualified Mortgages

The Dodd-Frank Act and the CFPB's Ability to Repay (ATR) rule requires lenders to determine that a borrower has a reasonable ability to repay a mortgage before the loan is consummated. The law provides significant penalties and liability for failing to meet this requirement. The ATR rule also provides a presumption of compliance for loans that are originated as Qualified Mortgages (QMs), which provides greater certainty to lenders and mortgage investors regarding potential liability where there has been compliance but a claim is made.

In order for a loan to qualify as a QM, it may not contain certain "risky" features, such as interest only or negative amortization terms, and it must meet specified underwriting standards. These standards include a debt-to-income (DTI) ratio cap of no more than 43 percent, or in the alternative, eligibility for Fannie Mae and Freddie Mac (the GSEs) programs (i.e., the so-called "QM patch"). Borrowers also may not be charged points and fees that exceed three percent of the loan amount for loans in excess of $102,894 (in 2017). Loans below that amount are permitted to have fees in excess of three percent, based on a sliding scale.

The rule establishes a compliance *safe harbor* for QMs only if the Annual Percentage Rate (APR) of the loan does not exceed the average prime offer rate (APOR) for that mortgage by 150 bps or more. Loans to borrowers that exceed the APOR by more than 150 bps receive a *rebuttable presumption* of compliance if the loans otherwise qualify as QMs. Given the legal uncertainties of non-QM and rebuttable presumption lending, safe harbor QMs comprise the vast majority of the mortgage loans available in today's market.

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[3] In a speech on March 9, 2015 at the Consumer Bankers Association, Director Cordray provided justification for employing agency and court orders instead of rules. He stated, "public enforcement actions have been marked by orders, whether entered by our agency or by a court, which specify the facts and the resulting legal conclusions." These orders provide detailed guidance. Director Cordray stated that "it would be "compliance malpractice" for executives not to take careful bearings from the contents of these orders about how to comply with the law and treat consumers fairly."

[4] One example of this practice is demonstrated in the current treatment of marketing services agreements between settlement services providers. While HUD had generally permitted these arrangements under Section 8(c) of RESPA as long as reasonable compensation was paid for the services, the Bureau asserted these arrangements were likely problematic and violative of RESPA regardless of the compensation. Moreover, the Bureau failed to provide any notice of its changed interpretation to the industry or the public prior to pressing its position in enforcement cases. Instead of issuing rules or guidance, Bureau positions have been articulated through settlements rather than through guidance or rules.

Although the level of additional risk outside the safe harbor has not yet been tested in litigation under Dodd-Frank, most lenders have understandably limited themselves to making only QM safe harbor loans to minimize potential liability and litigation. Non-QM loans have generally been available only to very low risk borrowers. As a result of some of the constraints in the QM definition, many borrowers who should qualify for a QM are unable to access safe, sustainable, and affordable mortgage credit.

MBA believes the ATR rule and QM standards must be improved and we continue to work with policymakers, including the CFPB, to responsibly widen the credit box.

While MBA appreciates some earlier efforts to address flaws in the QM definition, we believe changes to the ATR rule should not be confined to particular types of institutions or business models. The QM definition should be fixed holistically, not revised in piecemeal fashion with special exceptions for certain categories of lenders.

Specifically, MBA has made a number of key recommendations for refining the QM definition to cover additional creditworthy borrowers:

1. **Expand the Safe Harbor**
   All loans satisfying QM requirements should have a legal safe harbor regardless of their rate. The current 150 bps limit is too narrow considering the inclusion of fees in the APR.

2. **Increase the Small Loan Definition**
   The current definition of a smaller loan under the ATR rule – where points and fees may exceed three percent and still qualify as a QM – is set at $102,894 (for 2017). This metric is too low considering the average loan size is approximately $260,000. As a result, too many smaller loans do not qualify as QMs. The points and fees cap should apply only to loans of $200,000 or more, with a sliding scale that permits progressively higher points and fees caps for smaller loans. This change would increase QM lending to moderate-income borrowers who have smaller loan balances.

3. **Establish Alternatives to Appendix Q**
   For those loans not satisfying the QM patch, underwriting of QM loans must be conducted in accordance with Appendix Q of the rule. Unfortunately, Appendix Q is generally viewed as lacking sufficient guidance and flexibility to be used as an underwriting standard. To rectify this problem, MBA supports regulatory or legislative changes to allow the use of other commonly accepted underwriting standards such as those acceptable to the Federal Housing Finance Agency (FHFA), Federal Housing Administration (FHA), the Department of Veterans' Affairs (VA), and the Rural Housing Service (RHS).

