RE-ENGINEERING STUDY OF LOAN GUARANTY

DEPARTMENT OF VETERANS AFFAIRS
UNITED STATES OF AMERICA

VETERANS BENEFITS ADMINISTRATION

SEPTEMBER 8, 1992

I. BACKGROUND

A. Scope of this Study

On May 11, 1992, the Chief Benefits Director met with a task force composed of field and Central Office personnel from Loan Guaranty, with representation also from the Assistant CBD for Information Resources Management (20M) and the Assistant CBD for Planning (20P). (See Attachment E.) He gave us a charge: rethink, or "re-engineer," the Loan Guaranty program, from top to bottom, from start to finish. Given the fact that this program is mandated by Congress as a housing benefit for veterans, we were challenged to recommend ways in which the program might be restructured to provide better, more economical service to our veteran customers.

The task force was not charged with proposing fundamental changes in the program (i.e. no new legislative initiatives), nor were increased resources promised. We were, however, challenged to take a fresh look at the program in the light of the new technologies which are becoming available. The following pages represent the findings and recommendations of the team members on how the Loan Guaranty program can be restructured and redesigned (re-engineered) to provide better service to veterans in the most cost-effective manner possible.

B. Challenges Facing Loan Guaranty

While the Department of Veterans Affairs takes great pride in the integrity and efficiency of its Loan Guaranty program, the passage of time and our desire to improve service to our veteran customers mandate that we periodically examine our operations to determine if we are providing the most complete, compassionate and efficient service possible to our veteran constituency.

The general goal of Loan Guaranty, i.e. to provide the housing benefit to qualified veterans, has been further specified as follows:

Outreach: To encourage veterans and their spouses, members of the housing industry, and members of the lending industry to participate in the program.

Credit Assistance: To provide timely credit assistance to eligible and qualified veterans who are acquiring, altering, selling, or refinancing their homes.

Grants: To provide timely specially adapted housing grants to all eligible veterans who are acquiring specially adapted housing or are altering their permanent residences.

Valuation: To appraise properties in a timely and accurate manner in order to establish the reasonable values for the purposes of financing proposed or existing homes, financing alterations of homes, refinancing existing homes, or liquidating securities for loans.

Habitable Homes: To ensure that veterans and their families acquire safe, sound, and sanitary homes which are free from hazards affecting livability.

Loan Servicing: To assist mortgagors in retaining their homes by providing timely primary servicing for VA portfolio loans or supplemental servicing for guaranteed or insured loans in order to cure the maximum number of delinquent loans while minimizing the government's liabilities.

Claims: To minimize losses to concerned parties when loan defaults are insoluble, by using the most economical and expeditious means of terminating loans.

Cost Recovery: To obtain through the timely sale of acquired properties the maximum recovery of costs incurred by the VA and associated with the acquired properties.

As perceived by this task force there are several areas which require action to provide opportunities to bring our operations into line with contemporary business practices in the industry or to remedy persistent problems with service delivery, such as inability to provide consistently timely, quality service. These areas of challenge are divided into three main areas of discussion. Those are (1) opportunities for improvement of the work processes themselves, (2) an examination of the potential for improvement in the geographic locations of the workforce, and (3) a discussion of the lines of authority which would best serve veterans by improvement of the delivery of Loan Guaranty benefits.

VA's experience with the real estate finance industry has resulted in an understanding of industry expectations of our products and services. It is important to provide accurate and efficient delivery of our products and services. Participants must be confident that they have easy access to our services with little "red tape." Information and training on the loan program are critical to the ability of some participants to meet program guidelines. We also see a need to develop and maintain compatibility with emerging technologies which our participant customers will be employing in their operations.

Despite the initiation five years ago of a very proactive program to modernize the ADP resources supporting the Loan Guaranty program, we continue to trail the industry we must work with in this vital area. VA must improve the availability of automated assistance to workers in the field and make possible speedy, reliable, electronic communications with the lending industry if we are to continue to be a viable factor in the home loan market. Because VA represents less than 10% of the home mortgage market, we cannot impose our technology on the industry, but must bring ourselves into correspondence with the direction of technological change as it occurs.

The geographic distribution of our workforce is a reflection of our historical beginnings and the market as it existed in the late 1940's. The present decentralization of all aspects of the Loan Guaranty operation does not reflect the realities of the present market or the composition of the private sector which directly provides most of the housing benefits to veterans. The present situation appears to produce frequent inconsistencies in our dealings with veterans and program participants. Those inconsistencies tend to reduce acceptance of our product in the market and thus lower the number of veterans served. Additionally, the present workforce configuration appears to make both economies of scale and proper internal control procedures virtually impossible at some of the smaller regional offices.

Finally, this is an opportunity to examine the present organizational lines of authority with an eye to improvement of service delivery. Any such examination and discussion must center upon the ability of the Veterans Benefits Administration in general, and the Loan Guaranty Service in particular, to react to the conditions of the home loan mortgage market in order to improve service to veterans and program participants. The areas in which VA appears to be weak at this time are providing a unified position at times of policy and procedural change and redistributing resources in times of rapid market fluctuations.

C. For Nearly 50 Years

The home loan program was originally conceived in 1944 as part of the Nation's response to the economic problems facing returning service men and women at the close of World War II. Millions of these men and women had spent years at war, with no opportunity to accumulate the cash or credit which would enable them to become homeowners. The provisions of the law have been modified numerous times over the nearly 50 years since then, but the basic intent remains the same: veterans who have met the criteria of military service established by law are offered assistance in purchasing a home, with the VA guaranty generally substituting for a mortgage downpayment. Traditional underwriting criteria are modified somewhat to fit the unique needs of returning veterans, and special steps are taken to enable financially troubled veterans to retain homeownership.

Cumulatively through March, 1992, the VA guaranty has enabled private lenders to extend approximately $374 billion in mortgage loans to over 13.3 million veterans to purchase or construct homes. Figures 1 and 2 depict the trends over the last dozen years in numbers of loans closed, defaults reported, claims filed, and properties on hand.

FIGURE 1. GI LOANS CLOSED

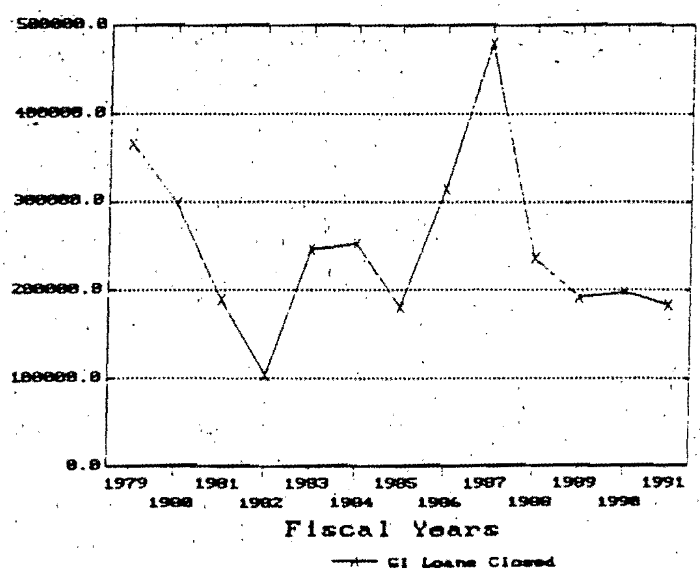
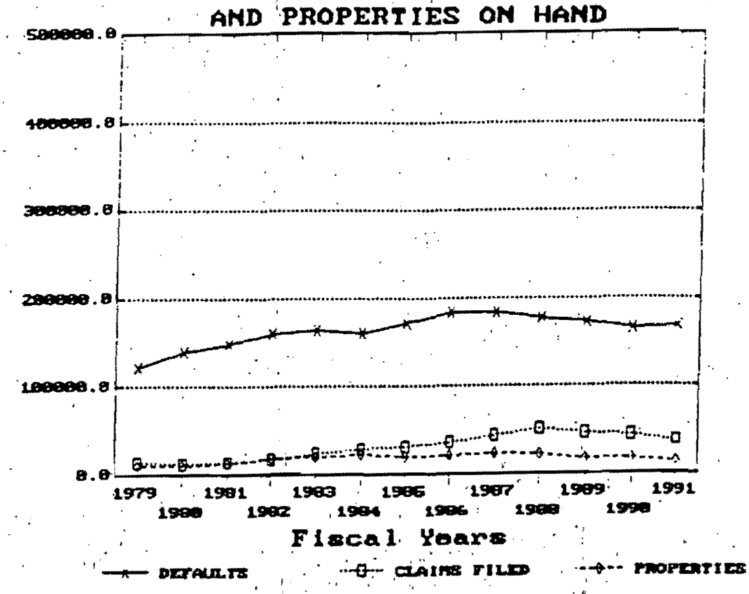
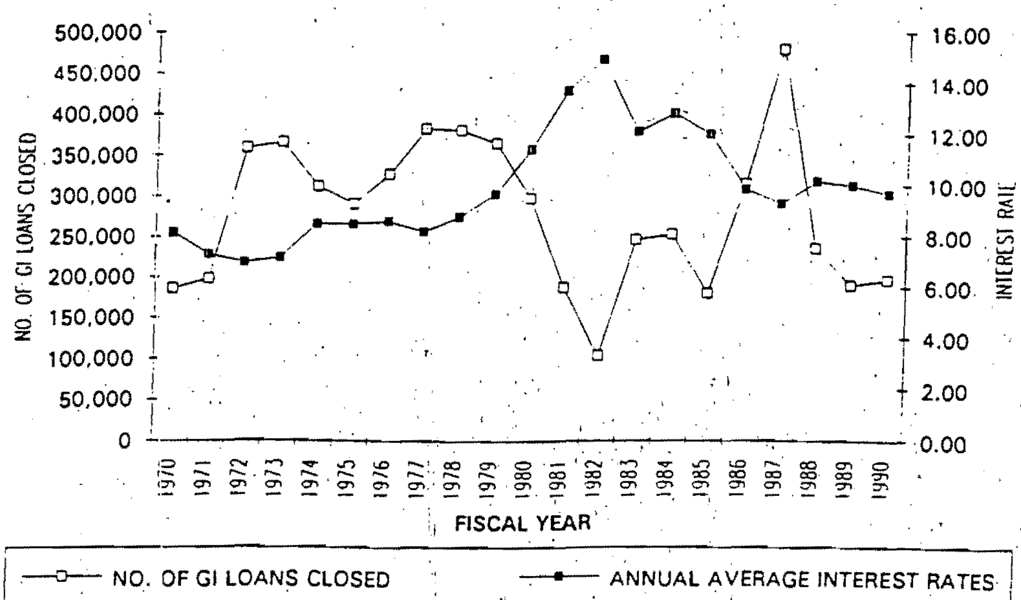


FIGURE 2. GI DEFAULTS, CLAIMS AND PROPERTIES ON HAND



The extreme volatility of loan origination workload is evident on a national scale, and is related inversely to mortgage interest rates (Figure 3). Defaults, foreclosures, and property acquisitions have been equally volatile, although on a regional, rather than a national, basis. In the past decade, for example, our country has experienced a series of local recessions: first the "Rust Belt" in the Midwest, then the "Oil Patch" in the Southwest, then New England.

FIGURE 3. AVERAGE ANNUAL INTEREST RATES & NUMBER OF GI LOANS CLOSED, 1970-90



D. How Loan Guaranty Operates

The veteran's primary housing benefit is the GI home loan program, which provides partial guaranty on loans made by private lenders to veterans for purchasing homes, condominiums or manufactured housing units. The program operates by substituting the guaranty of the Federal government for the investment protection afforded under conventional mortgages, which require a downpayment and/or private mortgage insurance. Over 80% of the purchase loans guaranteed by VA have no downpayments.

VA relies heavily on private individuals or firms in providing this benefit. Generally, veterans locate a home they wish to purchase through contacts with real estate agents who are very familiar with the GI home loan program. Real estate agents usually help veterans find a mortgage lender who will process the loan. In most cases VA has limited or no contact with the veterans in processing these loan applications.

Operating in 46 Regional Offices, Loan Guaranty services are provided within four functional areas: Construction and Valuation, Loan Processing, Loan Service and Claims, and Property Management. In 1991, approximately 36 percent of program FTEE were devoted to the appraisal and loan processing function. The remaining 64 percent of Loan Guaranty employees have been involved in the servicing of delinquent loans, foreclosures and property management.

1. Construction and Valuation

When a veteran decides to buy a home, the veteran or his/her lender will request an appraisal of the property to be purchased.

VA will assign an independent professional fee appraiser to conduct a formal appraisal of the property which will secure the loan. Most appraisal reports are subsequently reviewed by VA staff for acceptability. Based on the appraisal report and data in VA files, a Certificate of Reasonable Value (CRV) is issued, which sets a limit on the maximum loan VA will guarantee. The CRV also provides vital information to the veteran regarding the value of the property in relation to the list price. Because timeliness is critical in real estate transactions, VA has established a target time standard of 20 days after the initial request for the issuance of the CRV.

Under an alternative process, the Lender Appraisal Processing Program (LAPP), VA also assigns the fee appraiser. However, the fee appraiser's completed report is forward to the lender, not VA, for review by the lender's VA approved staff appraisal reviewer (SAR). The lender's SAR performs the same basic process as a VA staff appraiser; however, in setting the maximum loan amount the lender issues its own notification of value to the veteran and not a CRV. The LAPP lender can then close the loan on the automatic basis. The principal benefit of LAPP is to speed the time to loan closing for veterans.

2. Loan Processing

Concurrently, the lender will assist the veteran in obtaining a Certificate of Eligibility from VA, if one was not previously obtained, and develop the case, i.e., obtain verifications of employment, deposits, credit history, etc. In approximately 88 percent of the cases, lenders will close GI loans on an automatic basis, i.e., without prior approval of VA. In these cases, the closed loan package with appropriate documentation is submitted to VA which reviews the case and issues a guaranty certificate to the lender. For the other 12 percent of the cases, lenders submit the loan application to VA for prior approval. VA reviews the case and issues a commitment to guarantee the loan when it is closed. After closing, the lender submits a loan package to VA to obtain the guaranty certificate. The LP system automatically generates Certificates of Guaranty and commitment letters, as well as workload activity reports.

When VA issues the guaranty certificate, the veteran is mailed a pamphlet which explains his or her obligations to the lender and VA, and provides guidance regarding maintenance of the property, what to do if financial difficulties occur, and how to arrange the subsequent sale of the property. As long as the veteran makes regular mortgage payments to the lender, this will be the extent of service provided in most cases, although additional contacts with veterans occur when they call or write VA with questions about their loan or to request release from liability, incident to the sale of the home.

3. Loan Service and Claims

VA is notified by lenders that veterans are delinquent on their guaranteed loans when the third consecutive payment is missed. Lenders inform VA of the reason for the default and what servicing actions have been taken by the lender. VA then codes the default into the Liquidation and Claims System (LCS), which automatically generates servicing letters to the borrower emphasizing the serious nature of the situation and encouraging the borrower to contact VA. The lender/servicer continues to have primary responsibility for servicing the default. VA also attempts to make personal contact (usually by telephone) with the borrower. These personal contacts are the most effective means of finding cures for defaults. In appropriate cases, VA may intercede on the borrower's behalf and obtain a forbearance agreement or arrange a reasonable repayment schedule. Also, VA may contact local agencies that provide assistance in finding jobs for borrowers or aid with their daily subsistence needs, or help in making mortgage payments.

If no arrangements for reinstatement are made the lender/ servicer sends VA a Notice of Intention to Foreclose. VA regulations preclude the initiation of foreclosure for an additional 30 days to allow VA more time to find a solution to the veteran's problem. VA servicing continues even after foreclosure has begun, to explore every possibility to assist the borrower. These include refunding (purchasing the loan from the lender), accepting a deed-in-lieu of foreclosure, and encouraging a private sale of the property even at less than the amount owed on the VA loan. The goal of the Loan Service and Claims function is to help veterans to retain their homes and avoid financial loss and to protect the government's interests by minimizing claim payments and property acquisitions.

