



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

December 30, 2013

Mortgagee Letter 2013-46

To All Approved Mortgagees

Subject FHA's Tier Ranking System II; Final Notice and Responses to Comments

Purpose The purpose of this Mortgagee Letter is to announce the implementation of FHA's Tier Ranking System II (TRS II) and to provide responses to public comments. TRS II will be used to evaluate a mortgagee's compliance with FHA's Loss Mitigation guidance, default servicing regulations, and default reporting requirements.

Effective Date The results of the first TRS II rankings will be released no later than December 31, 2013, and will be based on the 12-month scoring period ending September 30, 2013.

Implementation of TRS II Round 1 of TRS II will be based on data collected from October 1, 2012 through September 30, 2013, in accordance with regulations at 24 CFR 203.605(b) which require that a 12-month period be used to evaluate a mortgagee's performance under FHA's Tier Ranking System. This evaluation will be utilized to determine which mortgagees are eligible for additional incentive payments during the January 1, 2014 through December 31, 2014, calendar year.

Changes to the TRS II Scoring Methodology Based Upon Public Comment The public comment period for the TRS II Mortgagee Letter published on June 12, 2013, closed on July 12, 2013. HUD received comments from FHA-approved mortgagees, a consumer advocacy group, and a legal aid organization. Updates were made to the TRS II methodology based upon the public comments received. All public comments, as well as HUD's responses, are contained in Attachment A, "Public Comments Received per Mortgagee Letter 2013-21."

In addition, the TRS II scoring methodology was updated using new default status codes delineated in Mortgagee Letter 2013-15.

Full details of the TRS II methodology, including scoring elements, grades, extra credit, and information about improving scores are provided in the TRS II Servicer Narrative at <http://portal.hud.gov/hudportal/documents/huddoc?id=spsnarrative.pdf>.

Issuance of TRS II Scores

On a quarterly basis, mortgagees will be provided their TRS II scores and grades, including case level detail as requested. The final fiscal year TRS II scores and grades will also be distributed at the end of the calendar year.

Notice of a mortgagee's TRS II score may be sent via email to those mortgagees that qualify for scoring, if at least one valid email address has been provided to HUD.

- Mortgagees may request to have their TRS II notices emailed to them by contacting sfdatarequests@hud.gov.
 - If at least one valid email address has not been provided, a hard copy notice of the mortgagee's TRS II score will be sent to the mortgagee's mailing address of record.
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Access to TRS II Scoring Data

Mortgagees can perform self-evaluations for improving their TRS II scores by accessing the data used in their scores via FHA Connection and Neighborhood Watch or by contacting the NSC at sfdatarequests@hud.gov.

Appeal Rights under TRS II

The appeal rights in 24 CFR 203.605(b)(3) are applicable to all mortgagees receiving a grade of "F," which is considered Tier 4 under TRS II.

Within 30 calendar days after the issuance date of the TRS II notice, a mortgagee that received a grade of "F" may appeal its grade to the Deputy Assistant Secretary for Single Family or the Deputy Assistant Secretary's designee and request an informal conference.

As a reminder, the only basis for appeal by the mortgagee receiving an "F" is disagreement with the data used by HUD to calculate the mortgagee's grade. If HUD determines that the mortgagee's grade of "F" was based on incorrect or incomplete data, the mortgagee's performance will be recalculated and the mortgagee's TRS II score will be corrected accordingly.

Information Collection Requirements

The information collection requirements contained in this document have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB Control Number 2502-0589. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB Control Number.

Questions

Any questions regarding this Mortgagee Letter may be directed to the HUD National Servicing Center at (877) 622-8525. Persons with hearing or speech impairments may reach this number by calling the Federal Information Relay Service at (800) 877-8339. For additional information on this Mortgagee Letter, please visit www.hud.gov/answers.