4. **Broaden Right to Cure for DTI and other Technical Errors**
   MBA has long advocated for an amendment that would permit the correction of errors where the three percent points and fees limit is exceeded. To encourage lending to the full extent of the QM credit box, MBA also urges that the right to cure or correct errors be extended to DTI miscalculations and other technical errors. There is an existing points and fees cure, but it will apply only to loans closed on or before January 10, 2021. So there needs to be a permanent points and fees cure as well as a DTI cure.

5. **Revise the Points and Fees Definition**
MBA supports H.R. 1153, the Mortgage Choice Act, which would exclude title insurance fees paid to lender-affiliated companies from the calculation of points and fees under the QM definition. Under the ATR rule, the QM points and fees calculation includes fees paid to lender-affiliated settlement service providers – but not to unaffiliated settlement service providers. Excluding fees paid to affiliates would result in greater competition between providers and benefit consumers. In addition, the treatment of mortgage broker fees results in identical loans being treated differently under the rules.

6. **Replace the Patch and the Default QM**
The "QM patch" – which allows loans approved by the GSEs' underwriting systems to qualify as QM – is essential at this time, however, it is only a temporary solution while the GSEs are in conservatorship or until 2021. Loans must be consummated on or before January 10, 2021 (unless the conservatorship ends earlier). MBA urges the CFPB to start the process of working with stakeholders to develop a transparent set of criteria, including compensating factors, to define a QM – replacing both the QM patch and the 43 percent DTI standard. Such a standard must provide workable, flexible underwriting standards that are consistent with the Dodd-Frank Act without injecting undue complexity or uncertainty into the process of serving consumers' credit needs.

Servicing Market Regulations

Mortgage servicers currently have to deal with an interconnected and sometimes conflicting landscape of regulatory requirements and government program imperatives. As noted above, in this period of intense regulatory change, MBA data show the cost to service a performing loan has increased by $170 between 2008 and the first half of 2016. For a non-performing loan the jump is even more dramatic, as costs have risen by $2,040 between 2008 and the first half of 2016 (see Chart 3). These additional costs ultimately get passed through to consumers in costs for new loans. Likewise, they directly impact consumer access to credit as defaulted loans cost more than 11 times as much to service as performing loans, consequently causing lenders to reduce their exposure to borrowers that are perceived to pose greater risk.

MBA believes mortgage servicing market regulations would benefit from review under President Trump's recent Executive Order's direction to "make regulation efficient, effective, and appropriately tailored." Coordination among federal agencies and streamlining of existing regulations would go a long way toward lowering costs and increasing the availability of credit.

For example, VA, FHA, and GSEs all have divergent loan modification programs despite a broad consensus on what constitutes a successful program. To stem these differences, MBA strongly urges government insurer and guarantor alignment toward the recently released GSE "Flex modification" program to harmonize these requirements, reduce cost for servicers, and lessen confusion as well as disparities in outcomes based on loan products.

Additional Authoritative Guidance and Clarity is Needed in Key Areas

Notwithstanding the CFPB's preeminent role in consumer regulation, the Bureau has, with limited exceptions, followed a policy of only offering authoritative guidance in the form of formal rules and commentary. Most other guidance in the form of webinars, handbooks or other oral statements is prefaced with the caveat that only formal commentary and rules can be relied upon. While MBA believes that rules and commentary with an opportunity for public comment must remain the primary means of implementing the myriad laws for which the CFPB is responsible, its reluctance

to also offer authoritative written guidance as questions arise – through interpretative rules, FAQs or supervisory memoranda – has made lenders excessively cautious and defensive in their approach to lending.

Absent changes in the CFPB's practices, MBA supports congressional action to require the CFPB to develop an appropriate framework with public comment for its issuance of rules, policies, and supervisory guidance. This would include criteria for issuing rules, commentary, supervisory memoranda or compliance Bulletins to put the industry on notice regarding supervisory expectations on what the CFPB regards as illegal practices. Such legislation should provide that notices from the CFPB of potentially illegal conduct must be provided in sufficient time to permit compliance prior to any CFPB enforcement actions. MBA believes this type of legislation will ensure that consumer credit will not be lessened because of unnecessary confusion or fear regarding the legality of particular actions.

