

**Department of Veterans Affairs
Report to Congress
on Document Disclosure and
Consumer Education
Public Law 115-174, Section 309**



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Introduction

Section 309(d) of the Economic Growth, Regulatory Relief, and Consumer Protection Act (the Act), Public Law 115-174, directs the Secretary of Veterans Affairs to issue a publicly available report, not less frequently than once each year, that examines the following, with respect to loans provided to Veterans under chapter 37, title 38, United States Code (U.S.C.):

- The refinancing of fixed-rate mortgage loans to adjustable rate mortgage loans;
- Whether Veterans are informed of the risks and disclosures associated with that refinancing; and
- Whether advertising materials for that refinancing are clear and do not contain misleading statements or assertions.

The report must also include findings based on any relevant complaints VA received from Veterans and the Secretary's assessment of the refinancing market.

This report covers the period May 24, 2019, through April 9, 2020.

Background

Initial Concerns over Serial Refinancing/Loan Churning

The mission of VA's Home Loan Guaranty Service (LGY) is to maximize opportunities for Service members and Veterans (collectively "Veterans") to obtain, retain and adapt their homes by providing viable and fiscally responsible benefits in recognition of the Veterans' service to our country.

For many years, VA has partnered with other government agencies, including the Consumer Financial Protection Bureau (CFPB) and the Office of the Comptroller of Currency to address lender advertising materials that contain misleading statements or assertions. In November 2016, CFPB released a report detailing over 12,500 mortgage complaints from Veterans. The complaints ranged in topics such as misleading loan solicitations and lenders continuously communicating with Veterans even after a cease contact request.

A considerable amount of the complaints centered on lenders soliciting Veterans on refinance loan products. As a result, VA and CFPB issued in November 2017, the first joint Warning Order to Veterans who had a VA-guaranteed loan. Specifically, the Warning Order advised Veterans of the dangers associated with refinance loans that inaccurately purport items such as extremely low interest rates, the ability to skip loan payments or provide cash back.

Also, in 2017, stakeholder concerns relating to misleading advertising and serial refinancing¹ of VA-guaranteed loans prompted multiple Congressional inquiries and briefings. In October 2017, VA and the Government National Mortgage Association (GNMA) established a joint task force to examine the frequency of loan churning and predatory lending practices, to include an examination of the aggressive and misleading refinancing propositions outlined in CFPB's November 2016 report.² On December 7, 2017, the VA-GNMA task force issued a GNMA All Participant Memorandum (APM), which imposed a 6-month seasoning requirement for streamlined and cash-out refinance loans to be eligible for certain GNMA securities. This action strongly discouraged lenders from soliciting Veterans immediately after a VA-guaranteed loan closing because of the lengthened seasoning requirement for GNMA securities.

Shortly thereafter, in January 2018, VA announced its plans to issue a proposed rulemaking addressing churning practices and predatory lending in the refinance loan market.³ While the proposed rule was under development, VA sought to mitigate predatory lending practices by issuing administrative policy guidance. On February 1, 2018, VA published Circular 26-18-1, *Policy Guidance for VA Interest Rate Reduction Refinance Loans (IRRRL)*.⁴ The Circular advised lenders that certain loan disclosures should be provided early in the application process such that Veterans have the opportunity to make informed decisions and determine if an IRRRL is in their best interest.

On May 24, 2018, the President signed the Act into law. Section 309 of the Act, codified in part at 38 U.S.C. § 3709, provided new statutory criteria for determining when VA may guarantee a refinance loan. The Act required VA to promulgate regulations for certain cash-out refinance loans within 180 days, i.e., refinance loans where the principal balance of the new refinance loan is larger than the payoff amount of the loan being refinanced.

¹ "Serial refinancing" and "loan churning" are used interchangeably and reflect the practice of refinancing a mortgage multiple times within a short timeframe. Serial refinancing negatively impacts Veterans, often through increasing the principal balance, stripping equity from the home and increasing the loan-to-value ratio, which potentially raises the risk of loan default.

² VA Press Release: VA, Ginnie Mae Create Task Force to Address Mortgage Refinancing Issues. October 12, 2017. <https://www.va.gov/opa/pressrel/pressrelease.cfm?id=2962>.

³ Loan Guaranty: Revisions to VA-Guaranteed Refinance Home Loans. RIN 2900-AQ25. VA withdrew this proposed rulemaking in June 2018, following enactment of the Act. <https://www.reginfo.gov/public/do/eAgendaViewRule?publd=201810&RIN=2900-AQ25>.

