



Member Mortgage Bankers Association of America

Mr. Edward De Marco
Acting Director
Federal Housing Finance Agency
1700 G Street, NW, 4th Floor
Washington, DC 20552

December 22, 2011

Dear Mr. DeMarco:

Guild Mortgage Company appreciates the opportunity to comment on FHFA's September 27, 2011 discussion paper on servicing compensation reform. Guild has been in business since 1960 originating, selling and servicing residential mortgage loan products. Our current servicing portfolio is over \$7.5 billion. We have reviewed the two alternative approaches and have outlined our opinion on the following pages.

After reviewing the proposed options, the MBA Reserve Proposal, or the FHFA Fee for Service Proposal (FFS), we recommend that the MBA Reserve proposal be adopted, with its modest changes to the current enterprise servicing compensation model, rather than the much more extreme FFS proposal.

Our leading concerns about the FFS proposal are that, contrary to its expressed design, we anticipate that, if adopted, there may be unintended consequences such that servicing will become more concentrated among a few large entities, that many independent servicers will exit the business, that those servicers that remain will be in effect subservicers to the GSE's, that markets will remain troubled, and that costs to consumers will rise.

Sincerely,

A handwritten signature in cursive script, reading "Mary Ann McGarry", is written over a solid horizontal line.

Mary Ann McGarry
President and CEO

The remainder of this letter addresses questions that FHFA raised in its discussion paper.

1) What are the impacts of these proposals on the competitive landscape in origination and servicing markets, service to borrowers, and efficiency in secondary markets?

The mortgage origination and servicing industries are highly concentrated. The uncertainty and demanding regulatory environment associated with both the origination and servicing of loans has made it difficult to attract private money into this market.

If a change is required, the MBA's proposal will do a better job of matching cash flow needs of servicers to the needs and interests of consumers. Under both the current Enterprise servicing model and FHFA's proposed FFS model, there is no monthly cash flow to offset the cost of increased customer contact for the period from first delinquency to the final modification or foreclosure of the loan. The MBA's reserve proposal could make cash flows available from balances that had previously been escrowed.

If implemented, the MBA's reserve proposal would keep the secondary markets intact and would be the least disruptive in a fragile housing market; the reserve method would increase servicers' "skin in the game," which would be seen as beneficial to investors and guarantors.

On the other hand, the FFS proposal would move most profits from the mortgage origination/servicing cycle to the origination part of the equation. If the FFS proposal were implemented, the servicer would become a subservicer for the GSE's and the business model would become less attractive.

Drastically altering the nature of the servicing contract as suggested with the FFS proposal could conceivably impact the structure, processes, and investment in the servicing industry, although the results are by no means certain. The FFS proposal would reduce the complexity and capital costs associated with the servicing function by eliminating the MSR asset but would push the servicing opportunity to high volume, low cost companies, at the expense of the small independent mortgage bankers.

We are concerned that the impact of simply maintaining the status quo in face of impending Basel III regulations would reduce or eliminate the correspondent channels, which would have a negative impact on small originators. Small banks and independent mortgage companies depend on the correspondent lenders to purchase loans. Driving the small originator to exit the business would diminish service to the consumer since the large banks are not effectively servicing this market.

The TBA market is one of the largest, most efficient markets in the world. We believe the MBA reserve proposal preserves the basic structure of the current model and would be more readily accepted in the market similar to the favorable trading of Ginnie Mae II's.

FHFA's proposal suggests that servicers retain a non-servicing Orphan IO, to make up for lost cash flows from the MSR. Based on our research, the IO's may have limited marketability and sell at multiples significantly lower than MSR's. It would become taxable and further reduce cash available to originators. Our concern is that in order to obtain the best execution from the IO strip, a small servicer would be at a disadvantage. It will be difficult to compete with large

aggregators, and the market may be nonexistent. Will Europe invest in this market as they do today with the MBS's? It appears risky to rely on the assumption the IO market will be liquid. The ability to retain any IO will be dependent on the spreads that the market makers decide are appropriate. We believe this would be detrimental to the consumer because interest rates would rise.

2) What are the benefits and/or impediments to your business model of having a capitalized MSR asset?

As an independent mortgage banker, we enjoy the flexibility of selling servicing and/or retaining the asset. We analyze the economic value of the present value of cash flows and compare it to the market value of the asset. We book a deferred tax asset which allows us to manage cash. Loss of the tax safe harbor benefits would adversely impact the initial value placed on the MSR asset, reducing the gain on sale. We believe this would ultimately raise interest rates on the consumer.

