

ARVEST[®]

MORTGAGE COMPANY

December 16, 2011

Mr. Edward DeMarco
Acting Director
Federal Housing Finance Agency
1700 G Street, N.W., 4th Floor
Washington, D.C. 20552



received
12.22.11

RE: Comment Letter regarding Servicing Compensation

Dear Mr. DeMarco,

After extensive review and analysis, we have concluded the existing service fee structure is the proper compensation model. Without question, it was strained during the Great Recession over the last four years, but remains viable today.

In consideration of the alternative compensation plans recently identified and for which the comment period is open for public feedback, we offer the following response accordingly. We are an active market participant in both originating approximately \$1.5 Billion in new loans annually and servicing in excess of \$36 Billion of FannieMae, FreddieMac, GNMA and Private MBS Securities. We are an active daily buyer of Mortgage Servicing Rights whereby we provide liquidity through Co-issue, Flow and Bulk Servicing acquisitions of approximately \$1 Billion monthly.

To properly evaluate the compensation alternatives, you must first assess the issues that caused the debate to arise. Opinions vary as to the reasons many big Servicers failed to adjust fast enough to the market downturn and why government programs like HAMP, HARP and many other modification and short sale initiatives did not have better results. The first thought process was the service fee compensation was ill suited because the fees were only collected when the loans were paying current. Costs to service are higher for loans past due and more labor intensive to handle bankruptcy filings, foreclosures, process short sale approvals and provide modification programs. There is no question that the industry faced a tidal wave of default volume no one ever contemplated. Common practices established over many years proved to be impediments during the rapid deterioration in the economy. Legal restrictions inherent in contracts such as modification prohibition, restraining Investor guidelines, and the lack of excess capacity within the servicing platforms created barriers to respond timely as well. The overwhelming call volume caused by the market downturn created a disconnect between offshore outsourced call centers and the regional default centers designated to handle those issues. While solutions were being created in real time to handle the evolving modification and short sale programs, the distance between the facilities made coordination of processes difficult at best. During this period extra compensation has been introduced by the GSEs to motivate the Servicers to enhance behaviors that would achieve the desired results for successful workouts, modifications, and short sales.

The list of industry changes rolled out over the last three years to react to the meltdown was simply amazing. In fact, the Servicing industry is now equipped to respond to future crises in ways never before imagined. Contracts, policies, procedures, programs, standards, expectations and industry practices have been reestablished, and hopefully will never be needed again to such a level.

Now we sit in the classic posture of potentially closing the barn door after the horse is gone by changing the compensation methodology to react to pre-meltdown servicing practices even though the industry is now forever changed as referenced above.

The FHFA White Paper offers two compensation alternatives under consideration; a reduced service fee or a pay for service. These compensation alternatives are offered in conjunction with the current existing structure whereas the service fee is negotiated at the point the loan is sold into the secondary market.

In consideration of the fee for service model, it is by far the highest risk while appealing only to those Sellers looking to avoid the impact of capitalizing MSR's on their balance sheets. The suggestion of a flat fee, of say \$10.00 per month, and higher fee when loans are past due, requires a known "cost to service" not just at the time of sale, but over the lifetime of the loan. As we are all aware, the future costs to service at this time are anything but known. Even the most recent MBA Cost to Service survey showed the average cost for a current loan is \$19.38 per month, or nearly twice the proposed fee. New agencies like the CFPB are still in their development phase, and compliance and servicing standards are still being introduced by Investors and Regulators. Additionally, various new state regulations are still being enacted which will add additional costs over time.

The consideration of a lower service fee to say, 20 basis points, and perhaps a 5 basis point reserve paid later, creates other consequences as well. In reflection on the meltdown, if the 25 Basis Point model did not incent the large servicers to have robust programs in place to react, then how can reducing the fees be a better solution? That question aside, there are many other factors that must be considered. The biggest and most important factor is the basic "Cash Flow" of the loans to be serviced, as compared to the overhead of the Servicing Platform performing the extensive servicing duties demanded by Investors, Regulators, Courts, Rating Agencies, Customers and Shareholders. The most obvious problem is the fact that in today's environment the service fee cash flows have already decreased due to the reduction of real estate prices across the country and causing the average loan balance with larger down payment requirements, to be lower than in the past resulting in less servicing income per loan. This is compounded with the fact that servicing platforms have witnessed inflationary costs from all the additional obligations and duties brought on by all stakeholders involved. As the economy recovers and the real estate prices level out and perhaps begin to advance in the future equilibrium will return to the relationship between the service fee income and the cost to service expenses increasing over the life cycle of the loans.

When we analyzed the two alternatives, compared to the existing model, we were able to determine the well intended alternative plans under review would disrupt the Servicing

industry and cause the same type of impact as deregulation on the airline industry a decade ago. We believe our analysis of substituting the lower fee and lower capitalization, which directly affects amortization of the asset, to be an effective representation of the results to the bottom line. In the current low interest rate environment, using the lower fee of 20 basis points would result in a breakeven situation at the current volumes.

In review of the fee for service, while it would change the capitalization impact on the balance sheet, the results create such a loss that questions the viability to remain in the Servicing business especially considering the uncertainty of future costs to service.

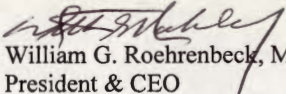
The MSR's impact on the Servicer's Balance Sheet with the Basil III limitations on the percentages that can be counted toward risk based capital requirements (if adopted by the United States) provides reasonable concern. If you step back and look at the dramatic changes already underway in the Servicing Industry towards valuing the servicing asset, fundamental changes have been realized already. When you look at servicing multiples in the years following FASB 140 and pre-meltdown, it was not uncommon to see multiples in the 5.5 to 6.5 range being capitalized across the country. Post-meltdown values with extremely low earnings rates show multiples have continued to move downward to levels of 3.5 to 4.5 times annual service fee, or 40% lower capitalization rates. While earnings rates may move up later and provide more cash flow potential, the Servicing Asset value will not recover to pre-meltdown levels as the industry has been forever changed to reflect the risks of buybacks, ever changing regulations, compensatory penalties, reputational risk, legal challenges in the courts and all around higher costs to do business.

Our conclusion is that the existing servicing fee compensation structure, with all the enhancements already identified, has positioned the industry to be much more viable than to reduce the revenue, which will cause market participants to exit the servicing business in pursuit of other investment alternatives, for return on its precious Capital.

The other major risk of making either of the changes being considered is to the Investors who will have their servicing concentrated in perhaps only a handful of supersized Servicers with worldwide access to less efficient labor costs to handle their MBS investment. The housing industry as we know it would no doubt suffer as well as causing there to be fewer Servicers to carry the load during the next potential market disruption.

Please leave the compensation model in use today unchanged as it is working appropriately even with all the new changes coming down the pike.

Sincerely,


William G. Roehrenbeck, Master CMB
President & CEO
Arvest Mortgage Company
Central Mortgage Company