

Is Change Coming to GSE Mortgage Servicing?

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The mortgage finance industry is abuzz over a rumored change to the way the government-sponsored enterprises (GSEs) Fannie Mae (FNM: 1.00 -2.91%) and Freddie Mac (FRE: 1.19 - 3.25%) would assign and manage mortgage servicing rights.

The rumors have different nuances depending on the source, but most senior servicing executives speaking with HousingWire have suggested that the GSEs have been quietly looking to revamp their servicing models in the wake of a historic collapse in the nation's housing markets. The prevailing theory is that agency servicers would either be categorized as performing or non-performing loan servicers, but not both — a drastic change from current servicing models, where the same servicer often manages both performing and non-performing loans.

According to sources, so-called 'performing servicers' would continue to get paid via a traditional servicing strip arrangement. 'Non-performing servicers' would receive a smaller servicing fee, but would be eligible to receive more substantial cash incentives each time a delinquent loan reperforms, or if other loss mitigation efforts (such as a short sale or deed-in-lieu) succeed.

Specialty servicer BSI Financial Services in Irving, Texas, already has similar arrangements with its private investor clients, the company's president and CEO, Gagan Sharma, told HousingWire.

"In a specialty servicing model, there's a base fee for loan servicing and the rest of the fee is all incentive based," Sharma said. "There's a base fee for handling a performing loan and then there are varying levels of incentives."

A source within Fannie Mae contends that the GSE's executive staff has no knowledge of such a shift. A Freddie Mac spokesperson told HousingWire that the agency was not working on any plan to change its approach to servicing loans, and directed questions about future initiatives to the Federal Housing Finance Agency (FHFA). As the GSEs' conservator, the FHFA had no official statement on the issue.

Yet in February of last year, Freddie Mac announced a pilot program it called 'Workout Strategy for High Risk Loans.' The program saw Freddie place troubled and delinquent loans with separate special servicers in an effort to implement more aggressive loss mitigation strategies.

Earlier this week, REO Insider, a sister publication, reported that Wilshire Credit Corp., which is in the process of being purchased by IBM (IBM: 125.24 +0.46%) from Bank of America (BAC: 15.63 +1.36%), will shutter its REO operations effective March 1 — making it the only major servicer in the nation without a viable real estate department, a move that has left many industry executives scratching their heads.

Wilshire Credit is set to receive a substantial portfolio of loans from Fannie Mae, as well, sources suggested Friday morning. Some industry sources wonder if IBM's move into mortgage servicing is being timed to coincide with the rumored changes allegedly in the works at Fannie and Freddie.

BSI's Sharma said he's aware of the rumors regarding the GSEs, and said some have suggested the agencies would create a "forced placement" model, where servicers would lose their servicing rights to a special servicer that's more experienced in high-touch loss mitigation whenever a troubled loan

hits certain triggers. “To a certain extent, the rumor is recognition of the appropriateness of the specialty service model that we work under,” he said.

The devil is in the details. What would be an appropriate threshold for the GSE to trigger a reassignment of servicing rights? There are contractual considerations that come into play as well. Mortgage servicing rights (MSRs) are an asset companies account for on their balance sheets, and actively hedge against. Losing servicing rights to a specialty servicer could affect a firm’s financial condition.

Which is one explanation as to why the GSEs and the FHFA may keeping mum if any changes are in the works, Sharma suggested.

“They’re probably not confirming it because they haven’t figured out the whole program,” he said.

Even before the Making Home Affordable Modification Program (HAMP), the GSEs already had incentives built into servicing contracts when delinquent loans are brought back into performance, Sharma said. And the recent distribution of bankrupt Taylor Bean & Whitaker’s (TBW) mortgage servicing portfolio may also have shed some light on any future changes to agency servicing.

After TBW’s bankruptcy, Freddie Mac dispersed the servicing rights to three servicers. All of the performing loans went to Cenlar, while Ocwen Financial Corp. received 90% of the servicing for the non-performing loans and Saxon Mortgage Services received the remaining 10% of the non-performing portfolio.

Sharma said small specialty servicers like his stand to benefit greatly from the rumored change. With the experience his firm has bringing non-performing loans back to performance, Sharma said BSI could serve as a pilot model for any proposed change.

“This would be a very interesting opportunity. We are a smaller, more agile shop and a lot of the newer things are going to get tried out with someone like us, like the private investors who come to us and say let’s try some other options,” he said.