June 21, 2022

Ms. Luvenia Potts
Regulations Development Coordinator
Office of Regulation Policy & Management
Office of General Counsel
Department of Veterans Affairs
810 Vermont Ave NW
Washington, DC 20420
Submitted via e-mail to: http://www.regulations.gov

Re: Docket No.: VA-2022-VBA-0013, AR42-ANPRM-Loan Guaranty: Servicer Tier Ranking Procedures

Dear Ms. Potts,

The Mortgage Bankers Association (MBA)[1] and Housing Policy Council (HPC)[2] appreciate the opportunity to comment on the Department of Veteran's Affairs (VA) Advance Notice of Proposed Rulemaking (ANPR) requesting assistance to develop a servicer tier ranking procedure (a.k.a., "scorecard"). We support the concept of a servicer tier ranking process but offer several recommendations for the VA to consider.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 390,000 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 more than 2,100 companies includes all elements of real estate finance: independent mortgage banks, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies, credit unions, and others in the mortgage lending field. For additional information, visit MBA's website: www.mba.org.

[2] 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. For more information, visit www.housingpolicycouncil.org

Our comments address the specific questions and topics requested in the ANPR, and we propose edits to 38 CFR § 36.4318 to illustrate the changes that we recommend. Our feedback is based on the core principles that the scorecard should be simple and actionable, aligned with other agency scorecards and sustainable prior to the effective date.

In summary, we respectfully request a VA a tier ranking procedure that:

1. Does not compare participating servicers based on portfolio volume or composition;
2. Establishes objective metrics for evaluating a servicer's execution of VA's default servicing policy and data quality standards;
3. Implements performance metrics and methodology consistent with those of the Federal Housing Administration (FHA) and Government-Sponsored Enterprises (GSE's);
4. Tests the methodology with a pilot program, allowing servicer feedback on the procedures prior to final implementation;
5. Reflects, and expands as necessary, the VA's operational capacity to analyze complex data and timely communicate evaluation results to participating servicer's; and
6. Proceeds with final rulemaking after the COVID-19 National Emergency has expired.

A Performance-Based Tier Ranking Procedure Should be Simple, Actionable and Align with GSE and FHA Scorecards

To begin, a fundamental component of a successful tier ranking procedure is to ensure that servicers easily understand how their performance is being evaluated. The metrics themselves need to be simple, clear, well-defined for participants to understand, and measure a servicer's ability to implement VA's default servicing policy. We believe VA should consider the best practices of both the FHA and GSE scorecards that evaluates each servicer based on quality of service provided to Veteran homeowners over the course of the default cycle.

Implementing a simple performance-based tier ranking procedure has several benefits, including that it appropriately rewards the best performers with the highest level of incentives for completing successful loss mitigation actions as required by 38 CFR § 36.4319. A successful tier ranking procedure also provides a clear roadmap for the necessary steps servicers will need to take to improve performance and, subsequently, their respective tier ranking.

Accordingly, the VA should consider the following recommendations:

1. <u>Portfolio Composition.</u> A servicer's portfolio composition inherently varies due to origination credit risk or portfolio acquisition strategy and will inherently favor certain business models over others. For example, servicer performance could be affected by composition based on geographic concentration; location may impact likelihood of default, based on housing price volatility or regional employment or natural disaster trends. In short, though the VA should remain aware of how portfolio composition could potentially skew results, the VA should adopt a tier ranking system that evaluates the performance of each servicer and does not establish a peer comparison based on portfolio composition.

2. Performance Methodology. A successful tier ranking process should provide clarity to servicers about how to improve their performance. We suggest that VA adopt a scoring model like FHA's Tier Ranking System II. There are three components in the FHA Tier Ranking System that the VA should consider:

    I. *Monthly ratios and thresholds*. A scoring model should utilize metrics based on simple ratios and calculations. This clearly communicates a numeric score to servicers that is easily understood, sets clear expectations for measuring performance, and identifies opportunities for improvement month over month.
    II. *Quarterly Average*. Each monthly score per metric should be averaged per quarter, not aggregated as mentioned in the ANPR. Like the above metric, an average is an accurate reflection of how well a servicer performed their loss mitigation servicing responsibilities.
    III. *Annual Tier Ranking.* After averaging each metric each quarter, all quarter scores should be averaged for the year to establish a tier ranking. A servicer that achieves a 90% or above is Tier 1; 80% - 89% is Tier 2; 60% - 79% is Tier 3; anything less than or equal to 59% is Tier 4 and ineligible for incentives.

3. Performance Metrics. The VA should adopt, where appropriate, similar loss mitigation metrics utilized by FHA and the GSEs. This approach builds upon data that is already readily available through VALERI.