Signature

Carol J. Galante
Assistant Secretary for Housing-Federal Housing Commissioner

Attachment

Public Comments Received per Mortgagee Letter 2013-21

Comment: Generally, the scoring elements focus on the proper behaviors to reduce delinquency and improve loss mitigation engagement and compliance with HUD Regulations. At this time, there does not appear to be any crossover/duplicate scoring.

HUD Response: HUD appreciates the support of the commenter.

Comment: The Servicer Narrative is extremely clear in its overall explanation and specifically for the calculations (simple explanations for even the most complex calculations) and case level data is provided in an organized fashion and promptly upon request.

HUD Response: HUD appreciates the support of the commenter.

Comment: It is extremely helpful that HUD provides the case (loan level) data after the TRS II is issued for the quarter, but having it monthly would provide efficiencies to both HUD and the servicers. Since TRS II is on a quarter lag and since HUD must build the calculation, it appears it would be more efficient for HUD to create and for servicers to monitor if data was built and available monthly rather than quarterly. This would help servicers focus on appropriate areas and reconciliation efforts better for both HUD and the Servicers. Previous Mortgagee Letters on SPS indicate servicers are to rely on their internal reporting systems (especially challenging for the more complex calculations).

HUD Response: At this time, HUD is unable to provide the data monthly due to constraints on resources. As the calculations use data that is reported to HUD by the servicer, the servicer does have knowledge and access to what is utilized in the calculations on a monthly basis. Additionally, monthly case level data can be obtained from Neighborhood Watch and from FHA Connection for two of the four the scoring elements in their entirety. For the other two elements, pieces can be obtained from those same two systems. Several servicers have already accurately replicated the calculations using their HUD reported data.

Comment: Publish the TRS II according to schedule. Given TRS II uses data on a quarter lag, results for Quarter 3 (data from April, May, June) have past or are in motion (for some calculations) and results cannot be influenced. Though aggressive efforts continue to assist borrowers, engage them in Loss Mitigation, reduce delinquencies, and comply with all HUD regulations, access to the results timely will assist with efforts.

HUD Response: TRS II is issued after the quarter closes so proactively influencing that quarter's results can be achieved by 1) a general awareness of the elements and their fundamentals and 2) replication of the calculations. Servicers know that, in general, HUD is looking at the timeliness and appropriateness of foreclosure initiation, performance of loss mitigation after reinstatement, default reporting, and monthly loss mitigation engagement. Additionally, the narrative provides descriptions of the calculations so replication of HUD's calculations is possible.

Comment: As outlined in Mortgage Letter 2013-21, the evaluation period, once active, will be fiscal year (FY) 2013 and will determine incentives for the calendar year 2014. The commenter feels that because there may be changes based on the comments from the industry and because the scorecard is still in pilot for the majority of FY 2013, the first evaluation period should be the FY 2014, to determine incentives for the calendar year 2015.

HUD Response: HUD has advised servicers for two years that this scoring model may at any time become the basis for determining increased incentives. As outlined in Mortgage Letter 2013-21, HUD has established that FY 2013 will determine those increased incentives for calendar year 2014.

Comment: Currently, FHA is providing the scorecard approximately three months after the quarter ends. This delay makes it difficult for servicers to make timely corrections to improve their scores. The commenter would recommend a shortened timeframe so that scores are provided a month after the quarter ends.

HUD Response: FY13 Quarter 1 scores were issued three months after the quarter ended because of internal data processing. HUD still received the data that the servicers routinely provide, and so servicers could still use that same data to calculate their scores. Additionally, TRS II will always be issued after the quarter closes so proactively influencing that quarter's results can be achieved by 1) a general awareness of the elements and their fundamentals and 2) replication of the calculations.

Comment: Large servicers depend on HUD to deliver a neglected open defaults report on a monthly basis. After reviewing FY13 Quarter 1 data, one commenter discovered items that were not delivered with the reports, which influenced the commenter's neglected reporting rate. In addition, there were instances where the report was not delivered until the following cycle and thus the same items affected the neglected rate for two consecutive cycles. The commenter proposes that HUD provide the data more consistently and that the data be sent out automatically on a monthly basis rather than requiring a request from the servicer.