4. Property Management

In the event that foreclosure cannot be prevented, VA will pay a claim under the guaranty and, in approximately 90% of cases, acquire and ultimately resell the property securing the loan. VA's property management function provides the principal source of funding for the Loan Guaranty Program through sale of acquired properties on both a cash and vendee loan (VA financed) basis.

The primary purpose of the VA Property Management program is the sale of acquired properties at prices which will result in the maximum recovery of the Government's investment in these properties. VA utilizes the services of local brokers in the management and sale of properties which are owned or are to be acquired by VA. When a property is conveyed to VA, it is assigned to a management broker for custodial care. Management brokers are responsible for making periodic inspections of properties and recommending to VA the need for repairs and other expenditures.

When a property is assigned to a management broker, he/she makes an initial inspection of the property and prepares a report which indicates the condition of the property and the property value based on comparable properties in the neighborhood. VA staff will then complete an analysis of the property based on the management broker's information, in-file data, previous appraisals, and other staff inspections. A determination is then made as to whether a repair program will be undertaken. If the decision is made to repair the property, repair specifications are prepared and bids are solicited. The management broker is responsible for supervising repairs while they are in progress and certifying to VA that they have been satisfactorily completed. Once the repairs are completed, the property is ready to be listed for sale.

Independent sales brokers negotiate the sale of properties listed by VA. When offers are submitted with acceptable terms and conditions, and in conformance with the listings, they are held for an interval following the date of public appearance of the sales listing. A preliminary credit analysis is then made and those offers requiring VA financing which are clearly unacceptable from a credit standpoint are rejected. The others are retained for further consideration when the credit reports, employment verifications, and other supporting information are received. Upon receipt of all required information, Loan Guaranty personnel complete a formal underwriting analysis. If more than one offer is being considered, a comparison of these offers is made, and the one found to be in the best interest of the VA, based on established criteria, is accepted. After approval and execution by VA, the purchaser and sales broker are given appropriate notification. VA prepares the instruments required for closing the sale. Once the sale is closed and the necessary documents are recorded, all required papers are returned to VA. Currently, VA finances about 70 percent of acquired property sales, with the rest sold for cash or financed by non-VA sources.

5. Specially Adapted Housing

VA also provides housing benefits to disabled veterans in the form of specially adapted housing (SAH) grants, direct loans and loan guaranties. Housing grants are made to permanently and totally disabled veterans to assist in acquiring new or existing housing units which are adapted to meet the needs of these veterans, e.g., wider doorways and ramps to accommodate wheel chairs. The grant may not exceed one-half of the purchase price of the dwelling up to a maximum of $38,000. Grants up to a maximum of $6,500 are also available to veterans with service connected blindness or the loss or loss-of-use of both upper extremities. Normally, veterans obtain VA guaranteed loans to purchase homes in connection with SAH grants. However, if veterans are unable to find guaranteed loan financing, VA will make direct loans up to a maximum of $33,000 to supplement the grant.

Personal service to the disabled veteran begins when the Adjudication Division notifies the Loan Guaranty Division that a disabled veteran has been determined to be eligible for an SAH grant. Loan Guaranty then forwards an application to the veteran with a notification of his/her basic eligibility for benefits. When the veteran returns the application, Loan Guaranty personnel arrange for a personal interview, usually at the veteran's residence. During this interview, VA discusses the veteran's housing plans or desires and the entire SAH process is explained in detail. If the veteran elects to go ahead with a home purchase or an adaptation of an existing property, a Specially Adapted Housing agent from the Loan Guaranty Division assists the veteran through each step, i.e., selection of property, contract negotiations with builders or contractors, review of plans and specifications, compliance inspections, escrow of funds and final disbursement. The SAH grant program often requires several hundred man-hours over a 3-6 month period to complete a single case.

E. Who Does the Work?

The work of administering the Loan Guaranty program, which is a unique partnership of government and private lending institutions, is conducted by approximately 2,000 Loan Guaranty personnel in 46 regional offices. A detailed breakout of Loan Guaranty FTEE is found on page B-3 of this report. As of May, 1992, field personnel were allocated as follows. Note that the Office of the Chief in some cases includes indirect labor for all functions.

Office of the Chief	213.7 FTEE
Construction & Valuation	310.5 FTEE
Loan Processing	338.6 FTEE
Loan Service & Claims	680.1 FTEE
Property Management	401.4 FTEE
Files	58.8 FTEE
Total	2,003.1 FTEE

The Central Office Loan Guaranty Service functions in a staff role to the Chief Benefits Director, recommending policy and providing program oversight. Training for regional office personnel is provided in a number of ways: on the job training, a centralized technician training program, OPM training courses, a few accounting courses made available free by the Treasury

Department's Financial Management Service, and locally available courses in real estate, finance, and appraisal principles.

F. Where is the Action?

Because the housing benefit is more likely to be exercised by relatively young veterans, and is strongly affected by local economic conditions, the Loan Guaranty workload is not distributed strictly along the lines of veteran population. Loan origination workload varies dramatically with fluctuations in the mortgage interest rate, while defaults and claims are influenced primarily by the local economy. Attachment A ranks the stations by order of volume of loan originations in FY 1991, by order of defaults reported in FY 1991, and by size of the Loan Guaranty division.

G. Loan Guaranty is Unique in VA.

Unlike other Services within VBA, it is impossible to predict Loan Guaranty workloads with any precision. The real estate market is tied to the local economies of thousands of communities. Market interest rates fluctuate based upon scores of unforeseeable variables. Plant or base closings, layoffs, or the peaks and valleys of the cyclical real estate market are virtually impossible to anticipate on a national level.

Because the government provides a guaranty to private lenders (rather than making the loans directly), Loan Guaranty has a unique relationship with the private sector. In this case, the VA housing benefit is actually provided by the private sector, with support from the government. All other VA benefits, from vocational rehabilitation to pension checks, are provided directly by VA to the veterans. This means that VA depends on its program participants to take initiative in providing this benefit; this action will be taken, of course, only if the lenders can receive a reasonable profit for their efforts. Anything which works against the interests of the lenders will make them less willing to provide the benefit; anything which makes it easier or more profitable will encourage them to make GI home loans available to veterans. It is the challenge of Loan Guaranty to balance the interests of the veteran, the government, and private sector participants in such a way that none will be harmed and all will benefit.

Because of this voluntary involvement of the private sector, VA needs to constantly "sell" the program not only to veterans, but also to lenders and to real estate brokers, who are the single most influential group affecting the choice of mortgage financing. Efforts to change the way we do business must be carefully coordinated with the requirements of our program participants, since VA's market share is too small (less than 10%) to require the market to adjust to us. We must work toward industry standards for ready acceptability.

At the same time, it is sometimes the perception of Loan Guaranty personnel both in the field and in Central Office that the program needs to be constantly "sold" within VA as well. Loan Guaranty personnel for years have felt that they were considered "outsiders" by the rest of the agency, who often were less than sympathetic to the unique requirements of the program.

II. ANALYSIS OF FACTORS AFFECTING THE LOAN GUARANTY PROGRAM

A. Factors External to VA

1. Economic Conditions

To a large extent, future changes in the workload of the Loan Guaranty program will be driven by forces external to VA, primarily external economic factors. To the extent that mortgage interest rates vary, a greater or lesser number of eligible veterans will be able to afford a home mortgage in a given year. In turn, the interest rate and current economic conditions will also affect the rate of foreclosure of existing mortgages. In times of economic downturn, higher rates of bankruptcies, job losses, unemployment, and property depreciation will result in fewer loan originations and a greater rate of foreclosures.

Local economic conditions also play a large role in the potential workload of the Loan Guaranty program. Even with similar national mortgage interest rates, local economic conditions and investment and banking practices can result in varying rates of loan originations and foreclosures from area to area. While these effects may tend to cancel each other out or lessen somewhat at the national level, fluctuations in workload may be dramatic at the local or regional level. For example, the severe recession in the energy industry in the southwestern United States during the mid and late 1980's resulted in heavy foreclosures of GI loans in that region.

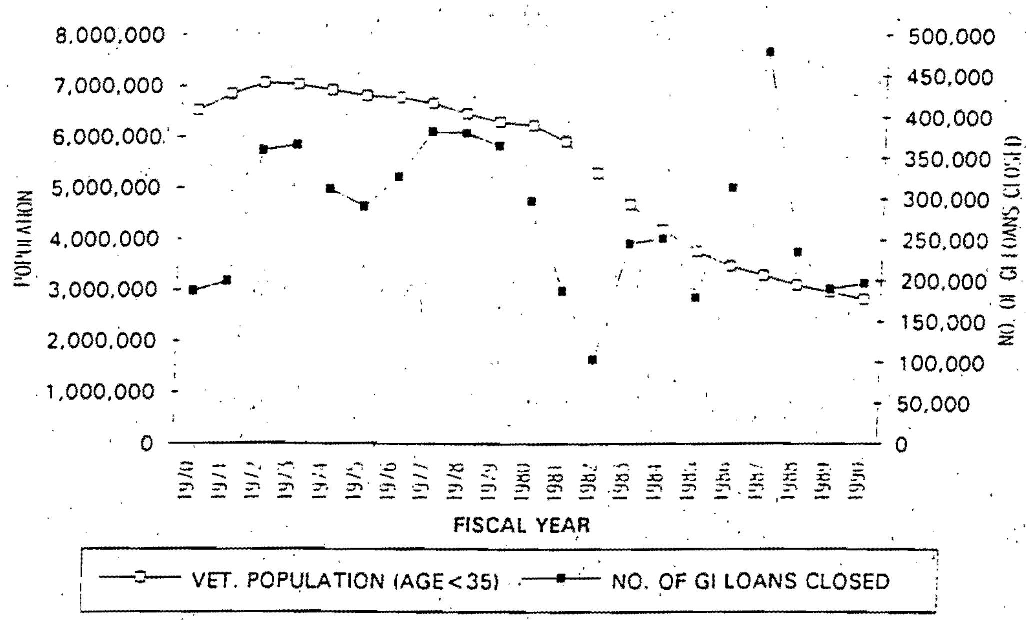
While it is difficult to predict future economic trends, the announcement of closings of automobile plants in the Midwest and continued competition from Japan and the newly-united European nations, indicate that structural changes in the U.S. economy will continue, with local, regional, and perhaps national implications for VA's Loan Guaranty program.

As shown in Figure 3, the fluctuations in the number of GI loans closed from year-to-year are related to changes in mortgage interest rates. In general, these two trends are a mirror image of one another: as interest rates go up, the number of GI loans closed goes down. However, the overall number of loans closed has declined over the period as well. An average of 315,000 loans were closed during the 1970 to 1980 period, in contrast to an annual average of 233,000 loans during the 1981 to 1991 period.

2. Veteran Population Trends

While interest rates and local economic conditions are important factors, the future workload of the Loan Guaranty program will also be affected by changes in (1) the veteran population, (2) eligibility standards, and (3) the degree to which veterans choose a VA mortgage over other options (usage rate). As shown in Figure 4, the veteran population aged under 35 (those most likely to buy a home under the VA loan program) was also declining during this period. This is due to the aging of the Vietnam and Post-Vietnam veterans, and the reduction in the size of the standing military.

FIGURE 4. VETERAN POPULATION (AGE<35) & NUMBER OF GI LOANS CLOSED, 1970-90



The size of the veteran population eligible to elect a VA mortgage is affected by the number of active-duty military personnel (potential new veterans). The Department of Defense has announced a planned 21 percent reduction in the active duty military forces, and an 18 percent reduction in the total selected reserve forces from 1990 to 1997. Over the drawdown period, the increased number of separations from the military (relative to recruits) could result in an increase in the number of VA loans. However, with a smaller standing military, the number of persons eligible for VA loans will remain at a lower level than in the past, resulting in fewer potential applicants over time.

3. Eligibility

Eligibility standards can also affect the number of persons who can potentially apply for a VA loan. The service requirements have changed over the years, ranging from 90 days of active duty during wartimes to up to 24 months during times of peace. The advent of the Persian Gulf War (August 2, 1990 to present) brought another change to the service requirements. However, this change had little overall effect on the number of veterans eligible for home loan benefits since many of the active duty personnel would have become eligible for home loans anyway. Only a small number of reservists and National Guard members who had no prior military service became eligible for the Loan Guaranty program as a result of being called up for Persian Gulf War service.

4. Usage Rate

The usage rate of VA loans will also affect the future workload of the VA Loan Guaranty program. The 1990 Census data indicated that approximately 7.7 percent of all mortgages on owner-occupied units were VA loans. VA's market share over the last decade has averaged somewhat less than ten percent of all mortgages.

Clearly not all veterans use the VA loan program. According to data from the 1987 Survey of Veterans, 34.3 percent of veterans responded that they had used the VA Loan Program during their lifetime. Of those veterans with mortgages, 31.8 percent used VA to finance or refinance their home, 5.0 used FHA, 0.5 percent used FmHA, and 55.6 used conventional or other financing. Of the total veteran population, 14.3 percent reported current use of a VA mortgage to finance or refinance their home.

The main reason given for not using a VA home loan was "no need for a VA home loan" (20.5 percent), followed by "other financing preferred" (17.8 percent), "did not know I was eligible" (8.9 percent), and "too long to process VA loan" (8.5 percent). Clearly, several factors come into play as a veteran considers whether to purchase a home through the VA home loan program.

5. Relative Value of VA Loans

As the VA Loan Guaranty program was established as a veteran benefit program, several advantages accrue through participation. Short-term benefits include reduction of up-front cash requirements to purchase a home, as no downpayment is required for a VA loan, and closing costs are reduced as all points are paid by the seller rather than the veteran. By reducing up-front cash requirements, the VA loan program enables those veterans who do not have the initial cash needed for FHA or conventional financing to purchase a home with a VA loan. In addition, VA credit standards emphasize use of residual income guidelines as indicators of loan acceptability rather than strict reliance on debt-to-income ratios such as those used for FHA and conventional loans. This allows a greater degree of flexibility to be employed when qualifying a veteran for a VA loan.

The relative value of VA loans to other loans is a dynamic situation. The interest rate for VA loans is generally set at about one/half percent below conventional loans. However, the VA's rates fluctuate somewhat less rapidly than market rates, so that for certain periods, the actual difference may be more or less. In addition, in 1989 PL 101-237 Title III, the Veterans' Home Loan Indemnity and Restructuring Act of 1989, established a loan fee of 1.25 percent for the veteran making no downpayment, with some exceptions. To the extent that funding fees increase, the relative value of VA loans compared to other loans will decline. Changes in the relative value of VA loans will also occur as a result of changes in other loan programs. As an example, VA loans became more attractive when FHA raised closing costs to remain self-sustaining.

Deciding whether to choose a VA loan is not based entirely on strict financial accounting issues. First, as mentioned above, the veteran must know about the program and determine that he or she is eligible. The potential customer (the veteran) must also take into account real or perceived delays in loan processing, and evaluate advice given by the seller or real estate agent regarding the relative merits of a VA loan.

6. Program Funding

Unlike commercial loan programs, the VA home loan program was not mandated to be financially self sustaining. Having its roots in the original GI Bill, program expenses were funded from 1944 to 1961 through annual appropriations. In 1961 the Loan Guaranty Revolving Fund was established. Through this fund, receipts, which had originally been returned to the U.S. Treasury, were now deposited into the fund and were made available for ongoing expenditures. The loan program had transfers or appropriations to offset program expenses for the first 21 of the 23 years of its existence.

However, for the period FY 1968 to 1977, the loan program operated without transfers from the Direct Loan Revolving Fund or appropriations. This relatively favorable revolving fund performance was a reflection of the following economic conditions: a relatively stable economy, a maximum GI mortgage interest rate of 7-9 percent, low foreclosure and unemployment rates, and appreciating real estate values averaging 10.9 percent annually.

