Entry Form
2017 Annual Awards for Program Excellence

Entry Deadline: Thursday, June 15, 2017, Midnight ET

Each entry must include a completed entry form. Please complete a form for each entry your HFA is submitting. The completed entry form will become the first page of your entry.

This form is a fillable PDF. Type your information into the entry form and save it as a PDF. Please do not write on or scan the entry form. **Questions: Call 202-624-7710 or email awards@ncsha.org.**

Entry Title: Enter your entry's title exactly as you wish it to be published on the NCSHA website and in the awards program.

MFA Servicing Expansion

Category: Management Innovation

Subcategory: Financial

Entry Summary: A 15-word (max) summary of the program, project, or practice you are entering.

An innovative sub-servicing model generates new revenue and reduces reliance on third-party master servicers.

HFA: New Mexico Mortgage Finance Authority (MFA)

HFA Staff Contact: Monica Abeita, Policy Director

Phone: 505-767-2252

Email: mabeita@housingnm.org

Visual Aids:
Are you mailing to NCSHA 10 copies of any visual aids that cannot be included in your entry PDF? ☐ Yes ☑ No

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MFA Servicing Expansion

NCSHA 2017 Annual Awards Entry

Dearth of Master Servicers: A Management Challenge. Since the adoption of a mortgage-backed securities (MBS) structure in 1994, master servicing for MFA's single family program had primarily been provided by Charter Bank, a long-time partner and local mortgage lender. When Charter Bank closed in 2009, MFA's lenders were obliged to use US Bank as MFA's master servicer, as US Bank was the only master servicer under contract at that time. Unfortunately, US Bank's business model was not a good fit with MFA or its lender network; it did not provide high-touch customer service and required overlays that excluded many New Mexicans from homeownership.

In 2012, MFA was required to re-bid its master servicing contract and was hopeful about attracting new third-party master servicers. However, we became acutely aware of a risk to core operations when we received only two proposals, one of which was from US Bank. Fortunately, Idaho Housing and Finance Association (IHFA) also responded to the request for proposals and became MFA's master servicer in 2013.

At that time, MFA had already launched its servicing expansion project. The project's initial purpose was to consider different servicing models in response to the strategic objective of *diversifying and generating new revenue*. The dearth of master servicers apparent through the RFP process increased impetus for the project and gave rise to the additional strategic objective of *reducing reliance on third-party master servicers*. MFA's Servicing Expansion committee quickly determined that it would not be economically feasible for MFA to service its own first mortgages and turned to sub-servicing, where servicing responsibilities would be shared between MFA and a third party.

Sub-Servicing: A Management Opportunity. In a standard sub-servicing arrangement, MFA would maintain control over mortgage servicing rights, which provide an ongoing revenue stream, while the sub-servicer would perform most major servicing functions on MFA's behalf. However, MFA would perform front end functions, including the purchase of loans from lenders, loan tracking, transfer of loans to the sub-servicer, and pooling and securitization using MFA's own seller/servicer and issuer approvals. MFA would also perform compliance oversight of the sub-servicing operations, including default and foreclosure activity. MFA found that sub-servicing would generate positive revenue in year five. However, new front end functions would be costly and difficult for MFA to ramp up in a short period of time.

Through an understanding of MFA's strategic objectives and IHFA's experience with flexible master servicing models, our two HFAs saw an opportunity and collaborated on a solution. We jointly designed an innovative sub-servicing model by which IHFA provides both the sub-servicing and front end functions for a reasonable fee. This allows MFA to develop capacity for front end functions over time, through a mentor relationship with IHFA. After signing a cooperative agreement, MFA and IHFA developed the following processes to support the launch of the sub-servicing model on June 1, 2016:

- IHFA purchases loans from MFA's lenders and MFA provides warehouse financing for those loans to IHFA.
- Use of MFA's single family pipeline to establish MBS and deliver MBS to respective investors.
- Concurrent transfer of mortgage servicing rights to MFA as MBS pools are settled.

- Document custodian partnership with IHFA and MFA coordinating the use of the same custodians to simplify access to the Federal Home Loan Bank line.
- Sub-servicer oversight by MFA of IHFA's quality control process and servicing activity.
- Special approvals from Fannie Mae and Ginnie Mae. While MFA had Fannie Mae and Freddie Mac seller/servicer and Ginnie Mae issuer approvals in place, it needed special approval to utilize this unique sub-servicing model.