An example of an area where insufficient guidance has been provided is the Truth in Lending Act (TILA) Real Estate Settlement Procedures Act (RESPA) Integrated Disclosure (TRID) or "Know Before You Owe" (KBYO) rule. This CFPB rule requires the use of new, standard disclosure forms to be provided for virtually all mortgage borrowers nationally at the time of mortgage application and settlement, known as the Loan Estimate and the Closing Disclosure, respectively. Significantly, the rule not only changed the disclosure forms but also changed real estate transactions themselves by introducing a three-day waiting period before closing to allow borrowers to review their closing forms. Under the new rule, both lenders and assignees face significant potential liability for failures to comply.

The CFPB produced several webinars and helpful issuances, and participated in numerous conferences and forums leading up to implementation and beyond, and the MBA thanks the Bureau for these efforts. However, many questions regarding this uniquely detailed and complex rule arose and for long periods remained unanswered. Yet the CFPB steadfastly refused to offer timely, accessible FAQs or other authoritative guidance to regulated entities as other regulators do, except on a handful of technical matters.

The absence of timely, authoritative written guidance from the CFPB resulted in confusion and further complicated the implementation process. Most importantly, the lack of such guidance in some areas – such as cures and corrections – seized the market for a time, and other issues deprived some borrowers of timely closings and beneficial features of transactions such as lender and seller credits. Because of the lack of guidance, investors take different positions on issues, and often conservative positions. This results in delays when lenders try to sell loans, and in various cases lenders ultimately cannot sell loans because of perceived technical errors. This is contributing to constraints on the availability of credit to consumers. The provision of clear, written guidance from the CFPB would provide greater certainty to the industry and facilitate the flow of private capital into the mortgage marketplace.

Despite the extensive liability that can arise from TILA violations, the CFPB has largely foregone providing guidance on TRID liability taking the position that such questions will be settled by the courts. This uncertainty can be expected to spawn litigation, increase costs and limit credit to consumers.

Home Mortgage Disclosure Act (HMDA)

The HMDA rule implements provisions of Dodd-Frank that will vastly increase the loan level data collected and reported to the government on applications from and loans to individual borrowers.

The rule's new requirements for data collection and reporting generally go into effect in 2018 and 2019.

While we appreciate that the CFPB has recognized the problem of potential harm to privacy by virtue of the public disclosure of HMDA data and has committed to engaging in a public discussion about these issues, conclusions about the extent this data may be disclosed have not yet been reached. Given this uncertainty, MBA is concerned that if not resolved appropriately, the extent of disclosure may harm individual borrowers and the mortgage market.

We urge Congress to carefully monitor this issue and we support legislation, if necessary, to stop disclosure and possibly reporting of the new data until borrower privacy is adequately considered and protected from harm.

Rules Imposed by International Regulators Need Revision

In certain instances, regulations imposed on U.S. institutions by international regulatory bodies are acting as an impediment to lending and servicing, and should be reconsidered.

Basel III

The punitive treatment of mortgage servicing rights (MSRs) under the Basel III risk-based capital standards threatens to undermine the value of this important asset, with adverse implications for the entire mortgage finance chain. The new Basel III rule increases the risk-weighting of MSRs held by banks from 100 percent to 250 percent. It also decreases the cap on MSRs that a bank may hold on its balance sheet from a 50 percent common equity component of tier one capital to a more stringent 10 percent limit with MSR assets above the limit deducted from regulatory capital. In addition, MSRs, deferred tax assets and equity interests in unconsolidated financial entities are limited, in aggregate, to a 15 percent common equity component of tier one capital before they must be deducted from regulatory capital. This unnecessarily punitive treatment of MSRs makes them one of the most costly asset classes in the entire Basel III framework, despite any clear linkage of MSRs to the financial upheaval that Basel III is intended to address.

MSRs are not widely utilized outside of the United States but are a vital component of the American housing finance system's ability to provide a 30-year fixed-rate mortgage. These negative effects of the Basel III agreement on the mortgage market is an area particularly ripe for reevaluation in light of the President's Executive Order asking agencies to re-evaluate regulations to "enable American companies to be competitive with foreign firms in domestic and foreign markets" and "advance American interests in international financial regulatory negotiations and meetings."

MBA believes that performance, capacity and consumer service quality should be the primary drivers of which servicers gain market share, not excessively high capital standards on a particular segment of the industry. Nor should American banks be handicapped by an international agreement that discriminates against an asset that is uniquely integral to the American mortgage finance system. The current Basel treatment of MSRs, amid the backdrop of complicated and conflicting servicing rules, discourages many community banks from originating mortgage and retaining the servicing, or from acquiring servicing assets. Moreover, it impacts nonbank lenders by removing an important bid for MSR assets from the market.

