Mortgage Servicing Rights Valuation – "Value It"

A growing number of credit unions are selling their residential mortgage loans into the secondary markets as a way to control mortgage concentration risk, avoid excessive interest rate risk and manage liquidity. Many of the credit unions retain the servicing function on these mortgage loans. This servicing function creates a financial asset called mortgage servicing rights (MSR). MSRs can produce significant servicing revenue for the credit union over the life of a loan.

In order to adhere to the Financial Accounting Standards Board's SFAS 140, SFAS 156 or SFAS 159, (as measured under the guidelines in SFAS 157), credit unions that originate and retain the mortgage servicing function must determine the fair market value of this servicing portfolio – also referred to as a MSR portfolio. Since MSR activity is normally reported on audited financial statements, external auditors and examiners may evaluate how credit unions calculate these MSR portfolio valuations.

Balance Sheet Solutions' **Value-It** program provides a valuation of MSR based on realistic market assumptions. Setting the proper assumptions has proven to be very important when calculating the fair value (rather than an institution-specific value).

Matching Need with Methodology

Determining MSR value goes beyond simply complying with regulations. Many mortgage servicing rights owners determine the MSR portfolio value for their management reports. Others use the report to assess the value of the MSR portfolio to determine whether to retain or sell the servicing rights.

Balance Sheet Solutions' program uses the discount approach to determine market value. This is a commonly accepted technique favored by regulators and GAAP. This program offers users the flexibility to set a variety of assumptions or to allow Value-It to establish assumptions.

The Program

Balance Sheet Solutions' Value-It program offers a choice of two methods: amortization or fair value measurement. Once selected, Value-It will delivers mortgage servicing rights valuation with:

- Understandability
- Common Sense
- Transparency
- Low Cost
- Integrity
- Clarity
- Flexibility
- Industry Expertise

Reports and Analysis

Value-it provides valuation reports, analysis and explanatory companion pieces, including:

- **Overview - Valuation Report and Assumptions**
  Discloses the valuation and assumptions for the mortgage servicing portfolio in an easy-to-read and comprehensive report.
- **Analysis – Outlook and Insight**
  A customized examination of major market components relevant to the servicing valuation, with a focus on the credit union's specific servicing portfolio characteristics.

Reports and Analysis (continued)

- **Cash Flow Report**
  Detailed numerical data, including independent calculations of income and expenses that support the model and are designed to add dimension to the valuation.
- **Analysis – Details of Assumptions**
  This file lists assumption particulars (Excel format) including an "error log" that can help pinpoint weaknesses in the original data from the credit union.

Factors Used in Valuations

Four factors are utilized during the portfolio valuation process.

- **Prepayment Speeds –** Value-It uses the Public Securities Association's (PSA) standard prepayment model and the constant prepayment rate (CPR) for calculating service rights. Prepayment speed can be adjusted to suit the unique characteristics of a credit union's servicing portfolio.
- **Strata –** Loans, loan plans, coupon ranges and other criteria are organized into groups that share common risk characteristics. Each stratum possesses a number of parameters used in calculating the value of the loans' servicing rights.
- **Loan Plan Overview** – Loan plans can be grouped into similar loan products serviced with substantially the same risk characteristics. Each loan plan specifies the term and amortization of the associated loans.
- **Options Overview –** This tool has the flexibility to make global assumptions, loan plan assumptions and strata assumptions that can be adjusted to work with incomplete information.

Advantages

Peace of Mind – By participating in the program, credit unions can determine the fair value of their mortgage servicing portfolios within the guidelines outlined in SFAS 157, and for use under SFAS 156 or SFAS 159.

Save Money – Pricing is scalable and economical, based on the number of loans in the credit union's mortgage servicing rights portfolio.

Resource Allocation – Utilizing Balance Sheet Solutions' seasoned team enables credit union staff to have time to focus on other priorities.

Increase Valuation Awareness – This simple and efficient valuation model is designed specifically for credit unions and can be run monthly, quarterly, semi-annually or annually. The Balance Sheet Solutions team assists credit unions throughout the process.

Getting Started

To learn more about this program and how to participate, contact us at 888-796-6389 or info@balancesheetsolutions.org.