January 17, 2023

John E. Bell, III
Executive Director
Loan Guaranty Service
U.S. Department of Veterans Affairs
810 Vermont Avenue, NW
Washington, DC 20420

RE: Comment Regarding Advance Notice of Proposed Rulemaking, Loan Guaranty: Loss-Mitigation Options for Guaranteed Loans, 87 Fed. Reg. 62752

Dear Executive Director Bell:

In response to the questions posed in the VA's October 17, 2022 Advance Notice of Proposed Rulemaking, the National Consumer Law Center (on behalf of its low-income clients)[1] and the Center for Responsible Lending[2] urge VA to expand the opportunities available to help veteran borrowers avoid foreclosure. The mortgage relief options available for veteran borrowers should not be less favorable than the options available to other borrowers and should provide relief in all market conditions. We appreciate the VA's engagement with stakeholders and look forward to working with you to find solutions.

[1] Since 1969, the nonprofit **National Consumer Law Center**® (NCLC®) has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitative practices, help financially stressed families build and retain wealth, and advance economic fairness.
[2] The Center for Responsible Lending (CRL) is a non-partisan, nonprofit research and policy advocacy organization working to promote financial fairness and economic opportunity for all, end predatory lending, and close the racial wealth gap. CRL's expertise gives it trusted insight to evaluate the impact of financial products and policies on the wealth and economic stability of families of color, rural, women, military, low-wage, low-wealth, and early-career workers and communities. CRL is an affiliate of Self-Help, one of the nation's largest nonprofit community development financial institutions. We work in partnership with national and local consumer, faith, and civil rights organizations.

The average interest rate for VA-guaranteed loans originated after 2019 is 3%, which is less than half the current market rate. Because VA ties its foreclosure relief options to the market interest rate, the dramatic difference between the market rate and the note on existing loans significantly reduces the effectiveness of the available loss mitigation options. While VA has historically fared well in limiting the impact of borrower financial hardship, the current level of interest rates provides an unprecedented challenge that will require new tools.

Our proposals below include suggestions for addressing the current challenge presented by elevated interest rates and for shaping loss mitigation in all market conditions.

We urge VA to reactivate and update its partial claim program to allow borrowers to retain their contractual interest rates and resume their monthly payments. The increase in interest rates would impact fewer borrowers if VA had an effective partial claim program that allowed borrowers to keep their market rates when they can afford to resume their original payments. An effective partial claim program would allow veteran borrowers to cure their delinquency, retain their below-market interest rate, and resume making their monthly payments when feasible. The lack of a VA partial claim program puts veteran borrowers in a worse position than FHA-insured and USDA-guaranteed borrowers who have access to partial claim programs.

We do not see loan deferment as a viable alternative to a partial claim because deferments impose significant costs on the mortgage servicer. As a result of these costs, borrowers have not historically received deferments. Given that the increase in market interest rates has also raised the borrowing costs for servicers, veteran borrowers are unlikely to receive deferments going forward. Short of reimbursing the mortgage servicer for payments advanced to investors on behalf of the borrower, there is no amount of incentive payment that would make loan deferment an economically viable option for servicers. We also do not see the loan deferment and repayment plan hybrid as a viable option because it would increase the veteran's monthly payment and their likelihood of default. Similarly, we do not see value in a partial claim program that requires the veteran to be charged interest, even at a below-market rate.[3]

By contrast, non-interest bearing partial claim programs have worked well for other government-backed lending programs and are far more successful than repayment plans. The VA should implement such a program to help veteran borrowers avoid foreclosure

VA should explore using any partial claim program that it develops to give a borrower payment relief without modifying the loan. The current elevated interest rates make it challenging for servicers who rely on Ginnie Mae securitization to provide payment relief to VA-guaranteed borrowers who need it. In general, providing payment relief is crucial to helping borrowers with significant financial hardships avoid foreclosure. Because market interest rates

[3] As discussed in National Consumer Law Center's January 8, 2021 comment, available at https://www.nclc.org/wp-content/uploads/2022/08/Covid_Veterans_Assistance_Comments.pdfL we do not see value in partial claim programs that require charging the veteran borrower interest. This comment also discusses the problems with loss mitigation options that increase a borrower's monthly payment.

are significantly higher than the contractual interest rates on most VA-backed loans, loan modifications will likely increase the borrower's interest rate and as a result provide limited, if any, payment relief.

