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February 14, 2019

Submitted electronically via Regulations.Gov

Director, Regulations Management (00REG)
Department of Veterans Affairs
810 Vermont Avenue NW, Room 1063B
Washington DC, 20420

Re: RIN 2900-AQ42, Loan Guaranty: Revisions to VA Insured Cash-Out Home Refinance Loans

Dear Sir or Madam,

SIFMA[1] is grateful for the opportunity to submit these comments regarding the interim final rules referenced in the Re: line above. While SIFMA is not an originator of VA loans, we represent the market participants that provide funding for these loans – Ginnie Mae MBS investors and market makers. As such, we have carefully followed the performance of VA loans and supported the efforts of VA and Ginnie Mae to improve the quality of loan product originated by lenders, obtained by borrowers, and invested in by MBS investors.

SIFMA strongly supported the creation of the VA/Ginnie Mae task force and is grateful for actions taken by Ginnie Mae and VA since that time. MBS investors and VA borrowers have aligned interests regarding these matters. As we noted in a letter to Ginnie Mae supporting the Task Force, we are concerned that the activities of unscrupulous lenders "may negatively impact VA borrowers and believe they have negatively impacted the mutual funds, 401k plans, and other savers invested in Ginnie Mae MBS." [2]

Accordingly, we also support the issuance of interim final rules aimed at addressing the problem. While Ginnie Mae's actions have been helpful in reducing the amount of rapid refinancing, they have not solved the problem. Nor is Ginnie Mae best positioned to fix these problems – that is where VA has the

[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.
[2] See: https://www.sifma.org/resources/news/sifma-supports-ginnie-maeveterans-affairs-task-force-on-mortgage-issues/

opportunity and obligation to act to protect Veteran borrowers and investors in MBS containing their loans.

We briefly set out below our comments and suggested revisions for the interim final regulation.

1. We support the inclusion of a 90% LTV requirement in the net tangible benefit (NTB) test. Such a limit should help to ensure that borrowers do not see their equity stripped away in ill-advised transactions that do not provide meaningful benefit but do provide fees to originators. This is the simplest way to protect borrowers.

   We believe a 90% LTV loan should be the baseline – and to exceed 90% LTV lenders should be required to ensure the loan meets strict criteria that evidence a clear borrower purpose and benefit.

2. However, it is not clear to us that simply meeting one of the other NTB criteria detailed in the regulation should be sufficient to permit a 100% LTV cash out refi. Some of the criteria present significant evasion risk. For example, as drafted:

   a. **Term Reduction** - The term reduction component does not specify a required reduction in term. A lender could simply refi a borrower with 29 years remaining into a 28 year and 10-month term loan and (by our reading) meet the standard. This creates a clear route for evasion of the spirit of the rules.
      i. Solution: Require a meaningful reduction in term: For the purposes of the NTB test, a 10-year term reduction should be required (e.g., an originally 30 year loan would need to be refinanced into a 15 or 20 year term new loan).

   b. **Rate Reduction -** The rate reduction component is similarly deficient and presents evasion risk. A rate reduction is not specified, meaning that a borrower could see thousands of dollars in fees for a rate reduction of one basis point for a Type II cash-out refinancing.
      i. Solution:
         1. For the purposes of this test, a meaningful rate reduction for both types of refinancings should be required, not just Type I. We suggest 50 basis points across both types of cash-out fixed-to-fixed refis and 200 basis points for fixed-to-floating refis, as is required for Type I.
         2. The rule does not discuss how discount points may be used and the risk is that a borrower could be asked to pay points to lower the rate and not benefit overall. VA should include a requirement the lower interest rate is not produced solely from discount points, unless such points are paid at closing and such points are not added to the principal loan amount.

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c. **Reduced Payment / Residual Income Increase** – Similar to other items in the test, there is no specification of thresholds for payment reduction or residual income increases. This leaves borrowers open to exploitation – for a few dollars of payment reduction, a borrower could be charged thousands of dollars of fees. In some instances, any amount of payment reduction or residual income increase may be what a borrower is looking for and increased costs or terms may be worth it for them. However, we are concerned that borrowers could be abused in this process.
    i. Solution – To help avoid evasion risk and illusory benefit to borrowers, we believe the general rule should be that meeting these criteria should not be enough to pass the NTB test alone and that simultaneous achievement of another criteria should be required. E.g., a rate reduction (as amended by 2(b) above), MI elimination, LTV <90, shorter term, refinancing a floating to fixed-rate loan, or replacement of a construction loan.
        1. VA could allow for very limited exceptions to this rule, such as a hardship waiver from a borrower that evidences acknowledgement of the costs of the refinancing versus the benefits of it.

d. **MI Elimination** - It is not clear to us that simply eliminating MI should allow a loan to pass the NTB test and allow for a 100% LTV loan. We believe this criterion should be tied to simultaneous achievement of another of the criteria, either a lower interest rate (as amended by 2(b) above), a lower monthly payment, or higher residual income.

e. **Recoupment for Type II Refis** - VA notes in the preamble that determining the recoupment criteria for Type II refis is challenging. We agree that in situations where borrowers take out equity it is more challenging to determine appropriate recoupment criteria that do not disadvantage the borrower. However, we believe there is a general principle that could be applied – that the additional costs of the new loan are commensurate with the cash the borrower receives. One way to address this would be to add a requirement that any additional interest paid by the borrower on the cash-out loan as compared to their original loan over the next 36 months must be less than 25% of the cash, net of upfront costs and fees, received by the borrower at closing.

f. To the extent that VA is unable to make the sorts of changes we describe above in (a), (b), (c) and (d) to help reduce evasion of the spirit of the rules, we suggest that these criteria be removed from the NTB test. Leaving them in could do more harm than good.

We believe the adoption of these suggestions will create a safer program for VA borrowers and a safer environment for investors to buy Ginnie Mae MBS backed by VA loans. This will support valuations on MBS, which will improve borrowing costs for VA customers. It is a virtuous cycle.

On the other hand, if the rules are not changed and remain structured in a manner that provides easy avenues to evasion, the cycle could be reversed – further harm to borrowers will beget further harm to MBS investors, which will place downward pressure on MBS valuations, and upward pressure on mortgage rates. We note that, as VA knows, this harm would not be limited to VA borrowers – it would also impact FHA and other mortgage programs securitized by Ginnie Mae.

Please contact me with any questions or comments on these suggestions. We would be pleased to meet with your team to discuss these issues in more detail.

Sincerely,

Christopher B. Killian
Managing Director
Securitization and Credit Markets