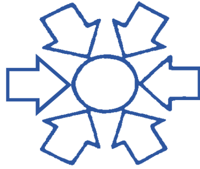

Wednesday, October 27, 2021

Servicing With a Costly Frown

Summary

After years of enforcement inactivity, the OCC has issued a tough set of restrictions against one of the increasingly few large mortgage servicers still willing to be a banks. This presages more to come from the OCC above and apart from its participation with the Department of Justice and CFPB in a new campaign against "modern redlining" that create pressure for like-kind action against nonbanks in another high-profile arena.

Impact

Cenlar is a federal savings bank (FSB) as well as the second largest U.S. servicer and the biggest sub-servicer. As warranted by its authority, the OCC's action focuses not on consumer safeguards, but on safety and soundness. This reaches to consumer protection and can be used to stipulate *de facto* protections as is partially done here. However, the OCC's authority is expressly limited to safety and soundness and the order thus couches its sanctions in these terms.

As is often the case, the OCC's hand is particularly heavy because Cenlar was warned of internal-control, MIS, IT, governance, and related problems across its front-line servicing operation and, the agency says, failed to correct them. Much in the order targets default management and loss mitigation, with the agency here focusing on internal controls that then affect compliance with all the requirements demanded in the CFPB's servicing standards.

The order specifically demands that the bank quickly set up an independent compliance committee that analyzes the scope of identified problems and manages their correction under both the authority and responsibility of the board. An action plan is demanded within sixty days detailing a wide array of remedial actions and when they'll be undertaken and completed. The bank is on a short leash, with much of what's demanded of it due by the end of the first quarter followed by semi-annual internal audits to ensure all that was done stays done.

Although press highlights the lack of monetary fines, the penalties are in fact stiff, including a prohibition on capital distributions without OCC concurrence and a ban on new sub-servicer clients. These differentiate what the OCC can do versus the CFPB in that the banking agencies have the power to hit a bank where it hurts -- capital distributions -- and the CFPB can only significantly reduce shareholder value if penalties are extraordinary or it determines it has the authority -- uncertain -- to bar a company from a targeted business activity.

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Outlook

How does this OCC action set the stage for nonbanks? Ginnie Mae is working on set prudential standards, but its proposal focuses principally on capital and liquidity, not all the issues outlined above. The CFPB of course has a broad reach to all servicers of size, but its ambit is consumer protection. It has taken a very broad view of the operational risks that pose consumer harm in its recent bigtech order and it could do the same for nonbank servicers, but we doubt it will. It's got his hands very full with all the anti-foreclosure and loss-mitigation rules more directly under its ambit.

The closest anyone can come to the OCC's safety-and-soundness powers are the eligibility standards set by Fannie Mae and Freddie Mac. FHFA Director Thompson told the MBA that her agency will return to this hot question in 2022. We continue to expect that, when it does, FSOC's systemic concerns about nonbank lenders and servicers will be reflected in FHFA-dictated eligibility standards. If not, the banking agencies and Treasury will surely have something to say about it.

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