    Our members find that a significant benefit of the GSE servicer ranking system is that there are simple calculations and definitions of each metric scored that provide clear guidance to servicers on how performance is measured. Notably, the GSEs use, and we would recommend that the VA consider adopting, a data quality standard as an appropriate measurement of servicer performance, as quality data is a core component of the VALERI system and would otherwise inhibit VA from providing a tier ranking to servicers. Based on our evaluations of both the GSE and FHA servicer ranking systems, we believe that a final VA tier ranking procedure should consider evaluating the following metrics:

    a. Potential Metrics:

    i. *Foreclosure Timeline Management.* Measures how well servicers manage the foreclosure timeline during the reporting period;
    ii. *Transition to 120+*. Like a roll rate, this metric could identify loans that transition from 60 days delinquent to 120 days delinquent[3];
    iii. *60+ to Cure.* Measures how many loans that were in default that reported the Electronic Default Notice (EDN) and have since cured in a given reporting period. This appropriately measures how well servicers engaged delinquent veteran borrowers early in their delinquency;
    iv. *Redefault Rate.* Like FHA and the GSEs, a redefault rate measures the modification performance after 6 months;

[3] The VA defines a consumer in "default" after a delinquency of 60 days. Additionally, the VA's Adequacy of Servicing is triggered at 120 days of delinquency.

v. *Default Resolution Rate.* Measures the percentage of VA-guaranteed loans that are successfully resolved via a loss mitigation option; and

vi. *Data Quality.* VA should establish a definition for the accuracy and integrity of the data provided, similar to the GSEs, to support the measurement of ongoing compliance with 38 CFR § 36.4317

b. Considerations:

vii. *Default Rate.* Similar to the FHA and GSE systems, a VA tier ranking system should not include a general default rate or delinquency rate when evaluating performance. A default rate metric is directly tied to origination credit risk and portfolio composition more so than it is associated with servicer performance throughout the default cycle. As the COVID-19 pandemic has shown, a default rate can drastically shift for a servicer and the industry based on external factors beyond the servicer's control. The focus of the tier ranking system should be on the quality of the work provided by servicers.

viii. *Challenges of a Hybrid Approach.* We recognize that implementing a scorecard that adopts elements from both FHA and the GSEs will be challenging as each has a model and features specific to each program that will need further consideration once a regulation is proposed. For example, servicers will need to consider the weight that should be given to each metric for the monthly, quarterly, and annual scores. Servicers will also need to consider the benchmarks of each metric to grade a servicers performance. Nonetheless, we believe the VA should implement a tier ranking procedure that is a simple evaluation of an individual servicer's quality of service.

ix. *VA Loss Mitigation Waterfall.* We also recognize that VA has a standard set of loss mitigation options available, as opposed to a prescribed waterfall. As a result of business model, not all servicers consistently offer all options available. We believe VA should strongly consider this fact when developing a tier ranking procedure and structure.

VA Implementation Should Ensure a Sustainable Tier Ranking Procedure Prior to the Effective Date

As the VA begins to consider the next steps in developing a proposed rule, we believe it is important to ensure that the scorecard is sustainable for the VA and servicers We believe one of VA's goals in finalizing a tier ranking procedure should be to facilitate an iterative process that sets up all parties for success. A proposed regulation should provide certainty to servicers on how they should expect their performance to be evaluated but be broad and flexible enough to adjust to future market conditions as needed.

To ensure the VA's tier ranking procedure sustainably measures performance, we recommend the VA address the following issues:

4. Effective Date. MBA and HPC believe that VA should not proceed to proposing the regulation to implement a VA scorecard until the COVID-19 National Emergency has passed and we have a more settled regulatory environment.

   Although COVID forbearance levels have generally declined to pre-pandemic levels, servicers continue to assist affected consumers. This work continues to evolve. For example, servicers continue to work with 50+ states, territories, and federally recognized tribes to implement the Homeowners Assistance Fund. Servicers must also contend with the uncertainty that a VA COVID forbearance may or may not be extended past September 30, 2022[4].

   Executing the servicer tier ranking system after the COVID-19 National Emergency would avoid introduction during a period of uncertainty, when rapid rises in defaults and the extended workout options that resulted from the CARES Act and subsequent policy changes are not measured against a servicers performance without first understanding the framework which they will be measured. In fact, once in effect, similar to what FHA and the GSEs have done, the VA tier ranking should build in appropriate flexibility to account for things like natural disasters or COVID workout options in any metrics proposed to ensure an accurate measurement of a servicer's performance.

5. Pilot Program. In Question 4 of the ANPR, VA is proposing to test *certain* aspects of the TRS internally with live servicer reported data and release certain information on a quarterly basis to servicers. We strongly support visibility into how the VA is internally testing live-data. However, currently, there is insufficient information available in the ANPR to provide a complete response. For example, we don't know *which* aspects will be measured in a live testing environment.

