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Mandatory Delivery Commitments? They're More Flexible Than You Thought

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Overview

Mandatory commitments are a little more flexible than you'd think. Before having to pair-off a commitment, there are different options available to you. With the current interest rate environment we are in, chances are pair-off fees won't be as financially detrimental as they were over the past couple years. Here are a few examples of some common misconceptions when it comes to mandatory delivery commitments:

1. There will always be a fee to pair-off a mandatory deliver commitment.
2. A mandatory delivery commitment is loan specific.
3. The loan that was intended to fulfill the commitment falls out, and I have to pair-off the whole commitment amount.

When an outstanding mandatory delivery commitment (DC) can no longer be fulfilled, what happens next? There are a few different options. First, the commitment can be extended up to 30 calendar days for a fee. Second, since a mandatory commitment is not tied to a specific loan, it can be filled with another loan. Lastly, if all else fails, the commitment can be paired-off for a potential fee.

But is there always a fee? It all depends on market conditions at the time of pair-off. If the current market price is **higher** (better) than the locked price, a pair-off fee will likely be assessed. If current market price is **lower** (worse) than the locked price, a pair-off fee may not be assessed.

Pair-Off Quick Hits

- Pair-offs apply to all Mortgage Partnership Finance® (MPF®) mandatory products: Traditional, MPF Xtra®, Traditional Government, and Government MBS. Pair-off fees do not apply to MPF Xtra best efforts DCs prior to submitting a funding request. Once funding is requested, the commitment flips to mandatory, and then all mandatory rules apply from there.

- Mandatory commitments come with a tolerance or a “cushion” above and below the commitment amount. This allows lenience where a loan can be delivered slightly above or below the commitment amount and not be assessed a potential fee. Tolerances vary by product (please refer to addendum on page four).
- Mandatory commitments can also be delivered over the commitment amount and above the tolerance. This is referred to as an “over delivery,” and the potential fee works similar to a pair-off. A fee is assessed when the commitment price is higher than current market price, because the Participating Financial Institution (PFI) would be funding more dollars into a higher price than what is offered on the current market. Over delivery rules vary by product (please refer to addendum on page four).

Mandatory commitments have a “rate stack,” which consists of the locked rate and four other rate options—typically two above and two below the locked rate. Each rate has a corresponding price premium/discount. A loan doesn’t necessarily have to be delivered to the locked rate, it can be delivered to any rate within the stack on the commitment.

Pair-Off Scenarios

In a rising rate environment, it is important to note that pair-off fees may not be as financially impactful as one would expect. In fact, as long as current pricing continues trending worse (lower), pair-off fees may not even be assessed. Below, we’ve mapped out two hypothetical pair-off scenarios:

Scenario One: Let’s say you take out a MPF Xtra mandatory DC, but the borrower ended up backing out of the loan. One way to avoid a potential pair-off fee is by swapping another loan into the commitment—as long as it fits in the rate stack and is within the tolerance amount. If you do not have a loan that fits the DC, there could be a pair-off if current market price is better (higher) than the lock price. Please refer to the example below:

Pair-Off With Fee Assessed	
DC Amount:	$100,000
Amount Subject to Pair-Off Fee:	$100,000
DC’s Original Pricing at 3.5% Note Rate:	1.10%
Current Market Price for 3.5% Note Rate:	1.60%
Difference in Pricing:	0.50%
Pair-Off Fee:	**$100,000 x .0050 = $500.00**

On the flip side, if current pricing is worse (lower) than the lock price, there may not be a fee at all. In fact, for MPF Xtra commitments, a credit can actually be received in cases like this. In the current environment, with rising interest rates and increased price volatility, the following example may be more aligned with what we have seen recently:

Pair-Off Without Fee Assessed	
DC Amount:	$100,000
Amount Subject to Pair-Off Fee:	$100,000
DC's Original Pricing at 3.5% Note Rate:	1.60%
Current Market Price for 3.5% Note Rate:	1.10%
Difference in Pricing:	-.50%
MPF Xtra: $100,000 x -.0050 = ($500.00) **MPF Traditional: $0.00**	

