



State of Washington

DEPARTMENT OF FINANCIAL INSTITUTIONS
DIVISION OF CONSUMER SERVICES

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DATE: April 20, 2010
TO: Consumer Loan and Mortgage Broker Companies
FROM: W. Kwadwo Boateng, Examinations Program Manager
SUBJECT: Modernization and Enhancement of the Mortgage Examination Process

The Washington State Department of Financial Institutions (the Department) is publishing this notice to Consumer Loan Company and Mortgage Broker licensees (Mortgage Originators) about the development of a new electronic documentation protocol for examination modernization called *Modernization and Enhancement of the Mortgage Examination Process* (the Examination Protocol). In order to determine your readiness to implement the protocol, we are sending this notice along with a Survey of Licensee Technology Readiness. **The deadline for completing the survey is May 20, 2010.**

This notice details changes in the examination process and will discuss the elements listed:

- New examination technology the Department and the Multi-State Mortgage Committee will use in examinations;
- The responsibility of licensees to retain transaction level data sufficient to facilitate the employment of new examination technology; and
- Proposed timeframe within which all licensees are expected to retain transaction level data for use with the new technology.

Background

The Department collaborated with other states to develop a protocol to conform to the requirement of the Safe and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act.). The SAFE Act set forth certain specific objectives for uniformity and effectiveness related to licensing, reporting, information sharing, consumer protection, training, examination, and complaint management. In 2008, the Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR) developed the Model State Law (MSL) as a template for states to use in passing legislation and implementing these objectives. The MSL addresses enforcement authorities; examination and investigation authorities; information sharing among regulators; modernization of the examination process, including the use of technology; and prohibitions on certain practices. As of July 31, 2009, the vast majority of states had implemented some or all of these. The Examination Protocol was developed to meet these objectives.

The cornerstone of the Examination Protocol is the CSBS/AARMR Nationwide Cooperative Protocol and Agreement for Mortgage Supervision (Agreement).¹ Within the agreement the Examination Protocol can be described broadly within the areas of Uniformity, Modernization and Effectiveness.

Uniformity in the Examination Process

The Examination Protocol supports uniformity in the examination process for both multi-state examinations and single-state examinations. Multi-state examinations fall under the Agreement and are selected and directed by the Multi-State Mortgage Committee (MMC)² representing all states. Multi-state examinations are joint sharing arrangements of resources and information between two or more states when examining Multi-State Mortgage Entities (MMEs).³

Modernization through Technology

CSBS and AARMR identified ComplianceEase's automated compliance system, ComplianceAnalyzer® as a technology solution for states for both multi-state and single-state examinations. The Department will be utilizing ComplianceAnalyzer as part of our examination process for the purposes of examining loans against federal and state laws and regulations including anti-predatory lending, the Truth-In-Lending Act (TILA), the Real Estate Settlement Procedures Act (RESPA), the Consumer Loan Act (chapter 31.04 RCW), and the Mortgage Broker Practices Act (chapter 19.146 RCW).

Mortgage Originators are strongly encouraged to begin a system readiness review and technology preparation process for loan origination and portfolio software, with the expectation that all Consumer Loan Act licensees will be able to participate fully in the new Examination Protocol no later June 30, 2011.⁴ Mortgage Broker Practices Act licensees will need to prepare with the goal of implementing the new Examination Protocol by December 31, 2011.

How the Technology Works

In order to facilitate the use of advanced technology in the new Examination Protocol, loan portfolio information will have to be maintained in a format that will allow the electronic extraction of information. The Department will be providing further information about that format and how to upload the required information. At a minimum, your systems must be capable of retaining and extracting the following data for each loan transaction:

1. Information sufficient to identify the residential mortgage loan and the unique identifier of the mortgage loan originator, mortgage broker (if applicable), and mortgage lender for the loan.