Small Lender Burdens Need to be Addressed

MBA believes nonbank mortgage lenders play a key role in the mortgage marketplace. MBA supports risk-based supervision of nonbanks, but we are particularly concerned that in addition to dealing with a mountain of sometimes vexing rules, these entities must also deal with frequent and sometimes duplicative examinations from the CFPB and the states in which they operate. This increases costs and unduly strains the resources of these companies.

MBA urges rationalizing this process through either regulatory action by the CFPB or legislation that requires the CFPB to establish by rule a binding written policy of how the CFPB prioritizes the lenders it examines. The CFPB's current approach to "risk focused" examinations is neither codified in a rule nor established in other transparent formal procedural guidance to the industry. A multifactor approach – similar to how the Federal Deposit Insurance Corporation prioritizes exam resources for community banks – could include:

1. Size or market share (without setting a hard cap);
2. Referrals from state regulators;
3. Significant participation or market share in higher risk products;
4. Consumer complaint volume (relative to size, or a high volume of a specific complaint type);

MBA urges that efforts to mitigate examination burdens for nonbank mortgage companies should focus on establishing risk-based supervisory standards that ultimately would provide relief and clarity for *all* lenders.

In addition, MBA supports other efforts to ensure small lender concerns are addressed:

1. Establishment of notice requirements to lenders by CFPB identifying the factors that give rise to a scheduled examination;
2. Establishment of an exam appeals process for smaller lenders, including independent mortgage bankers (IMBs). MBA supports H.R. 1941 from the 114th Congress, and urges IMBs to be added to the bill;
3. Create an IMB Advisory Council at the CFPB, similar to the Bureau's existing Community Bank Advisory Council and Credit Union Advisory Council; and
4. Passage of H.R. 2121 from the 114th Congress, which will provide transitional licensing authority for loan officers moving between bank and nonbank lenders, helping labor mobility and allowing nonbank lenders to compete fairly for talented loan officers.

Other Issues Impeding Credit Access

Given the rising costs to originate and service mortgage loans, lenders must make other important risk management decisions for their businesses that may ultimately lead to increased costs for consumers and affect the availability of credit.

According to MBA data, the United States will see 15.9 million additional households formed over the next decade consisting of 10.3 million additional owner households and 5.6 million new renter households.[5] These households will increase the need for all types of housing over the next decade including the need for affordable financing options for first-time homebuyers and low-to-moderate income borrowers. The following highlights the need for attention to regulatory clarity,

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[5] Lynn Fisher and Jamie Woodwell, Housing Demand: Demographics and the Numbers Behind the Coming Multi-Million Increase in Households, Mortgage Bankers Association, July 2015.

efficient and modernized systems, and other areas to help address these homeownership financing needs.

False Claims Act

FHA has played a significant role in helping families become homeowners since 1934 and continues to play a critical role in providing affordable credit access for many first-time and low-to-moderate income borrowers. MBA strongly supports FHA's mission and the need to protect and strengthen the financial viability of government-insured lending programs. In this regard MBA has supported efforts to improve the program and protect it from losses. However, the Department of Justice (DOJ) enforcement actions under the False Claims Act continue to overshadow HUD's certification process and lender participation in the FHA program. This resulting legal liability for participating lenders has caused some lenders to impose new credit overlays and/or limit involvement in FHA lending altogether to minimize risks from program participation. These factors have made FHA credit more expensive and less available.

Notably, on the same day FHA released its final loan-level certification on March 15, 2016, the Justice Department published a statement on its website defending its previous investigations of FHA lenders and the pursuit of certain lenders under the False Claims Act. In this statement, DOJ reaffirmed that "[t]he department will continue [its] enforcement efforts by using the False Claims Act, and will continue to be guided by the language of the act that prohibits the submission of knowing and material false claims."[6] Differing messages from HUD and DOJ have contributed to market uncertainty.

Moreover, despite DOJ's statement that "the False Claims Act requires more than mere negligence or a simple mistake to hold a person liable,"[7] our industry has found little comfort in these words. What is needed is a defined metric to classify various loan defects so lenders can focus their compliance efforts. In the absence of clear and unambiguous metrics for measuring loan defects, participating FHA lenders will continue using cautious, defensive underwriting to mitigate the risk of excessive enforcement actions for minor mistakes.

