The GAO and SIGTARP call for increased regulation of non-bank mortgage servicers

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Recently, reports issued by the Government Accountability Office (GAO) and the Office of the Special Inspector General for the Troubled Asset relief Program (SIGTARP) recommended increased regulatory oversight of non-bank mortgage servicers as a response to their increased role in the mortgage market.

Over the past few years, the $10 trillion mortgage servicing industry has changed as non-bank specialty servicers have assumed a much larger share of the market. Non-bank institutions include a diverse range of companies that facilitate financial services, but they are neither regulated nor organized similarly to banks. According to the GAO, non-bank servicers' market share in outstanding mortgage loans has risen from 6.8% in 2012 to 24.2% in June 2015.

The GAO report analyzed the effects of the growth of non-bank servicers in the mortgage market, noting that these servicers have specialized expertise, better high-touch servicing capabilities, and an improved capacity to monitor delinquent loans. However, the report also recognized certain risks to Fannie Mae, Freddie Mac, and consumers, that non-bank servicers pose relative to banks: immature infrastructure systems for managing risks, regulatory compliance, and internal controls; large acquisitions of mortgage servicing rights which are complicated by errors in servicer transfers; liquidity risks due to dependence on a small number of investors and reliance on short-term credit facilities; and lack of diversification which increases the volatility in pricing of master servicing rights.

While recognizing that non-bank mortgage servicers are already extensively regulated at the state and federal levels, the report identified gaps in that oversight. The GAO found that the Consumer Financial Protection Bureau (CFPB) lacked any type of mechanism to collect comprehensive data on the identity and number of nonbank mortgage servicers, and recommended that CFPB take action to require registration of non-bank entities. Additionally, the GAO report found that the Federal Housing Finance Agency (FHFA)'s lack of authority to examine non-bank mortgage servicers was inconsistent with its mission to ensure the safety and soundness of Fannie Mae and Freddie Mac. The GAO recommended Congressional action be taken to grant the FHFA authority to examine non-bank servicers, similar to the authority that bank regulators have to examine servicers which act on behalf of supervised banks. Senator Elizabeth Warren and Congressman Elijah E. Cummings responded to the GAO report by issuing a letter to the Director of the CFPB which requested he immediately provide a plan to effectuate these recommendations.

SIGTARP's report similarly recommended increased regulation for non-bank servicers, but focused on the increase of non-bank servicers' participation in HAMP. According to SIGTARP, non-bank servicers' role in HAMP has increased correspondingly with their growth in mortgage market shares. Taxpayers have already funded $1 billion to non-bank servicers, and will continue to fund more given the non-bank servicers increased role in HAMP. In 2010, 65% of HAMP loans were serviced by large banks. Today, the large bank share has declined to 35%, while 56% of loans modified through HAMP are serviced by non-bank firms.

"As non-bank servicers increase their role in HAMP, the risk to homeowners has also increased," the SIGTARP report stated. Previous reports from SIGTARP have found that service transfers conducted by non-bank mortgage servicers, as well as their treatment of homeowners, violated HAMP's rules. "Violations of the law and HAMP rules raises risks to homeowners," the report advised. "With less regulation, non-bank servicers making decisions in HAMP need strong oversight to ensure homeowners and this TARP program are protected."