In the late 1970's worsening economic conditions, reflected in loan interest rates of up to 12 percent (with a peak of 17.5% reached briefly in 1981), increased unemployment, and a sharp recession in 1980-82, resulted in increased VA foreclosures. From FY 1962 to FY 1983 over $1.0 billion were transferred from the Direct Loan Guaranty Revolving Fund as expenditures exceeded receipts. Since the end of FY 1983 almost $3.1 billion in external financing (transfers and appropriations) have been necessary to support the Loan Guaranty Revolving fund. The Direct Loan Program was suspended in 1981, and thus could no longer support the Loan Guaranty Program.

Recent legislation has had the effect of restructuring the funding and appropriation process for the Loan Guaranty program. As part of the Veterans Home Loan Indemnity and Restructuring Act of 1989, a new Guaranty and Indemnity Fund was established for loans closed on or after January 1, 1990. The veteran pays a loan fee into this fund; the government also contributes to the fund for each GI loan. Other provisions were added that generally tightened the terms of VA's loan program. The Credit Reform Act, which went into effect in FY 1992, ensures that the total lifetime costs for the set of loans made during a given year (under a certain set of economic conditions) are estimated and appropriated in the year of origination, rather than in the out years.

Given the scrutiny of the Loan Guaranty program over the past few years by Congress and OMB, there is undoubtedly a better understanding of the economic underpinnings of the program. New accounting and budgeting procedures such as those incorporated in the Credit Reform Act should do a great deal to prevent the sudden unexpected appropriations needed for the Loan Guaranty Program over the past 12 years. However, given the likely future economic constraints of the Federal Government, continued scrutiny of the LG program can be expected.

B. Factors Internal to VA

Aside from external conditions, several initiatives within the Department of Veterans Affairs will have an impact on the Loan Guaranty program in the future. These include initiatives on ADP Modernization, Corporate Information Management (CIM), Performance Indicators and Total Quality Management (TQM). The initiative which most directly affects the issues before this task force is the VBA ADP Modernization effort.

VBA is currently implementing a major initiative to computerize the information processing environment used to deliver VBA benefits. This program, which began in 1985, was designed to replace existing systems with a modernized computing environment that takes advantage of new technologies, including image processing, modern programming tools such as fourth generation languages, and expert systems. These systems will help VBA accomplish its mission of delivering benefits and services to veterans faster and more efficiently.

Specifically in terms of the Loan Guaranty program, the electronic exchange of information could allow better monitoring of the loan guarantee/mortgage industry, and allow access to data from HUD, Fannie Mae, Ginnie Mae, and the National Association of Realtors. Hopefully, this would facilitate the creation of LG policies and procedures which are more consistent with the industry and thereby gain participation of lenders, making VA loans more available and appealing to veterans.

C. Customer Needs and Expectations

1. Veterans

The primary customer of the Loan Guaranty program is the individual veteran. In 1990, in an attempt to determine veterans' satisfaction with current services, the Veterans Services Division (VSD) funded a Consumer Satisfaction Survey. The Loan Guaranty portion of the survey was based on the results of telephone interviews with 401 veterans who applied for or received VA home loans during FY 1988. The actual interviewing took place in May 1990. A variety of topics was covered in an attempt to get an indication of the overall level of satisfaction of veterans with the services they received.

In general, the respondents were pleased with their dealings with the VA. Nine of ten respondents were satisfied with the service they received when they applied for a Certificate of Eligibility. Of those who contacted VA directly about their home loan (33 percent), 95 percent said they were treated courteously, 94 percent said they understood completely the information the VA gave them, and 92 percent were satisfied with the information they received.

Of those veterans who dealt directly with a bank or institution, 97 percent were treated courteously, 96 percent understood the information they gave about the VA loan, and 94 percent were satisfied with the information received. In terms of the amount of time it took to process the veteran's loan application, 23 percent thought it took longer than expected, 53 percent reported it took the time they thought it would, and 25 percent said it took a shorter amount of time than anticipated. Among those who admitted being late in making payments to VA (13 percent), 67 percent were satisfied with VA's assistance, after being contacted by VA.

One of the limitations of this kind of survey is that the measurement of "satisfaction" is not detailed enough in many cases to suggest program modifications needed to meet program goals. Another survey is to be conducted for VBA's Office of Planning (the Customer Based Measures Survey) which will measure how well the provider meets the customers' expectations for service.

2. The Real Estate Finance Industry

The corporate customers with whom we do business are essential to Loan Guaranty. Due to the many functions that the financing and servicing of loans and management of property require, Loan Guaranty Service utilizes the resources and expertise of many VA and non-VA entities to help the program work. In the real estate finance industry, our most important customer is the mortgage lender. This group includes the banks, mortgage companies, savings and loan associations, credit unions and other financial institutions which make the loans we guarantee. Without their participation there is no VA Loan Guaranty program. The real estate agent and broker are also prime players in the program. Their role is critical in that they are often the initial contact the veteran has with VA financing. Retaining their support in advising the home buyer and seller to elect VA financing over other home financing options is a goal for which we strive.

The real estate appraiser furnishes the property valuations used by VA in several ways. Appraisers and inspectors help to assure that the security for the loan adequately protects the Government's interest. The role of the home builder in our program is significant. By building homes which are affordable for many veterans and offering VA financing for their products, the builder contributes to the vitality of the program. The title company and attorney play integral roles by identifying and helping to clear the legal hurdles of real estate transactions and by conducting loan settlement. Attorneys are also involved in several other ways including bankruptcy and foreclosure proceedings involving VA loans.

The loan holder and loan servicer help the veteran resolve loan repayment problems which may be encountered by helping mortgagors identify problems, arranging repayment plans to cure delinquencies and suggesting alternatives to foreclosure when loan defaults are insoluble. A substantial role is filled by secondary mortgage market entities such as the Government National Mortgage Association (GNMA) which provides an investment pool for mortgage loans and a conduit of capital for VA lenders. The participation of the insurance companies which insure homes and home mortgages and the taxing entities which assess real property and collect taxes are also elements of the program.

VA provides several products and services for the real estate industry. The services usually provided as the first steps in Loan Guaranty operations are our appraisal review and property inspection functions in which we review and approve the work of independent appraisers and inspectors who participate in the program. For about 10% of guaranteed loans VA also provides the loan underwriting necessary to establish that a borrower qualifies for the intended loan. When a closed loan is reported to VA, our issuance of the Loan Guaranty Certificate assures the loan holder and investor that VA protection exists for the loan.

When needed, VA assists holders and servicers by assisting in loan servicing matters such as loan assumptions and partial releases of security and by intervening in loan default situations to effect cures. Other foreclosure avoidance measures employed by VA include accepting deeds in lieu of foreclosure, refunding loans and making compromise claim payments. In the unfortunate event that a foreclosure occurs, VA makes claim payments to the loan holder and, in many cases, acquires the property which was security for the loan, relieving the holder of the chores of managing and disposing of the property itself.

Upon acquiring a property, our services to the industry continue. We make required tax and insurance payments, provide work for the contractors who manage, repair and market our properties and, in many cases, provide financing for the buyers of our acquired homes. From time to time VA also conducts loan sales in which interested parties may invest in mortgages held by VA.

3. Loan Guaranty's Customers Within VA

It is also recognized that "customers" of Loan Guaranty Service exist within VA. The Veterans Services Divisions regularly answer general Loan Guaranty questions for veterans in face-to-face and telephone interviews. They also assist with walk-in eligibility determinations at most regional offices. Adjudication personnel adjudicate the more complex eligibility claims. Involvement by the Finance Division is required for paying Loan Guaranty obligations such as guaranty claims and escrows, establishing debts resulting from guaranteed loans, considering debt waiver and compromise cases, receiving and refunding VA funding fees and processing inquiries on VA benefit-related indebtedness. Other Loan Guaranty support services are provided by VA employees in mailroom activities, forms and publications control, travel arrangements and personnel services.

On local and national levels, Information Resource Management provides ADP systems development and maintenance services. VA General and District Counsels furnish legal advice and assistance. The Office of Inspector General serves in the areas of program surveillance and fraud, waste and abuse avoidance. Even Loan Guaranty Service employees may be seen as customers. Their concerns of job stability, promotion potential, job satisfaction and work environment are issues to be addressed by the Service in the interest in maintaining a talented, motivated work force.

4. Other Customers

Aside from the needs of the real estate industry, internal VA customers, and veterans themselves, other entities are partially responsible for informing or counseling veterans regarding their loan benefits. These groups include the Veterans Service Organizations, state and county veteran representatives, and the military services.

III. OPERATIONAL RE-ENGINEERING OPPORTUNITIES

In this section, we concentrate on re-engineering opportunities which address the processes by which VA provides the housing benefit to veterans. Later, we will discuss the geographical location and organizational line of authority aspects of benefits delivery.

A. Loan Processing

1. Eligibility Determinations

a. Current Environment and Procedures

The function of determining eligibility for loan benefits is currently labor and paperwork intensive. Eligibility applications are processed at Central Office, all regional offices and some satellite offices. Applications may be mailed to the office or handled on a walk-in basis. Employees involved in the function include those in Loan Guaranty, Veterans Services and Adjudication Divisions. There are two application forms and several other forms and form letters used in the process. Special security paper is used for the eligibility certificate as it is a controlled document.

Applicants are required to attach proof of military service to their applications and, in cases involving restoration of previously used entitlement, must provide evidence of loan payoff and sale of a prior VA home. Review of military service documents can be complex, due in part to the number of versions of service documents that have existed over the years and a lack of uniformity in narrative descriptions of separation reasons. Procedures require checking the Beneficiary Identification and Records Locator System (BIRLS) when applicants do not provide satisfactory evidence of military service. Complicated cases and surviving spouse requests are referred to C&P Service for adjudication. Employees are also required to check VA microfiche records on every case for indications of prior use of loan entitlement. (Use of these records will be largely replaced in the near future when the first phase of the automated Loan Guaranty Index is implemented providing the capability to index veterans' names and service numbers electronically.) In FY 1991 over 345,000 initial determinations of basic eligibility were performed, 70,000 requests for restoration of entitlement were processed and over 12,000 determinations of eligibility for FHA certificates of veteran status were made.

b. Opportunities for Improvement

The existence of veteran and VA loan databases and today's computer technology provide the opportunity of re-engineering the eligibility determination procedures. Through the interfacing of Department of Defense service member files, BIRLS files and the LGY Index, it is estimated that sufficient information to make eligibility and entitlement determinations on over 90% of all requests will be available electronically. With this information in a central data base, employees would enter veteran names and/or service numbers and see on-screen whether the applicant is eligible and how much entitlement is available. Some of this information could also be made available to lenders via electronic call-ins. The system could provide evidence of eligibility for the lender's and/or VA use. Use of the paper certificate of eligibility could be eliminated or substantially reduced, and the number of eligibility clerks vastly reduced.

c. Recommendation

Loan Guaranty should continue to move toward an automated system of eligibility determinations.

2. Underwriting

a. Current Environment and Procedures

Loan Guaranty Service in conjunction with VBA IRM is now completing the implementation of a new automated system for assisting regional offices in the credit underwriting and guaranty review functions of the Loan Processing activity. This new, decentralized system automates the present paper based functions, provides automation tools at the forty-six regional offices, and provides for automated data transfer to centralized data bases for management reporting. For the first time, VA employees have the ability to track the progress of individual loans without having to physically access loan folders. Whether managing the correspondence associated with these activities or eliminating the paper code sheets used previously, this system both simplifies the work process and makes available an audit trail not present before.

b. Opportunities for Improvement

This new system provides considerable answers to some of the persistent problems encountered in the past and many of the needs of the present. It does not, however, provide answers for all the problems and opportunities presented by the present and future mortgage loan business environments. The next major issue to be faced in loan originations, is the necessity for maintenance of paper files. VA, like other mortgage loan guarantors and insurers, requires the submission of numerous paper documents and issues evidence of its guarantee of a loan on a paper document. These paper documents are issued and maintained largely to establish legal rights to recourse in the event of loss. As the legal barriers to substitution of electronic images for those paper documents are removed, the industry will move away from them. VA will be well served by moving with the market in this area and being as open and supportive as possible to such changes.

c. Recommendation

Loan Guaranty Service should continue to improve the existing Loan Processing system and should attempt to reflect the industry's movement to a less paper-bound process. In order to remain part of the competitive mainstream, VA should add its voice to those supporting the development of EDI (Electronic Data Interchange) standards for the exchange of loan origination information. Loan Guaranty Service personnel should participate in the EDI standards formulation process where appropriate. While VA's present market position is such that it cannot lead the market in this area, it should move as close to the leading edge as possible.

3. Release of Liability

a. Current Situation

The VA processing of Release of Liability and Substitution of Entitlement is governed by Title 38 USC, section 3713 and 3714. The process is handled differently depending on the date of loan commitment and type of holder. Federal law prescribes who may process requests for Release of Liability (ROL).

Loans with commitments made before March 1, 1988 are reviewed by the local regional office. For loans made under the automatic procedures with commitments made after 3-1-88, the veteran is relieved of all liability to the Secretary if the holder determines the loan is current; the purchaser of the property is obligated by contract to purchase the property and to assume full liability for the repayment of balance of the loan and has assumed by contract, all obligations of the veteran under the terms of the instruments creating and servicing the loan; and the purchaser qualifies from a credit standpoint to the same extent as if the transferee were a veteran eligible for the purchase of a guaranteed or insured loan in an amount equal to the unpaid balance of the obligation. If the holder of the loan is not an approved lender as described in Title 38, section 3702, the Secretary is considered to be the holder of the loan and must apply the same review criteria as above.

b. Opportunities for Improvements

Veterans have complained about the timeliness of the holders in processing ROLs. The holders have not adjusted to the workload and are not processing releases according to VA regulations. Veterans have also complained that the holders have been unresponsive to their requests for information. However, the law requires that holders process loans made after 3/1/88 and the Secretary is required to allow the holders to process these cases. VA must process all cases prior to 3/1/88 and allow the holder to process the cases after 3/1/88. Thus, the share of cases VA must process is a decreasing percentage of all these requests.

Assuming sufficient volume of these cases at any work site, the entire process can be computerized. This would give employees the ability to track the process of the release requests. Such automation, based on the Loan Processing model, would provide automated assistance in all phases of the Release of Liability process: credit review, correspondence, database updates, and so forth.

c. Recommendation

Lenders should be educated to ensure proper processing of ROLs, and the Monitoring Unit should ensure compliance by lenders. If necessary, the fee structure should be reevaluated.

B. Loan Servicing

1. Current Situation

Loan servicing consists of all actions performed by VA from the time a VA loan is made until the loan is paid in full or until it is terminated and accounts are settled with the loan holder. Additionally, there is post-foreclosure service provided to veterans relating to debt establishment and debt waiver activity. A more complete description of GI Loan Servicing is found as Attachment C.

The present Loan Service and Claims process is highly labor intensive, paper bound and characterized by demands for high levels of data entry, much of it redundant. A Loan Service Representative (LSR) in the present environment has virtually no automated assistance in considering the various courses of action which would assist a delinquent veteran in resolving the mortgage loan default episode.

2. Opportunities for Improvement

Loan servicing could become more effective and efficient by re-engineering the work processes to take advantage of new technologies and concepts: calling machines (auto-dialers), calling across time zones, rotating job assignments, and irregular tours of duty/working at home.

The following options are designed to increase VA's outreach to delinquent veteran-borrowers so that more veterans are assisted in retaining homeownership, thereby reducing program costs by fewer loan terminations. These options are complimentary to Loan Guaranty's long term effort to modernize its ADP systems.

a. Automatic Calling Machines and other Loan Servicing Technologies

Various technologies exist which could enhance the ability of the LSR to make contact with delinquent borrowers and also provide for better management of delinquent accounts. For example, names of delinquent borrowers and their accompanying telephone numbers are electronically loaded in the calling machine prior to the beginning of the Loan Service Representatives' tour of duty. The work assignment is to make a specific number of calls daily and provide appropriate guidance or advice based on the borrowers' circumstances. Calls are automatically dialed and the LSR performs servicing when the phone is answered.