   Given the importance of the new scorecard, we request that VA consider implementing a pilot program that allows for servicer feedback, prior to finalizing the tier ranking system. VA and servicers would benefit from an opportunity to assess whether the metrics provide a fair analysis representative of a servicer's performance, whether the metrics are weighted appropriately, and how accurately the VALERI data measures performance. Likewise, a pilot program would allow VA to determine the resources and capacity required to manage the scorecard, communicate results timely, and respond to any appeals from servicers.

   At this stage without knowing the specific details of a tier ranking procedure, it is difficult to provide an accurate reflection of the operational burden and potential costs it will place on servicers. A pilot program will provide an opportunity to provide that feedback. As a general matter, the greatest burden in operationalizing a tier ranking system will be the technology aspects. An iterative process will allow servicers and the VA to ensure that the appropriate data is included and reported in a manner that enables a proper tier system. Additionally, servicers will create their own internal reviews, likely calculators, that will reverse engineer their own performance forecast what the expected final VA tier ranking score should be. The

[4] VA Circular 26-21-20 provides that a veteran may request a VA COVID forbearance through the National Emergency. However, the Circular will rescind on October 1, 2022, on VA's expectation that COVID forbearances will end not later than September 30, 2022.

more complex the data and scoring models, the more extensive the internal calculations will be, and the more time consuming and costly the implementation will be for all parties.

We believe, therefore, that a pilot program is appropriate for at least 12 months or 4 full quarters prior to receiving the first annual tier ranking.

6. Ensure Operational Capacity. The VA must have the resources and operational capacity to seamlessly execute the new system. Currently, 38 CFR § 36.4318 requires the VA to evaluate a servicer's performance within 30 days of a quarter's end and advise a servicer of the outcome within 45 days of the last quarter-end. We believe the VA should retain these timeline commitments. Timely evaluation and communication enable servicers to take actions to improve performance, if necessary.

   Because VALERI will be analyzing a considerable amount of data within a short amount of time, we support an assessment of VA's operational capacity including, as identified in Question 5, an error review process for monthly, quarterly, or annual scores. Servicers should be given at least 30 days to identify and appeal, with the necessary supporting documentation, any inaccurate scores, based on incomplete or inaccurate data. VALERI must have the functionality to adjust the data retroactively, if necessary.

Thank you in advance for your consideration of these comments. Should you have any questions or wish to discuss further, please contact Brendan Kelleher at (202) 557-2779 and bkelleher@mba.org, or Matthew Douglas at (202) 589-1924 and Matt.Douglas@housingpolicycouncil.org.

Sincerely,

Mortgage Bankers Association
Housing Policy Council

RESPONSES TO ANPR QUESTIONS

Question 1: Are there concerns VA should be made aware of that could hinder the implementation of the TRS?

Yes. We believe the VA should not implement a tier ranking system until after the COVID-19 National Emergency has ended. Please see above for additional details.

Question 2: Should VA consider a servicer's volume of VA loans in developing the TRS?

No, the VA should not consider a servicer's volume of VA loans in developing the TRS. Please see above for additional details.

Question 3: Should VA expand the scope of the TRS to include consideration of factors beyond a servicer's performance in the areas of default resolution and foreclosure avoidance?

Yes, we agree that the VA should consider factors beyond the default resolution and foreclosure avoidance. For example, the VA could consider a data quality standard that measures compliance VA's default reporting standards.

Question 4: During the testing phase of the TRS, would servicers like to know their quarterly performance scores? If yes, for how many quarters prior to the TRS becoming effective?

Yes, we support a testing phase of the TRS for at least 4 full quarters. However, we believe VA should instead implement a pilot program prior to the TRS becoming effective. Please see above for additional details.

Question 5: What would be the anticipated burden for a servicer to participate in an error resolution process? Should VA provide servicers with such option in developing the TRS?

Yes, the VA should provide servicers with the option to participate in an error resolution process. We recognize that VALERI will be collecting and analyzing a considerable volume of data that can potentially incorrectly or inaccurately calculate servicers tier ranking.

At this time, without a proposed rule and the details on a tier ranking system, servicers cannot provide insight into the anticipated burden placed on servicers to participate in an error resolution process. Nonetheless, servicers will need sufficient time to review and validate inaccurate data and prepare the necessary documentation to submit to the VA for review. Please see above for additional details.

Question 6: Should VA consider providing a new VA servicer with a provisional tier ranking after 12 months of servicing has elapsed?

