



# Working Under Watchful Eyes

**As settlement terms, consent orders, and new rules fall into place, large servicers face a new reality for compliance technology. Will the big five join the revolution or stay in legacy limbo?**

**By Ryan Schuette**



## COVER STORY

**T**he Matrix stunned moviegoers with a 20th-century do-over of the post-apocalyptic film genre, splicing groundbreaking CGI effects with the story of a tech whiz able to tap into the world of machines, defeat government agents ... and dodge bullets. Following a historic \$25 billion settlement with state and federal officials, the nation's five largest servicers may want to revisit the pop-culture classic for a few lessons in digital kung fu. Insiders say they'll need it, as federal regulatory agencies increasingly walk the talk of national servicing standards and technology providers step up with a host of new software to comply with settlement terms.

The national deal deserves a bulk of the attention it receives, if only because of the multibillion-dollar swath it cuts into bank holding companies. The settlement requires \$25 billion from the big five—Ally Financial, Bank of America, Citigroup, JPMorgan Chase, and Wells Fargo—over roughly four years, with \$20 billion allocated for principal reductions, refinance opportunities, and forbearance measures.

But the settlement isn't the only source of compliance concerns. A backlog of consent orders from several agencies last year will force servicers to upgrade their compliance technology, experts say, even while the newly established Office of Mortgage Settlement Oversight (OMSO) sets up the conditions for a revolution in software programs.

Ed Delgado, COO of Wingspan Portfolio Advisors, says that servicers "have to explore new solutions based on the complexity ... that has been supplied to the marketplace. The level of scrutiny and detail involved requires new technology solutions to meet the needs of the [consent] orders."

Just what could these programs accomplish? Think software able to track borrower documents, automatically solve problem areas, report staff shortfalls, and—maybe most importantly—create auditable histories for watchful regulators.

The feds mean business if nothing else. Following the settlement, HUD Secretary Shaun Donovan said in a statement that

"the real work begins to hold these servicers accountable and ensure that the nearly 2 million homeowners who are expected to receive help and relief actually get it."

Whether large servicers comply with market demand may be an issue unsuited even to digital wizards. Sources tell us that the big five stay close to the sidelines, giving their smaller competitors a hand to play in the future of compliance technology.

### Compliance Revolution

It didn't take the landmark settlement to show servicers that the compliance landscape of today is one vastly—and increasingly—different from the industry of yesteryear.

Just last April, three federal regulators—the Office of the Comptroller of the Currency, Federal Reserve, and the now-defunct Office of Thrift Supervision—handed down consent orders to 14 servicers. The orders established a single point of contact (SPOC) for distressed borrowers, barred dual-tracking for workout evaluations and foreclosure processes, and called for rigorous internal oversight of third-party vendors.

Not one to stay out of the compliance limelight, the Consumer Financial Protection Bureau (CFPB) stepped into the foray last month with news that it will propose rules this summer to standardize the way servicers process home loan payments and foreclosures. The bureau said it will start on rules that require servicers to inform homeowners in

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distress of ways to avoid foreclosure, quickly credit payments to consumer accounts, and amend errors upon notification—all things that begot bad reputations for financial institutions during the crisis. CFPB Director Richard Cordray said in a statement that the rules will “put the ‘service’ back in mortgage servicing.”

Cordray isn’t alone. Joe Smith, now responsible for overseeing servicer compliance under the settlement, agrees with the bureau’s forward action and says more will likely follow—sooner rather than later if left to his office, a 501(c)4 nonprofit, which he uses to facilitate oversight of the settlement. (See our Five Minutes with Joseph A. Smith profile this month to read our full, exclusive interview with the settlement monitor.)

Smith—a widely respected former North Carolina banking commissioner and President Barack Obama’s onetime nominee to head up the Federal Housing Finance Agency—tells us that his office will finalize work plans in as few as 90 days to streamline the reporting process for servicers under terms of the settlement. Along with other accounting offices, a primary firm will help OMSO roll out the personnel—whom Smith likens to bank examiners—needed to pore over every step toward fulfillment of the settlement’s terms. And he says third-party contracts will eventually supplement the seven-member team currently under his direction in Raleigh, North Carolina.

If servicers make a misstep by skipping deadlines, the monitor says he will work with financial institutions to find cures. “If they don’t comply,” he adds, referencing his enforcement ability to pursue \$1 million or more in fines, “I have plenty of backup from

the [state attorneys general] to get injunctive relief from the courts.”

Experts say these requirements—and the threat of multimillion-dollar penalties—spur fresh demand for auditable compliance technology. Kelly Adkisson, an executive with Accenture Credit Services and an industry veteran, credits “integration” for the drive by financial institutions to new compliance software able to track the life cycles of loans—who works with the homeowner, whether a modification takes place, when foreclosure enters the picture, and so on.

She cites three elements in vogue for tech-minded servicers: Automatable workflow, customer contact, and the ability to “effectively and efficiently disseminate information,” both internally and externally to third parties—like federal regulators with the teeth for consent judgments.

She says servicers are “looking for new technology solutions” with the built-in ability to “incorporate changes into future releases of their software.”

The field isn’t large for technology firms that specialize in compliance solutions. LPS and Fiserv immediately stand out in a crowded market for servicers, sources tell us, with the former contending for many national servicers. The company, which did not immediately return requests for comment, released a so-called Mortgage Servicing Package in May of last year that it billed as a one-stop shop for SPOC issues.

That’s all well and good for certain servicers, experts say. But what would the latest tech upgrades and platforms mean if those with the largest footprints hang onto dated solutions?