⁴ IRRRLs are also referred to as streamline refinances. The terms are interchangeable in VA's program. https://benefits.va.gov/HOMELOANS/documents/circulars/26_18_1.pdf.

On December 17, 2018, VA published an interim final rule (AQ42) setting forth standards applicable to VA-guaranteed cash-out refinance loans.⁵ The rule became effective on February 15, 2019, and applies to all cash-out refinance loan applications taken on or after that date. VA notes that this rule did not conform to VA's existing IRRRL regulations to the Act. VA will, in upcoming months, provide additional rulemaking for IRRRLs.

Assessment of the Refinance Market

Between 2017 and 2019, the overall refinance market increased steadily in loan dollar amount and volume. This can be attributed to declining interest rates. According to Freddie Mac, in June 2019, the average rate on the 30-year fixed mortgage hit a 3-year low of 3.73%.⁶ This helped provide 8.2 million borrowers the ability to refinance and lower their interest rates by at least 75 basis points, according to Black Knight.⁷ As of June 2019, CNBC stated mortgage applications to refinance a home loan were up a striking 92% annually.⁸ According to the Mortgage Bankers Association (MBA)-*Economic and Mortgage Market Outlook Report*, prepared for the 2019 MBA Annual Convention, refinance originations in 2018 were 467 billion and increased to 793 billion in 2019.⁹ The chart below indicates the steady increase in refinancing loan balances from 2017 to 2019. This includes both refinance product types such as rate-term and cash-out.

ANNUAL MORTGAGE BANKERS PERFORMANCE REPORT 2019 DATA¹⁰			
LOAN BALANCES	2017	2018	2019
Refinancing	248,233	252,808	283,890
Rate-Term	260,789	266,697	301,282
Cash-Out	241,535	244,215	260,347

⁵ Loan Guaranty: Revisions to VA-Guaranteed or Insured Cash-Out Home Refinance Loans. RIN 2900-AQ42, 83 FR 64459 (December 17, 2018). <https://www.govinfo.gov/content/pkg/FR-2018-12-17/pdf/2018-27263.pdf>.

⁶ <https://www.cnbc.com/2019/07/01/8-million-homeowners-leave-cash-on-the-table-by-not-refinancing.html>.

⁷ Ibid.

⁸ Ibid.

⁹ <https://www.mba.org/news-research-and-resources/research-and-economics/forecasts-and-commentary/economic-commentary-archives>.

¹⁰ Annual Mortgage Bankers Performance Report (2019 Data).

Given the extensive advantages of the VA Home Loan benefit, there was a consistent increase in the number of VA loans guaranteed between fiscal year (FY) 2015 – FY 2017. In 2018, Public Law 115-174, *The Economic Growth, Regulatory Relief, and Consumer Protection Act* was passed. The requirements of the statute had an immediate impact on total loans guaranteed; specifically, refinance loans, which resulted in the reduction of the total loan volume. Thereafter, VA refinance loan volume contracted in FY 2018 from 160,051 to 145,188 in FY 2019. However, the impact of this event appears temporary, as VA guaranteed 90,532 cash-out refinance loans during the first 2 quarters of FY 2020.

VA Cash-Out and Other Refinance Loans Guaranteed by Fiscal Year

	2015	2016	2017	2018	2019
Cash-Out/Other Refinancing	114,222	136,911	169,038	160,051	145,188

Increased Streamline Refinance Loan Activity and VA Oversight

VA observes that while many of the public comments received in response to AQ42 predicted a contraction of the cash-out refinance loan market due to increased regulatory requirements, VA data does not reflect such long-lasting concerns. In this regard, in FY 2018, VA guaranteed 160,051 cash-out refinance loans. In FY 2019, VA guaranteed 145,188 cash-out refinance loans, and in the first 2 quarters of FY 2020, VA guaranteed 90,532 cash-out refinance loans.

While VA cash-out refinance activity remained steady since passage of the Act, the VA-guaranteed IRRRL (also known as a streamline refinance loan) volume rose dramatically. VA data reflects that VA guaranteed 67,347 IRRRLs in FY 2018, 94,861 in FY 2019, and 252,819 in the first 2 quarters of FY 2020. Much of this increase is likely attributable to a steady decline in interest rates, which have dropped approximately 1% over the past year.¹¹ As streamline refinance activity rose, VA undertook a systematic review of IRRRLs guaranteed since June 2018 to assess compliance with the Act’s statutory requirements regarding loan seasoning, net tangible benefits (i.e., interest rate requirements), and recoupment.