Such a system provides full documentation of the employee's daily performance. Each servicing action is electronically recorded. Computer assisted financial counseling worksheets, as well as other electronic worksheets, are on-line to help the LSR reach decisions about the types of assistance VA may be able to provide. VA's current computer system (LCS) is being redesigned and envisions such enhancements.

Other technologies permit calling out and leaving pre-recorded messages when it is not possible to make contact with the delinquent borrower. The Telephone Consumer Protection Act of 1991, effective December 20, 1992, prohibits leaving pre-recorded telephone messages without the consent of the called party. The Mortgage Banking Association is seeking an FCC ruling that exempts mortgage servicing calls from this prohibition.

When used in conjunction with other servicing tools, these technologies maximize the amount of servicing outreach that can be accomplished daily.

b. <u>Calling Across Time Zones</u>

A VACO study has indicated that the most effective time to service loans is late afternoon, evenings and weekends. Servicing phone calls made during regular business hours in the Pacific Time Zone can be targeted for late afternoon and evenings for Eastern, Central and Mountain Zones. This alternative is cost-effective since the increased phone bills would likely be less than overtime, night differential and keeping VA facilities open after regular business hours for stations in other than Pacific Time Zones.

c. <u>Rotating Job Duties</u>

For GI loans there are over 20 unique work processes, all with different volumes and priorities. (See Attachment C.) Typically LSRs are assigned to perform most or all of these duties. In situations featuring larger loan servicing operations these duties can be reassigned into workable units to achieve economies of scale. LSRs can produce larger quantities of work when performing one or a few duties, rather than all duties. Periodically, job assignments can be rotated so that LSRs develop and maintain full skills and this can have the effect of minimizing job burnout.

d. <u>Irregular Tours of Duty/Work at Home</u>

VACO studies and field testing have confirmed the common knowledge among servicers that afternoons, evenings and weekends are the best times to reach borrowers at home to discuss ways to assist the homeowner. The greater efficiency of evening and Saturday servicing comes from the increased likelihood of finding borrowers at home during these times, since the majority of home purchasers now depend on two incomes to qualify and are away from home during normal VA business hours.

At least one station is performing irregular tours of duty combined with working at home. Loan Service Representatives, on a rotational basis, work a Tuesday through Saturday schedule and use GSA FTS credit cards to place calls. Management controls are in place and include a telephone log of calls compared against telephone billings. Over one-third of calls made on Saturday result in successful contacts and additional messages are left on answering machines prompting homeowners to call the station during the week. This compares favorably to the usual weekday contact rate in that station of less than ten percent.

Servicing from home also has the public benefit of reducing the LSRs contribution to rush hour transportation and air pollution while saving the LSR one day's commuting cost per week.

3. Recommendation

The Loan Guaranty Service should pursue each of the suggested improvements as vigorously as possible. It is understood that all these suggestions will work best in an environment which will provide opportunities for economies of scale.

C. Liquidation Management

1. Current Situation

Liquidation Management really begins when a LSR decides that a GI loan default is insoluble and there is no reasonable belief that efforts to bring the loan current would be successful. At that point, the LSR must determine the most efficient and expeditious way to terminate the loan.

In the present operational environment, LSRs have little automation assistance to help them make or execute decisions. Additionally, the present paper-bound system results in inconsistent information to make and carry out informed decisions.

2. Opportunities for Improvement

Once the decision is reached that a loan is insoluble, the LSR will normally review the alternatives to foreclosure which might be available based on the servicing information obtained from the homeowner. These alternatives include deed in lieu of foreclosures, compromise agreements, and the refunding of the loan account from the holder if the circumstances indicate that a future ability to resume normal monthly payments may exist. Improvements can be made to the deliberations of these options and their execution as described below.

a. Develop Expert Systems

The LSR currently has no automated tools to help develop alternatives to foreclosure. Our concern is not just to identify the best alternative to VA financially. The circumstances of each case will still dictate which alternative would be best for the government and the veteran; the judgment of an experienced LSR cannot be automated. Our intent is, and has been, to develop expert systems which would take varying pieces of data and then calculate the results to quickly provide the LSR with the information needed to make the best possible decision.

Many tangible factors such as employment, degree of debt, income, health, etc. must be considered by the LSR when constructing "what if" scenarios. A user friendly automated system would significantly improve an LSRs ability to speed up the decision making process and provide accurate figures. This information would also provide the documentation needed which would help justify the reasons for the decision being made. The best automated system, however, cannot replace the judgment and intuition of an experienced LSR. This judgment is needed to evaluate the intangible factors, such as attitude, determination to retain ownership, etc. which are critical to a successful cure.

For example, on a sale by compromise agreement, the system could calculate how the proposed sales price and subsequent claim payment would compare to a claim payment if a foreclosure sale were pursued instead. On a potential loan to be refunded, the system could calculate the veteran's new P&I payment at the present note rate and other allowable interest rates while also using financial information to complete an initial analysis to be used to help determine a veteran's ability to repay the loan at the newly calculated rate. On a potential voluntary deed, the system could quickly calculate the cost to VA of the deed versus a potential claim payment on a foreclosure.

The automated assistance would not only improve the LSRs ability to make rapid decisions, but would also provide increased time to the LSR to concentrate on direct contacts with veterans. The system could also provide a source for instant information to be used in conjunction with the liquidation process if no alternatives to foreclosure are available.

b. Liquidation/Foreclosure of Loans

Should there be no viable alternatives to foreclosure available and the loan is insoluble, liquidation of the loan is required. Once again, automation of this process would greatly improve our efficiency and ability to quickly provide bidding instructions to loan holders and their attorneys. For example, the system could be developed so that when the foreclosure appraisal is requested by the holder, a status of the loan account is also automatically forwarded for completion and return by the servicer. Upon receipt by VA, this information would be input into the system along with the value information from the appraisal. The establishment of a sale date i the system could automatically calculate the pertinent data, generate all necessary letters, and forward the bidding instructions immediately to both the loan holder and his attorney by facsimile copy or other innovative means using electronic communications capabilities.

Any system should be sufficiently sophisticated to recognize many various scenarios which can impact VA's instructions to holders, such as VA delay or forbearance with regard to no specified amount cases. This system would greatly enhance the LSRs performance in both the current regional office setup as well as in any other proposed configuration.

3. Considerations

Factors which must be considered would predominately be ADP related topics such as the ability to integrate or develop these proposals in conjunction with existing and proposed systems.

Levels of review throughout the liquidation procedure would also have to be considered. For example, currently, proposed bidding instructions require review by Property Management and Construction & Valuation representatives. As visualized elsewhere in this report, these functional sections would not be available within the regionalized Loan Processing and Servicing Centers.

4. Recommendation

Loan Guaranty Service and VBA IRM should pursue the development and implementation of expert systems as rapidly as possible and ensure that those improvements contain the features described in this report.

D. Claims Management

1. Current Situation

VA guaranteed loans have been made by private lenders such as banks, savings and loan associations, credit unions and mortgage companies. The prompt and accurate payment of claims under the VA Loan Guaranty is the single most important item in causing lenders to continue to participate in our program. The Government's agreement to pay a claim to loan holders in the event of a default in loan payments is in effect for the life of the loan.

Claims under guaranty are paid when GI loans are terminated (through foreclosure or voluntary conveyance), when VA repurchases certain "vendee" loans from loan servicers, and when VA, the borrower, and the holder reach a compromise settlement. The law also allows VA the option to assist veteran borrowers in retaining homeownership by purchasing the delinquent loan and becoming the loan holder. This necessitates paying an amount for acquisition of the loan which is an action similar to the claims payment procedure.

Our current process for managing claim payments is extremely complicated and time consuming. The many circumstances and regulations which govern the amounts that are reimbursable to loan holders creates a tremendous burden on our claims analysts to accurately consider, calculate, verify and approve a holder's claim. Tracking, follow-up, suspension, and rejection of claims are done manually by clerical staff at our regional offices.

2. Opportunities for Improvement

Our process would benefit greatly from completing and extending our present automation plans. An automated process could contain tables for related advances and expenses which a loan holder might pay in a given jurisdiction. The system could verify these payments against the tables as proper, for the correct amount (less than or equal to a maximum), and timely (related to the foreclosure/cutoff date). If the payment is not timely, the system could also prorate the claim amount. A new system should also be versatile enough to calculate (amortize) the remaining principal balance of a loan when periodic prepayments to principal are made by the borrower or loan holder. Currently, we must manually prepare the analysis. A holder's buydown of interest due or total indebtedness is another complication to the claims process that should be made a part of the new system. It is also possible that more than one claim could be paid on a single account (supplemental claim). We currently lack a "supplemental claim analysis." Moreover, much effort and time are expended to prepare and release letters, forms, vouchers, and memoranda. An automated system could prepare and print these documents for our regional office staff.

3. Recommendation

Loan Guaranty Service should pursue the implementation of planned ADP improvements as rapidly as possible and ensure that those improvements contain the features described in this report.

E. Overall Recommendations

The present ADP Modernization effort as it applies to these areas of the Loan Guaranty operations should be continued and accelerated where possible.

The Loan Guaranty Service should work with both VBA IRM and the home mortgage industry to ensure that we are on the leading edge of technological advances adopted within this industry.

Where possible, increased efficiencies which can be obtained from such personnel changes as rotating assignments, alternative tours of duty and work at home arrangements should be explored.

IV. GEOGRAPHIC LOCATION OF THE WORKFORCE

In this section, we focus on opportunities to re-engineer how the organization works as a function of geographic location, rather than how the process works. By rethinking the necessity for particular geographic arrangements, improved service to our veteran customers may be attainable.

A. Maintain the Status Quo?

One option available to VBA is that Loan Guaranty operations remain located at the same forty-six regional offices as they are now, and continue to operate has they have in the past.

1. Description

What follows is a brief description of the present operating environment in which Loan Guaranty finds itself currently at the regional offices. The discussion includes the administrative organization of the regional office, the support services available to Loan Guaranty and a brief contextual overview of the functions accomplished by Loan Guaranty.

a. Regional Office Organization:

The typical VA regional office is hierarchical in nature with a Director as the chief operating officer. His or her immediate staff and several operational and support organizations called "Divisions" report directly to the Director. Loan Guaranty is one of those divisions reporting to the Director. One notable exception to this reporting scheme is the office of District Counsel. The role of the District Counsel is essentially to be the attorney for the regional office. However, they report directly to the Office of General Counsel in VA Central Office.

Loan Guaranty is often seen as a separate, somewhat unique, operation in the regional office. That perception has some basis in fact. The main functions of Adjudication, Veterans Services, and Vocational Rehabilitation and Counseling are designed to ensure the direct delivery of benefits to veterans. Loan Guaranty is a specialized discipline which operates to provide an environment conducive to prompting outside organizations to provide the housing and loans needed by veterans.

b. Support Services

One of the features of the present regional office alignment is that all functional areas such as Loan Guaranty and Adjudication are served by common support services. These services consist of Finance, Administrative Services, Personnel and Information Resources Management. Loan Guaranty must compete with the other divisions for these scarce resources.

c. Loan Guaranty Division Organization

Loan Guaranty services are provided within four functional areas called sections: Construction and Valuation, Loan Processing, Loan Service and Claims, and Property Management. Each Loan Guaranty Division operates a Specially Adapted Housing program, which helps severely disabled veterans obtain housing suited to their needs. The four functional areas and their duties and responsibilities are described in some detail in Section I of this report. The following paragraphs discuss how the present organizational alignment and set of geographic locations contributes to or detracts from the carrying out of those duties and responsibilities.

(1) Construction and Valuation

The duties and responsibilities assigned to the C&V functional area are tied closely to the local real estate market(s) within which the regional office operates.. It is generally conceded that appraisal work is at least as much an art as it is a science. As such, there is no substitute for knowledge of the local market and for VBA having a physical presence in areas with high concentrations of appraisal work. Regional offices have entered into a number of arrangements to ensure that physical presence when their active markets are at some distance from the regional office. As congressional and executive branch interest in the costs of the program have increased, the emphasis on the oversight functions of C&V have become more apparent and important.

(2) Loan Processing

The duties and responsibilities of the LP area have evolved over the past few years to be largely the review of lender-provided documentation. The movement from actively underwriting almost all VA loan applications under the prior approval methodology to mostly reviewing automatic lender guaranty requests has been swift and dramatic. This change in the type of work the LP area accomplishes has lessened but certainly has not eliminated the necessity for an intimate familiarity with the local market. Improved communications capabilities such as FAX machines have decreased the time necessary to perfect documentation so that the needed Loan Guaranty Certificates may be issued more quickly. The automated Loan Processing system (LP) has provided the capability to quickly process loans, generate pertinent documents and correspondence and code the actions taken. It has a loan status inquiry function which eliminates the necessity for physical loan file retrieval and it provides several loan production reports. Installation of LP at all regional offices is scheduled for completion by August 1992. The LP system is one of the first parts of a larger effort to automate all of the loan guaranty activities. An automated system for managing lender information is also under development. The Expanded Lender Information system (ELI) will provide a nationwide electronic file of information on the personnel and operations of participating lending institutions. The LP system is readily adaptable to consolidation of loan processing activities as will be the ELI system.

(3) Loan Service and Claims

The servicing of portfolio loans and the supplemental servicing of GI loans may be viewed as largely a process of communications. In the case of portfolio loans, the dialogue is between the borrower and the VA. In the case of GI loans, the VA often serves as intermediary between the veteran-borrower and the commercial lender. Liquidation management may be viewed as a process of communication between the servicer/holder and VA, while claims management is largely a document review and approval process. Demographic and technological changes have caused many modifications to the program. The returning World War II veteran was relatively likely to settle in his or her old home town. If that veteran encountered trouble making the monthly house payments, the local lender was likely to visit the house and/or arrange for a personal appointment to resolve the issue. The post Vietnam era veteran is considerably more likely to have settled in a new area of the country and is used to dealing with a mortgage lender who may be several states removed from the property. The present veteran is much more likely to complete his or her business with both the servicer/holder and VA via telephone and letter than by personal interview. Communications between VA and the servicer/holders is rapidly evolving from a process requiring a separate piece of paper for each step in the servicing, liquidation and claims process to a computer to computer environment. Due to technological improvements, the location of the individual providing the service has little impact on the quality of service rendered.

(4) Property Management

The marketing and disposition of real estate is always a very highly localized activity. While technological advances make efficiencies possible in the administrative processes associated with the PM area, the actual market strategy and sales tactics are highly dependent upon the conditions and customs of the local market. Additionally, PM provides an oversight function which is very important in limiting or eliminating losses from fraud and abuse. VA's own experience, as shown in a number of OIG audits over the years, has been that infrequent or non-existent staff oversight over inventory properties and/or contract-basis property managers increases the program's vulnerability to waste, fraud and abuse resulting from extended property holding time and/or funds being expended for work not accomplished or not accomplished in accordance with contractual requirements.

2. Reasons for Maintaining the Status Quo

The reasons for maintaining the status quo fall into two categories: the costs of making a change, and the benefits of maintaining the local touch.

One argument for maintaining the status quo is that the organization would avoid the disruption and confusion involved in a change in the location of the work sites. Leaving the operating divisions in their current physical locations avoids the significant costs associated with relocating employees to new locations and hiring employees at the new site(s). It also avoids the negative impact on productivity normally associated with changes in the work environment.

This "no change" option would also preserve the present corporate memory and knowledge of the local market. The present configuration of forty-six locations provides greater opportunity for face-to-face contacts between VA employees and veterans and other program participants than would a more centralized location scheme. The present situation provides Loan Guaranty Service with more information to respond to the demands of customs and conditions in the local real estate markets. Additionally, this highly decentralized mode makes it easier to accommodate politically sensitive local matters.

