More Stormy Seas Ahead?

When it comes to quality control, mortgage servicers are facing significant change, no matter what happens in the White House.

by Phil McCall & Kacey Olson

There is no doubt that the mortgage industry has gone through unprecedented tumultuous times and has seen a continual increase in new compliance rules and regulations that servicing entities must now adhere to at all times. And, when it comes to compliance in the mortgage industry, change is the only constant. New compliance rules arise all the time, and it is paramount that servicers stay on top of these regulations, or risk the possibilities of fines - some of which can be quite steep.

The industry has learned a great deal about what caused the mortgage meltdown in 2008. Once a daily headline wrought with negative mainstream press, the industry as a whole has finally arisen from the doldrums and is now operating at a healthy, controlled rate, albeit still under very close scrutiny by government policing. The mortgage industry is arguably now one of the most regulated industries in the country.

The industry-altering Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was officially signed into federal law by former President Barack Obama on July 21, 2010; it contained 2,300 pages of new rules and regulations and also spawned the creation of the Consumer Financial Protection Bureau (CFPB). Much of the Dodd-Frank Act has been implemented since being introduced, but there is a significant portion that has not taken effect. With a new governing administration taking over the reins from Obama, the extent and complexities of the Dodd-Frank Act will unequivocally be changed. But to what degree we don’t yet know. We won’t see any major changes immediately, but since President Donald Trump was sworn in on Jan. 20, his administration has swiftly begun work on his campaign promises, with deregulation being one of them.

Trump already has plans to remove CFPB Director Richard Cordray and also to significantly reduce the overall degree of the bureau’s power. What’s more, Dr. Ben Carson has been voted in to head the U.S. Department of Housing and Urban Development, and he will have a lot of influence to effectuate change in the mortgage industry. There are clearly significant unknowns that have put the industry in an interesting wait-and-see mode.

The compliance effect on servicing

After the default storm hit the market in 2008, there was an influx of delinquencies, loan modifications, workouts, short sales, foreclosures and more. Most servicers were ill-prepared and did not have the technology and processes in place to handle these influxes.

In January 2013, the CFPB issued a
number of different final rules concerning mortgage markets pursuant to the Dodd-Frank Act. Although the majority of these rules were heavily origination-laden, included in the final rules was the first set of servicing rules designed to address numerous deficiencies that were occurring before and after the mortgage crash. Since this time, the CFPB's focus on servicing has not wavered.

In June 2016, the CFPB released a report that indicated servicers did not invest enough in technology and compliance systems, which resulted in significant harm to consumers. Between January 2014 and April 2016, the CFPB identified that antiquated and insufficient technology can lead to greater risks for borrowers. "Mortgage servicers can't hide behind their bad computer systems or outdated technology," Cordray said in a June 2016 statement.

"Mortgage servicers and their service providers must step up and make the investments necessary to do their jobs properly and legally."

At last year’s Mortgage Bankers Association's Annual Convention and Expo held in Boston, Cordray reiterated that the bureau is concerned about the technology servicers are using, particularly with regard to its impact on compliance and the borrower experience.

"It is regrettable that much of the damage done during the crisis to consumers and the broader economy could likely have been contained early on by a more adequate system of mortgage servicing," Cordray said at the time. "A more effective system might have been up to the task of working with struggling borrowers to find appropriate ways to avoid foreclosure through loan modifications and short sales. But servicers were ill prepared and were unable to address even the best interests of their clients - the investors - let alone the consumers and our communities."

He noted that the CFPB has received more than 50,000 consumer complaints in the past year and has been committed to understanding and dealing with the nature of the complaints, along with trend identification.

"As we have publicly reported, we have seen some progress, most notably efforts by certain servicers to adequately staff up effective compliance management programs," he added. "But many troubling issues persist. While we applauded the investments made in compliance by certain servicers, others have not yet made satisfactory progress. Outdated and deficient servicing technology continues to put many consumers at risk. This problem is made worse by a lack of training to use their technology effectively. Needless errors impose harm to consumers facing delinquency or engaged in loss mitigation processes. These shortcomings can become chronic when servicers do not implement proper system testing and auditing processes."

"To spur needed improvements in servicer compliance, we will, in appropriate circumstances, be insisting and corrective action planning. This approach has proven to fail many a servicer and cannot ensure QC, let alone compliance - and, not to mention, the security of sensitive borrower information. Antiquated methods and processes wreak havoc and can be very dangerous.