HUD Response: HUD has provided instructions to lenders on how to obtain the data from Neighborhood Watch without having to request this report from HUD. As a further step, for the larger servicers that may have issues obtaining this data from Neighborhood Watch due to size limitations of case level downloads, HUD is now consistently providing this report monthly to those servicers.

Comment: Both the Claims Without Conveyance of Title (CWCOT) and Single Family Loan Sale initiative (SFLS) programs are weighted in the Work-Out Ratio, which weights 25 percent of the Loss Mitigation Engagement element. However, both programs are essentially foreclosure prevention and have positive impact on the insurance losses. The CWCOT and SFLS programs are high priorities for FHA and can assist FHA, the servicer, and the borrower. The commenter proposes that HUD considers extra credit points to the Foreclosure Prevention score for servicers that participate in these programs.

HUD Response: HUD has acted on this recommendation and has provided for extra credit for FY 2013 for these programs and other initiatives that have had a positive impact on HUD's insurance fund. This information was sent to all servicers receiving scorecards on August 16, 2013, and servicers had until October 31, 2013, to submit their initiatives for consideration.

Comment: The TRS II system still lacks a clear avenue for homeowners to report on servicer non-compliance with FHA standards and loss mitigation. A complaint process can be added through a strengthened National Servicing Center (NSC). At this time, the NSC is only focused on solving individual problems and not addressing systematic issues from homeowners. Complaints from homeowners through the NSC should be part of the TRS II.

HUD Response: TRS II determines scores based on compliance with policy, regulations, and benchmark standards. There are no policy regulations or benchmarks established for customer complaints by which to measure compliance. Additionally, HUD follows industry standards in its complaint and resolution process for homeowners. TRS II is intended to be a quantitative and qualitative method of assessing compliance with delinquent servicing requirements. As such, the metrics cannot be based upon borrower behavior because that is not a standard constant.

Comment: HUD must impose meaningful consequences on noncomplying servicers. Either through TRS II or other rulemaking, HUD should improve loss mitigation performance by imposing penalties in individual cases of non-compliance with its loss mitigation requirements.

HUD Response: HUD agrees with this comment and will be working with those enforcement divisions within HUD to achieve this. With the implementation of TRS II, HUD will have the granular data required for referral to those divisions for meaningful consequences to be imposed.

Comment: Of all the elements used to calculate the final tier ranking score, the commenter sees the rating for "Loss Mitigation Engagement" as by far the most important. Unfortunately, the impact of this rating is diluted substantially by combining it with a great deal of other data that measure less critical information. In addition, the way in which the Loss Mitigation Engagement score is calculated needs further refinement. A short sale or asset sale should not be given equal weighting as a modification, and forbearances do not preserve homeownership.

HUD Response: Loss Mitigation is just one aspect of delinquent loan servicing that HUD has the ability to review both quantitatively and qualitatively. Not all borrowers qualify for nor want certain loss mitigation tools such as mortgage modifications. Some borrowers may specifically want a short sale. Some may qualify for a forbearance, which can be done early in the delinquency. Weighting cannot be applied as suggested because it depends on individual borrower qualifications and situations, and not upon the servicer.

Comment: The score for "redefaults" appears to be designed to control for option failures. However, the scoring terms define a "redefault" as the report of a loan in 90-day default status within six months of an option's implementation. This is an unreasonably narrow definition and likely results in a substantial underreporting of actual redefaults. The redefault score as currently formulated will not effectively track a servicer that routinely offers unworkable forbearances, and then forecloses without considering the borrower for more effective options.

HUD Response: This score as formulated does effectively identify those servicers that routinely 1) do not utilize these tools, 2) fail to reinstate the loan as expected, and/or 3) fail to perform the appropriate underwriting of the tool. Additionally, Foreclosure Prevention and not Redefaults evaluates whether or not the servicer attempted to work with the borrower on a more effective option prior to foreclosure initiation.

