CSBS Proposes Prudential Standards for Servicers

December 2, 2020 By Nanci Weissgold and David McGee

A&B Abstract: The Conference of State Bank Supervisors ("CSBS") proposed regulatory prudential standards (the "Standards") to develop a consistent regulatory structure of nonbank mortgage servicers. Comments on all aspects of the Standards are encouraged by December 31, 2020.
Since the financial crisis, the rapid growth of mortgage bank mortgage servicers has led regulators to call for the enhanced oversight of such entities. The Financial Stability Oversight Council (charged under the Dodd-Frank Act with identifying risk to the stability of the U.S. markets) recommended in its 2014 and 2019 annual reports that state regulators work collaboratively to develop prudential and corporate governance standards. Earlier this year, the Federal Housing Finance Agency (FHFA) proposed new financial eligibility requirement for nonbank servicers doing business with Fannie Mae and Freddie Mac.

In 2015, state regulators working through the Mortgage Servicing Rights Task Force proposed baseline and enhanced prudential regulatory standards (including capital and net worth requirements) for nonbank mortgage servicers. Although those standards were not finalized, several states – including Maryland, Oregon and Washington –imposed new net worth requirements for nonbank servicers.

The CSBS's newly released proposed standards update the 2015 proposal “to reflect a changed nonbank mortgage market, continued significant growth and complexity and an evolved understanding of state regulators concerning the need for supervisory standards.” The stated goals of the Standards are to: (i) provide better protections for borrowers, investors, and other stakeholders in the occurrence of a stress event, which could result in borrower harm; (ii) enhance regulatory oversight and market discipline; and (iii) improve transparency, accountability, risk management, and corporate governance standards.
The Standards apply to state-licensed nonbank mortgage servicers and investors, including MSR investors, originator servicers, monoline servicers, subservicers and owners of whole loans. The Standards are not intended to apply to servicers solely owning and conducting reverse mortgage servicing and they have limited applicability to entities that only perform subservicing for others.

The Baseline Standards, as proposed, will cover eight areas:

- Capital
- Liquidity
- Risk management
- Data standards and integrity
- Data protection (including cyber risk)
- Corporate governance
- Servicing transfer requirements
- Change of control requirements

Notably, CSBS and state regulators intend to align supervisory approaches wherever possible, and the proposed standards are intended to do so with the calculations for capital and liquidity under FHFA eligibility requirements but apply the calculations to the entire owned servicing portfolio, including whole loans. To prevent double counting of MRS, the Baseline Standard’s capital and liquidity requirements differentiates “owned” servicing and servicing for others.

The Enhanced Standards, as proposed, cover four areas:

- Capital
- Liquidity
- Stress testing and
The Enhanced Standards are intended to apply to Complex Servicers, companies servicing whole loans plus mortgage servicing rights (“MSR(s)”) totaling the lesser of $100 billion or representing at least 2.5% total market share based on Mortgage Call Report quarterly data of licensed nonbank owned whole loans and MSRs. State regulators may determine that specific servicers, including subservicers only, that do not meet the definition of Complex Servicers are subject to the Enhanced Standards based on their unique risk profile, growth, market importance, or financial condition of the institution.

**Request for Feedback:**

While the CSBS is seeing comments on all aspects of the Standards, they specifically seek feedback on the following questions:

**General**

- Is the need for state prudential standards sufficiently established?
- Do any of the standards threaten the viability of a servicer or a specific subsector within the industry?
- What is a reasonable transition period to implement the standards?
- Are there specific standards that would require additional time to implement?
- What effect will the enhanced standards have on the warehouse and advance facility borrowing contracts/capacity of large servicers?

**Coverage**

- Is a scaled approach appropriate where all servicers are subject to Baseline Standards and Complex Servicers only subject to Enhanced Standards?
- Nonbank servicer coverage in the proposal is intentionally unspecific. What should be the appropriate coverage triggers? Should reverse
- Are the capital and liquidity aspects of the proposal alignment with existing and future FHFA Seller/Servicer requirements the right approach?
- Should there be an alternative net worth calculation method?
- State supervisors hold jurisdiction over a nonbank servicer’s entire portfolio. Should the FHFA calculations to all owned servicing the appropriate approach?
- Do you agree with the Standard’s definition for the two types of liquidity needs (servicing liquidity for the direct performance of servicing and operating liquidity for general operations of the organization)?
- Do you agree that allowable assets for liquidity should align with FHFA’s 2019 Servicer Eligibility 2.0 Proposal?
- Do the risk management standards appropriately capture the risks faced by nonbank mortgage servicers?

**Corporate Governance**

- Should all covered servicers be expected to establish a risk management program under a board of directors scaled to the complexity of the organization?
- Is it appropriate for the data standards to incorporate the CFPB’s Mortgage Servicing Rules Standards or is there a different alternative that should be considered?
- Are the data protection standards appropriate for the data risks inherent in nonbank mortgage servicers?
- Are the Ginnie Mae audit standards the appropriate standards for corporate governance under the Standards?
- Should all covered nonbank mortgage servicers be required to have a full financial statement audit conducted by an independent certified public accountant?
For change of ownership and contract, do the Standards reflect the correct number of days for notification (30 business days) and appropriate ownership percent trigger (10% or more)?

**Takeaways:**

Some have called for the imposition of federal capital and liquidity standards. The states, on the other hand, believe that they should be the primary prudential regulator over nonbank mortgage servicers and have developed the Standards to comprehensively cover safety and soundness and consumer protection concerns. While the Standards are very detailed in some areas, they are vague in others such as coverage and implementation. Consistent implementation, interpretation, and enforcement of the standards will be imperative for the state's to achieve their objectives.

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About Nanci Weissgold

Nanci Weissgold is a Chambers-ranked, American College of Consumer Financial Services Lawyers fellow who co-leads the firm's consumer finance practice and maintains a national practice representing consumer financial services providers in a wide array of federal and state regulatory and supervisory matters. Her clients value her pragmatism preparing for and responding to CFPB, FHA, state, and other administrative actions.
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David McGee is an associate in Alston & Bird’s Financial Services & Products Group and the Consumer Financial Services Team. He focuses his practice on federal and state regulatory compliance matters relating to consumer financial services, including the Real Estate Settlement Procedures Act (RESPA), Truth in Lending Act (TILA), Equal Credit Opportunity Act (ECOA), Fair Credit Reporting Act (FCRA), Fair Debt Collection Practices Act (FDCPA), and the unfair, deceptive, or abusive acts and practices (UDAAP) authority of the Consumer Financial Protection Bureau (CFPB) under the Dodd–Frank Act.