



October 27, 2021

Lopa Kolluri, Principal Deputy Assistant Secretary for Housing
Julienne Joseph, Deputy Assistant Secretary for Single Family Housing
Office of Housing / Federal Housing Administration
Department of Housing and Urban Development
451 7th Street SW
Washington, D.C. 20410-8000

Re.: 40-Year Loan Modification COVID-19 Recovery Loss Mitigation Options

Ms. Kolluri and Ms. Joseph:

Thank you for the opportunity to provide input on the Federal Housing Administration's (FHA) proposal to expand the COVID-19 Loss Mitigation programs to include a 40-year loan modification. The Housing Policy Council¹ (HPC) and Mortgage Bankers Association² (MBA) members appreciate FHA's engagement with key stakeholders throughout the pandemic and commend the FHA for its commitment to continual program refinement. That said, the demand on servicers to implement a wide array of policy changes over the last several months has been challenging and we expect this to continue well into the first quarter of 2022.³ Given the critical demands on the servicers' time and attention, we recommend that FHA delay introduction of a 40-year modification until after the 1st quarter of 2022 and provide an adequate implementation timeframe of at least 90 days.

¹ The Housing Policy Council is a trade association comprised of the leading national mortgage lenders and servicers, mortgage and title insurers, and technology and data companies. HPC advocates for the mortgage and housing marketplace interests of its members in legislative, regulatory, and judicial forums. Our interest is in the safety and soundness of the housing finance system, the equitable and consistent regulatory treatment of all market participants, and the promotion of lending practices that create sustainable homeownership opportunities in support of vibrant communities and long-term wealth-building for families.

² 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 to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,300 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.mba.org

³ Servicers have been called upon to dedicate resources to high-intensity process and technology updates and personnel training to effect these changes as quickly as possible. This resource-intensive work will continue throughout the last quarter of 2021 and early 2022. Servicers are already fully occupied, negotiating workouts for the high volume of forbearance expirations, implementing the FHA Advance Loan Modification (ALM) and other COVID program changes, executing the VA partial claim program, and building out the infrastructure required for the state Homeowner Assistance Fund (HAF) programs.

As you know, our members have been generally supportive of FHA's idea to implement a 40-year modification for some borrowers, due to the additional relief it could offer households with exceptional financial difficulties. Of note, this type of program could be part of FHA's permanent suite of loss mitigation options, available for those borrowers who redefault after a previous modification, due to new occurrences of economic hardship. In fact, we would like to suggest that FHA take the time necessary to carefully construct a permanent 40-year modification program, with a comprehensive and disciplined assessment of the full array of financial implications for borrowers, industry, FHA, and Ginnie Mae.

We make this suggestion because many of the program features included in the FHA proposal will have a negative impact on borrowers. The use of a 40-year term extension, rather than a shorter-term modification combined with a non-interest-bearing second lien, to achieve monthly payment reduction, will cost the borrower more over the life of the loan and delay the accumulation of equity in the property. This latter drawback is of particular concern to HPC and MBA members, given that wealth-building is generally considered to be the greatest benefit of homeownership. In this letter, we suggest changes to minimize these adverse effects.

Of equal concern, for a 40-year modification program to be successful, the market for these loans must be transparent and liquid. Given that no market for 40-year modifications exists today, the proposal should address this deficiency prior to launch. It is critical to eliminate uncertainty and capital market risk related to introducing a new financial instrument before the program is implemented. We offer suggestions to overcome these obstacles as well.

Our comments address the following issues:

- *Partial Claim Requirement:* We do not believe that the statutory authority to offer a modification with a term of up to 40-years stipulates that a modification must be offered in conjunction with a partial claim. Rather, the authority to offer a modification is separate from the partial claim authority and a partial claim *may* be combined with a modification but is not obligatory.
- *Pre-Existing Partial Claim:* If FHA determines that it is in the agency's interest to mandate the combination of a 40-year modification with a partial claim, FHA should consider permitting a pre-existing partial claim to satisfy the requirement.
- *Incremental Adjustment from 30-Year to 40-Year Modification Term:* Under the proposal, the servicer would determine whether a 25 percent reduction in the borrower's principal and interest payment could be achieved with a 30-year modification, with arrearages covered by a partial claim/second lien. If not, the servicer would recalculate using a 40-year term. We recommend that FHA allow the mortgage term to be extended incrementally to achieve the targeted payment reduction, rather than requiring the full 40-year term.