Comment: The weight given to the scores for “Foreclosure Prevention” and “SFDMS Reporting” further dilutes the usefulness of the final aggregate score as a measure of how effectively a servicer carries out its loss mitigation duties. The “Foreclosure Prevention” score gives overwhelming weight to the timing of foreclosure actions and very little weight to how effectively that time is used to consider loss mitigation options. HUD obviously must enforce standards for accurate record-keeping. A separate and distinct scoring system for accurate record-keeping would be appropriate. However, it would be much more useful for consumers and the general public if HUD produced scores and rankings that focused directly on loss mitigation performance. The reporting element in the scoring rewards a poorly performing servicer with a higher overall score because it fills out forms properly. The overall score thus becomes less useful as a tool for comparing servicer performance and targeting improvement where it is needed.

HUD Response: As stated previously, Loss Mitigation is one aspect of delinquent loan servicing that HUD has the ability to review both quantitatively and qualitatively, and while an important aspect, it is not the only aspect. Foreclosure Prevention is extremely important because foreclosures do happen, and it needs to be determined if servicers are initiating these actions in compliance with HUD’s regulations. SFDMS Reporting is very important because this data is key in assessing the effectiveness of HUD’s programs. Having all of these aspects in one unified delinquent servicing scoring model so that a servicer’s delinquent servicing as a whole can be evaluated is very important.

Comment: It is difficult to fully analyze the changes with so little detail provided within the recent servicer letter. Sizeable changes are being made to the TRS and right now, only four bullet points are provided to discuss the changes. These broad categories are not enough to fully comprehend the changes that are being made. Therefore, the commenter asks that more detail be given as to how these will specifically apply, as well as a more meaningful calculation, and again released for public comment.

HUD Response: Mortgagee Letter 2013-21 also referenced a servicer narrative posted on HUD’s website. This narrative goes into much more detail on calculations for each element and also includes suggestions to increase scores, helpful checklists, and more. This has been available to servicers online for at least two years. As this has been available, there is not a need to re-release this for public comment.

Comment: Under the current TRS, FHA does not take into account the size of the servicer or the size of its portfolio. This means that if a smaller servicer has one loan that receives a negative score, that loan can drastically affect the overall score.

HUD Response: Size of the servicer is taken into consideration for TRS II scoring. This size is based on the number of seriously delinquent loans a servicer has. Servicers servicing less than five seriously delinquent loans are not scored. Servicers servicing between 5 and 25 seriously delinquent loans have the option to opt out of the public availability of their scores and their number of seriously delinquent loans is considered in the Loss Mitigation Engagement element. Additionally, two of the other scoring elements have been carefully structured so that each case is scored individually on its performance so that servicing portfolio size has no bearing on the those scores.

Comment: In the SFDMS reporting calculation, there is a factor of five as part of the score equation. There is currently no description of why this factor exists, which calls into question the accuracy and legitimacy of the calculation. The commenter believes that the new TRS II should take into account some way to weight the score based on servicer portfolio size.

HUD Response: The factor of five was determined based upon the premise that a 2% fatal error rate was still indicative of “A” level performance, so 2% multiplied by 5 and subtracted from 100% is 90%, or an “A”. The portfolio size is indirectly utilized because the basis for determining the fatal error rate is the number of reported upon delinquent loans in a servicer’s portfolio.

Comment: If FHA wants all claims filed expeditiously, then a six-month average of claims should be used for the monthly score.

HUD Response: It was important that these calculations be based upon monthly activity. If there are an unusually high number of conveyances one month, the score can still recover much better than if numbers were averaged. A six-month average may actually have a negative impact on the score if there were a high number of conveyances one month.

Comment: A commenter takes issue with the timing and lag time of the scorecard. Currently, there is a six month delay from when reporting is submitted to when servicers receive the scorecard for that month. Servicers can utilize the reports that are made available in the FHA Neighborhood Watch within 30 days to calculate their own scores but must wait six months to validate the data.