We view servicing as a natural hedge to loan production. When production profits are strong, servicing is typically down and vice versa. Under the FFS model, the MSR value in the balance sheet would be eliminated, resulting in a diminished natural hedge to the production side of the mortgage business.

Currently, we enjoy the flexibility to maximize profits through best execution in the secondary market. Under the FFS model the GSE's gain additional control over the pricing structure, reducing our flexibility. This appears to create a process depending more on government control and less on private market involvement in housing finance.

My concern is that the business model under the FFS is not attractive and would result in most independent servicers exiting the business. The FFS would drive the business overseas to low cost servicers and would not attract private capital to enter the market.

a) Does a capitalized MSR impede competition in the servicing and origination market?

It is not clear what the actual cost will be compared to the FFS amount so the accounting treatment of capitalizing some portion may be necessary and difficult to determine.

The competitive landscape results from the volume based G-fees provided to the largest aggregators. This has always been a disadvantage which the FFS does not resolve.

The capital markets are functioning, with new competitors moving into servicing. The value of the MSR versus the SRP is an important factor in the decision to hold MSR's versus selling for SRP's. Another important factor is that SRP's are taxable immediately where MSR's are only taxed as earned over the life of the related mortgages.

The subservicing business has grown that small originators can now retain servicing without having to build a servicing platform from the ground up. If the fee were to be substantially reduced, there would not be enough revenue to outsource. Barriers to entry would become greater. Because of these economics, we anticipate that the FFS proposal could lead to more servicing consolidation and concentration with the largest players.

c) Does the impact vary across size of servicers and originators?

As we see the FHFA's FFS proposal, small servicers would have a difficult time entering the servicing business, contrary to the stated objectives. The economics of the low fee would make it impractical to hire a subservicer. To compete in this environment, a servicer would have to have a large portfolio with high economies of scale. This would result in more concentration with the big banks which would clearly be a disadvantage to the medium and small servicers.

d) Would greater transparency in MSR valuation improve the competitive landscape?

MSR valuation is very transparent today with the disclosures added by FAS #156 and the related fair value disclosures. The accounting is not clear under the FFS proposal, which would cause many discrepancies when comparing companies.

e) What is the impact of a potential reduction in tax Safe Harbor?

The reduction of the Safe Harbor servicing compensation guides would subject any IO or excess servicing not covered by the Safe Harbor to an immediate taxation of non-cash income. Again, this is detrimental to a small servicer.

f) Should the servicer be required to hold a capitalized MSR asset (effectively be an IO investor) as a condition of performing servicing activities?

No, we do not see the benefit; today we have successful subservicers that do not invest in MSR's.

3) Should a lender's excess IO remain contractually attached to the MSR, or would seller/servicers prefer to have the excess IO be a separate stand alone asset (unencumbered by the Enterprises)

In theory, the IO that stands alone should have more liquidity than one tied to the MSR. My understanding is that the Orphan IO will likely trade at multiples considerably lower than MSR multiples. Today, excess servicing associated with MSR's receives a lower relative valuation.

It's important to note that the IO will be taxable in the year of creation instead of paid over the life of the loans, as the MSR is now. Paying taxes on a non-cash income item is a practical option for a small servicer.

4) Would these proposals encourage greater investment in non-performing loan operations or abilities in a benign market cycle?

We can't answer this question until the FHFA outlines the NPL compensation plan.

a) How does this impact the alignment between guarantor and servicer interests?

We believe that the FFS proposal places the guarantors at greater risk because the collateral will be worth much less. Therefore, in the event of a servicer failure the GSE will hold the risk.

b) Would this improve service to borrowers?

No. NPL's would be transitioned to other servicers, which seems inefficient, and would not improve customer service. We are having difficulty following the logic that reducing the profits of a business will improve the quality of service to borrowers. We are concerned that the FFS proposal appears to be a flawed economic plan and will not attract private capital.

5) What would be the impact of the proposals on the TBA market if there were no MSR capitalization?

If there were no MSR at all, then all the profits would be pushed to the origination side of the business. We believe it would ultimately go to the consumer leaving very thin margins or reserves for future unintended consequences.

Uncertainty will have a negative impact on the TBA market and will be reflected in bond prices and yields.

6) Should any of the following provisions that were proposed in the fee for service proposal be considered independent of any other changes to servicing compensation structure?

The bifurcation of selling and servicing representations and warranties should be considered separately from servicing compensation. Requiring the servicer to hold all risk limits the ability to transfer servicing.

Limitation of P & I advance requirements

Sellers have long had the option to sell mortgages to the Cash Window and receive an Actual/Actual remittance method, where no delinquent P & I is advanced.