VA initially identified approximately 22,132 loans from 480 lending institutions determined to be potentially noncompliant with requirements established in the Act. Of the loans that VA identified as being potentially noncompliant, 21,584 did not meet recoupment requirements, 544 did not meet the interest rate reduction requirement and four did not satisfy the recoupment provisions of the Act. VA notified the lending institutions of the potential noncompliance, requiring each lender to review and validate

¹¹ [Ellie Mae Origination Insight Report](https://static.elliemae.com/pdf/origination-insight-reports/EM_OIR_FEBRUARY2020.pdf), February 2020. https://static.elliemae.com/pdf/origination-insight-reports/EM_OIR_FEBRUARY2020.pdf.

the data provided, self-report additional loans in their database that they believe to be noncompliant, and provide a plan to cure all deficient loans at no cost to the borrower. VA has reviewed and approved all lender plans to cure loan deficiencies and is currently conducting oversight of lender cure efforts to date. At present, VA has reviewed loans from 413 of the 480 lenders with non-compliant loans and completed oversight of 267 lenders who successfully cured loans validated as being noncompliant.

In reviewing lender plans and cases, VA determined a large percentage of loans from the initial data were incorrectly identified as being noncompliant due to the way lender data is reported to VA at the time of guaranty. VA subsequently issued additional reminders and guidance to assist all lenders in correctly calculating and entering recoupment information into VA systems. In addition, VA implemented preventative controls in its system of record to mitigate the risk of any lender incorrectly entering the data for loans guaranteed in the future. VA continues oversight work for the remaining lenders with a target completion date of June 30, 2020.

VA's Examination of Fixed-to-Adjustable-Rate Loan Transactions

Transactions where a fixed-rate housing loan is refinanced to an adjustable-rate loan represent a small percentage of VA's guaranteed loan portfolio. Since the enactment of the Act, VA guaranteed 365,819 IRRRLs and 289,345 cash-out refinance loans. Of those loans, less than 1% (848 loans) were to refinance a fixed-rate loan to an adjustable rate loan. For the period covered in this report, VA guaranteed 338,262 IRRRLs and 150,410 cash-out refinance loans. Of those loans, 27 loans were made to refinance a fixed-rate loan to an adjustable rate loan.

Understanding the Risks of Fixed-to-Adjustable-Rate Loan Transactions

Adjustable rate loans are often higher risk loans. Despite fixed-to-adjustable rate transactions representing a small percentage of VA's guaranteed loan portfolio, VA pays special attention to lending practices that target Veterans for such refinances. Generally, borrowers obtain adjustable rate loans to aid in affording a home for a short period, i.e., 3 to 5 years. However, adjustable rate loans have a higher risk of payment shock. An increase in the dollar amount that a Veteran owes for a monthly loan payment increases the probability that the Veteran will refinance again or even default. This increases the risk of serial refinancing or a foreclosure. Fixed-rate loans, on the other hand, provide a stable interest rate over the life of the loan and may provide more certainty in the long term.

Decreasing Veteran Risk through Disclosure

Because of the increased risk associated with fixed-to-adjustable rate loan transactions, VA believes it is imperative that Veterans fully comprehend the financial risks and outcomes associated with such refinances. Ensuring that clear information is provided to Veterans during the loan process will help Veterans better understand the financial

implications of the refinance loan. This will enable the Veteran to make more informed decisions about whether to proceed.

Even prior to enactment of the Act, VA required lenders to provide a loan comparison statement to Veterans who obtain IRRRLs. Through promulgation of AQ42, VA expanded this requirement to cash-out refinances. Under this regulation, lenders must provide a comparison statement and an equity statement to Veterans not later than three business days from the date of the loan application and again at loan closing.¹² Requiring lenders to provide Veterans this information on two separate occasions enables Veterans to better understand the cash-out refinance transaction, including fixed-to-adjustable rate transactions.

The comparison statement provides the Veteran with up-front information about the overall cost of the new loan. It compares loan data and costs associated with the existing loan, with data and costs associated with the proposed refinance loan. The equity statement informs the Veteran of the amount of home equity that would be removed from the property as a result of the refinance. The disclosure also explains that removal of such equity may affect the Veteran's ability to sell the home in the future. A Veteran must certify that he or she received these disclosures on both occasions. VA provided a sample disclosure to assist lenders in satisfying this regulatory requirement.

