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Regulations Division  
Office of General Counsel  
Department of Housing and Urban Development  
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Room 10276  
Washington, DC 20410-0500

Reducing Regulatory Burden: Enforcing the Regulatory Reform Agenda under Executive Order 13777; **Docket Number HUD-2017-0029**

To the Office of General Counsel:

Thank you for the opportunity to respond to the Department of Housing and Urban Development's request for input on HUD regulations that may be outdated, ineffective or excessively burdensome. This request follows from the review directed by Executive Order 13777. The Housing Policy Council, a division of the Financial Services Roundtable, is pleased to provide suggestions focused on FHA regulations and policies that today hinder broad participation by mortgage lenders and servicers in this important federal program.

The member institutions of the Housing Policy Council are among the largest providers of housing finance. Many of our member firms have long-standing histories of active participation in the FHA single-family program, and they desire to continue that tradition. Regrettably, lack of clarity with post-financial crisis rules and recent program interpretations, combined with a new regime of enforcement activities have greatly altered the costs and uncertainties in originating and servicing FHA loans. The result is that many quality lenders, including HPC members have limited their participation in the FHA program. This, in turn, harms the program's intended beneficiaries – the low and moderate-income families and first-time homebuyers who find it increasingly difficult to finance a home purchase. It also increases, rather than decreases, the financial risk the program presents to American taxpayers.

As the new leadership team at HUD and across the new Administration undertakes its evaluation of the FHA program, we commit to providing constructive feedback and suggestions to make this program work more efficiently and effectively so that borrowers are served and taxpayers are protected. A common denominator to our comments in this letter is that the heavily prescribed - yet ambiguous - framework that marks the FHA program today needs to be simplified, clarified and balanced.

Simplification of FHA origination and servicing requirements will lower costs and improve loan quality, which will broaden the number and range of lenders and servicers competing in this market for customers.

Clarifications to loan certifications and various default servicing rules will reduce lender and servicer uncertainty that result in overlays and other self-imposed protections that limit borrower access.

And balance in the enforcement approach will restore a business prudence to rules, penalties and enforcement actions that align inevitable imperfections in lending and servicing with penalties and remedies commensurate with harm and intent.

FHA program rules need to protect borrowers and the MMI fund. At the same time, we do not want to continue seeing quality lenders and servicers shy away from participating in this program because of the enormous burdens and uncertainties extant in today's environment.

Beyond administrative reforms, to the extent HUD finds that prudent changes and modernization of the FHA program requires statutory change, we urge HUD to include such changes in the Administration's overall commitment to seek comprehensive housing finance reform. Indeed, since FHA lending does not occur in a vacuum but rather in a larger, competitive housing finance system currently dominated by two GSEs in federal conservatorships, it is hard to conceive how lawmakers can address one part of this market without also addressing the other. As just one example, FHA competes with private mortgage insurers and other capital providers. So, as we applaud and support the new Administration's commitment to housing finance reform, that initiative also presents an opportunity to define the role and responsibility of the FHA program in our housing finance ecosystem and an opportunity to ensure FHA and Ginnie Mae have the resources and mandate to fulfill their public mission in the years ahead. We look forward to working with the Administration, the Department and the FHA to review those issues.

### **Recommended regulatory changes that are high priority and on which immediate HUD action can begin**

- a. Address and resolve the many certification issues remaining at the FHA.

All FHA stakeholders – government and private – need to have a common understanding of what is a good loan versus a bad loan. HUD must ensure that any attestations by lenders are consistent with a comprehensive quality management system. FHA's loan level certifications are a component of this by allowing lenders to attest to their systems for identifying errors and that their level of loan quality meets the standard agreed to by all parties. Unless FHA, lenders, HUD-OIG and the Department of Justice find consensus in a single interpretation of loan quality, the barriers limiting program access will persist.

As a result of the legal risk arising from certifications, many major banks have either exited entirely from, or reduced dramatically, their participation in FHA programs. To the extent they continue to participate, many lenders have added credit overlays to the loans, which reduces the universe of loans made. Non-bank lenders and servicers have assumed a much larger share of FHA lending but require greater monitoring by Ginnie Mae and FHA because of the absence of prudential

federal supervision from bank regulators. The recent Ginnie Mae President repeatedly noted this fact as a key risk because Ginnie Mae lacks the resources to perform this oversight.

