



March 24, 2009

The Honorable Benjamin S. Bernanke
Chairman
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable John C. Dugan
Comptroller of the Currency
250 E Street SW
Washington, DC 20219

The Honorable Sheila C. Bair
Chairman
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Mr. Scott Polakoff
Acting Director
Office of Thrift Supervision
1700 G Street NW
Washington, DC 20552

Re: Warehouse Lines of Credit for Real Estate Finance

Lady and Gentlemen:

The current turmoil in the capital and credit markets has resulted in a significant, yet avoidable, “bottleneck” in the funding channels for real estate finance. The Mortgage Bankers Association¹ (MBA) believes this problem stems, in part, because the loans from banks to independent mortgage lenders to fund residential mortgages incur a significantly higher capital requirement than the underlying mortgages themselves.

Therefore, MBA formally requests the Board of Governors of the Federal Reserve System (Fed), Federal Deposit Insurance Corporation (FDIC), the Office of Comptroller of the Currency (OCC) and Office of Thrift Supervision (OTS) study the current risk weightings for warehouse lines of credit for real estate financing and make appropriate changes to better reflect the risk associated with lines backed by Fannie Mae, Freddie Mac or Ginnie Mae eligible loans and related servicing advances. Our proposal does not extend to other single family mortgage loan types such as non-agency subprime or Alt A loans.

¹ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

Recently, MBA has identified a growing threat to a source of capital for many mortgage lenders – warehouse lenders going out of business, terminating or adding restrictions to their warehouse lines of credit causing independent (non-depository) mortgage lenders to struggle to maintain their ability to lend. Warehouse lenders serve as crucial short term lenders for mortgage bankers. According to *National Mortgage News*, in 2007 there were approximately 90 warehouse lenders; today there are approximately 10 warehouse lenders.

Warehouse lending is a line of credit provided to a mortgage banking company to fund the closing of mortgages. It is a short term revolving credit facility that funds a lender's pipeline from the closing table to sale in the secondary market. The mortgage note is used as collateral for interim financing until the mortgage is sold and delivered to the permanent investor. The loans have to be pre-committed to an approved investor takeout, and those takeout commitments are part of the collateral pool for the warehouse line. Mortgage bankers draw upon the line of credit to fund a mortgage at closing or to purchase a closed loan from another originator. The line of credit is paid down when the loan is sold to the permanent investor.

The decline in warehouse lending capacity has outpaced the decline in overall mortgage originations. The 2008 estimated residential mortgage originations of \$1.8 trillion are 20.9 percent, or \$483 billion, less than in 2007. For the warehouse lenders, the capacity of the warehouse lines to serve non-depository mortgage originators is declining at a much faster rate – from over \$200 billion in 2007 to approximately \$20 to \$25 billion in 2008, a decline exceeding 85 percent. For the originator that depends solely on warehouse lines of credit, this reduction could extinguish their lending business and will impact the consumers in their market.

Recently, several commercial banks have purchased other institutions that are active in the warehouse lending business. While it is uncertain what the future of institutions' engagement in warehouse lending will be, many banks have pulled-back on warehouse lines, ceasing to issue new lines or increase existing lines, or have closed down lines altogether. These actions have left many non-depository lenders without adequate and viable sources of capital.

Other warehouse lenders may not continue to extend credit to lenders for various reasons, including it is a simple means of reducing a balance sheet, the perceived risk is too high, or headline risk of products associated with mortgages is too great despite the fact that underwriting is extremely rigorous today. Mortgage bankers that rely on warehouse lines of credit will be unable to maintain their businesses and cannot serve their local communities if their sources of warehouse lines are not maintained.

MBA has held recent meetings with representatives of the Department of Treasury, the Fed, Federal Housing Finance Agency and Ginnie Mae pursuant to working out a short term solution to the warehouse lending problem that would help the industry through this time of crisis. MBA, however, believes that some permanent improvements in risk-based capital (RBC) rules should be made to better reflect the risks inherent in warehouse lending for single family (1-4 units) and multifamily mortgages eligible for sale to Fannie Mae or Freddie Mac, insured by the Federal Housing Administration (FHA), guaranteed by the Department of Veterans Affairs (VA) or Rural Housing Service (RHS). This would provide a longer term solution to part of the problem.

Currently, RBC rules for banks and savings and loan associations treat warehouse lines of credit as commercial loans by assigning them to the 100 percent risk-weighted asset category, along with other commercial loan exposures. MBA believes that warehouse lines of credit, if properly managed, have risks comparable to conventional and government-insured mortgage exposures, and, in the final few days in warehouse, the risk is comparable to holding a government or government agency mortgage-backed security (MBS). Banks are exiting warehouse lending to shore up their risk-based capital positions. As a result of the fast turn of loans in warehouse (generally less than twenty days) and given the 100 percent risk weighting assigned thereto, winding down warehouse lending is a quick way for a bank to improve its capital position. Further, banks can replace warehouse assets by holding the same types of mortgages in whole loan form, which has a more favorable RBC treatment.

By way of background, warehouse lenders define three stages of the warehouse process:

- 1) Wet Funded² Stage:** Mortgage warehouse lenders frequently send money to the closing table on the day of loan closing. The closing agent, simultaneous with the closing, assigns the mortgage to the warehouse lender. This is generally governed by closing instructions from the warehouse lender to the closing agent. The mortgage banker provides the warehouse lender with a Uniform Commercial Code (UCC) form that serves as collateral until the underlying collateral documentation is received from the closing table. Such documentation includes the mortgage note. According to the UCC, the UCC document is valid collateral for up to 20 days.