- *Preferable Treatment of 40-Year Mod / 30-Year Mod Limitations:* The proposed restriction on the use of the partial claim/second lien to cover only arrearages and not additional principal, to achieve the 25 percent payment reduction with the 30-year modification will drive more borrowers into the 40-year modification. This will be more costly for the homeowner and will delay the accumulation of equity.
- *Ginnie Mae Pooling:* Ginnie Mae recently announced plans to create a new pool type to support the securitization of modified mortgages with terms up to 40 years.⁴ We understand that these pools will be custom/non-TBA eligible, single issuer pools with a minimum pool size of \$25,000. The pools will be exclusive to modified mortgages with terms between 361 months and 480-months to accommodate FHA, VA, and USDA mortgages that may have terms between 360 and 480 months. We have concerns that, without additional action by FHA and Ginnie Mae, the new pools will be subject to substantial variance in pricing across issuers and face liquidity constraints that could be harmful to the FHA program and the government-backed servicing segment. To avoid inadvertent harm, we urge FHA to provide servicers additional flexibilities in setting the interest rates for the 40-year modifications.
- *Modification Interest Rate:* The rate spreads for the 40-year modification must be informed by the demands of the secondary market, and we believe that the rate spreads proposed may not be representative of yield requirements for the new, unveiled and untested, Ginnie Mae pools. For this reason, we would prefer that FHA obtain market feedback on the appropriate pricing for 40-year Ginnie Mae pools before setting a maximum interest rate. If FHA determines that a maximum rate must be set now, we recommend basing the rate on PMMS and permitting spreads of up to 50 basis points (bps) to align with existing operational workflows as well as with Veterans Administration (VA) and U.S. Department of Agriculture's Rural Development (USDA/RD) modification programs.

Recommendations:

Eliminate FHA Requirement for the Contemporaneous Partial Claim

The sections of the National Housing Act that provide for FHA's loss mitigation authorities [12 U.S.C. 1710 and 1715(u)] acknowledge that FHA may establish programs that serve as an alternative to foreclosure and permit FHA to design program features and parameters that satisfy the policy objective. Section 1710 does not stipulate the term permitted for loan modifications and Section 1715(u) allows for a maximum modification term of 40-years but does not explicitly state that a loan modification with a 40-year term must be simultaneously accompanied by a partial claim. In fact, this section of the National Housing Act seems to state only that a partial claim may be offered in conjunction with a loan modification. The attached legal review of the statute and regulations (Addendum 1) presents an

⁴ <https://www.ginniemae.gov/newsroom/Pages/PressReleaseDispPage.aspx?ParamID=209>

interpretation of the relevant sections of the National Housing Act, to make the case that FHA is not required to combine the 40-year loan modification with the partial claim. Given that there is not statutory bar to offering a 40-year modification without a partial claim, FHA need only waive the existing regulation to introduce this program.

Of primary concern, the requirement to combine the 40-year loan modification with a new partial claim will render some customers ineligible. In fact, this segment of borrowers may be most in need of the payment relief afforded by a 40-year modification option. Therefore, as stated above, we believe FHA has the discretion to implement a 40-year modification without the concurrent use of a partial claim and that FHA's proposal would be more effective if this requirement were removed from the proposal.

If Combination Required, Permit Pre-existing Partial Claims to Satisfy Requirement

If FHA determines that the agency benefits from binding the 40-year modification to a partial claim, despite the agency's statutory discretion under Sections 1710 and 1715u, we suggest that FHA consider accepting pre-existing partial claims to satisfy the requirement. With this approach, borrowers previously assisted by a partial claim who have exhausted the maximum available could receive the benefit of the longer-term modification without an additional subordinate lien.

It should be noted that some borrowers whose pre-existing partial claim accounted for either the statutory 30 percent maximum or the 25 percent cap announced under Mortgagee Letter 21-18, would not be eligible for the 40-year modification unless FHA were to accept the pre-existing partial claim to satisfy the requirement. Since borrowers who have defaulted on their payments multiple times are some of the most likely to benefit from the lower payments associated with the 40-year modification, denying them access to the 40-year modification would be an unfortunate policy outcome.

