The Honorable Timothy Geithner Secretary of the Treasury Department of the Treasury 1500 Pennsylvania Avenue, N.W. Washington, D.C. 20220

The Honorable Edward DeMarco Director (Acting) Federal Housing Finance Agency (FHFA) 1700 G Street, N.W. 4th Floor Washington, DC 20552

The Honorable Sheila Bair Chairman Federal Deposit Insurance Corporation 550 17th Street N.W. Washington D.C., DC 20006

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

The Honorable Mary L. Schapiro Chairman Securities and Exchange Commission 100 F Street, N.E. Washington, DC 20549

The Honorable John Walsh Comptroller of the Currency (Acting) Administrator of National Banks 250 E Street, S.W. Washington, DC 20219

Dear Secretary Geithner, Chairman Bair, Chairman Shapiro, Acting Director DeMarco, Chairman Bernanke and Controller Walsh:

We are writing to urge that any exception to the credit risk retention requirements of section 941 of the Dodd-Frank Act include rigorous requirements for servicing securitized residential mortgages.

The Act requires that securitizers retain five percent of the credit risk on mortgage-backed securities. The requirement is the subject of a study by Christopher M. James published by the Federal Reserve Bank of San Francisco dated December 13, 2010, and entitled "Mortgage-Backed Securities: How Important Is 'Skin in the Game'?", which finds that the requirement will have the intended effect of reducing "moral hazard" and significantly reducing the loss ratios on mortgage-backed securities.

The Act provides for an exception, however, for "qualified residential mortgages" and for other "exemptions, exceptions, and adjustments" to the risk-retention requirement. We strongly urge that you use great care in allowing any exception to the risk retention requirement, and that you be vigilant in assuring that any exception not defeat the purpose of the requirement. Recent experience in financial regulation has been that seemingly modest, reasonable exceptions have swallowed the rules and allowed abusive practices to continue unabated. In considering any requested exception under section 941, please remember that the advocates for rule-swallowing exceptions to other financial regulation have not been entirely candid with regulators or legislators on the likely effect of those exceptions.

The rules adopted pursuant to section 941 must, of course, require rigorous underwriting standards for "qualified residential mortgages" or any other mortgages excepted from the risk retention requirement, but underwriting requirements are not enough. The rules must also address the servicing of securitized mortgages. Much of the turmoil in the housing market, which is largely responsible for the painfully slow recovery, is the result not just of poorly underwritten mortgages, but of conduct by mortgage servicers.

We direct your attention to the "Open Letter to U.S. Regulators Regarding National Loan Servicing Standards" dated December 21, 2010, and signed by 51 people with extensive knowledge of mortgage servicing (the "Rosner-Whalen letter"). We strongly urge that you consider closely the recommendations included in that letter.

The Rosner-Whalen letter makes sensible recommendations regarding the treatment of payments by homeowners, "perverse incentives" in servicer compensation, mortgage documentation, and foreclosure forbearance during mortgage modification efforts.

We especially urge that any exception require that servicers modify mortgages pursuant to established criteria to avoid foreclosure where possible. The statute governing "Farmer Mac" mortgages provides a useful example of such criteria. See 12 U.S.C. 2202a ("Restructuring Distressed Loans"). Foreclosures are catastrophic for homeowners, holders of mortgage-backed securities, the housing market, and the economy as a whole. The conduct of servicers is largely responsible for much unnecessary hardship. A requirement that servicers modify mortgage according to established criteria to avoid foreclosure can avoid that hardship in the future. Neutral, established criteria will also avoid "tranche warfare" between classes of investors.

We also especially urge that any rule for securitized mortgages require that servicers not be affiliated with the securitizer. There are obvious potential conflicts of interest, and no apparent countervailing justification. At a recent hearing of the House Financial Services Committee, several witnesses from major servicers were unable to offer any advantage in being affiliated with securitizers, other than to offer "full service" to customers. That justification is entirely unpersuasive. Homeowners may select the bank with which they have a credit card or a checking account, but they have no say in who services their mortgage.

In fact, community banks and credit unions have been reluctant to sell the mortgages that they originate to "private-label securitizers" for fear that the mortgages will be serviced by an affiliate of a bank, and the servicer will use that relationship to "cross market" other banking services to the homeowner. Requiring that servicers be independent of banks, therefore, would advance the goal of increasing the availability of credit on reasonable terms to consumers.

The Dodd-Frank Actives provides you ample authority to reform servicing practices, and regulation of mortgage securitization will be ineffective without such reform.

Sincerely,

Veronica K. Kemp
Mortgage holder

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