In addition to implementing and enforcing its own disclosure requirement, VA reviews lender compliance with CFPB-required disclosures, e.g., those specifically related to adjustable rate loans.¹³ VA's oversight process includes sampling loans for full file reviews. This process helps ensure that Veterans are provided with the required disclosures. If, during these reviews, VA does not see evidence of CFPB disclosures, VA can refer the case to CFPB for potential action.

Decreasing Veteran Risk through Oversight of Advertising Material

Lenders' advertisements or solicitations, regardless of form, concerning VA-guaranteed loans must not include any information falsely stating or implying that such advertisements or solicitations were issued by, or at the direction of, VA or any other department or agency of the United States.¹⁴ Lenders also cannot use such materials to falsely state or imply that the lender has an exclusive right to make VA-guaranteed loans.

VA routinely conduct audits to ensure that lenders comply with VA's statutes, regulations and policies, including those relating to loan advertising materials. When VA learns of lenders who violate VA's advertising standards, VA can act against such lenders, e.g., withdraw a lender's ability to automatically close VA-guaranteed loans.¹⁵

¹² See 38 Code of Federal Regulations (C.F.R.) § 36.4306(a)(3).

¹³ See 38 C.F.R. § 36.4312(d)(6); see also 12 C.F.R. § 1026.20(c) and (d).

¹⁴ See 38 C.F.R. § 36.4370.

¹⁵ See 38 C.F.R. § 36.4353.

For the period covered in this report, VA's Loan Guaranty Service has not taken severe punitive action, e.g., removal of automatic authority, against a participating lender for misleading advertising practices.

VA Findings on Complaints

As mentioned above, VA and CFPB issued a Warning Order in November 2017 that advised Veterans of the dangers associated with misleading solicitations and provided information on what to consider when receiving refinance materials from lenders. Both agencies published the Warning Order and took steps to disseminate the document, e.g., by sharing it on official social media platforms and informing news organizations, Veterans advocacy groups and lending industry trade groups of its publication.

CFPB's publicly available database reflects the receipt of 137 complaints relating to VA-guaranteed loans in calendar year 2019. This is a 38% increase from 2018 (99 complaints) and a 12% decrease from 2017 (112 complaints). In 2019, 28 complaints (or 20%) referenced misleading advertising and/or solicitations. Of the complaints submitted in 2018, 21% (21 complaints) referenced misleading advertising and/or solicitation. The most common complaint related to solicitations which invite Veterans to "skip" payments and refinance their loan. Another common complaint involved certain companies sending out mail that falsely appears to be from the Veteran's current mortgage lender. The solicitations claim that it is an urgent matter and to contact them immediately to refinance to a lower rate. More recently, from January 2020 through April 2020, CFPB received 35 complaints relating to VA-guaranteed loans. Five of these complaints referenced misleading advertising and/or solicitations.

On March 27, 2020, the President signed into law the Coronavirus Aid, Relief, and Economic Security Act (the CARES Act), Public Law 116-136. The CARES Act protects borrowers with federally backed mortgage loans who are experiencing financial hardship due to the COVID-19 national emergency. VA has recently been made aware of marketing materials promoting the so-called benefits of an IRRRL transaction when compared to forbearance available under the CARES Act. VA continues to monitor developments with respect to the Cares Act, relative to false and misleading advertising and the potential development of a wide range of unprecedented impacts on the VA Home Loan program and will continue to work with CFPB and the VA Office of Inspector General as appropriate.

Conclusion

VA and CFPB continue to inform Veterans that they might receive misleading solicitations from unscrupulous lenders. Both agencies are also continuing to help assist Veterans in understanding the costs and benefits of refinancing their existing loans. VA encourages Veterans to contact VA with any concerns or questions about advertising materials they receive.

Veterans who have questions about refinancing or other home loan issues may contact VA through email or telephone to speak directly with a VA representative. VA Loan Specialists are readily available to provide information to lenders and Veterans. The availability of VA Loan Specialists to assist Veterans and lenders reflects the commitment by VA to provide the highest level of customer service. Congress enacted section 309 of the Act, in part, to assist Veterans in securing refinance loans that are in their best financial interest. VA appreciates the opportunity to implement Congress's objective, thereby improving the financial outlook for our Nation's Veterans.

Department of Veterans Affairs
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