The MFA/IHFA sub-servicing model has operated successfully for nearly one year and MFA is actively working to prepare for the next phase in project—assuming responsibility for front end servicing operations. MFA is currently evaluating its core software system and other software to determine which will best support these functions. MFA is also building a Federal Home Loan Bank warehouse line to provide more capital for MFA mortgages. This will support the record production and growth we have experienced in the past year and a half.

Benefits that Outweigh Costs/Effective Use of Resources. MFA evaluates each new initiative or program to ensure that benefits outweigh costs. MFA's Servicing Expansion project included an economic feasibility study for each model: self-servicing, standard sub-servicing and the MFA/IHFA sub-servicing model. As mentioned previously, self-servicing was not economically feasible. While both sub-servicing models generated additional revenue for MFA, the MFA/IHFA model was more advantageous because it reduced initial costs for front end functions. During the first several years of the arrangement, IHFA provides the front end functions, allowing MFA to effectively utilize its resources by investing new sub-servicing revenue in the infrastructure and staffing needed to assume front end operations by 2019.

MFA is on track to realize the revenue estimated in the economic feasibility study and meet its strategic objective of generating new and diverse revenue for the organization. MFA's Servicing Expansion committee estimates that the IHFA/MFA sub-servicing model will generate a positive change in net assets for MFA in year three and a cumulative change in net assets of $15 million in the first ten years. The two primary sources of new revenue for MFA are the warehouse line provided to IHFA for the purchase of New Mexico loans and the annuity stream from the purchased mortgage servicing rights. Monthly service fee income for MFA's aggregate portfolio started at $17,000 in December 2016 and has increased to $49,000 in April 2017. When MFA assumes front end functions from IHFA, costs to support these functions will be reduced and sub-servicing fees will decrease. This will increase the revenue that MFA can invest in its own servicing capacity and other affordable housing needs.

Improvements in Agency Operations. MFA realized record production in its single family program in 2016 and is on track to surpass last year's production in 2017. While this increase is largely a result of market forces, MFA is also able to make more loans because IHFA does not insist on the overlays required by MFA's former master servicer. The alignment of IHFA and MFA's missions precludes overlays that would otherwise prevent many credit-worthy New Mexicans from qualifying from homeownership.

Agency operations have also improved in the sense that MFA has achieved its strategic objective of eliminating reliance on a single master servicer. By moving away from master servicing and into sub-servicing, MFA now has a more diverse landscape of third-party servicers with whom it can work.

Finally, the mentorship provided by IHFA through this unique sub-servicing model is building capacity among MFA staff and in MFA processes. This a thoughtful and responsible approach to developing internal capacity for new operational functions, as opposed to ramping up quickly, stressing agency operations, and potentially failing our customers.

Innovative and Replicable. Clearly, the MFA/IHFA sub-servicing model is innovative. It is the first of its kind among housing finance agencies (HFAs) and was built as a custom approach to a serious management challenge. While innovative and unique, the process for designing similar models is also replicable, especially among HFAs. Any HFA relying on a master servicing arrangement is constrained to find more than a few third parties that offer master servicing, and the lack of a competitive environment means that HFAs are often forced to work with master servicers whose missions and business models are not aligned with affordable housing goals. Therefore, HFAs developing flexible models to support one another is both innovative and extremely practical. This approach allows us to share our strengths and address our weaknesses so that we are stronger together.

Here are some reflections on the MFA/IHFA partnership:

"This unique partnership has been very beneficial to MFA. Through this collaboration MFA is able to mature as an organization and become less dependent on third-party service providers while also improving financial performance to benefit affordable housing programs in New Mexico. We have been impressed with the professional staff IHFA has provided to support the training and technical assistance required to move forward. They are truly a sister organization!"

--Gina Hickman
Deputy Director of Finance and Administration, MFA

"IHFA began offering master servicing to state HFAs to give HFAs another option in the administration of their affordable housing programs. Idaho Housing's loan servicing business model evolved from the traditional master servicer to a model that enables us to open up our resources to other HFAs. This model worked well within MFA's servicing expansion objectives, the buying of servicing rights, and was part of our decision to assist them in activating their seller/servicer number and Ginnie Mae issuer number. The partnership works very well and we appreciate MFA's insight and desire to become more independent while strengthening their financial outlook."

--Susan Semba
Executive Vice President, Homeownership Lending, IHFA