## Take the Red Pill

In *The Matrix*, Laurence Fishburne’s Morpheus confronts Keanu Reeves’ Neo with a now-famous line that involves two pills—one blue, one red. By swallowing the latter, he turns his back on a world of delusion and false hope—a decision that ultimately leads Neo to freedom in the franchise.

Insiders familiar with the industry tell us that the nation’s servicers have by and large chosen the red pill, as it were, accepting a somewhat collegial relationship with federal regulators without much fuss.

“The industry is going through a period of self-examination where they are attempting to go to the solution,” says Delgado. He calls the settlement one that “goes a long way toward restoring some degree of confidence” in servicers, allowing financial institutions hurt by the foreclosure crisis to put public relations battles “in the rearview mirror.”

Statements by several servicers in the wake of the settlement would seem to suggest a win-win—and a movement toward the compliance technology revolution. Mark Rodgers, a spokesman for Citigroup, tells *DS News* that Citi has “already been implementing aspects of the [settlement’s] programs” and has been taking calls from customers since early March.

Without disclosing the third-party vendor, Rodgers nodded at an unnamed “analytics tool ... to determine whether or not we believe a borrower may qualify for the program” and said that the bank has “already moved a number of cases into the pipeline.” Insiders say the other big four bank holding companies quietly lauded the settlement.

But others say that servicers—especially the big five affected by settlement terms and consent orders—largely continue to brake on system-wide change, preferring legacy asset solutions to newer software for the management of their mortgage debt.

And that’s due in part to the terms of the settlement itself, Adkisson tells us. She says that “a lot of the legacy technology solutions are not adaptable and flexible to adjust to the timeline” required of servicers under the deal.

“The largest servicers have had less time to react because they have been under time-sensitive consent order mandates and requirements from Fannie and Freddie,” she says. “The smaller servicers have been able



to think about it and organize around these changes.”

That may leave more elbow room for technology solution providers like DRI Management Solutions. The Newport Beach, California-based company went live with DRI Business Office at the height of the financial crisis in 2009 and continues to promote the software as an all-in-one solution to track the life cycles of loans.

Fred Melgaard, EVP and COO with DRI, describes the current state of compliance technology for the industry as “a whole lot of Band-Aid solutions.” He says that DRI adopted policies like SPOC “right away,” revamping its systems to require reports by department and task. Results like these, he says, offer managers the ability to “determine who is doing well and who needs more training” when it comes to compliance evaluation.

Are smaller servicers leaving their bigger competitors in the dust in the movement toward newer, better versions of compliance technology? Tech giant Fiserv seems to think so. The company touts queue-driven software like LoanServ, which it renamed in 2010, as evidence of the shift toward products like theirs in a still-evolving compliance market.

Joe Dombrowski, Fiserv’s chief mortgage strategist, references a customer base that includes specialty servicers, retail banks, Wall Street firms, even new startups, many of which see opportunity in the space for upgrades left unfilled by major players.

“The larger servicers aren’t looking to change,” he says, describing the field as one in which financial institutions have “turned inward to prevent loss.

“We’ve seen a lot of growth here,” he adds.

Dombrowski says Fiserv recently added a real-time feature to its solution that distinguishes it from the so-called batch systems that continue to characterize legacy asset solutions for larger servicers. He refers to preferences for in-house IT systems—the same that lawmakers and regulators argue helped embroil servicers in signing errors and wrongful foreclosures—as “built-in handicaps,” unfavorable for servicers seeking to comply with OMSO, CFPB, and other regulators.

### One-Size-Suits-All?

Large or small, the need for compliance upgrades leaves some to speculate that high-demand tech could set the conditions for an informal national servicing regime, not unlike the way Fannie Mae and Freddie Mac call the shots today for lenders with tough underwriting standards. Think a uniform and artificial reality like The Matrix, servicer-style.

Delgado expects that there “may be some standardization of compliance vis-à-vis technology.

“If you’re looking for operational defects and tech app solutions to identify those defects, you build for a better system—a better approach to defective action,” he says.

Dombrowski sees de facto national servicing standards somewhat more skeptically. He thinks that different service providers will naturally develop and market their programs to different constituencies.

“If I’m a small bank with 50,000 loans, I’m going to treat things much differently than one with 5 million loans,” he says. He cites evolving modifications to the Home Affordable Modification Program as one instance where “client-alterable solutions” worked well for servicers.

Dombrowski lays the creative license at the footstep of technology product managers. As long as these managers are sensitive to the diversity of their clientele and constituents, he adds, “all will be good.”

Speaking with *DS News*, Smith portrays plans under way for national servicing standards as those to which both government parties and bank holding companies all agree.

Asked whether adaptation by technology providers could presage a de facto set of standards for the servicing industry, the settlement monitor says he thinks it could—for the better. “Ultimately ... we’ll have national standards—and we ought to,” Smith contends.

Near the end of *The Matrix*, a film fundamentally about non-compliance, Reeves’ savior character learns to dodge bullets by adapting to new rules. Servicers may want to follow suit—if only to avoid bullets of the multimillion-dollar kind. **DS**

## ✓ Breaking Down \$25 Billion

**Contributed by Bank of America (\$11.82 billion), Wells Fargo (\$5.35 billion), JPMorgan Chase (\$5.29 billion), Citigroup, (\$2.20 billion), and Ally Financial (\$310 million)**

### \$10 Billion

principal reductions for underwater borrowers who are delinquent or at imminent risk of default

### \$3 Billion

refinancing for borrowers who are current but underwater

### \$7 Billion

forbearance for the unemployed, anti-blight programs, benefits for service members

### \$5 Billion

paid directly to federal and state governments