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YES, STATES ARE STEPPING UP THEIR SCRUTINY OF SERVICERS

By Jennifer Keys, SVP – Compliance Solutions, Covius

Servicers are sensing increased scrutiny from state regulators. Recently, the Conference of State Bank Supervisors (CSBS) reported that in 2023 it increased the number of mortgage company exams it conducted by more than 40%. CSBS also announced that it has entered an information-sharing arrangement with the Federal Home Finance Agency (FHFA) to share audit findings for non-bank lenders.

These two announcements—combined with a steady stream of new mortgage-related legislation and proposals at the state level—are just the latest examples of the increased regulatory scrutiny that mortgage companies are facing. And as the economic landscape changes, state regulators will be stepping up the frequency of their exams.

In case you missed it, CSBS reported that it initiated 2,085 exams of mortgage companies in 2023 through the state examination system within the Nationwide Multistate Licensing System and Registry. That number was up from 1,481 mortgage exams started in 2022. The new CSBS-FHFA information-sharing agreement focuses on non-bank mortgage companies. The ostensive purpose of the agreement is to increase efficiency with a more coordinated approach to exams. What observers fear, however, is that servicers that are issued a finding by a state regulator may also face one at the federal level.

NEW FOCUS, MORE FREQUENCY?

Regulatory exams aren't new, of course, and they have been on the rise, at both the state and federal level since the mortgage crisis. Historically, there have been a handful of activist states, such as New York, California and Florida, which are known for their stringent regulatory environments and heightened oversight of financial companies. As this continues, there have also been several other states enacting new rules, or tweaking old ones, in the name of consumer protection. Recently, borrower communication has been a focus of several state-level changes. Even though many of the changes are relatively minor, future state exams are likely to review compliance with recent legislation.

Here are just a few recent examples of changes where servicers might be scrutinized:

Kansas' newly revised UCCC and Mortgage Business Act

Effective January 1, 2025, the law repeals and replaces multiple sections of the Kansas UCCC and moves mortgage-related provisions to the Kansas Mortgage Business Act (KMBA). The previous version of the UCCC included a model notice of right-to cure-for borrowers in default, and many servicers include parts of this model notice in their default letters for consumer mortgages in Kansas. HB 2247 omits this model form; however, the mortgage default notice requirements that are being added to the KMBA are substantially the same as existing requirements.

Wisconsin's recently updated Collection Agency Disclosure

The Wisconsin Department of Financial Institutions (Wisconsin DFI) recently updated many of its regulations that apply to industries under its authority. The updates included a change to the Wisconsin collection agency disclosure to reflect the new web address for the Wisconsin DFI. The former web address, www.wdfi.org, now redirects to the new web address: www.dfi.wi.gov. The updated collection agency disclosure should now read: "This collection agency is licensed by the Division of Banking in the Wisconsin Department of Financial Institutions, www.dfi.wi.gov." The new regulation went into effect April 1, 2024.

New Mexico's Updated HAF Notice Form

The New Mexico Supreme Court issued an order updating the "Notice to Defendant of the Homeowner Assistance Fund and Ability to Request a Stay While Applying for HAF" (HAF Notice Form), which must be provided to borrowers in default prior to filing a foreclosure complaint. The original form explained that homeowners could receive up to $20,000 in assistance, but after the form was published, the New Mexico Housing Authority increased the maximum grant size to $30,000. The latest version of the form leaves out a dollar amount and instead refers generically to "an amount approved under the HAF program." The updated form was effective immediately when published on December 18, 2023.

Origination Considerations on the Horizon

On the origination side, some states are currently considering legislation that could have sweeping consequences for lenders, particularly when it comes to the use of AI and automated decisioning. California, for example, is considering a bill that would allow consumers to "opt out" of automated underwriting.

This increase in regulatory activity will impact how servicers operate. Compliance with these changes will demand more resources, including staff and technology aimed at streamlining data management and reporting for state regulators.

BEST PRACTICES FOR COMPLIANCE

In the normal course of preparing for exams, servicers need to ensure all documentation is accurate, up to date and readily available. They will also need to demonstrate the steps they are taking to properly train their staff, and compliance groups will need to maintain a proactive line of communication with regulators.

Looking ahead, servicers can expect more scrutiny at the state level and another set of eyes on exam results from the FHFA. Servicers must remain agile so they can meet deadlines in adhering to new regulations. Participation in industry groups and forums is critical, so the industry can help shape regulation that balances consumer protection with business operations. It is more important than ever to engage with advisors and service providers to ensure your operations align with current and upcoming state (and federal) standards.