Allow Incremental Adjustment to Modification Term

While the proposed term extension to 40 years will reduce the borrower's monthly payment, there are negative consequences that some borrowers may want to avoid. Specifically, a 40-year loan product significantly slows the pace of equity accumulation and will result in larger interest expense over the life of the loan (see Addendum 2). To avoid or minimize this impact, FHA should allow for incremental extension of the term, calculated to achieve the target payment reduction.

Reconsider New Limitations on 30-Year COVID Recovery Modification

The existing 30-year COVID Recovery Modification utilizes the partial claim to cover both arrearages and some amount of the outstanding principal balance, if necessary, to achieve the target payment reduction of 25 percent. Most borrowers with extended forbearance can achieve the target payment reduction with these program features. Yet, for the 30-year COVID Recovery Mod, the proposal eliminates the use of the partial claim to defer principal and allows

only arrearages to be covered by the partial claim. This change will result in more borrowers receiving a 40-year modification to achieve the 25 percent payment reduction -- an outcome that will be more expensive and less advantageous from a wealth-building perspective (See Addendum 2), for most borrowers in COVID forbearance.

Further, we are concerned that this shift in the program availability will create communication issues and borrower confusion. For months now, servicers have repeatedly communicated the suite of loss mitigation options available to them upon forbearance exit. Significant changes in these options will result in increased consumer complaints and avoidable borrower confusion.

Assess Impact of Ginnie Mae Pooling Parameters

A market for 40-year single family MBS does not exist currently, which makes it nearly impossible for servicers to determine with certainty the interest rate spreads for 40-year modifications that will not result in losses.

The 40-year loan modifications performed under GSE programs are held on the government-sponsored enterprise (GSE) balance sheets. Hence, the rates associated with those modifications cannot be relied on to illustrate the requirements from MBS investors to price the new Ginnie Mae 40-year pools at par or higher. FHA and FHA servicers must have a reliable, consistent market for the delivery of 40-year loans in order for this option to succeed. Our initial inquiries indicate that pricing for these theoretical pools would be anything but certain at this point.

The pricing for the new custom pools will be specific to each pool and influenced by factors that are known in their totality only after the modification rate is set. These factors can include: the characteristics of the mortgages in the pool, including the mix of VA/USDA/FHA loans in the pool and average terms; the total pool size; the identity of the issuer; the experience with or expectation regarding the coupon prepay rate of these new pools for that specific investor; and whether FHA 40-year mortgages will continue to be originated past the end date of the COVID loss mitigation options. Ginnie Mae's own press announcement acknowledges that the pricing for the pools will be individualized and subjective.⁵ Moreover, the industry does not have the full suite of parameters governing Ginnie Mae's 40-year pools because the program has not been announced or implemented in an official manner.

Servicers cannot fully opine on FHA's program recommendation with so much uncertainty regarding the companion program from Ginnie Mae. To provide industry necessary assurances of the pricing and liquidity of the 40-year modifications, we request that FHA: 1) provide servicers with additional flexibilities in setting the applicable interest rate, as detailed below, and 2) work with Ginnie Mae to fully disclose the 40-year MBS program and the findings from any investor feedback obtained to date prior to adopting the 40-year option into its

⁵ Acknowledging that "pool content and related issuer" will be the drivers of market value for these new pools.

waterfall. This would allow servicers the opportunity to provide further comment to FHA's proposal - only after fully digesting the Ginnie Mae program requirements.

Delay Setting Cap on Modification Interest Rate

The FHA proposal requires the servicer to use the Freddie Mac modification rate, rounded to the nearest one-eighth of a point, with an additional margin of 25 bps. One problem with this approach is that the Freddie Mac (and Fannie Mae) modification rate methodology is not updated routinely and is not based on market fundamentals because the GSE modifications are not delivered back into the market. It is our understanding that the GSEs calculate a four-week average of the PMMS, compare it to the PMMS at that point in time, then add one-eighth of a point in cases where the PMMS is higher than the average, to ensure that the modification rate is greater than the PMMS. The fact that this index is updated infrequently (only four updates in calendar year 2020), irregularly, and manually makes it less appropriate for a program with market execution considerations. Further, the margin is inconsistent with the USDA and VA 40-year modification programs, which allow for a 50 bps spread to be added to the index.