² The term "wet funding" refers to the ink not being dry on the closing documents.

- 2) **Dry Funded Stage:** This stage represents the period that the warehouse lender has the mortgage note and other collateral documents in its collateral vault.
- 3) **Gestation Repo Stage:** Prior to delivery of a Ginnie Mae, Fannie Mae or Freddie Mac security (government MBS) to the secondary market, the mortgage banker will obtain an initial pool certification. Often, the certifying agent is the warehouse lender itself. Upon initial pool certification, the pool is said to be “in gestation” awaiting delivery to the takeout investor upon security issuance. Fifteen years ago, Wall Street firms would take delivery at this point and provide gestation repo funding from initial pool certification date to trade settlement. During the last ten years, commercial banks have added a gestation repo tranche to the typical warehouse line agreement in order not to lose this segment of the warehouse business.

MBA believes that the following RBC rules should be promulgated to more properly risk-weight these assets:

- 1) **Wet Funded Stage:** The current RBC weighting of 100 percent should be maintained until all collateral documents are received from the closing table.
- 2) **Dry Funded Stage:** Dry funded loans provide as collateral to the warehouse bank the mortgage note endorsed in blank. This allows the warehouse lender to step into the shoes of the mortgage lender and own these loans if the mortgage lender defaults. The warehouse lender also has a perfected interest in all forward sale agreements. So, not only does the warehouse lender have the ability to own the loan, it can deliver that loan into the secondary market within weeks at a pre-determined price. Thus, the warehouse lender has collateral that is perfected, has little credit risk (since newly originated), and has little market risk (since pre-sold into the secondary market). Present RBC rules for mortgage loans held by a bank require from 50 percent to 100 percent RBC weighting, depending on the mortgage’s loan-to-value (LTV) ratio. For FHA and VA loans, the RBC weighting is 20 percent. Proposed Basel II “standardized approach” provides for RBC weightings from 20 percent to 150 percent depending on the LTV and whether the loan is current. MBA proposes that RBC weighting of 50 percent be accorded that portion of a warehouse line that is dry funded and is collateralized by loans conforming to Fannie Mae or Freddie Mac requirements, FHA loans, VA loans, Rural Housing Service loans, and Home Equity Conversion Mortgages (HECM’s).

- 3) Gestation Repo Stage:** Upon initial pool certification, a new government MBS will be issued in a matter of days. Since the warehouse lender has a blanket lien on all forward sale commitments, these MBS are pre-sold. Present RBC rules call for zero percent capital on Ginnie Mae MBS and 10 percent on Fannie Mae and Freddie Mac MBS. MBA recommends a RBC weighting of not more than 20 percent for that portion of a warehouse line that is backed by gestation collateral.

A much smaller yet very important piece of a typical warehouse relationship is a working capital line to finance a mortgage servicer's advances required under Fannie Mae, Freddie Mac and Ginnie Mae servicing agreements for principal and interest passed through to certificate holders prior to receipt of a borrower's payment and for tax and insurance escrow advances. As the Treasury's recent loan modification and refinance initiatives are implemented, and as a result of the current moratorium on new foreclosure actions, these advances are expected to rise dramatically, resulting in further warehouse line needs. The warehouse lenders appropriately require a discount for this collateral for amounts not directly receivable from Fannie Mae, Freddie Mac and Ginnie Mae. We recommend an RBC weighting of 20 percent for this collateral.

Although this proposal provides a warehouse capacity shortage solution specifically tailored for loans with actual or effective government guarantees (GSE, FHA, VA and RHS-eligible residential and multifamily mortgages), it is not an appropriate solution for non-government guaranteed private label residential, commercial and multifamily loans. In order to address this issue, MBA will work with our members and the administration to craft solutions that provide for increased warehouse lines of credit capacity for private label residential, commercial and multifamily loans. By addressing both government guaranteed and private label loan categories, a complete solution to the capacity shortage for warehouse lines of credit can be developed.

MBA commends the bank and thrift regulators for your concerted efforts to address the housing finance crisis while bolstering the safety and soundness of the institutions that you regulate. However, MBA believes that the success of most of these efforts hinges on improving the liquidity and availability of warehouse lines of credit that are needed to support the recovery of the housing market.

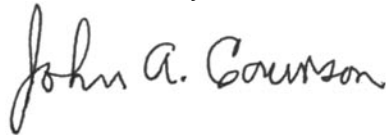
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MBA looks forward to working with you and providing representatives of independent mortgage lenders and warehouse lenders to discuss more fully the warehouse lending process. MBA's point of contact on the proposed change to risk-based capital rules is Jim Gross, Associate Vice President and Staff Representative to MBA's Financial Management Committee, and he can be reached at (202) 557-2860 or jgross@mortgagebankers.org.

Most sincerely,

A handwritten signature in black ink that reads "John A. Courson". The signature is written in a cursive, flowing style.

John A. Courson
President and Chief Executive Officer
Mortgage Bankers Association

CC: The Honorable Timothy F. Geithner
The Honorable Shaun Donovan
The Honorable James B. Lockhart, III
The Honorable Joseph J. Murin