As an example, a delinquent borrower who resides in any given state must be handled with 100% accuracy in terms of what stage he or she is at with missed payments. Manual audit oversight of these types of system-driven processes could easily allow auditors to miss basic requirement details or fail to adequately identify red flags that can be to the servicer’s detriment. Therefore, implementation of an automated QC and compliance system should be viewed as a mandatory requirement of any QC department responsible for servicing oversight.

All major entities, including the government-sponsored enterprises (GSEs), the Federal Housing Administration (FHA), the CFPB and state-based...
regulators, have mandated new processes and rules to keep the mortgage meltdown of 2008 from happening again. Servicers must establish a solid, well-documented QC program that is regimented but agile enough to accommodate new rules that are introduced by these entities.

Not only must servicers ensure that they comply with such rules, but investors and master servicers also want assurances that their loans are being serviced properly. In addition, any entity that is looking to purchase a portfolio or mortgage servicing rights will absolutely want to see that a well-structured, highly accurate QC program is in place and managed through a sophisticated platform.

A sophisticated QC platform will enable millions of servicing records to be easily imported to adequately perform random, discretionary and targeted audits and to fulfill the corresponding sampling requirements for the dozens of task-specific audits that servicing QC departments must complete each month. The platform should provide for template-driven customization to accommodate the nuances of an organization’s workflow but maintain and support the stringent requirements of regulatory oversight.

The platform must also provide simple administrative oversight of an audit checklists/scripts catalog, including routine updates necessary, to meet the ever-changing regulatory requirements. Checklists/scripts should dynamically populate audit requirements that are specific to individual loan parameters into the system.

**Technology is the answer**

So much of QC and compliance can be effectively handled using the right type of technology. By leveraging auditing technology that is rules-based and easily configurable, servicers can ensure operational compliance with federal, state and GSE requirements, as well as their own internal policies and procedures.

When interacting with borrowers, there are myriad rules that servicers must follow on both state and federal levels throughout the lifecycle of the servicing process. Configurable auditing technology puts the ability to create and make changes to audit checklists/scripts directly in the hands of businesspeople. Regimented audit checklists/scripts can quickly be incorporated into a servicer’s internal policies and procedures, which clearly guide staff on how and when and in what fashion they must consistently communicate with borrowers and proceed accordingly.

A few examples of areas for which servicers typically need to have detailed questionnaires for staff to follow include things such as collections, defaults, foreclosures, bankruptcies, claims and credit reporting.

Notable is that the technology vendor you use should maintain all relevant state and federal compliance rules for the servicers. Servicers shouldn’t have to worry about it. However, empowering servicers with technology to make internal changes to their own internal rules and policies is very important. In addition, auditing technology enables servicers to perform internal audit samplings of their own stratified sampling procedures, automated targeted samples, and statistical samplings to ensure compliance and loan quality.

With the click of a button, auditing technology can instantly review samplings of loans for missing information, errors and possible compliance issues. As an example, sophisticated auditing systems can be configured to regularly draw on the industry standard 10% sampling percentage, rifling through thousands of loans and returning business-critical insight and actionable data. Loans can be set to auto-audit via statistical, straight random, stratified random and discretionary sampling.

So, if one wanted to filter by conventional loans, FHA loans, non-qualified mortgage loans, modifications, workout programs, adjustments, collections, or even down to the branch performance level, it can easily be done and reported on by the click of a button. Using auditing technology, servicers can electronically capture data for audits, establish checklists/scripts, provide benchmarking, produce detailed reports, and more. In addition, because everything is time- and date-stamped, anyone who touches a file can be held accountable. Auditing technology is the ultimate solution to help servicers navigate through the waters of uncertainty. It improves loan quality, reduces costs, mitigates risk, and provides much-needed transparency and control. Further, it also dramatically reduces loan defects and repurchase risk.

Now, some servicers are already using auditing technologies, but in many cases, they are out-of-the-box, are inflexible and require the assistance of internal IT resources to support. Changing rules and regulations often require immediate action on the part of QC to implement new or revised audit checklists/scripts. That’s why the degree of configurability with auditing technology is paramount for ease and speed of change management. If your current auditing technology doesn’t allow you to configure changes and updates to existing or new checklists/scripts, you probably need to re-evaluate your vendor.

With regularly changing GSE and CFPB requirements, different checklists/scripts are needed for audit types, large sample sets with different data points and business rules for proper sampling. In addition, identifying areas of operational issues and the insight to create and track corrective action plans require auditing technology that can tackle these challenges head on.

QC was put in place to protect not only the consumers, but also the institutions servicing them.

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