No, the VA should not consider providing a new VA servicer with a provisional tier ranking after 12 months of servicing have elapsed. A provisional ranking would be based on the immediate past 4 quarters that could potentially place a new servicer at a lower tier. A new servicer should have the opportunity to understand their portfolio and how the VA scorecard measures their performance of servicing Veteran borrowers in default.

Question 7: Are there other servicer tier ranking systems that VA should review and consider, in part or full, for developing its TRS? Please describe.

Yes, both FHA and the GSE have servicer performance scorecard. In addition to the top issues identified above, we believe the VA should adopt additional considerations of both.

1. Servicer Narrative/White Paper/Training. Prior to becoming effective and throughout the Pilot program, VA should create clear instructions regarding which metrics are scored, how they're defined, how they're calculated, and how servicers are ultimately assigned a tier ranking.

2. Extra Credit. Like FHA, VA should allow for servicers to receive extra credit equal to 1% at the end of the scoring year if a servicer has completed additional trainings throughout the year and provided documentation of that training to the VA. This could also be a condition of the error resolution process.

Question 8: Based on other servicer tier ranking system(s) that servicers may have implemented, approximately how long does it take a servicer to review and understand a new servicer tier ranking system?

Unfortunately, we are unable to answer this question without additional details at this time. However, once a rule is proposed that advances the principles articulated above, we can provide a more accurate assessment. In short, however, a simple scorecard that analyzes the data already available will allow for a more efficient review.

Question 9: Based on other servicer tier ranking system(s) that servicers may have implemented, as an estimate, what costs and burdens do servicers expect to incur for implementing a new servicer tier ranking system? Please describe the type(s) of cost(s) and provide dollar figures, if available.

Unfortunately, we are unable to answer this question without additional details currently. Once a rule is proposed, however, we can provide a more accurate assessment of the potential costs and burdens, including potential dollar figures.

Question 10: Based on other servicer tier ranking system(s) that servicers may have implemented, what impact, if any, would a lower tier ranking (and smaller incentive payments) have on servicer participation in the VA home loan program? Would smaller incentive payments, due to a lower tier ranking, result in any costs for borrowers, either existing or new?

Neither MBA nor HPC expects a lower tier ranking and smaller incentive payments received will negatively impact participation in the VA home loan program. Additionally, although we cannot provide a thorough response to Question 9 above, any potential costs to implementing a scorecard will not result in any costs for Veteran borrowers.

§ 36.4318 Servicer tier ranking ~~– temporary~~ procedures.

(a) The Secretary shall assign to each servicer a "Tier Ranking" based upon the servicer's performance in servicing guaranteed loans in default by computing ratios analyzing portfolio-wide data reported in the VA Electronic Interface (VALERI) measuring a servicers loss mitigation effort, including but not limited to metrics measuring (metric 1), (metric 2), (etc.) There shall be four tiers, known as tier one, tier two, tier three, and tier four, with tier one representing the highest rated servicers and best performance and tier four representing the lowest rated servicers and least satisfactory performance. ~~Upon the effective date of this regulation, every servicer of loans guaranteed by the Secretary shall be presumed to be in servicer tier two, and shall remain in tier two until the date specified in paragraph (c)(2) of this section~~. The precise methodology for calculating the tier rankings will be provided through Federal Register notice.

(b) For purposes of this section, the term "calendar quarter" shall mean the 3-month periods ending on March 31, June 30, September 30, and December 31.

(c)

1) No later than 30 calendar days after the last business day of the first calendar quarter occurring after the rules for determining tier rankings take effect, and then not later than 30 calendar days after the last business day of each subsequent calendar quarter, the Secretary shall provide each servicer with an evaluation of their performance under such rules.

2) No later than 45 calendar days after the last business day of the fourth calendar quarter during which the Secretary evaluates the performance of servicers, and then annually thereafter, VA shall advise each servicer of its tier ranking.

3) Any entity which begins servicing guaranteed loans after the first calendar quarter occurring after rules for determining tier rankings take effect shall be presumed to be in tier two. The Secretary will evaluate the performance of such servicer as provided in paragraph (c)(1) of this section. The Secretary will advise such servicer of its tier ranking at the time other servicers are advised of their tier rankings pursuant to paragraph (c)(2) of this section, provided the servicer has received evaluations for at least four continuous calendar quarters.

(d) Within 30 days of a servicer's quarterly evaluation, a servicer may contest its quarterly, annual, or tier ranking score to the Executive Director of the Loan Guaranty Service if this dispute is based on incorrect or incomplete data that affect a tier ranking. Based on such appeal, the VA shall correct any tier ranking score as appropriate and reasonable.

(e) The quarterly evaluation and tier ranking of a servicer shall be deemed to be confidential and privileged and shall not be disclosed by the Secretary to any other party.