3. Reasons for Changing the Status Quo

The argument for changing the status quo centers on efficiency and consistency of operations and on internal acceptance and support of the program by the local area.

VA organizational alignment and structure has not kept up with the changes in the mortgage finance industry during the years the program has been in operation. When the Loan Guaranty program was implemented in the 1940's, the home loan market was dominated by small, self-contained lending units, primarily savings and loans institutions. These local lenders typically made, serviced and held loans from their inception to their termination. When a customer obtained a GI loan, he or she could be fairly confident that the payments would be made to the same firm until the loan was paid in full. Loans were rarely sold. When they were sold, the numbers were small and the sales were based on the loan instruments themselves.

Today, the market is dominated by large, regional loan originators supported by a multitude of local loan origination offices, national loan servicing operations, loan sales in the billions of dollars arranged on the basis of security instruments far removed from the underlying loans themselves and national, governmental and quasi-governmental entities for holding loans. A veteran obtaining a GI loan today is likely to make payments to a series of mortgage companies over the life of the loan.

The present Loan Guaranty organizational structure provides economies of scale in only the largest of our urban settings. This means that the average size of the Loan Guaranty operation at a medium- or small-sized office precludes any great degree of specialization. This in turn requires a more difficult training regimen since the new employee must be trained quickly over a greater span of duties. With the relatively large number of small offices, the required infrastructure of finance, administrative and personnel support is costly to provide.

Nationally, the result of the present organizational alignment has too often been the dissemination of inconsistent information to veterans and other program participants from regional office to regional office. Despite increased communications capabilities over the past few years, it has proven difficult to provide guidance to Loan Guaranty operations in regional offices to ensure consistent national standards of operation. This has been particularly apparent when dealing with larger lenders, servicers and holders operating in multi-VARO jurisdictions.

4. Conclusions

The present organization of forty-six regional offices is a legacy of our beginnings. The clear-cut differences between the four operational elements of the Loan Guaranty operation make obvious that some operations are more tied to local markets than others. Construction and Valuation and Property Management clearly require a local presence in order to adjust to the imperatives of the marketplace and to ensure adequate oversight to protect the interest of both our veteran customers and the government. There is no such strong indication that the document review and counseling functions of Loan Processing and Loan Service and Claims need to be localized. In fact, those document review and counseling functions would benefit from a degree of relocation which would result in some economies of scale and facilitate consistent policy communication. Maintaining the status quo for all aspects of Loan Guaranty operations allows for correction of the identified problems to a more limited extent.

5. Recommendation

Even if other functions are centralized or regionalized, Construction and Valuation and Property Management operations should remain at as many regional offices as feasible. The Loan Processing and Loan Servicing and Claims operations are prime candidates for relocating into a centralized scheme of one or more processing centers. Changes such as those described later in this report should be made with the Loan Processing and Loan Service and Claims portions of the program.

B. Consolidation Into Fewer Offices

A second organizational and geographical option available to VBA would be to consolidate the present Loan Guaranty regional office organizations into a smaller number of regional offices. The following discussion of this option considers the history of consolidations, the pros and cons of the issue and conclusions reached. It should be emphasized that this section of the paper is considering the consolidation of entire Loan Guaranty divisions with each other. Consolidation of some, but not all, of the functions of a present Loan Guaranty division is discussed elsewhere.

1. History

This is an option which has been reviewed many times over the years. There have been no fewer than nineteen different studies of consolidation and realignment. Those studies were conducted at varying intervals from 1949 to 1989. Generally, those studies have not resulted in large scale consolidations. The following is a listing of some of the more recent consolidations which have occurred:

ELIMINATED LOAN GUARANTY DIVISION	DATE CLOSED	SURVIVING LOAN GUARANTY DIVISION
San Diego, CA	1958	Los Angeles
Wilmington, DE	1959	Philadelphia
Providence, RI	1959	Boston
Reno, NV	1960	San Francisco
Fargo, ND	1960	St. Paul
Cheyenne, WY	1960	Denver
Sioux Falls, SD	1962	St. Paul
White River Junction, VT	1984	Manchester
Boston, MA	1990	Manchester
Togus, ME	1990	Manchester
Hartford, CT	1990	Manchester

The most recent consolidation (Boston, Togus and Hartford into Manchester) has taught some lessons which should be taken into account in any analysis of consolidations of entire Loan Guaranty divisions. First and foremost, consolidations are politically sensitive actions. Even if they do not reach the thresholds which require Congressional approval, the local congressional delegations from both the losing and gaining states and districts are highly aware of any such action and extremely sensitive to the effects or perceived effects of consolidation on their constituents. This is an area that must be handled adroitly.

If the Manchester consolidation is typical of what might be expected in future consolidations, a way to increase flexibility in planning for space, equipment and staffing must be found. The Manchester consolidation was complicated by a rapid, significant increase in business in all functional areas. Thus the receiving Loan Guaranty division found itself lacking space, all types of equipment but especially computing tools, and trained employees.

To ensure having a competent, trained workforce in place at the time the consolidation effort is executed, Manchester Loan Guaranty management has suggested that new employees be hired prior to the actual consolidation. They also suggest visits between employees at the surviving Loan Guaranty division and similarly sized Loan Guaranty divisions around the country. There are marked differences in the ways small, medium and large-sized divisions do Loan Guaranty work. If all the trained employees at the surviving division are from a collection of small stations, they will have no corporate expertise in managing the work in a medium or large station environment.

The morale of the workforce is critical during consolidation. Manchester reported very high stress levels requiring great amounts of encouragement, support and understanding on the part of management. Channels of communication must be established and remain open throughout the consolidation period.

2. Reasons to Consider Consolidation

In summary, the arguments for consolidation of Loan Guaranty divisions center on the possibilities of achieving greater efficiencies, consistencies in operations and internal acceptance and support. Larger divisions produce the opportunities to achieve some economies of scale. This means that there would be an increased ability to specialize in the various disciplines necessary to execute the Loan Guaranty program. With more employees available, management would have greater flexibility in dealing with fluctuations in the workload. Logistical difficulties, such as space, communications, equipment, and the costs of training employees should be reduced. Larger operating divisions also give the potential for increased internal support within the regional office itself. For example, increased activity in Loan Guaranty should produce increased familiarity and interest on the part of personnel employees and increased demands for ADP service should help justify IRM staff increases with attendant specialization.

Quality assurance should be easier to achieve with fewer, larger Loan Guaranty divisions. With a smaller management superstructure, there should be a reduction in the instances of inconsistent or incorrect information being provided to veterans and other program participants. The execution of policy matters such as the allowance or disallowance of particular items in a claim or the enforcement of occupancy requirements should be more uniform in this environment.

3. Reasons which Argue Against Consolidation

Any discussion of consolidation must address the issue of how many or how few Loan Guaranty divisions should remain in existence after the consolidation is completed. If the number of divisions is reduced to a number small enough to provide true opportunities of scale, these remaining divisions may be too isolated from major markets to provide the local knowledge and presence required especially by the functions of Loan Guaranty which are tied to the real estate, i.e. appraising, marketing and selling properties. A decreased availability to veterans and other program participants, and increased difficulty in overseeing program participants and properties may result.

If consolidation involves only a few regional offices with marginal levels of production and employment, very little in terms of economies of scale will be possible at a high fiscal cost and a potentially high political cost. The cost in personnel disruption and congressional opposition must be given great weight in any consideration of consolidations when such consolidations will provide only marginal increases in efficiency and lowered operating costs.

Finally, our experience with the Manchester consolidation reveals that sudden changes in the local economy can invalidate the best-laid plans in terms of the space, equipment and personnel requirements of the surviving station.

4. Conclusions

Consolidation of a number of existing Loan Guaranty divisions into a smaller number of functionally identical divisions does not appear to be a comprehensive solution to the problems facing this program. The human, financial and political costs associated with consolidation as a sole solution have the potential to be as high as the execution of a more comprehensive solution, with much less potential for achieving measurable success.

5. Recommendation

The task group feels that some consolidations of remaining C&V and PM functions may be in order if Loan Processing and Loan Service and Claims functions are relocated into either national or regional processing centers. Further study is necessary to determine the minimum viable size for a Loan Guaranty operation in a regional office.

C. Regionalization of Some Functions

1. Description of this Scenario

This option proposes to regionalize the Loan Processing and Servicing functions into a small number of processing centers. Resources (FTE and IRM) would be based on workload volume. The locations would be determined following review of options presented by the Loan Guaranty Service to the Chief Benefits Director.

2. Reasons for Regionalization

The following factors argue for the regionalization of all loan processing and servicing/management into a small number of stations. These reasons are similar to the reasons for centralization of management of the vendee portfolio as described later in this report.

An economy of scale would be gained, enabling all loan origination and servicing functions to be accomplished by a specialized group of staff personnel. Having processing and servicing under one roof would facilitate shifting of personnel between functions as the workload fluctuated. There would be more flexibility to work employees on staggered shifts or cover for vacation due to a larger pool of similarly trained personnel. Policy or procedural changes could generally be directed to one group for primary implementation and general information to other personnel.

A larger operation would facilitate identification of high potential employees for advancement. Training of personnel could be consistent and geared to certain aspects of the loan origination and servicing processes (bankruptcy, workouts, foreclosure, etc.) Rotational assignments for cross training could be handled in a more effective manner due to the larger pool of Loan Specialists.

While efficient use of "800" numbers with call director to enable the borrower to access a data bank to hear information on a specific loan can be implemented without regionalization of staff (provided the data is maintained centrally), auto dialing requires a large pool of loans and servicers in order to be economical.

There would be additional benefits which would assist the servicing function. The size of the operation would make specialization easier, so that Loan Assistants could be used to make preliminary servicing calls to ascertain reasons for default and potential for resolution. Journeyman Loan Specialists could concentrate on servicing, working out pay plans, reamortizations, etc. Other Loan Specialists could monitor and handle bankruptcy cases which require coordination with attorneys, courts and others. Other Loan Assistants could specialize in handling the actual foreclosure process.

Regionalization would allow us to concentrate servicers in the West. Studies have indicated that the most effective time to service loans is late afternoon, evenings and weekends. Servicing phone calls made during regular business hours in the Pacific Time Zone can be targeted for late afternoon and evenings for Eastern, Central and Mountain Zones. This alternative is cost-effective since increased phone bills would likely be less than overtime, night differential and keeping VA facilities open after regular business hours for stations in other than Pacific Time Zones. The same logic hold true to a lesser degree for both the Mountain and Central time zones. Automatic callout devices can facilitate calling across time zones during early evening and Saturdays in addition to regular business hours. Other technological innovations such as folderless processing and servicing could be implemented more readily in such a setting due to economies of scale and automation.

3. Arguments Against Regionalization

The primary arguments against regionalization are that relocation costs of transferred employees would be substantial, and there would be a loss of experienced people who do not transfer. The latter problem might be offset by outside hires of private sector loan origination and servicing personnel. There would also be a reduction of institutional knowledge and expertise at the remaining ROs to deal with loan origination and servicing problems by personal contact, since the bulk of knowledge and expertise would be relocated. This could lead to poor morale at the remaining ROs, loss of goodwill and working relationships with local lenders and holders, and diminished ability to provide training to local lenders, servicers and holders. There could also be a decreased ability to recognize local conditions that may adversely affect the program. In addition, the fact that real estate and foreclosure laws vary in each state could cause complications, and lack of familiarity or face-to-face contact with VA attorneys may hamper legal actions. There may also be difficulty in transferring security and title documents from the centers to local PM sections at Regional Offices.

4. Considerations

There needs to be an assessment of the likely effects of regionalization on personnel and career opportunities. Some of the questions to be addressed would include: Would the two sections remaining at the vast majority of ROs continue to be treated as a separate division within the RO, with the LGO positions being retained? If not, what would be the organizational relationship of the two sections to the Director's office? If the LGO positions are retained at all current offices, what kind of grade levels could be supported, in view of the truncated nature of the remaining LG Division? If many mid-level management positions were lost, what would be the long-term implications for the desirability and feasibility of a career in the LG program? With the loss of one-half of most LG Divisions and the associated supporting services from Admin. and Finance, would there be any impact on the supportable grade levels of station Directors?

Criteria for the selection of sites for the processing centers and the determination of the numbers of these sites should include an estimate of the optimum size and span of control, the cost and availability of space, salary costs (especially important when the location differential become effective nationwide), and the usefulness of the western time zones for servicing purposes. Centers should preferably be located in geographic areas which provide an educated and motivated workforce.

VA's IRM systems capabilities are not presently comparable to private sector technology. This was confirmed through visits by members of the task force to private sector Loan Centers which possess "state of the art" IRM systems. Support services for loan origination and servicing functions will need to be provided to fulfill the needs of the center (Finance, Administration, Personnel, District Counsel). District Counsel or General Counsel advice and review will be critical in dealing with state and local jurisdictions with regard to foreclosure (judicial and non-judicial), redemption and title requirements.

Training of RO personnel will be necessary to handle customers who visit the RO for loan origination and servicing functions. Travel costs may be higher due to training needs at local ROs and for lenders/holders.

Notification procedures to the local Property Management section regarding protective custody assignments, title acceptability and various other issues will need modification.

Labor/management impact must be considered.

5. <u>Recommendation</u>

The Loan Processing and Servicing, Liquidation Management and Claims Management functions presently carried out at forty-six regional offices should be relocated in a small number (3-5) of regional processing centers. Fewer than three centers would render the centers too large for an effective span of control; more than five would defeat the proposed economies of scale.

Dependent upon a final configuration being determined, those Loan Guaranty functions remaining in local regional offices must be reviewed. The small size of the remaining Loan Guaranty functions at some offices may preclude efficient operations and not be financially justifiable, and the effectiveness of service to veterans and achievement of program goals could possibly be improved by consolidating several of the smallest LG divisions. Such consolidations should balance the need for minimum sized operations with access to and knowledge of local real estate markets. Consolidation of smaller, inefficient offices would permit more effective use of support services functions and expensive resources such as ADP equipment. Higher travel costs which might be incurred would be offset by the lower support costs to those offices from which Loan Guaranty functions are removed.

The consolidation review of remaining Loan Guaranty offices should not be limited to a review of sites within state boundaries. Geographic location and relationships should also be examined. The customer satisfaction and efficiency achieved by offices which are geographically close but in separate states should be reviewed to determine whether small outbased or satellite offices could more effectively meet our customers' needs.

D. <u>Centralization of Portfolio Loan Management</u>

This option proposes to centralize the management of the portfolio loan accounts from the 46 regional offices with LGY Divisions to one central location where all aspects of portfolio loan management can be performed.

1. <u>As the System Currently Exists</u>

Currently VA manages ± 50,000 portfolio loans among 46 RO LGY Divisions. Of this portfolio approximately 20% of the loans are in default. This includes default of portfolio loans, delinquent VAR 4600 loans and portfolio loans in bankruptcy. The balance of the portfolio accounts are current loans which require VA to handle loan assumptions, name changes, payoff information, tax payments and homeowner hazard insurance premiums out of escrowed funds and loan sales that may occur periodically throughout the year. Depending on the size of the portfolio and staffing at various ROs this work is accomplished by LSRs and clerks who specialize in various functions (large offices) or by LSRs who are responsible for all aspects of the portfolio (small offices).

LSRs must perform primary servicing in a similar manner as the private sector lenders. They must be cognizant of federal and state laws, VA regulations, terms of the Notes and Deeds of Trust, bankruptcy laws, local tax collection requirements and insurance coverage requirements as well as attorney requirements (in some instances). They deal with borrowers/homeowners by telephone, office visit, mail and by field visit.