<u>Scenario Two</u>: Let's say you have a locked MPF Traditional mandatory DC and the borrower's appraisal comes back low. The loan amount needs to be lowered, and, in turn, it will not match the original delivery commitment amount. The first question you may ask yourself is, "How much is the loan amount changing?" With tolerance coming into play and depending on the product and if the loan amount is within tolerance, you can still deliver without a fee. If the new loan amount is outside the tolerance, you have the same option as in scenario one—another loan can be swapped in. If the new loan amount ends up being outside of the tolerance and you do not have a loan to replace it with, a pair-off may be assessed if the current market price is higher. However, the fee can be lower than expected as the whole commitment amount won't be paired-off. Here is an example:

Funded DC Example With Pair-Off Fee	
DC Amount:	$100,000
Funded Amount:	$80,000
Pair-Off Tolerance 5%:	$100,000 x 5% = $5,000
Amount Subject to Pair-Off Fee:	$100,000 - $80,000 - $5,000 = $15,000
DC's Original Pricing at 3.5% Note Rate:	1.25%
Current Market Price for 3.5% Note Rate:	1.65%
Difference in Pricing:	.40%
Pair-Off Fee:	**$15,000 x .0040 = $60.00**

As we saw in scenario one, as long as current pricing is worse than the locked price, there may be no fee or a credit back depending on the product. The calculation is ultimately the same as described above:

Funded DC Example Without Pair-Off Fee	
DC Amount:	$100,000
Funded Amount:	$80,000
Pair-Off tolerance 5%	$100,000 x 5% = $5,000
Amount Subject to Pair-Off Fee:	$100,000 - $80,000 - $5,000 = $15,000
DC's Original Pricing at 3.5% Note Rate:	1.65%
Current Market Price for 3.5% Note Rate:	1.25%
Difference in Pricing:	-.40%
MPF Xtra: $15,000 x .-0040 =($60.00) **MPF Traditional: $0.00**	

Delivery Commitment Characteristics by Product

	MPF Traditional	MPF Govt. MBS	MPF Xtra	
	Mandatory	**Mandatory**	**Mandatory**	**Best Effort**
Extensions	The maximum extension length available is 30 calendar days.			
Tolerances	**5% tolerance** on funding amount. For DCs over 2 million, the tolerance is only 1% **Example**: For a $100,000 DC, you can deliver from $95,000 to $105,000 and not be charged a pair off fee.	**1% tolerance** on funding amount **Example**: For a $100,000 DC, you can deliver from $99,000 to $101,000 and not be charged a pair off fee.	**$10,000 or 2.5%** tolerance (whichever is greater on funding amount) **Example**: For a $100,000 DC, you can deliver from $90,000 to $110,000 and not be charged a pair off fee.	**No tolerance**, the DC amount must match the loan amount. Best Efforts DC amounts can be easily adjusted with no fee.
Over Delivery	The maximum over delivery is **$100,000 on DCs under 2 million or 1% on DCs over 2 million**. **Example**: For a $100,000 DC, you can deliver up to $200,000 max and be potentially assessed with an over delivery fee for the amount over.	The maximum over delivery is **$100,000 or 1%** (whichever is greater) **Example:** For a $100,000 DC, you can deliver up to $200,000 max and be potentially assessed with an over delivery fee for the amount over.	The maximum **over delivery is 25%** of original commitment amount **Example**: For a $100,000 DC, you can deliver up to $125,000 max and be potentially assessed with an over delivery fee for the amount over.	**No limit on over deliveries** until the maximum conforming limits (high balance).
Pair-Offs (Reductions)	**Reduction fees** will be based off any change to the market rate at the time at which the original DC was locked.			**No reduction fees** unless the commitment status is "closed" then reduction fees are based off market rates.

To Learn More

Contact your Sales Director to learn more about the benefits of our different MPF products. To request a quote on a pair-off or to execute a DC related transaction, contact the MPF Service Center by email or at 877.345.2673.

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