¹http://www.csbs.org/Content/NavigationMenu/RegulatoryAffairs/SupervisoryAgreementsApplications/regulatory_agreement.htm

² The MMC is a ten state committee appointed by the states to implement the Agreement and oversee the multi-state supervision process. Additional information about the MMC and national uniform examinations may be found in the document MMC Report to State Regulators August 2009 at <http://www.csbs.org/Content/NavigationMenu/Home/2009MMCREPORTTOSTATEREGULATORSFinal.pdf>

³ Multi-State Mortgage Entities (MMEs) are licensees conducting business in two or more jurisdictions.

⁴ More information about the modernization initiative can be found in the 2009 MMC Report to State Regulators at this link: <http://www.csbs.org/Content/NavigationMenu/Home/2009MMCREPORTTOSTATEREGULATORSFinal.pdf>

2. Information sufficient to enable computations of key items in the federal Truth in Lending Act disclosures, such as the annual percentage rate, finance charge, a schedule of payments, and any deviations between initial and final disclosures.
3. Information included in the Good Faith Estimate (GFE) disclosure, such as the rate, the date of any interest rate lock, the itemization of amount financed and all broker compensation.
4. Information included in a HUD-1 or equivalent Settlement Statement.
5. Information related to the terms and conditions of the loans, such as adjustable rate loan features (including timing of adjustments, indices used in setting rates, maximum and minimum adjustments, floors and ceilings of adjustments), undiscounted interest rate, penalties for late payments, and penalties for prepayment (including computation of penalty amount, duration of prepayment penalty, and the maximum amount of penalty).
6. Information typically used in underwriting, such as appraised value of the property, sales price of the property (if a purchase loan), borrowers' income, monthly payment amount, housing debt-to-income ratio, total debt-to-income ratio, and credit score(s) of borrowers.
7. Information included in a Loan Application Register for mortgage lenders required to submit such information pursuant to the federal Home Mortgage Disclosure Act.

This data will be uploaded to RegulatorConnect.org in order to analyze the loans for regulatory compliance.

Pre-built export capabilities may already exist for your existing technology platforms allowing you to upload your data directly to RegulatorConnect.org in the appropriate format. If pre-built export capabilities do not exist you may wish to contact your technology providers to encourage them to build exports in the necessary format.

If you are currently employing a vendor program to analyze regulatory compliance (e.g. Mavent, Interthinx, etc.), you may want to consider contacting your vendor for possible assistance in the upload of data to RegulatorConnect.org.

Note: The Department does not endorse or require you to use any specific software program or analytical service. Numerous vendors offer sophisticated analytical tools for determining an institution's compliance with applicable laws and regulations. ComplianceAnalyzer® is made available to the Department through CSBS and AARMR free of charge and our licensees do not need to be a customer of the system to upload their company loan data for our examination process.

Effectiveness

In its simplest approach, the new Examination Protocol accomplishes effectiveness by assigning more resources to licensees posing greater risk and fewer resources to licensees exhibiting less risk while maintaining a regulatory presence for all licensees through advanced offsite reviews and limited scope visits. In other words, we expect to spend less examination time on licensees whose loan files indicate compliance.

Pilot Program for Washington State

The Department's communication outreach program relating to technology will include a pilot testing phase. The pilot testing phase will include five lenders participating in the technology driven enhanced examination. This phase will begin after the Department has received the Survey of Licensee Technology Readiness, as discussed above. The Department will continue with the pilot throughout the remainder of 2010. We expect Consumer Loan Act licensees to participate fully in the new Examination Protocol no later than June 30, 2011. Mortgage Broker Practices Act licensees will need to prepare with the goal of implementing the new Examination Protocol by December 31, 2011.

This new Examination Protocol will require effective communication on both sides, and we appreciate your support in making this a success.

If you have questions relating to any aspect of this initiative, please send them to amanda.harvey@dfi.wa.gov. Additionally, Financial Examiner Supervisor Rick St. Onge can be reached at rick.stonge@dfi.wa.gov or by telephone at (360) 902-8817.