Loan sales include the performing and/or newer loans. This results in the lower balance, older, generally delinquent loans remaining in the portfolio. Because of this, much primary servicing must be conducted. The various state laws permit loan termination either by judicial or non-judicial process. Some states also provide borrowers with a period of time after foreclosure in which to redeem their property. During this redemption period no final disposition of the property can be accomplished by VA.

The most cumbersome activity of managing the portfolio is payment of ad valorem property taxes and the hazard insurance premiums from the escrow accounts and the property taxes due on VA owned properties (PMS accounts). Depending on portfolio size and personnel, assigned clerks or LSRs actually voucher payment. Some ROs are assisted by private tax service companies for collection of tax bills and preparation of payment.

2. Reasons for Centralizing Management of Vendee Loans

The following factors argue for the centralization of all vendee loans in one location.

There would be an economy of scale by having all ± 50,000 loans serviced by a specialized group of LSRs/clerks. Specialization of servicing efforts would provide several benefits: Loan Assistants can be used to make preliminary servicing calls to ascertain reasons for default and potential for resolution. Journeyman LSRs can concentrate on servicing, working out pay plans, reamortizations, etc. Other LSRs can monitor and handle bankruptcy cases which require coordination with attorneys, courts and others. Other Loan Assistants can specialize in handling the actual foreclosure process. There would be more flexibility to work employees on staggered shifts or cover for vacation due to a larger pool of similarly trained personnel. Policy or procedural changes could generally be directed to one group for primary implementation and general information to other personnel.

Efficient use of "800" telephone numbers with call director could enable the borrower with a touch tone phone to access a data bank to hear information on his specific loan, information regarding loan balances, payoff amounts, escrow account balances, changes of ownership. Automatic callout devices can facilitate calls, which can be made across time zones during early evening, and Saturdays, in addition to regular business hours.

In a larger Portfolio Unit, there would be a larger pool of employees from which to identify high potential future managers. Training of personnel can be consistent and geared to certain aspects of the loan service process (bankruptcy, workouts, foreclosure). Rotational assignments for cross training can be handled in a more effective manner due to the larger pool of LSRs.

It is estimated that the loan sale process can be handled more efficiently at one location than at 46 ROs and VACO. After the property is sold at the RO, the vendee loan file would be shipped immediately to the centralized loan management center for PLS loan establishment.

Tax service contracts could be more advantageous when escrowed accounts or PMS accounts are of sufficient volume to entice competition. Insurance premiums can be paid electronically by VA to major insurance carriers (Allstate, State Farm and others) based upon tape to tape exchanges.

3. Arguments Against Centralization of Portfolio Loan Management

There could be difficulty in transferring paper loan documents from the various PM sections to a centralized locale - problems of incompleteness and delays. This could lead to a diminished ability to obtain corrected documents for loan sales.

Relocation costs of transferred employees would be substantial, and there would be a loss of experienced people who do not transfer. This might be offset by outside hires of private sector loan servicing personnel. There would be a concomitant reduction of expertise at field station level to deal by personal contact with servicing problems.

The over 16,500 local tax collectors have varying requirements, due dates and degrees of "workability" with VA. It could be more difficult to deal with them from a centralized locale. Foreclosure laws also vary in each state and lack of familiarity or face-to-face contact with VA attorneys may hamper processes.

It should be noted that the existing VA mortgage loan accounting system is antiquated and would be cumbersome as a centralized database.

4. Considerations

Our ADP capabilities are not presently comparable to private sector resources which makes our loan management function "unique" and in need of major overhaul. In this process, we should ensure that our systems are compatible with the large lenders, servicers, and insurance companies which deal with our program. Neither centralization nor regionalization are feasible unless our modernized ADP systems are in place.

In choosing a site for this function, consideration must be given to those geographic areas that possess an educated and motivated workforce that would form the core for potential recruitment necessary to provide full portfolio loan management. VBA Circular 26-91-26 describes a Loan Servicing Workload Model for both vendee and guaranteed loans. A visit to a nationwide mortgage servicing company by a member of the task force enabled us to observe firsthand how portfolio loan servicing can be handled on a nationwide basis. Cognizant of the fact that VA will continue to conduct loan sales on the secondary market ("VINNIE MAC") with the remainder of the portfolio being newly originated loans awaiting sale or unsalable loans, we would suggest that this centralized loan management function could be accomplished with less than 200 FTE.

Support services (Finance, Administration, Personnel, IRM, District Counsel) are critical to the success of any centralized function. There is a need for daily interaction with Finance for mortgage loan accounting (e.g. account reconciliations, payment applications). District Counsel or General Counsel advice and review will be important when dealing with state and local requirements with regard to foreclosure (judicial/ non-judicial) and redemption.

Some offices now have PM property taxes paid by the PM section while others incorporate it with LS&C to be handled simultaneously with PLS escrow accounts. Notification procedures to local PM sections of protective custody assignments, title acceptability and various other current interfaces now conducted at ROs would require restructuring.

Travel costs will be higher with one centralized location, since management personnel will need to travel to other cities to meet with various firms who provide service to the centralized portfolio servicing office. Training must also be provided to VA field personnel to handle the portfolio loan customers who visit their facility for various services (current/delinquent).

There could be problems coordinating foreclosures, and referrals for bankruptcy representation in different jurisdictions. Some stations now contract with private attorneys, some use only US attorneys, and others "deputize" their District Counsel staff as U.S. Attorneys.

5. Recommendation

The portfolio loan management operation should be centralized into one national processing center to bring VA into conformance with contemporary industry practices. It should be co-located with one of the regional servicing/processing centers. Our modernized ADP systems must be in place in order for a centralized operation to make sense.

V. Organizational Lines of Authority

Among other issues, the task force was asked by the Chief Benefits Director to examine the organizational lines of authority within VBA as they affect Loan Guaranty's veteran customers. The task force phrased the question thus: "Is the veteran better served if the Loan Guaranty Service (CO) has a line or staff relationship with its field operations?" The task force spent more time wrestling with this issue than any other, and we did not always agree on every point.

A. Existing Organizational Structure

Although it was not always the case, for many years, the CO Loan Guaranty Service has been a staff office, providing only program oversight and policy advice to the CBD. In the field, the Loan Guaranty division reports to the regional office Director, not CO Loan Guaranty Service. "Line" authority goes from the CBD to the Area Director, thence to the station Director, and finally to the LGO. This line/staff dichotomy is identical for each of the Services within VBA; the only exceptions are the District Counsel, who reports directly to the General Counsel, and the Loan Guaranty Monitoring Units, which report to CO Loan Guaranty Service. In those two cases, the regional office Director is "landlord" and District Counsel and the Monitoring Units are "tenants."

B. Problems with the Current Organizational Structure

From the perspective of the CO Loan Guaranty Service, there is a certain frustration in being in a position where the top VA management, Congress, OMB, and the public expect the Service to be responsible for the program, yet in reality the Service has no direct authority to allocate resources or manage workloads. Dealings with program participants who operate in several or all jurisdictions are difficult to coordinate, and the lack of operational authority hampers CO's ability to respond to complaints of untimely, uncooperative or rude service by program officials in regional offices. These problems, it is felt, ultimately result in poorer service being provided to our veteran customers and other program participants.

From the perspective of the field, there are also some frustrations. It is cumbersome to respond to changes in workload and to shift work or resources from one field station to another, especially from one Area to another. And disparities in grade levels, position descriptions, and performance standards from one office to another cause some dissatisfaction. These difficulties also impact on the service provided to veterans.

C. Alternative Organizational Model

It could be possible to operate the Loan Guaranty program like the District/General Counsel's office, with direct line authority from CO, even though the program would be housed in the regional office and receive administrative, personnel and finance support from there. The Loan Guaranty Service Director would still report directly to the CBD, but would have a line rather than staff position.

D. Possible Advantages to "Line" Authority

The primary benefit would be the unity of purpose that occurs with incorporation of line authority with program direction. Those who have the authority for a program would be the ones who are held accountable for its performance. Control of resources and management of workload would be simplified, and dealings with regional or national lenders, servicers, etc. would be facilitated. Staffing could be apportioned on a consistent and rational basis nationwide.

It should be easier for local LG programs to obtain assistance from other parts of the country when faced with sudden increases in workload, either through shifting of personnel or transferring work from one part of the country to another. Consistent performance standards, job descriptions, and grade levels should help improve morale and productivity. There would be fewer problems in dealing with lenders and servicers whose activities cross station boundaries, and who claim to be receiving different information from different offices.

E. Potential Problems with "Line" Authority

In the present situation, where the Loan Guaranty division reports to the RO Director, the division receives support from the Veterans Service Division, Information Resources Management, Administration, Personnel, Finance, etc. (Loan Guaranty also depends to a lesser degree on the assistance of Compensation, Pension and Education and Vocational Rehabilitation and Counseling.) A persistent concern was expressed, particularly by the members of the task force who are from the field, that if the Loan Guaranty divisions in the field did not report to the Regional Office Directors, they would not "belong," and would be isolated, without the necessary support to perform adequately. Nationwide, Loan Guaranty operations are supported by several hundred FTEE who are on the rolls of the regional offices, but not Loan Guaranty. For Credit Management reporting purposes, this figure is estimated in the VA FY 1993 Budget Submission as follows:

Veterans Services	197
Compensation, Pension and Education	3
Vocational Rehabilitation and Counseling	4
Information Resources Management	39
Support services	721
Total	964

If a transition were made to a "stand-alone" situation for Loan Guaranty, it was feared that these resources would not be transferred to the Service. This, they felt, would impact adversely on the service they were able to provide to their veteran customers.

In a stand-alone mode, the Loan Guaranty program would clearly be separated from the other package of services and benefits provided to veterans by VBA. While this would establish direct accountability by the Service Director, it would also increase the exposure of the Service to other political pressures, increasing the vulnerability that the VA's housing benefit program might eventually be absorbed by, or merged with, other Federal housing programs. VA would then run the risk of having a major veterans benefit managed and directed by another agency which would not have the veterans' interests as their primary concern.

F. Recommendation

When asked the question, "Would the veteran be better served by Loan Guaranty (CO) having line authority over the 46 LG divisions in the field?" the response was unanimously negative. It is the recommendation of this task force that a change from staff to line not be made in the present geographical configuration of regional offices. When the question was reformulated to ask if the veteran would be better served by Loan Guaranty (CO) having line authority over the proposed regional servicing/processing centers, the response was mixed, though with a clear majority still in the negative.

G. Minority Opinion

A minority of the task force believes that a synergism (the sum of the parts is greater than the whole) occurs and veterans, as well as our other constituencies, are best served when management is organized along program lines:

* Currently the Chief Benefits Director has sole authority and responsibility for the Loan Guaranty Program. Conferring equal authority and responsibility to the Program Director creates program-specific accountability at a lower level within VBA.

* The structure would bring higher level executive direction closer to program operations and create a broader horizontal organization for the Loan Guaranty program.

* With unity of direction and purpose, one head and one plan for a group of activities, organizational objectives are more likely to be declared and achieved.

* An organization whose executives and managers share similar technical expertise is better poised to understand, support, and achieve program objectives.

* Such managers are better prepared to exercise leadership and communicate those objectives throughout the organization.

* Similarly, employees will identify with program objectives, believe in them, and do their part to accomplish them.

* Organizing along program lines would provide consistency throughout the program -- benefits and services delivery, allocation of resources, standardized operating procedures, attention to all constituencies, etc.

* Private sector program participants who operate regionally or nationally could conduct discussions and obtain decisions from one person on issues which affect their program participation.

* The size of the Loan Guaranty function (over 2,000 FTE, plus supporting personnel from other offices) would be large enough to maintain internal political clout to get its fair share of VBA resources.

* Large processing centers reporting to the Service Director in CO could be workable because the centers would be large enough to support their own administrative support staff, which could also be used to support small outreach offices (PM & C&V) in each area.

* The span of control (Service Director to Regional Processing Center Director) would be more efficient than to 46 ROs.

VI. COST - BENEFIT ANALYSIS

This cost/benefit analysis considers the consolidation of the 46 separate loan processing and loan servicing and claims functions into three(3) locations (existing regional offices).

A. <u>Assumptions</u>

The following presents the assumptions considered in execution of the consolidation plan, the specific assumptions for the cost/benefit analysis, the methodology for determining savings, the detail of the savings and a summarization of the findings.

PLAN EXECUTION ASSUMPTIONS

- Consolidation at three locations in the Western time zones.
- Consolidate all portfolio loan functions at one location.
- Consolidation will take place in three stages over a period of three years beginning in 1995. One-third of the consolidation will take place in 1995, one-third in 1996 and the final one-third in 1997. However, consolidation of the portfolio function will take place in 1996.
- Consolidation will only begin once stage one of modernization is complete at the first location and LCS redesign has been prototyped and certified as ready for nationwide installation.
- Portfolio loan consolidation will take place only after commercial portfolio loan accounting software has been purchased and modified according to Loan Guaranty needs.
- Rental costs of space at the three locations equal the savings in rental costs as a result of downsizing of the remaining Loan Guaranty divisions. Certainly rental costs would be an important part of site selection. In the long term there probably would be a savings, however, no attempt was made to sort out each field station's space costs or lease arrangements.
- 1995 costs were arrived at by inflating '92 costs by 3% and each subsequent year by 3%.

COST ASSUMPTIONS

- Those personnel eligible for retirement will take retirement in lieu of moving to a new location.
- 30% of technical staff (GS-7 and above) will accept reassignment.
- 10% of clerical staff (GS-6 and below) will accept reassignment.
- 5% FTE savings for loan processing and loan service & claims activity.

- 15% FTE savings for portfolio loan activity.
- 30% of those identified for separation find other employment at no cost to VA. This includes positions within VA, other Federal agencies, or the private sector.

B. Cost Computations

COST COMPUTATIONS PER EMPLOYEE

Average salary in '92 dollars =	32,722
Average leave balance in hours =	150
Average total cost of unemployment compensation for separated employees =	8,710
Severance pay based on 10 years of service in weeks =	10
Average severance pay in '92 dollars =	6,293
Average relocation costs in '92 dollars =	50,577

DATA USED TO COMPUTE THE COSTS

Total FTE available for relocation	1,071
Retirements	96
Relocations	215
Separations	760
New Hires	685

COMPUTED COSTS OF CONSOLIDATION

Costs of relocating 215 employees in '92 dollars =	10,874,055
Costs of 760 separations in '92 dollars =	11,402,280

Costs of relocating 215 employees in '95 dollars =	$ 11,882,190
Costs of 760 separations in '95 dollars =	$ 12,458,680

C. Benefits

The benefits of consolidation of the Loan Processing and the Loan Service and Claims functions at a few locations are described earlier in the study. In the Loan Processing function, the dollar benefits that will accrue to the government are generally intangible. The primary benefit will be better service to veterans and those individuals and organizations that help veterans obtain GI loan financing. We have made a general assumption that economies of scale and reduced level of supervisory overhead will produce a five percent decrease in Loan Processing personnel. After full implementation, this saves 17 FTE. A five percent reduction in Loan Service and Claims personnel can also be achieved corresponding to 21 FTE.

We have made a similar general assumption in connection with the consolidation of portfolio management. However, we believe a 15 percent FTE savings is realistic considering that consolidation will be coupled with modern loan management systems and that employees will be dedicated full time to this activity. A 15 percent FTE reduction saves 32 FTE.

The potential for savings in the Loan Service and Claims function is very substantial. The major costs of operating the Loan Guaranty program stem from foreclosures of GI loans. These costs are offset by fees paid by veterans and subsidy appropriations from the Congress. One of the major operational goals of program management is to minimize the number of foreclosures. Defaults which can be cured provide a duel benefit. Cures help veterans retain their homes and reduce the cost of the program to the taxpayers. VA closely tracks the cure ratio as a measure of the level of foreclosures compares to total defaults. The cure ratio is expressed as a percent of defaults that do not result in a claim paid to the lender/servicer. Therefore, a cure ratio of 75 percent for a fiscal year indicates that 75 percent of all the defaults processed during that fiscal year did not result in a claim payment by VA. During the past 20 years the cure ratio has ranged from about 65 to 90 percent. The most important influence on the cure ratio is the economy, i.e., inflation, unemployment, interest rates, growth in GDP, etc. It represents the environment in which the program operates.