In order to encourage traditional lenders to reenter the market in a way consistent with the FHA mission and to give all lenders more confidence in the FHA review process, these issues should be addressed and resolved. We encourage the Department to review the detailed recommendations on certifications made by the Mortgage Bankers Association in its submission to the Department.

b. Create certainty in FHA Defect Taxonomy to reduce unreasonable litigation risk under the False Claims Act.

FHA has published a defect taxonomy called the FHA's Single Family Housing Loan Quality Assessment Methodology, which attempts to describe the standards for accepting or rejecting a loan for FHA insurance. That taxonomy divides loans into four levels of severity from one (the most severe) to four (the least severe). FHA will accept insurance claims from a lender for loans in severity four, even if the loans have defects. However, no safe-harbor is provided at any severity level, and the taxonomy is incredibly subjective. As a result, the taxonomy has not been successful in providing the certainty needed to encourage traditional single-family residential lenders to return to the FHA market.

To provide such certainty and improve economic growth by increasing the number of regulated banks making FHA loans, FHA should promulgate a rule that clearly states loans classified in severity tier four of the FHA Loan Quality Assessment Methodology will be acceptable to the agency and that insurance claims against FHA may be made against such loans. The rule also should state loans in severity tier three will be acceptable to the FHA, if the errors are cured so as to meet FHA approval limits and loan guidelines.

Additionally, in cases under the False Claims Act, DOJ should adopt a policy indicating, a finding of "materiality" generally will not be made if the agency responsible has concluded the actions of the party are acceptable, notwithstanding minor or *de minimis* mistakes or errors. Such a policy would reduce litigation risk associated with FHA lending.

It is also important to understand that changes to certifications and the defect taxonomy are necessary, but not fully comprehensive, to achieve the broader goals of quality management at FHA. Most of these are contained in HUD's own Blueprint for Access to Credit, which was published in 2014 but to date has not been fully implemented.

c. Loan servicing

FHA also needs to address the servicing of loans. The cost to service mortgage loans has increased dramatically since the housing crisis, particularly for non-performing loans. The cost to service a seriously delinquent loan (over 90 days delinquent) tends to exceed income, regardless of investor type. The loss is nearly twice as large for a seriously delinquent FHA loan as for a similarly delinquent GSE loan. This is caused primarily by FHA's unnecessarily complicated and confusing rules and the fact that their default servicing toolkit is inadequate to keep people in their homes. Specifically, FHA should:

1. Expand loan modification options beyond simply lowering borrower rates to the current market rate;

2. Overhaul foreclosure timelines including development of a unified timeline for default servicing and
3. Implement a direct conveyance process for foreclosed properties.

d. Information technology at FHA is outmoded

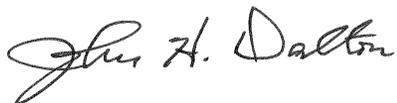
While it is not specifically a regulatory burden, the outmoded information systems and technology at FHA is certainly a major burden hampering the FHA program. It is crucial that FHA have modern information technology as an integrated part of its system.

e. Ginnie Mae

While our comments have focused on FHA, Ginnie Mae is a critical business partner to our members in the actual financing of FHA mortgages. The platform under which Ginnie Mae operates needs general review and modernization. It must be able to support a very large volume of securities and must do so with the best processes available. Currently the platform cannot support loan level considerations but rather is limited to pool level. That should be changed. Ginnie Mae should also provide updated guidance on title insurance for modified loans, and it should refrain from making retroactive changes to custodial requirements, such as those made in the custody area that covers unrecorded modifications. It should recognize that the improvements it has made in the Acknowledgement Agreement is still incomplete and must continue to work on improving it.

We appreciate the Department's interest in obtaining obtain public input on the question of regulatory burden. The recommendations in this letter are intended to contribute to reforms that would reduce such burden, lead to more efficient markets and create new job opportunities as the chill currently enveloping the FHA market would thaw. The HPC is eager to work with the Department on these issues so that together we may serve homebuyers more effectively and efficiently.

With best wishes,



John Dalton  
President  
Housing Policy Council  
The Financial Services Roundtable

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