United States Senate
WASHINGTON, DC 20510

April 8, 2020

The Honorable Steven T. Mnuchin
Chair
Financial Stability Oversight Council
U.S. Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, D.C. 20220

Dear Chair Mnuchin:

Thank you for your ongoing work to help stabilize the U.S. economy and provide assistance to businesses and workers during the unprecedented health emergency caused by the onset of the novel coronavirus (COVID-19). We applaud recent efforts by regulators to consider and address liquidity constraints in the U.S. housing market, including the formation of a taskforce within the Financial Stability Oversight Council (FSOC) that is appropriately focused on these matters. We believe urgent action is required to avoid a critical strain on liquidity for certain home mortgage servicers. Failure to quickly address the liquidity challenges facing servicers could have much broader, systemic implications for our economy.

As you know, the Coronavirus Aid, Relief, and Economic Security (CARES) Act provides much-needed protections for most homeowners. Any homeowner with a mortgage that is insured or guaranteed by the federal government who is experiencing financial hardship is eligible for up to 6 months' forbearance on their mortgage payments, with a possible extension for another 6 months. These provisions will provide substantial relief to homeowners and will reduce the risk that reductions in homeowners' income caused by this public health crisis will trigger a housing crisis in the months ahead.

Given the magnitude of the economic stress that many Americans will face as a result of the virus, and the early numbers we are seeing from lenders across the country, it is likely that many families will be unable to make their payments as scheduled, triggering widespread participation in the program, with potentially up to 25% of borrowers seeking assistance.[1] While this is a reminder of the program's importance, it also presents a challenge. As you know, the companies to which borrowers would normally make these payments, mortgage servicers, are obligated to pass those amounts on to investors, whether borrowers make them or not. Thus, as borrowers participating in this program don't send in their payments, the mortgage servicers will have to step in to pay investors on their behalf.

Given that we could see as much as $100 billion in mortgage payments forborne through this program,[2] it presents an existential threat to these companies, and thus to the broader mortgage market. To put this in perspective, according to Moody's Analytics, last year servicers had total net profits of less than $10 billion. The institutions that normally provide servicers with their

[1] https://newslink.mba.org/cmf-newslinks/2020/march/mba-commercial-multifamily-newslink-march-26/mba-urges-feds-to-take-immediate-further-steps-on-market-stabilization-liquidity/
[2] https://newslink.mba.org/cmf-newslinks/2020/march/mba-commercial-multifamily-newslink-march-26/mba-urges-feds-to-take-immediate-further-steps-on-market-stabilization-liquidity/

liquidity will be unwilling to provide this unprecedented level of support, at least at a rate that many servicers could possibly afford. This will leave many servicers with no way to cover the growing obligations. Since this liquidity need was created by the CARES Act's entirely appropriate, but extraordinary, requirement to provide widespread forbearance, measures should be taken to ensure that the businesses required to execute on that commitment can survive to see it through.

While it may be sustainable, if not difficult, for servicers that are part of banks, which have other business lines and also access to bank-centric sources of liquidity to remain solvent, it is likely especially unsustainable for non-bank mortgage servicers, which are typically monolines and currently account for fully half the $7 trillion market for agency mortgages.[3] At some point in the not-too-distant-future, the strain on these nonbank mortgage servicers will become too much for many institutions to bear, and we fear that the repercussions of their failure to homeowners and the market will be severe.

While we understand that some nonbank lenders may have adopted practices that made them particularly susceptible to constraints on their liquidity during a severe downturn, imposing a broad liquidity shock to the entire servicing sector is not the way to go about reform. Stated differently, even if there are servicers whose thin capital and poor risk management structure make them inappropriate for assistance, ignoring the broader liquidity strain on the market right now would risk stress well beyond these companies.

The reasons for acting are systemic. First, as weaker nonbank mortgage servicers begin to struggle they may be forced to unload their mortgage servicing rights (MSRs) to stay afloat. This will drive down the value of MSRs generally, reducing the value of the assets of all other nonbank lenders. This will deteriorate the financial position of healthier nonbank lenders so that they face some of the same risks that forced the less healthy nonbank lenders into a sell-off. At best, we are disabling a large swath of previously healthy lenders at the worst possible time. At worst, we may be risking a downward spiral.

Moreover, when these nonbank lenders fail, regulators will be forced to find a home for their servicing at a time when there will be very few parties interested in absorbing these obligations. MSR values will be declining, the costs and risks of servicing will be skyrocketing, nonbank lenders will be weakened, and we fear that banks will still be reticent to get into servicing for many of the same reasons they have stayed away in recent years.

As we are learning again in this crisis, it takes time for programs to be established and for the assistance to reach the necessary parties. Therefore, we are calling for immediate action to avoid an impending crisis in the mortgage servicing sector, that could further threaten the mortgage market.

The CARES Act includes an appropriation of $455 billion for purposes of economic stabilization activities under Section 4003. Congress made these resources available to the Federal Reserve in order to address the types of liquidity challenges we expect mortgage servicers to encounter in the coming days and weeks. Thus, action in accordance with this Section would be entirely

[3] https://www.urban.org/sites/default/files/publication/101766/february20chartbook202020.pdf

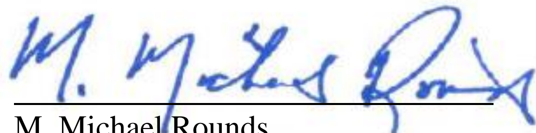
appropriate under the circumstances. Moreover, we also believe that the FHFA and the GSEs should ensure their policies mitigate, not increase, the liquidity demands facing servicers, consistent with the GSE's mandate to serve all markets at all times.

When workers are able to return to their jobs and millions of households can resume making the payments they intended to make, we must all take the opportunity to examine the many challenges, successes and failures of our current regulatory regime, including whatever steps are needed to strengthen the servicing sector going forward. While some servicers entered this crisis with too much exposure to liquidity constraints, the focus now should not be on longer-term reform, but on ensuring that the crisis now unfolding does as little damage to the economy as possible.

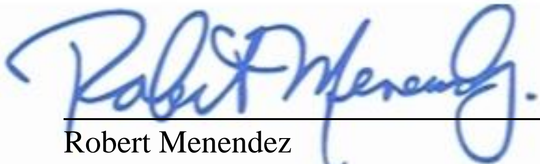
We appreciate your continued efforts to help sustain the American economy and our housing finance system during these challenging times and look forward to working together to protect homeowners during the COVID-19 pandemic. Thank you for your consideration.

Sincerely,

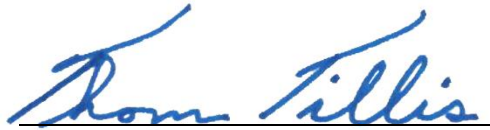
Mark R. Warner
United States Senator



M. Michael Rounds
United States Senator

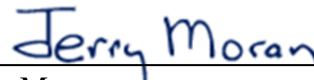


Robert Menendez
United States Senator

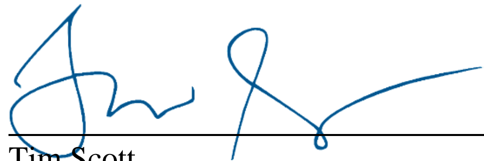


Thom Tillis
United States Senator

Tim Kaine
United States Senator



Jerry Moran
United States Senator



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United States Senator

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