However, VA can take actions that influence the cure ratio in a positive way. Data over the past nine years indicates that the level of supplemental servicing, as measured by contacts with borrowers, can on margin influence the cure ratio. In seven of the last nine years the cure ratio increased or decreased in relation to increases or decreases in total supplemental servicing contacts. In the last four fiscal years the level of contact has increased each year as the cure ratio improved each year. During the Houston Pilot project on loan servicing increased FTE were able to increase contacts by 176 percent. The cure ratio increased from 50.5 percent to 63.0 percent during the same period. There is ample evidence that increased supplemental servicing contacts will cure more defaults over the long run. The economy will always play the strongest role in the level of defaults and cures but supplemental servicing can produce positive results. Even if the cure ratio is decreasing because of a deteriorating economy, supplemental servicing can slow the rate of descent.

At consolidated servicing centers, total contacts with delinquent borrowers will increase significantly. Well organized units using up to date ADP equipment and the redesigned LCS will undoubtedly make more contacts. This is especially true considering the advantages of servicing from the Western time zones. Borrowers in the East can be contacted at 6-7 PM during normal business hours in the West. Conservatively we estimate that total contacts will increase by 20 percent. Using data from the Houston Pilot we estimate that this would improve the cure ratio by 2.82 percent.

$\frac{\text{Percentage Increase in Contracts}}{\text{Percentage Increase in Cure Ratio}}$		$\frac{176.0}{24.8}$ = 7.0967
$\frac{\text{20 Percent Increase in Contacts}}{7.09}$	=	2.82 percent

Assuming 165,000 defaults processed in fiscal years 1995, 1996 and 1997 the following savings are projected:

<u>FY 1995</u>

$\frac{165{,}000}{3}$ = 55,000 defaults processed at the first consolidated site

55,000 x .0282 = 1551 additional cures

average claim $15,455 x 1551 = $23,970,705

In addition, VA will acquire properties in 82 percent of the foreclosure cases and incur an average loss on sale of $3,600

.82 x 1551 x $3,600 = $4,578,552

Claim Savings	$23,970,705
PM Savings	4,578,552
TOTAL	$28,549,257

<u>FY 1996</u>

Total additional cures are projected to be 3102 from two consolidated sites.

3102 x $15,950 (Avg Claim) = $49,476,900

.82 x 3102 x 3600 = $9,157,104

Claim Savings	$49,476,900
PM Savings	9,157,104
	$58,634,004

<u>FY 1997</u>

Total cures from all three sites is estimated to be 4,653

4653 x $16,460 (Avg Claim) = $76,588,380
.82 x 4653 x 3,600 = $13,735,656

Claim Savings	$76,588,380
PM Savings	13,735,656
	$90,324,036

D. Cost Benefit Analysis of Loan Processing and Loan Service and Claims Consolidation

COSTS

	1995	1996	1997
ONE TIME COSTS			
RELOCATIONS	$2,818,566	$6,432,410	$2,990,217
SEPARATIONS	$2,950,740	$6,753,916	$3,130,440
TOTAL	$5,769,306	$13,186,326	$6,120,657

SAVINGS

	1995	1996	1997
PERSONNEL			
LP	$258,516	$532,543	$777,069
LS&C	$301,602	$621,300	$959,909
PL		$1,420,115	
CURES	$28,549,257	$58,634,004	$90,324,036
TOTAL	$29,109,375	$61,207,962	$92,061,014

SUMMARY

3 YEAR TOTAL COSTS (DISCOUNTED 5.6%)	$23,671,535
3 YEAR TOTAL SAVINGS (DISCOUNTED 5.6%)	$168,928,574
BENEFIT/COST RATIO	7.136

Fiscal years 1996 and 1997 costs and savings discounted at current (9-1-92) 5 year Treasury note rate.

VII. CONCLUSION

The task force has examined the Loan Guaranty program from one perspective: "How can our veteran customers be better served?" We have looked at the history and current operation of the program, and analyzed the various internal and external factors which affect it. We specifically examined the work processes themselves, the distribution of the workforce, and the lines of authority under which the program operates.

Our conclusion is that although no radical restructuring is called for, there are a number of opportunities for improvement. On the operational level, most of our recommendations are toward further automation, and are dependent upon implementation of the VBA ADP Modernization efforts. We feel that the loan processing and servicing operations would be more efficient if they were regionalized into a small number of larger processing centers, as is the growing practice in the industry. Centralization of management of all vendee loan activity in one of these locations seems logical. Significant ongoing cost savings can be achieved by concentrating these activities. If these moves are made, the resulting Loan Guaranty divisions in the regional offices would be about half the size they are now, and would consist mainly of activities tied directly to the real estate (appraisals, property management, property sales). Some of these operations would be so small that they might logically be consolidated into nearby regional offices. Finally, the task force felt that the Loan Guaranty operation across the country functions better under the present reporting structure than it would outside the Regional Office umbrella.

REGIONAL OFFICES RANKED BY WORKLOAD AND SIZE

STATION	FY1991 LOANS CLOSED	STATION	FY1991 DEFAULTS REPORTED	STATION	FY1991 PAID FTE
STPE	15490	STPE	14578	HOUS	138.3
LOSA	14212	LOSA	12479	LOSA	134.3
ROAN	10249	WACO	11019	WACO	112.8
ATLA	8638	HOUS	10652	DENV	105.6
WASH	7708	ATLA	7285	STPE	105.1
SANF	6859	ROAN	6961	CLEV	92.4
PHOE	6364	CLEV	6882	CHI	81.4
SEAT	6166	PHOE	6117	DETR	73.8
WACO	5944	CHIC	5788	ROAN	66.5
WINS	5811	DENV	5765	STPA	62.5
DENV	5760	WINS	5646	WINS	58.7
STPA	5036	DETR	4392	MUSK	57.8
CLEV	5010	NASH	4355	PHOE	54.5
CHI	4854	WASH	3990	ATLA	53.5
HOUS	4749	INDI	3845	SANF	50.9
NASH	4451	SANF	3828	NEWO	49
BALT	4030	STPA	3817	SEAT	48.7
DETR	4026	MUSK	3518	IND	42.9
MANC	3999	COLU	3351	MONT	40
COLU	3834	NEWA	3287	WASH	38.7
MILW	3622	NEWO	3208	NASH	37.4
MONT	3586	MONT	3099	PHIL	36.4
MUSK	3337	PHIL	2925	NEWA	33.5
STLO	3218	STLO	2584	STLO	33.4
IND	3114	SEAT	2373	COLU	33.4
WICH	2662	MANC	2304	LITT	29.2
PHIL	2308	BALT	2008	MILW	28.1
ALBU	2291	WICH	1962	MANC	26.4
NEWA	2250	MILW	1773	WICH	24.4
LINC	2142	LITT	1762	LOUI	23.5
LOUI	2125	SANJ	1752	DESM	21.8
NEWO	2004	JACK	1700	BALT	21.4
PORT	1980	NEWY	1661	JACK	20.1
LITT	1717	LOUI	1450	NEWY	19.9
NEWY	1468	PITT	1365	PITT	19
BOIS	1369	SALT	1181	SALT	18.4
JACK	1268	ALBU	972	BOIS	16.7
DESM	1224	DESM	944	PORT	16.7
SALT	1199	LINC	898	SANJ	15.9
PITT	875	BUFF	654	ALBU	14.6
FTHA	678	PORT	635	FTHA	14.1
SANJ	634	BOIS	615	LINC	14
ANCH	616	HUNT	472	BUFF	11
BUFF	596	FTHA	418	HUNT	10.6
HUNT	521	ANCH	334	ANCH	10.4
HONO	428	HONO	230	HONO	8
	180422		166834		2025.7

ATTACHMENT B

LOAN PROCESSING BY REGION - FY 91

EASTERN REGION - Maine, New Hampshire, Vermont, Massachusetts, New York, Rhode Island, Connecticut, New Jersey, Pennsylvania, West Virginia, Maryland, Virginia, DC, Delaware.

CENTRAL REGION - Ohio, Kentucky, Indiana, Illinois, Michigan, Wisconsin, Minnesota, Iowa, Missouri, Kansas, Nebraska, South Dakota, North Dakota.

SOUTHERN REGION - North Carolina, South Carolina, Georgia, Florida, Puerto Rico, Alabama, Mississippi, Tennessee, Texas, Oklahoma, Arkansas, Louisiana.

WESTERN REGION - Alaska, Hawaii, California, Nevada, Arizona, Utah, New Mexico, Colorado, Wyoming, Montana, Idaho, Oregon, Washington.

EASTERN REGION

East-1 - Maine, Rhode Island, Massachusetts, Vermont, Connecticut, New Hampshire, New York, New Jersey, Pennsylvania, Delaware
11,496 Closed Loans in FY 91
Current ROs - 6

East-2 - Maryland, DC, Virginia, West Virginia*
22,508 Closed Loans in FY 91
Current ROs - 4

10 current ROs in the region. 34,004 closed loans in FY 91.
* Pittsburgh RO currently has jurisdiction over some West Virginia counties.

CENTRAL REGION

Central-1 - Ohio, Indiana, Kentucky, Michigan, Wisconsin, Illinois.
22,751 Closed Loans in FY 91
Current ROs - 6

Central-2 - Minnesota, North Dakota, South Dakota, Iowa, Nebraska, Kansas, Missouri.
14,283 Closed Loans in FY 91
Current ROs - 5

11 ROs currently in the region. 37,034 closed loans in FY 91.

SOUTHERN REGION

South-1 - North Carolina, South Carolina, Tennessee, Georgia.
22,734 Closed Loans in FY 91
Current ROs - 4

South-2 - Florida, Alabama, Mississippi, Puerto Rico
20,978 Closed Loans in FY 91
Current ROs - 4

South-3 - Texas, Oklahoma, Arkansas, Louisiana.
17,751 Closed Loans in FY 91
Current ROs - 5

13 ROs currently in the region. 61,463 closed loans in FY 91.

WESTERN REGION

West-1 - Arizona, New Mexico, Colorado, Utah, Wyoming.
15,614 Closed Loans in FY 91
Current ROs - 4

West-2 - Alaska, Washington, Oregon, Idaho, Montana.
10,809 Closed Loans in FY 91
Current ROs - 5

West-3 - California, Nevada, Hawaii.
21,499 Closed Loans in FY 91
Current ROs - 3

12 ROs currently in the region. 47,922 closed loans in FY 91.

The breakdown of the existing VBA field areas presented above is a suggested scenario aimed at dividing loan processing activities roughly evenly by FY 91 workloads while retaining as much geographic identity as possible. ROs that currently have jurisdiction over several states or that share a state with another RO have been kept together. They represent loan processing units within the region that may or may not be under the same roof. The areas of responsibility for loan examiners, while larger than present, would still be manageable with respect with such differences as income tax rates and laws, labor market trends, rental markets; i.e., the knowledge of the subtleties that make underwriting an art. A review of the existing geographic regions used for residual income guidelines may be appropriate before implementing these regional processing units. Loan Servicing workloads have not been considered here and it is probable that dividing the regions as above would not result in similar workload levels.

LOAN GUARANTY EMPLOYMENT

	O/C	C&V	LP	LS&C	PM	Files
NEW YORK	2.3	4.2	5.8	5.5	1.8	1.6
BUFFALO	3.6	1.1	2.0	2.3	1.9	0.4
NEWARK	5.0	5.9	7.7	16.4	6.3	0.7
PHILADELPHIA	6.9	3.6	4.9	12.8	5.0	3.0
PITTSBURGH	3.0	1.9	2.7	6.9	3.6	0.6
BALTIMORE	4.0	4.3	5.1	6.4	2.4	1.0
ROANOKE	8.2	9.8	12.3	19.9	22.4	0.0
HUNTINGTON	2.2	2.0	1.0	2.8	2.0	0.2
ATLANTA	4.0	11.1	5.7	24.3	10.0	1.2
ST. PETERSBURG	4.1	20.4	16.6	42.6	23.4	4.0
WINSTON SALEM	3.9	11.1	14.8	18.9	8.4	1.9
COLUMBIA	2.8	3.7	6.6	8.3	6.9	2.0
NASHVILLE	3.3	9.0	7.4	10.9	7.3	0.0
NEW ORLEANS	3.2	6.6	5.8	19.1	12.3	1.8
MONTGOMERY	2.6	6.3	6.9	13.5	6.5	1.7
JACKSON	2.0	3.1	3.3	7.2	2.3	1.3
CLEVELAND	15.4	9.5	9.2	30.6	19.2	4.2
INDIANAPOLIS	3.7	7.1	5.6	18.2	10.2	0.0
LOUISVILLE	7.9	2.5	4.2	6.8	3.4	1.3
CHICAGO	4.0	9.7	11.8	30.6	23.8	4.4
DETROIT	4.5	6.2	9.9	32.2	12.4	0.0
MILWAUKEE	2.0	3.8	5.0	8.8	6.0	1.0
ST. LOUIS	3.7	4.9	8.1	9.3	6.3	2.5
DES MOINES	2.0	3.8	3.9	5.7	4.9	0.5
LINCOLN	3.4	1.4	3.5	3.7	1.5	0.3
ST. PAUL	11.0	9.2	12.7	18.2	10.0	2.0
DENVER	13.8	11.3	13.0	32.8	23.6	0.0
ALBUQUERQUE	2.0	1.7	2.1	6.1	3.1	1.1
SALT LAKE CITY	1.0	3.8	5.0	4.3	2.4	1.1
SAN FRANCISCO	4.3	11.4	14.3	12.8	6.0	2.0
LOS ANGELES	5.1	29.7	30.1	38.5	19.2	0.0
PHOENIX	3.0	6.6	10.0	20.6	14.2	3.0
SEATTLE	8.3	9.2	8.7	11.7	4.5	2.7
BOISE	3.0	3.0	3.1	3.9	3.0	1.0
PORTLAND	1.7	4.0	4.1	4.3	1.0	0.7
WACO	17.9	12.2	11.9	43.7	28.8	0.0
LITTLE ROCK	6.4	3.1	5.0	7.9	6.0	1.4
MUSKOGEE	3.0	9.9	8.8	17.7	12.2	4.1
SAN JUAN	2.0	2.4	1.4	5.4	1.0	1.0
HONOLULU	1.9	2.0	2.1	1.6	0.1	0.2
HOUSTON	7.0	15.7	13.9	55.0	35.4	0.0
ANCHORAGE	2.4	1.4	1.2	2.0	0.8	0.3
WASHINGTON	4.8	10.0	5.8	8.4	6.7	0.0
MANCHESTER	3.0	7.3	8.7	10.4	3.3	2.1
FT. HARRISON	2.6	2.0	3.3	4.1	3.0	0.0
WICHITA	1.9	1.8	3.9	6.7	6.9	0.5
NATIONAL TOTALS	213.7	310.5	338.6	680.1	401.4	58.8

NOTE: Source for manpower numbers in this study - DOOR Report 2611 May, 1992 "Total Hours." Totals may vary because of rounding. Indirect labor is reported under the Office of the Chief's cost center, but may reflect work done in functional areas; thus the figures may be slightly misleading.

Region	Chief	C&V	LP	LS&C	PM	Files
Eastern	43.0	50.0	55.9	91.9	55.3	9.7
Central	59.6	60.0	77.9	171.0	104.7	16.6
Southern	62.2	114.5	108.0	274.4	160.5	20.5
Western	49.0	86.1	96.9	142.7	80.9	12.1
TOTALS	213.7	310.5	338.7	680.1	401.5	58.8

Based on the above, a staffing-neutral consolidation of LP and LS&C would affect about 1,019 employees, leaving 712 C&V and PM employees to fill the required field presence. An additional 272 employees in Offices of Chiefs and Files could conceivably be redistributed between consolidated locations and field stations.