HUD Response: As previously stated, TRS II is issued after the quarter closes, so proactively influencing that quarter’s results can be achieved by 1) a general awareness of the elements and their fundamentals and 2) replication of the calculations. Servicers know that, in general, HUD is looking at the timeliness and appropriateness of foreclosure initiation, performance of loss mitigation after reinstatement, default reporting, and monthly loss mitigation engagement. HUD is always available to discuss performance and to assist in verifying self-replication metrics put in place by the servicer.

Comment: If the goal of the SFDMS score is to change the behavior for the reporting, servicers should be able to test their files against known HUD logic.

HUD Response: Servicers have the ability to send test files to make sure their Electronic Data Interchange (EDI) transmission is functioning correctly. Additionally, HUD advises servicers to review their transmission files prior to sending to ensure that the reporting is occurring within logic parameters. HUD staff is always available for questions about default reporting, troubleshooting errors, as well as fatal error prevention.

Comment: The scorecard only provides insight into the servicing of a servicer's delinquent FHA loans and does not look at a servicer's overall servicing for all FHA loans.

HUD Response: HUD receives no data on the servicing of current loans, so at this time, it is not feasible to develop a scoring model that encompasses this. If in the future HUD obtains standardized data on the servicing of current loans, HUD will review it for the possibility of inclusion into either this or a separate scoring model.

Comment: The commenter believes that the Foreclosure Prevention calculation is flawed and does not set servicers up for success in this metric. In order for loans to score 100% in this metric, servicers must have approved and reported three different loss mitigation workout options as well as "Ineligible for Loss Mitigation." There are no accommodations made for deceased clients, unresponsive clients, or clients who are not interested in a workout option. This metric must take into account those loans where loss mitigation was successful in order to provide an accurate assessment of servicers' Foreclosure Prevention efforts.

HUD Response: While possible to capture four loss mitigation actions if proper reporting occurs, this metric has now been updated to include the new SFDMS status codes. Thus, the ability to capture four loss mitigation actions prior to foreclosure initiation is improved. There are accommodations made in the calculation for borrowers who do not occupy the property and who are unresponsive. A servicer that timely initiates foreclosure may receive a "B" level score; if a servicer performs and reports loss mitigation actions, the servicer may potentially receive a higher score. Successful loss mitigation is taken into account in the Loss Mitigation Engagement element.

Comment: A gradual increase from the current TRS threshold of 80% to 85% is recommended, as opposed to the 90%, which is outlined in the TRS II Servicer Narrative. Adjusting the threshold to 85% would help servicers account for factors that are out of their control such as the Foreclosure Prevention metric, which is unattainable, and negative impacts to performance as a result of Mortgagee Letter 2012-22.

HUD Response: The benchmarks were established in order to make the scoring process easier and more transparent. HUD will not be changing the benchmarks at this time but may consider this in the future if the need arises and as the scorecard evolves. In order to help servicers to better transition into these benchmarks and to help counteract any negative performance impacts from implementation of new policy, an additional extra credit opportunity has been provided for fiscal year 2013.

Comment: It is recommended that the logic for the Foreclosure Prevention component be revisited to account for realistic servicing expectations, as achieving the full amount of points available on this component is not possible.

HUD Response: The full amount of points was possible as servicers have already achieved a full 100% on many cases scored. However, the new SFDMS loss mitigation codes are now included in the logic and the logic has been streamlined so achieving full points is still possible.

Comment: In order to achieve the available five points on the Ineligible for Loss Mitigation score (AO), servicers would need to code every loan with a first legal date as being ineligible for loss mitigation.

HUD Response: This was the interpreted use of the AO code, that more often than not it should be reported on every loan prior to foreclosure initiation. With the implementation of the SFDMS AP status code, it still holds that most cases will have an AO or an AP (Ineligible for Loss Mitigation Due to No Response) reported prior to foreclosure initiation.

Comment: It is requested that HUD revise the logic to allow loss mitigation attempts that occur in the same month as the first legal date.

