

The Latest on Third-Party Risk Management (TPRM) and Vendor Oversight: Heightened Regulatory Expectations

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What role does a third party provider play?

- ▶ Third party servicer providers play an integral role in the residential mortgage servicing industry.
- ▶ Vendors are utilized at nearly every stage of the mortgage servicing life cycle and include:
 - ▶ Technology providers: 70% of mortgage loans serviced on vendor systems.
 - ▶ Escrow administration: Hazard and flood insurance, real estate taxes, homeowner assessment (HOA) bill procurement and payment, payment processing lockbox vendors, billing and statement printers.
 - ▶ Customer service: Third party call centers
 - ▶ Default management life cycle: Collectors, loss mitigation counselors, field service personnel, property management, bankruptcy and foreclosure representation.

Why use a third party service provider?

Cost benefit analysis for service companies:

- ▶ Extensive financial investment in hiring, training and supporting an internal staff of knowledgeable professionals.
- ▶ Significant startup investment in technology.
- ▶ Cost to develop a compliance-oriented business culture to comply with pervasive Consumer Financial Protection Bureau (CFPB) and other regulatory requirements.
- ▶ Extensive startup time to develop the requisite infrastructure and enterprise-wide management and performance measurement systems and protocols.

Why use a third party service provider?

Brain power, business expertise and compliance knowledge

- ▶ Provides a ready pool of educated employees well-versed in the applicable loan servicing best practices.
- ▶ Eliminates the significant time and financial investment in building it internally.
- ▶ Ability to 'load balance' during volume lows and peaks, minimizing expense of maintaining excess capacity.
- ▶ Provide a strong compliance culture where the vendor is the 'expert' and you should be able to rely on that expertise.
- ▶ Agility and flexibility when bringing new products to market.

Third party service providers: Evaluation factors we consider

- ▶ Centralized vs Decentralized oversight model
- ▶ Third party service provider review, selection and approval process
- ▶ Annual recertification process
- ▶ Establishing comprehensive service level agreements
- ▶ Key performance indicators: incentives and penalties
- ▶ Monitoring vendor performance, scoring and providing feedback

Third party service providers: Managing Risk

- ▶ Customer-centric functions present enhanced risk: Is your third party service provider in compliance with all of the CFPB rules?
- ▶ Industry issues such as administrative fee sharing (lender placed hazard insurance) and ineffective loan modification processing.
- ▶ Inaccurate bankruptcy proof of claims (quality control process)
- ▶ Improper or incomplete foreclosure affidavit and notarization processes (Robo-Signing)
- ▶ Heightened regulatory scrutiny and pervasive CFPB/OCC rules and oversight means that the functions you outsource by extension are scrutinized as well.

Third party service providers: Managing Risk (cont'd)

- ▶ The vendor's performance should meet or exceed key performance indicators as established in the service level agreements.
- ▶ Feedback: Does the vendor provide daily performance reporting?
- ▶ If customer-centric work is involved, can the client monitor calls?
- ▶ How frequently does the servicer meet with the third party service provider to review performance?
- ▶ Does the servicer periodically complete a scorecard to evaluate the third party service provider's performance?

Third party service providers: Managing Risk (cont'd)

- ▶ Increased regulatory oversight and complexity creates new demands on the servicers and their third party service providers relationships. The need to develop “partnerships”.
- ▶ Servicers need to expand the internal role of legal, compliance, information technology, and audit within the vendor oversight framework.
- ▶ Vendor performance data, scorecards and servicer-vendor feedback must be ‘looped’ back among quality control, internal audit, information technology, compliance and legal areas.
- ▶ Servicer’s epicenter should be a centralized vendor oversight function rolled up into a pervasive enterprise-wide corporate governance initiative.

Third party service providers: Managing risk through oversight

- ▶ Vendor oversight review analyzes ongoing business viability, financial stability and is in compliance with CFPB/OCC and other mortgage servicing rules and industry best practices.
- ▶ A viable third party service provider oversight program should include the following:
 - ▶ Evidence of proper insurance coverage
 - ▶ Organizational matrix and key bios of executive and senior management
 - ▶ Capacity: Number and size of current business relationships
 - ▶ Management succession plan

Third party service providers: Managing risk through oversight (cont'd)

- ▶ Processes for ensuring file security and confidentiality of borrower/customer data (Graham-Leach-Bliley)
- ▶ Employee and management turnover data
- ▶ A review of policies and procedures, training curriculum and staffing needs
- ▶ Disaster recovery and business continuity plan and evidence of successful testing
- ▶ Network security and intrusion testing protocols
- ▶ Audit and quality control reports; SSAE16 report
- ▶ Audited and pro forma financial statements (SEC Forms 10-K and 10-Q where available)
- ▶ Systems architecture and capacity for business growth in line with business projections and new product rollouts

Third party service providers: Managing risk through oversight (cont'd)

- ▶ Review and certification of policies for sub-sourcing or outsourcing work to another third party service provider domestically or offshore
- ▶ Telephony and fax capacity sufficient to handle customer volume
- ▶ Fair Debt Collection Practices Act (FDCPA) training for all personnel in customer-centric functions
- ▶ Review fees that are assessed and ensure that they are reasonable and customary in relation to industry standard
- ▶ Monthly number and type of regulatory inquiries/complaints
- ▶ Monthly number and type of incoming litigation

Third party service providers: Conclusion

- ▶ Develop a centralized vendor oversight function that reviews third party service providers on a periodic basis for effective performance management in accordance with service level agreements as well as effective compliance with local, state and Federal laws
- ▶ Ensure that centralized vendor oversight function is enterprise-wide and encompasses the relevant servicing areas as well as legal, compliance, information technology and audit to provide a continuous feedback loop.

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