GI Loan Servicing

1. Definition

GI loan servicing consists of all actions performed by VA from the time a GI loan is made until the loan is paid in full or until it is terminated and accounts are settled with the loan holder. Additionally, there is post-foreclosure service provided to veterans relating to debt establishment and debt waiver activity.

2. Background

VA-guaranteed loans are made by private sector lenders to veterans who meet eligibility and underwriting criteria established by law. Veterans, as a group, are good credit risks and over 90% repay their loans. Approximately 8% of the loans are terminated.

a. Loan holder's responsibility. The loan holder or its servicing agent (servicer) has the primary responsibility for managing its portfolio of VA-guaranteed loans. The servicer collects the monthly loan payments, makes disbursements to pay property taxes and hazard insurance premiums, provides customer services and responds to borrower's loan questions, processes loan assumptions and payoffs, and conducts delinquent loan collection, foreclosure, and claims settlement.

b. Loan holder's responsibility to VA. From a practical perspective, we estimate that in 80% of all loans, the only requirement is to report to VA that the loan has been repaid. In about 20% of the cases servicers will have to make other reports to VA. The reasons for those additional reports are loan delinquencies, involvement in legal actions, or loan foreclosures.

c. VA involvement. For the majority of loans VA has little, if any, involvement except to offer customer service when a veteran has a dispute with his/her loan servicer. For the estimated 20% of loans that become delinquent and are reported to VA, there is considerable involvement, both in assisting the veteran to retain homeownership, and minimizing losses to the government.

3. VA's Role

VA's assumes the following role in assisting veterans to retain homeownership and minimizing program losses.

a. Supplemental Servicing

Due to the nature of the Loan Guaranty Program as a benefit, VA requires that servicers report loan delinquencies to VA. Upon receiving notice, our staffs determine whether the servicer has performed adequate loan servicing and developed sufficient information to conclude whether the loan can be expected to reinstate or whether the loan is insoluble and should be terminated.

It has been the longstanding policy of VA to encourage GI mortgage lenders to extend forbearance to borrowers who find themselves in temporary difficulties through no fault of their own. In loan default cases, the lender is responsible for contacting the borrower, determining the reason for the default, and making arrangements for repayment of the delinquency. Early servicing is extremely important, and this responsibility falls on the lender. Later servicing is also effective, and this responsibility falls in large part on the VA.

If the lender's efforts to effect a reinstatement of the loan are not successful by the time three installments are due and payable, the default must be reported to VA, together with the holder's explanation of the reason for the default and a summary of its servicing efforts. Upon receipt of such notice, VA performs supplemental servicing and takes an active role in working to protect the interests of the veteran-borrower and the Government.

VA closely reviews the lender's servicing of the account and follows up by attempting to contact the borrower by letter, mailgram, telephone and/or personal visits to the property. Once contact has been established, based on the facts in the case, VA personnel may offer financial counseling and/or may intercede with the lender on behalf of the veteran in order to obtain forbearance or arrange a reasonable repayment schedule in appropriate cases. Also, VA is in contact with local agencies that provide assistance in finding jobs for veterans, or aid with their daily subsistence needs or help in making direct mortgage payments. When appropriate, delinquent borrowers are referred to such agencies so that they may apply for assistance.

Lenders are afforded considerable latitude by VA regulations in modifying the terms of a loan to prevent foreclosure and help a veteran to retain and pay for his or her home. The lender has broad discretion in extending or reamortizing a loan in order to cure a default or to prevent imminent default. VA also has an Interest Rate Reduction Refinancing (IRRR) program which can aid in reducing monthly loan installment amounts if interest rates have dropped since the time the original loan was made. The VA does not have the authority, however, to require a lender to modify or refinance a loan if it is unwilling to do so.

If no arrangements for reinstatement are made and the lender files a Notice of Intention to Foreclose, VA regulations require that foreclosure procedures cannot be started for 30 days, during which period VA is afforded additional time to try to service the loan. Even after foreclosure has been initiated, supplemental servicing continues to explore every possibility to assist the borrower.

When our efforts to secure additional forbearance are unsuccessful, VA has discretionary authority to "refund," i.e., to purchase the loan from the lender. The law providing this authority to VA does not vest borrowers with any right to have their loans refunded, or to apply for refunding. Nevertheless, VA considers whether refunding is in the best interests of the veteran and the Government in every case before foreclosure. When VA refunds a loan, it may be reamortized to eliminate a delinquency and the interest rate may be reduced up to three percent below the maximum rate for new GI loans in order to lower the monthly installment payments.

When a borrower has no realistic prospects for maintaining even reduced mortgage payments, VA will encourage a private sale of the home to avoid foreclosure. We realize such a sale can be difficult to arrange if the property is worth less than the total amount owed on the loan, as is often the case in areas with depressed resale markets. In such a situation, VA may be able to offer assistance by using a procedure which enables us to compromise a Loan Guaranty claim. This procedure can be considered if the difference between the loan indebtedness and the purchase price is less than the amount of VA's maximum guaranty. In such cases, if a veteran finds a buyer who will purchase the property for its fair market value and the proceeds of the sale are applied to the existing indebtedness, a compromise agreement would enable VA to pay a claim for the difference between the sale price and the loan indebtedness. Under such an arrangement, the veteran would remain liable only for the amount of claim paid by VA, which should be considerably less than the claim payable if foreclosure occurs. Any such compromise agreement would have to be approved in advance by the local VA office of jurisdiction.

When a borrower is unable to cure the default, refunding is not appropriate, and a private sale cannot be arranged, VA considers approving the acceptance of a deed in lieu of foreclosure. If acceptance of the deed will be in the best interests of both the borrower and VA, then VA will approve it. If a deed in lieu of foreclosure is not feasible, the lender will generally proceed with foreclosure.

The assertion that servicing loans (providing default assistance) is beneficial to lenders is evidenced by the fact that virtually all lenders (loan holders) provide such servicing, and Government (and Government-chartered) agencies including VA, HUD, GNMA, FNMA, FHLMC etc., require lenders to ensure that such servicing is performed. Mortgage banking publications constantly extol the virtues of default assistance, and provide advice on how to maximize these efforts, such as contacting mortgagors on evenings and weekends, when they are more likely to be available.

b. Termination/Monitoring the Holder

Another function of the LS&C Section is to monitor the holder's actions in the default and foreclosure of a GI loan, to ensure that the holder services (and terminates when necessary) the loan in accordance with industry standards as well as pertinent laws and regulations.

Based on information provided by the loan servicer and information developed by our staff, if there is no reasonable likelihood of the veteran retaining homeownership, then it is necessary to reduce VA's claim liability when the loan is terminated. Efficient loan termination also reduces veterans' debts.

(1) Termination of the loan is the sole responsibility of the mortgage holder. However, VA monitors the holder's actions and under 38 CFR 36.4319f may establish a cutoff date for the accrual of interest and expenses on the account if foreclosure is unduly delayed. This serves to limit the guaranty liability of VA and the resulting indebtedness for which a veteran may become liable. Also, VA attempts to ensure that the loan account is credited with a reasonable amount as the proceeds of the foreclosure sale. Prior to a foreclosure sale VA determines the fair market value of the property based on an appraisal made by a reputable and qualified fee appraiser. The net value of the property is then established by reducing the fair market value by VA's estimated expenses for acquiring, maintaining and reselling the property. Stations have recently received PC software which will automatically generate the net value advice letters to lenders.

When a GI loan is foreclosed, VA normally accepts conveyance of the property from the holder for its net value to VA. If the total outstanding indebtedness exceeds the net value of the property, VA will generally pay the holder the difference as a claim under Loan Guaranty. Any failure on the part of the holder to service the loan properly or foreclose promptly may result in an increase in the amount of the claim payable by VA. VA takes several steps to ensure that our liability, as well as that of the veteran, is limited in such cases.

(2) Monitoring Seriously Delinquent Loans. Our efforts to monitor the holder's actions with regard to timely foreclosure of GI loans are reflected in a report available to our field stations which lists those cases that are 6 months delinquent and not yet in foreclosure.

This report, the Serious Default Action List, was created to assist stations in identifying those cases where delays in initiating foreclosure exist. Effective use of the report has resulted in lower costs to VA in the form of reduced claims under Loan Guaranty. These cutoffs act to limit the veteran's liability as well as VA's.

In addition to the use of interest cutoffs, field stations perform a review of the information provided by the lender when the default is reported, when the status of the loan is updated, when correspondence or legal documents are received, and when the claim under Loan Guaranty is filed. During these reviews, the station becomes aware of any servicing deficiencies on the part of the lender. In cases where such deficiencies are indicated, the station sends the file to VA Central Office for advice and/or a review of their recommendations for reducing the lender's claim commensurate with the amount by which the lender's failure to service the loan properly has increased the Secretary's liability.

4. Basic work processes

In order to manage the annual workload of approximately 175,000 reported defaults of VA-guaranteed loans, 35-40,000 foreclosures and claims, 30-35,000 property acquisitions, and provide numerous other services, the work at 46 regional offices is organized into the following work processes regardless of station size or number of employees assigned to do the work:

a. Notice of Default processing

b. Notice of Intention to Foreclose processing

c. Supplemental servicing

(1) Financial counseling

(2) VA intervention with servicer

(3) Alternatives to foreclosure

(a) Deed in lieu of foreclosure

(b) Compromise claim

(c) Refunding

d. Servicer performance monitoring

e. Interest cut-off monitoring

f. Delinquent loan monitoring and diary control

g. Foreclosure monitoring

h. Claims processing, debt establishment, and debt reductions

i. Property acquisition processing

j. Release of liability

k. Release of security

l. Committee on Waivers and Compromises and Debt Management Center referrals

m. Internal controls and program surveillance

n. Customer service - telephone, mail, and personal appointments

o. Systems maintenance

p. Administrative and management support

5. Analysis of GI Loan Servicing

Present GI servicing policy is the result of law and regulation which is designed to assist veterans retain homeownership and reduce program costs. It has proven valuable and assisted veterans. In FY 1990 VA offices assisted 7,612 veterans reinstate their delinquent home loans or complete an alternative to foreclosure which saved approximately $80 million. Similarly, in FY 1991, 8,949 veterans were assisted and program costs were reduced by approximately $85 million.

Primary servicing of VA-guaranteed loans should remain with private sector loan servicers who are generally efficient in controlling loan defaults. Basic servicing (collections) is a well-documented and practiced discipline. VA's supplemental servicing is an extension of the servicer's efforts and becomes cost-effective when the cost to the Government on a loan termination is either eliminated or reduced as a veteran reinstates the home loan or chooses an alternative to foreclosure. The average claim payment is $14,000 for each loan termination. Preventing foreclosure on 5,000 to 10,000 loans annually provides savings between $70 and $140 million. It follows, therefore, that GI loan servicing should continue and methods implemented to improve this policy.

For purposes of analyzing GI loan servicing, it was assumed that the existing decentralized servicing organization would be reorganized through consolidation, regionalization, or a centralized structure. This would be consistent with private sector servicing operations which tend to be centralized at one location.

GLOSSARY OF TERMS

Ad Valorem Property Taxes: Taxes assessed to real property.

Automatic Lender: An approved mortgage lender who can make a guaranteed VA mortgage loan without any prior approval from the VA.

Compromise claim payments: Payments to make the holder of a loan whole when a distressed veteran-borrower sells to a private purchaser at a price less than the amount owed on the VA guaranteed mortgage. This avoids the expense of a full claim following a foreclosure.

Deed-in-lieu of Foreclosure: Situation where the veteran- borrower is willing to deed the property back to the lender instead of having the property foreclosed. No debt will be established against the veteran.

Direct Loan Revolving Fund: A revolving fund established by Congress to account for loans made directly by VA in credit shortage areas. There have been very few disbursements from this fund in the last decade.

Fannie Mae: An acronym for Federal National Mortgage Association. One of the major providers of mortgage funds in the United States.

Forbearance: The act of refraining from taking legal action despite the fact that a mortgage is in arrears. It is usually granted only when a mortgagor makes a satisfactory arrangement by which the arrears will be paid at a future date.

GI Loan: A mortgage loan which is made by a private lender to a veteran, and guaranteed or insured by the VA.

Ginnie Mae: An acronym for Government National Mortgage Association. One of the major providers of mortgage funds in the United States.

HUD: Department of Housing and Urban Development; one of the departments of the federal government of the United States.

Loan Guaranty Revolving Fund: A revolving fund established by Congress to account for funds disbursed and received in connection with the guarantying of loans by VA. This fund was superseded by the Guaranty Indemnity Fund for loans made after 1989.

Loan Instrument: The legal document signed by the borrower giving evidence of the loan.

Loan Sale: Process by which VA's portfolio loans are sold to private entities to provide funds for the Loan Guaranty Revolving Fund.

No Specific Amount: The situation where VA, upon examination of the value of the property and the amount of the guaranteed mortgage debt, determines not to set an amount which the holder may bid at the foreclosure sale and for which the VA will subsequently purchase the property from the holder. Also commonly referred to as a "No bid".

P&I Payment: Principal and Interest payments, which for most loans are fixed for the term of the loan. T&I (tax & insurance) payments may be adjusted to reflect changes in taxes or insurance costs.

Participants: More usual usage "program participants". These are mortgage lenders, servicers and holders, management brokers, corporations, etc., involved with the services necessary for the proper functioning of the Loan Guaranty program of the Department of Veterans Affairs (VA).

Portfolio Loan: A loan made by VA, and held, at least for a time, in VA's portfolio. Also called Vendee Loan.

Prior Approval Loan: A GI Loan which must be approved by VA before it is closed by the lender.

Primary Servicing: The initial and direct contacts between the holder of a loan and a borrower to resolve any issues or problems, such as delinquent payments, concerning the loan in question. VA conducts the primary servicing for loans in its portfolio but depends upon holders and servicers to conduct the primary servicing for guaranteed loans.

Private Sale: A sale involving one individual selling real property to another individual. In this instance, a situation where a distressed veteran-borrower sells his property to another person to avoid foreclosure.

Protective Custody Assignments: Notice given first to Property Management sections and subsequently to management brokers that a given property is being placed in the custody of VA for maintenance and protection.

Redeem: The act of redeeming a property subsequent to a foreclosure sale. A legal option in a limited number of states, this process allows first the owner and subsequently junior lien holders to protect their interest by paying amounts bid at the foreclosure sale plus any legally allowed costs such as accrued interest and thereby retaining or obtaining title to the property.

Refunding: The purchase of a VA guaranteed loan by VA from a private holder under the provisions of CFR 36.4318. Normally, the loan is reamortized for the benefit of the veteran-borrower.

Reinstatements: In this instance, the paying of necessary monies to bring a loan account to a current status.

Security Instrument: The mortgage or trust deed evidencing the pledge of real estate security as distinguished from the note or other credit instrument.

Tax Service Contracts: Contractual arrangements which provide a bundle of services connected with the obtaining and paying of real property tax assessments on properties which are security for loans in a mortgage loan portfolio and for properties owned or in the process of being acquired.

Title Acceptability: A determination made by Loan Service and Claims and District Counsel that the documentation incident to the conveyance of a property to VA is complete and proper.

Underwriting: Analysis of the risks involved in making and guaranteeing a loan.

VAR 4600 Loan: A vendee loan sold by VA to a private sector investor under VA Regulation 4600, which obligates VA to buy the loan back in case of default. Current loan sales are without recourse.

Vendee Loan: A loan made by VA to an individual who purchases an acquired property from VA.

Voluntary Deed: See deed-in-lieu of foreclosure.

Workouts: The process of negotiating and monitoring a plan for periodic payments which will eliminate a delinquent loan situation over the course of time. Individuals who negotiate such arrangements for servicers and holders are often referred to as "workout specialists".

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