All of us serving you®

U.S. Bank Home Mortgage

1550 American Boulevard E., Suite 880
Bloomington, MN 55425
952 851-5499
952 814-3373 fax

Daniel A. Arrigoni
President and CEO

December 22, 2011

Mr. Edward DeMarco
Acting Director
Federal Housing Finance Agency
1700 G Street, NW, 4th Floor
Washington, DC 20552
edward.demarco@fhfa.gov

Submission to: Servicing_Comp_Public_Comments@FHFA.gov

Re: Alternative Mortgage Servicing Compensation Discussion Paper

Dear Mr. DeMarco:

U.S. Bank appreciates the opportunity to comment on FHFA's Alternative Mortgage Servicing Compensation Discussion Paper. We consider this a very important issue to the future of housing finance. It is our belief that a significant change to the servicing fee compensation as proposed in the Flat Service Fee (FSF) structure will have negative impacts to affordable borrowers, the TBA market, Freddie Mac, the mortgage banking profit model and the viability of being a servicer and are opposed to this idea. We would however be interested in discussing other reduced servicing fee ideas, such as that proposed by the MBA and others.

U.S. Bank services approximately 850 thousand GSE loans for a unpaid principal balance of $141 billion (primarily for Freddie Mac). Our percentage of seriously delinquent loans (including loans in foreclosure) runs about half the average for Freddie Mac. U.S. Bank currently ranks 6th in mortgage servicing and originations nationally.

The proposed $10 per loan per month service fee (flat service fee) would not improve service to borrowers. Under the current model our interests are strongly aligned with both our customers, as well as with investors. When a loan goes delinquent, or to foreclosure, our MSR value goes from thousands of dollars positive, to thousands of dollars negative. We have costly advances to make, subject to much greater representations and warranty exposure, and incur foreclosure timeline penalties. These

costs drive us not only to produce a better book of business, but to service in such a manner so as to produce the best outcomes for our customers and investors. The proposed flat service fee may make it more profitable to service delinquent and defaulted

mortgages. This proposed flat service fee may even promote the production of riskier loans as lenders will be incented to generate more delinquent inventory in order to collect the additional fees. Raising guarantee fees to cover incentives to servicers for servicing delinquent loans, would apparently be born by the consumer in the form of higher interest rates, which will further hinder the housing and economic recoveries. The current model, or one with a slightly reduced service fee (20 basis point proposal), puts originators and servicers at significant financial risk when loans are either produced or serviced poorly. The model in place today incentivizes sound underwriting and production.

The proposed flat fee will reduce "skin in the game" for the servicers directly in conflict with the aim of the Dodd-Frank Act's risk retention efforts. The proposal would promote churning and cause greater negative convexity for TBA's. This would likely cause a significant negative impact on premium pricing. Affordable borrowers rely most heavily on premium pricing. These borrowers will suffer the most from a flat service fee proposal. It is possible that churning could become so rampant that investors shun premium priced MBS's all together.

We believe that any significant reduction in service fees is likely to negatively impact liquidity for TBA's. Since Freddie Mac PC's already suffer price degradation due to illiquidity verses Fannie Mae MBS's, it stands to reason that any change decreasing liquidity would likely impact Freddie security prices disproportionately and put their business model at risk. We believe that more competition benefits both our industry and consumers.

State and local housing authorities (HFAs) will also likely suffer under a flat service fee model. Most servicers have exited this business leaving state and local HFA's authorities fewer options in the market place. Given that these transactions are highly complex and have a low margin today, the institution of a flat fee will eliminate all economic incentive (including the potential loss of Safe Harbor provisions) to service these products. The HFAs are heavily reliant on premium priced bonds to fund their assistance programs and with the end of the NIBP program (Treasury currently buys the Mortgage Revenue Bonds produced by these entities) the HFAs are likely to be heavily reliant on GSE MBSs and premiums generated by their sale. State and local governments are struggling to meet the affordable housing needs of their citizens. This proposal would further complicate their mission.

Mortgage Banking is a volatile business and in recent years many investors have exited the industry. The current service fee structure is counter cyclical to the origination business and helps mitigate some of the large profitability swings associated with the origination business. The flat service fee would make the mortgage business model more volatile and even less favorable for investors in this industry. The result will be fewer competitors higher return requirements and the potential for higher rates for borrowers. Small and medium sized servicers would be driven from the business by larger servicers who have the economies of scale and other businesses to off set the volatility, The result will be increased risk to the system at a time when regulators are seeking to reduce this systemic risk.

A flat fee for service model could impair capital investment (new buildings, computers and other infrastructure) in servicing. Return on capital objectives would be very difficult/impossible to meet under a flat fee for service model. This could preclude further capital investment in servicing infrastructure and impair the ability to grow the business, and further present a risk that large servicers might choose to exit the business.

National servicing standards have yet to be determined. Altering the servicing fee structure prior to determining national servicing standards and the accompanying cost structure is akin to "putting the cart before the horse".

This very large change to servicing compensation has many potential impacts and creates a lot of uncertainty for the housing finance system. At the very least additional research to study the impact on the issues discussed above as well as potential impacts to the various production channels is warranted.

In conclusion, we do not support the flat service fee proposal, however, would support a reduction in the current minimum service fees. We do fear the flat service fee would:

- Negatively effect affordable borrowers
- Reward bad behavior
- Put the TBA market in jeopardy (including negative impacts to premium pricing)
- Negatively impact state and local Housing Finance Authorities
- Put Freddie Mac's securities at a greater disadvantage
- Negatively impact the economics of both the origination and servicing business
- Increase risk to the financial system
- Add a great deal of uncertainty to an already fragile industry

All of us serving you®

U.S. Bank Home Mortgage

That being said U.S. Bank acknowledges that the current servicing compensation structure is not without flaws and we are open to discussing other alternatives.
U.S. Bank appreciates to opportunity to comment on FHFA's Alternative Mortgage Servicing Compensation discussion paper. If you have any questions about U.S. Bank's comments please contact me at 952-876-5499.

Sincerely,

Daniel A. Arrigoni
President and CEO