Because FHA-insured lenders also rely on Ginnie Mae securitization, FHA is facing the same challenge of providing payment relief in the current, high-rate environment. We have recommended to FHA an option that would use partial claim funds to first bring borrowers current and then provide borrowers with monthly payment relief.[4] Under this program, known as a "payment supplement," FHA would deposit the partial claim funds needed to reduce the borrowers' monthly payment in an account held by the loan servicer. The servicer would then draw from the account each month the amount necessary to supplement a partial payment from the borrower, in order to submit the full contractual payment to Ginnie Mae. This system avoids increasing the borrower's interest rate through a loan modification while still providing payment relief. VA should consider adding a payment supplement option once it implements a full partial claim program.

VA should implement enhancements to its permanent loan modification program to provide payment relief when interest rates decrease from their current levels. As described above, loan modification programs are successful in avoiding foreclosure when they can provide payment relief to borrowers who have faced significant financial hardships. VA recognized the benefits of payment relief when it implemented the COVID-19 Refund Modification that included a payment reduction target of between 20-25% of the borrower's monthly principal and interest payment. In order to hit the target, VA allowed for the combination of a modification and a partial refund so that arrearages and a portion of the borrower's loan could be purchased by the VA and held at 0% interest. As was the case over the second half of 2021, the refund modification can provide ample payment reduction when the prevailing mortgage rate is low, keep the veteran borrower in their home, and avoid the foreclosure-related claims on the VA.

VA should make the COVID-19 Refund Modification a permanent feature of its loss mitigation waterfall. Should interest rates once again fall to levels below the note rate on outstanding VA loans, the refund modification can provide significant payment relief. In addition, VA should explore allowing for a 480-month term to provide additional payment relief when needed to reach the target. FHA's current COVID-19 waterfall, as described in Mortgagee Letter 22-07, provides a useful example of how to incorporate a 480-month term into a waterfall.

VA should expand its refund program as an additional option for providing deeper payment relief. The refund program gives the VA considerable latitude to adjust the terms of a mortgage, including leaving the contractual note rate unchanged or reducing it regardless of the

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[4] For a description of payment supplement accounts, see Center for Responsible Lending, Payment Supplement: A Loss Mitigation Option to Provide Payment Relief for FHA Loans in a High Interest Rate Environment (Nov. 28, 2022), available at https://www.responsiblelending.org/research-publication/payment-supplement-loss-mitigation-option-provide-payment-relief-fha-loans-high

market rate, if necessary, to provide a borrower with deeper payment relief. As a result, a loan refund can provide relief to borrowers in an amount that VA's other options do not achieve.

For borrowers who cannot afford the lowest available payment created by the payment supplement (if adopted) or a refund modification, whether they reach the target payment or not, VA should retain the requirement that the servicer evaluate the borrower's financial information and, if deemed eligible, apply for a loan refund. While the loan refund has been used sparingly in the recent past, VA will need to scale up the program to assist seriously delinquent veteran borrowers should interest rates remain elevated. Given the limited effectiveness of modifications in a high interest rate environment, expanding the refund program will be particularly important should VA be unable to implement the payment supplement.