In order to truly improve and expand access to credit, MBA urges HUD to take all necessary steps to limit the overly broad certification regime that can lead to subjective judgments of what may constitute a "material" false claim under the False Claims Act when these errors may in fact be immaterial. To this end, MBA strongly recommends that HUD adopt a comprehensive, transparent, and predictable Quality Control program in conjunction with the full implementation of the Single Family Loan Quality Assessment Methodology (Defect Taxonomy). Accompanying clear and formal guidance is also needed to specify remedial actions for particular types of underwriting errors. In the absence of an amendment to the False Claims Act, these critical steps could establish a consistent regulatory hierarchy for identifying and classifying material errors to avoid harm to the FHA fund and ultimately its borrowers.

HUD Rules

In addition to False Claims Act liability concerns, a continued lack of clear program guidance paired with conflicting, complex, and antiquated FHA servicing rules has resulted in higher costs for the many smaller lenders that service this segment, the exit from the program of some traditional market participants, and ultimately tighter credit availability standards.

[6] Department of Justice, Justice Blogs, The False Claims Act & Federal Housing Administration Lending, March 15, 2016, at https://www.justice.gov/opa/blog/false-claims-act-federal-housing-administration-lending
[7] *Id.*

Complexity and risk in FHA servicing has also influenced decision-making for FHA program participants due to the increased costs associated with the servicing of FHA loans. FHA's conveyance process regulations and bifurcated timelines dramatically increase the risk of loss for FHA servicers and require different processes than those necessary to serve GSE loans. Reforms to FHA servicing are necessary to add cost certainty and reduce operational inefficiencies. Such reforms should include:

1. **Direct conveyance of foreclosed FHA properties**
   FHA should allow lenders to directly convey foreclosed properties to FHA, eliminating costly inspection regimes and delays – consistent with the GSE approach. At the very least, FHA should continue to expand the Distressed Asset Stabilization Program and Claims without Conveyance of Title program since they limit losses to both the FHA fund and servicers by providing an alternative path to the costly conveyance process.

2. **A unified timeline for FHA servicing process rather than three separate milestones**
   Eliminate the current three milestone timeline (first legal action, reasonable diligence, and conveyance) and hold the servicer responsible for compliance with one overall timeline. This is consistent with the GSE approach and incentivizes servicers to "catch up" if issues with the loan result in a slower process initially.

3. **Streamline FHA loss mitigation processes**
   There is widespread consensus that reduced documentation and targeted payment reduction are the factors to consider when designing a successful and accessible loan modification regime. Despite this, FHA persists with a documentation heavy approach that results in greater borrower fallout and higher servicing costs. As mentioned above, FHA should, to the extent possible, align with the recently released GSE "Flex Modification" which reduces borrower documentation burden and results in lower payments. This would help more borrowers stay in their homes and reduce losses to the FHA fund.

Government Housing Resources

Current FHA, VA, and Ginnie Mae program operations require modernization to operate efficiently and handle the volume of these programs. This lack of needed updates is adversely impacting the availability of affordable credit to FHA borrowers. To remedy this, MBA urges Congress to provide FHA, VA, and Ginnie Mae funding for this purpose at requested levels through the regular appropriations process.

Specifically, in order to sustain FHA's current operations and accommodate the work processes of its participating lenders, FHA requires additional funding for effective risk management processes, necessary staffing increases, updates to outdated technology systems, support for new systems (i.e. FHA's new Loan Review System), and the critical maintenance of FHA's program guidance. Notably, the HUD Inspector General has expressed specific concern about the current state of FHA's technology and the lack of its systems capabilities and automation to respond to the changes in business processes and the current IT operating environment. For example, FHA still relies on COBOL programming, while systems like Neighborhood Watch and FHA Connection frequently suffer from system crashes and limited maintenance.

Although MBA recognizes the need for fiscal responsibility in a difficult budget environment, we urge Congress to ensure that the FHA, VA and Ginnie Mae programs operate as 21st Century

programs. Up-to-date resources are critical to risk management functions, effective oversight of issuers and lenders, and protection of the American taxpayer from financial loss. Since their inception, FHA, VA, and in turn Ginnie Mae, have helped over 60 million Americans realize the dream of homeownership and build wealth while stabilizing communities across the nation. To continue this important work, adequate funding levels are vital to the FHA, VA and Ginnie Mae programs.

Conclusion

We commend the efforts of this Subcommittee to examine the regulatory hurdles limiting consumers from accessing affordable mortgage credit. No matter how well-intentioned rules and enforcement may be, we are concerned that key rules and practices are unduly restricting credit opportunities for qualified borrowers.

We thank the Subcommittee for the opportunity to offer our recommendations on these issues and look forward to working closely with you to improve both the affordability and the availability of sound mortgage credit for American families.