HPC and MBA recommend that FHA work with issuers and investors to obtain market feedback on the appropriate pricing for 40-year Ginnie Mae pools before setting a maximum interest rate. However, if FHA determines that it must set a maximum now, it should be commensurate with the VA and USDA programs, given that these loans are intended to be pooled together in the new Ginnie Mae MBS, designed specifically for these products. VA reiterated that it permits a spread of 50 bps in their July 2021 Circular 26-21-13⁶ and USDA stipulates that an additional 50 bps is permitted unless the agency publishes a Federal Register notice that sets other rules. The USDA's most recent COVID-19 Loss Mitigation guidance affirms this policy.⁷

This approach is likely not sufficient, however. As noted above, the bigger problem here is that the reference rate proposed by FHA is not established with the deliberate advice of capital market implications and MBS investor appetite. The rate on 40-year loan modifications performed under GSE programs is set without regard to immediate liquidity. The 40-year GSE loans are not sold on the open market, so pricing is not a guiding force behind the interest rate offered on the modifications. While this may work for Fannie Mae and Freddie Mac, who retain the modifications and do not deliver them into the capital markets, this is not the recipe for a sustainable market for this new Ginnie Mae MBS, which will impact hundreds of servicers and thousands of consumers in the coming months.

⁶ Veterans Benefits Administration Circular 26-21-13 Department of Veterans Affairs July 23, 2021 Washington, DC 20420 COVID-19 Home Retention Waterfall and COVID-19 Refund Modification, https://www.benefits.va.gov/HOMELOANS/documents/circulars/26_21_13.pdf.

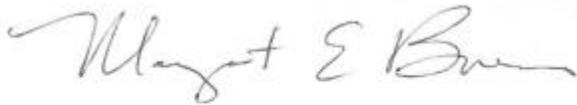
⁷ USDA job aid, COVID-19 Special Relief Measures; <https://www.rd.usda.gov/resources/usda-linc-training-resource-library/loan-servicing>.

FHA and Ginnie Mae should be engaging with investors on the appropriate interest rate for 40-year modifications before deciding on an arbitrary rate that could have, if not carefully considered, a reverberating impact on FHA servicers and the FHA program. Market discipline must dictate the interest rate to minimize secondary marketing risk.

Conclusion:

Our organizations have been generally supportive of the addition of a 40-year loan modification to the suite of loss mitigation programs offered by FHA. To ensure this modification option is successful for borrowers and servicers alike, this letter sets forth our recommendations to address concerns with (1) the timing of the introduction of this program, (2) the proposed program rules and uncertainties, and (3) the potential negative consequences for FHA customers. We would welcome the opportunity to discuss these issues with you. Should you have any questions or an interest in meeting with us, please do not hesitate to contact Matt Douglas, HPC VP for Mortgage Policy at 202-589-1924 and Sara Singhas, MBA Director of Loan Servicing at 202-557-2826.

Sincerely,



Meg Burns
Executive Vice President
Housing Policy Council



Pete Mills,
Senior Vice President
Residential Policy and Member Services
Mortgage Bankers Association

Review of Relevant Sections of the National Housing Act

The National Housing Act should be interpreted to permit HUD to insure an FHA loan that has been modified to extend the term of the mortgage to 40 years from the date of the modification, regardless of whether such modification is accompanied by a partial claim.

As an initial matter, we recognize that HUD's statutory authority to insure a mortgage under the FHA program is limited to a 30-year mortgage. See 12 U.S.C. § 1709(b)(3). That limitation, however, presumably applies only to the mortgage term at the time of initial endorsement for insurance. The National Housing Act provides HUD with separate statutory authority to modify insured mortgages, and that authority broadly references the ability to provide loan modification, without any limitation on the term of a modified mortgage. See 121 U.S.C. § 1715u(a).

In implementing this authority, HUD's existing regulations authorize the modification of FHA-insured loans to a term not to exceed 30 years from the time of the modification. See 24 C.F.R. § 203.616. This language demonstrates that the cumulative term of a modified mortgage may exceed 30 years from the date of FHA insurance endorsement. For example, if a borrower defaulted in the third year of a loan and received an approved modification with a new 30-year term, the cumulative term of the loan would be 33 years. HUD would have no authority to permit such a change if the cumulative term upon modification cannot exceed 30 years from the FHA insurance endorsement date. Indeed, if the 30-year limitation applied to both the initial and modified loan terms, no modified mortgage could have an extended term, unless it were modified on the day it was made, which would produce an absurd result. Section 1710 of the National Housing Act supports this interpretation, as that provision of the statute authorizes HUD to establish terms and conditions upon which a mortgagee can provide for a modification of the terms of the loan over the remaining term of the mortgage or over a longer period of time set forth by guidelines prescribed by HUD. See 12 U.S.C. § 1710(a)(6)(B). This provision does not set forth any limitation to the time period by which HUD can authorize servicers to extend a loan term via such modification.