To make the refund program work well, VA should publish clear and prudent criteria for which loans are eligible for a refund. Veteran borrowers and the advocates working with them should be able to clearly understand the program rules to determine what loans are appropriate for a refund. Establishing clear rules will help servicers avoid unnecessary costs and help borrowers focus on the most appropriate option for their financial situation.[5]

VA's refund criteria should focus on providing payment relief to veteran borrowers facing financial hardship. Veteran borrowers who lose their homes to foreclosure will need housing in a market with skyrocketing rents. Payment relief provides the best path for helping veteran borrowers stay in their homes. Eligibility criteria based on the value of the borrower's home do not help provide payment relief and should not be part of the refund program.

Once the VA revamps its loss mitigation program to include options that are economically viable for the veteran, the servicer, and the VA, now and going forward, the VA should set out a mandatory order in which servicers should evaluate the veteran for available options. A mandatory waterfall that prescribes the specific steps servicers must take in evaluating foreclosure alternatives will give servicers and borrowers important clarity. The flow charts VA created in response to the COVID pandemic were clear and can be incorporated in a future model.[6] Once VA improves its loss mitigation options as discussed above, we believe that servicers should be required to follow the prescribed order of the new waterfall, as it would help ensure a consistent loss mitigation experience for all veteran borrowers and remove any incentives for servicers to offer one loss mitigation option over another.

We also believe that streamlined loss mitigation should continue to be part of VA's waterfall as there are significant benefits to borrowers from not having to submit an application (i.e. a streamlined process). We discussed the benefits of streamlined loss mitigation extensively in

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[5] See December 1, 2022 Letter to VA from National Consumer Law Center, available at https://www.nclc.org/resources/letter-to-the-va-advocating-for-the-expansion-of-a-foreclosure-alternative-program/

[6] Exhibit A of VA Circular 26-21-13.

our November 28, 2022 comments to the CFPB, and we would appreciate any opportunity to discuss these benefits with you.[7]

The VA should publicly report data about its loan portfolio, including characteristics of the portfolio and loan performance. In order for stakeholders outside the VA to make informed comments on the VA's programs, they need data about the loans in the VA's portfolio and how they are performing. FHA provides its Neighborhood Watch data,[8] which provide performance information broken down by geographies and by mortgage servicer, and issues its monthly FHA Single-Family Loan Performance Trends Report, which further breaks down its loan performance.[9] VA should also provide similar reporting. In addition, we urge VA to report more specific data about how its loss mitigation programs are working, such as which options are being provided, the amount of payment relief (if any) provided, and subsequent redefault rates. Without this information, it is hard to provide the comprehensive feedback on the program that the VA is requesting.

The VA must be provided with adequate resources to provide assistance to borrowers in need. We fully recognize that VA may need additional financial resources to operate a permanent partial claim program and expand the use of the loan refund. It is our shared objective to give veterans a comprehensive home loan program that meets their needs throughout their lives, especially when they face challenging financial circumstances. Therefore, we strongly support giving the VA the additional financial resources necessary to expand their loss mitigation options as described above.

Immediate action is needed to prevent avoidable foreclosures. There is compelling evidence that providing assistance, especially payment reductions for borrowers facing financial hardship, leads to fewer foreclosures and fewer claims on the guarantor / insurer. Additionally, providing such assistance comes at a considerably lower cost than the claims associated with foreclosures. Regardless, if the budgetary costs associated with our recommendations require additional appropriations, we support the VA in getting these resources.

Thank you for your consideration of these comments. If you have any questions or would like to discuss these recommendations further, please contact Steve Sharpe at ssharpe@nclc.org.

Sincerely,

National Consumer Law Center (on behalf of its low-income clients)
Center for Responsible Lending

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[7] NCLC, CRL & NHLP Comment to CFPB on Mortgage Refinances & Forbearances (Nov. 28, 2022), https://www.nclc.org/resources/nclc-crl-nhlp-comment-to-cfpb-on-mortgage-refinances-forbearances/
[8] HUD Neighborhood Watch, https://entp.hud.gov/sfnw/public/
[9] FHA Single-Family Loan Performance Trends Report, available at https://www.hud.gov/program_offices/housing/hsgrroom/loanperformance