HUD Response: If loss mitigation is reported in the same month as the first legal filing, servicers do in fact get credit for this. What servicers do not get credit for is loss mitigation reported one month, loss mitigation reported the next month, foreclosure initiation reported the month after, and loss mitigation reported the month following that. This indicates that the servicer initiated foreclosure while the loan was actively in a loss mitigation tool. Correctly reporting the AQ option failure code is very important to this interpretation, as that breaks the cycle of active loss mitigation.

Comment: It is requested that HUD consider giving credit for loans coded as 08 (Trial Payment Plan) or similar type of an option that fails. Currently, if those types of options fail, they should be coded as AQ (Option Failure) and would not receive an AO, further preventing a Servicer from earning points on the eligible population.

HUD Response: Servicers do get credit for these codes. HUD also expects to see an AO/AP after an AQ, not one or the other.

Comment: It is requested that HUD consider credit to servicers for borrowers who are contacted and offered loss mitigation but are uncooperative or unwilling to work with the Servicer in curing the delinquency and for borrowers who are determined to be ineligible for loss mitigation due to no response (incorporate new Delinquency/Default Status Code of AP into the scoring logic).

HUD Response: HUD agrees, and with the implementation of the new SFDMS status codes, this scenario is incorporated into the logic.

Comment: It is requested that TRS I continue to be utilized until there are no longer negative impacts on scorecard performance from factors outside of the servicers' control to determine the tier ranking for calendar year 2014.

HUD Response: HUD will use TRS II as the basis for determining increased incentives for calendar year 2014. Accommodations have been made that includes incorporation of new SFDMS status codes as well as an additional extra credit opportunity.

Comment: In the “Implementation of TRS II section” of Mortgage Letter 2013-21, it states that “The first TRS II evaluation of mortgagees’ performance will be conducted for the quarter July 1, 2013, through September 30, 2013, and will be based on data collected from October 1, 2012, through September 30, 2013 in compliance with regulations at 24 CFR 203.605(b) which require that a 12 month period be used to evaluate performance. This evaluation will be utilized to determine which mortgagees are eligible for additional incentive payments during January 1 through December 31, 2014 calendar year.”

HUD Response: The original Tier Ranking System (TRS) evaluated activity for a rolling 12-month period. The cut-off for each evaluation period or “round” was the end of each fiscal year quarter. The incentive round occurred every fourth round. In this manner, the incentive round for TRS evaluated activity that occurred from October of the previous year through September of the current year, which is HUD’s fiscal year. TRS II is similar in that the fourth quarter of our fiscal year signifies the end of the performance evaluation period. All four quarters’ scores, and thus 12 months of performance, will be used to determine those servicers that may qualify for increased incentives for the following calendar year and will be issued after the conclusion of the fourth quarter.

Comment: It is requested that the language that was in the original Servicer Narrative, where it recommended 25% of a servicer’s staff receive delinquent servicing training, be retained, making it possible for larger servicers to earn extra credit.

HUD Response: Adjustments have been made to the extra credit available for training and for an additional extra credit opportunity for this fiscal year 2013.

Comment: It is requested that HUD consider not publishing the scorecard performance on their website. If HUD feels that it is important to establish a list of servicers by tier ranking, it is requested that HUD consider only posting the tier ranking and not the actual performance on the metrics. This approach would be similar to the way that Fannie Mae and Freddie Mac approach their scorecard results publication

HUD Response: HUD is considering this commenter’s suggestions.

Comment: The Reported Engagement Ratio (RER) component of the TRS II Scorecard is negatively impacted by reassessment requirements outlined in Mortgage Letter 2012-22.

HUD Response: Not all servicers interpreted the reassessment requirements the same way and as such, many servicers did not experience a negative impact to their Loss Mitigation Engagement score. As previously stated, accommodations have been made that include incorporation of new SFDMS status codes and additional extra credit opportunity that should help offset negative impacts to scores.