Additionally, Congress itself acknowledged, through its amendments to the National Housing Act through the Helping Families Save their Homes Act ("HFSHA"), that HUD has the authority to modify a loan for a term that exceeds 30 years from the FHA insurance endorsement date. Specifically, the provisions of that legislation gave HUD the authority to extend a modification term to 40 years under certain circumstances.

While we agree with HUD's interpretation that the statutory authority provided to HUD under the HFSHA provides HUD the authority to, through the issuance of a Mortgage Letter, establish a 40-year Loan Modification in combination with a Partial Claim, we do not think this provision limits HUD's authority to providing a 40-year modification only in combination with a

Partial Claim. The National Housing Act, as amended by the HFSHA, gives HUD broad authority to exercise its discretion to develop a partial claim program subject to certain explicit limitations on the exercise of this discretion. One limitation is that any loan modification offered in connection with a partial claim may not have a term in excess of 40 years. The reference to a 40-year modification is not an explicit authorization to enter into 40-year modifications generally, but rather is a limitation of HUD discretion to set the terms of a partial claim program. Thus, provided that HUD offers the 40-year loan modification as part of a partial claim program, the modification would fit within the National Housing Act's existing authority, even if such loan modification were offered as a "stand-alone" option within that program – much like the stand-alone modification available in the existing loss mitigation waterfall.

In the alternative, HUD has authority to waive the 30-year term limit for FHA loan modifications currently set forth in Section 203.616 of the applicable FHA regulations based on the COVID-19 national emergency, much like it did in connection with the regulation regarding the face-to-face interview requirement for delinquent borrowers set forth in Section 203.604. Waiving the regulatory limitation of a 30-year modification term also would further HUD's mission to minimize losses to the Mutual Mortgage Insurance Fund ("MMIF") (see 12 USC §§ 1708(a)(3), 1709(r)) and the operational goal of the MMIF to meet the housing needs of the borrowers that the program is designed to reach (see id. § 1708(a)(7)(B)).

Addendum 2

Concerns with Customer Impact

There is a concern that many customers who do not meet the FHA-mandated 25% payment reduction will not want to extend their mortgage to 40 years. While the 40-year term comes at the end of the FHA COVID-19 Relief Waterfall where some consumers may not meet the 25% payment reduction target without extending the term to 480 months, this will likely impact complaints and the overall customer experience.

Additionally, although the FHA COVID-19 loss mitigation waterfall that includes a 40-year amortization loan that would lower the consumer's monthly payment, a 40-year term loan would be significantly more costly to the consumer over the life of the loan. Below is an example of the amount of interest and MI payable by a consumer with a 40-year term loan compared to a borrower with a 30-year term loan for the same amount and at the same interest rate. The consumer with the 40-year term loan would pay \$62,294 more over the life of the loan.

30 year - Market Rate		Loan Summary		
Loan amount	225,000	Scheduled payment	\$ 979.21	
Interest Rate	3.250%	Scheduled number of payments	360	
Loan period in years	30	Actual number of payments	360	
Total Debt	260,550	Total interest	\$ 127,517	
		Total MIP 1%	\$ 67,500	*This is based on one leading servicer's historical average of how much partial claim is used in the typical modification/partial claim combination
		Principal paid (1st 3 years)	\$ 13,965	
		Combo PC - 15.8%*	35,550	
40 year - at 30 year Rate plus .25%		Loan Summary		Additional Costs for Life of Loan
Loan amount**	204,300	Scheduled payment	\$ 791.44	Increase in Interest \$ 48,074
Interest rate	3.500%	Scheduled number of payments	480	Increase in MIP \$ 14,220
Loan period in years	40	Actual number of payments	480	Loss of equity - 1st 3 years \$ 6,553
Total Debt	260,550	Total interest	\$ 175,591	Recapture of Equity takes an additional 82 months
		Total MIP 1%	\$ 81,720	Increase in Partial Claim Second \$ 20,700
		Principal paid (1st 3 years)	\$ 7,412	offset by UPB
**UPB \$225k less additional Partial Claim		Combo PC - 25%	56,250	