Emerging Trends in Mortgage Licensing:

Rise of Non-QM Lending
Equity Sharing Agreements
Other Housing Finance Options

Massachusetts Division of Banks

AARMR Summer 2019
Agenda

Revisionist’s History / Project’s Hypothesis

Housing Market / Statistics

Ability to Repay / Qualified Mortgages and Rise of Non-QM Products/Market

Financing Options (Equity Sharing)

Regulatory Approach: What to Watch
A Little Bit of History

“Those who fail to learn from history, are doomed to repeat it.”

~ Santayana 1905
~ Churchill 1948

Hypothesis: The subprime mortgage crisis/fallout assigned responsibility for the collapse of the mortgage industry and for the sharp rise in defaults & foreclosure in the wake of the sudden tightening of mortgage credit. Blame was laid at every link of the mortgage production chain (borrowers, brokers, LOC, wholesale lenders, federal housing policy, credit rating agencies, etc.). The ultimate culprits may rest w/ Wall Street that carelessly securitized mortgage loan pools without appropriate diligence and attention to the quality of the underlying loans.
2000-2008: A Blueprint for Future Financial Crises

- Loose underwriting standards
- Layering UW risks
- NINA / SISA
- Elevation of DTI
- VOI / VOE
- Skin / Downpayment
- Removal of reserve requirements
- Rating agency stamp of approval
- GSE and/or Congressional endorsement
- Secondary market appetite
Single Family Market Overview 2014 – 2018

- Median Sales Price ↑
- Inventory of Homes for Sale ↓
- Percent of Original Price Received ↑
- Affordability ↓
Single Family Market Overview
2014 – 2018

- Aggressive lending products to address affordability;
- Market Conditions – inverted effect upon underserved markets;
- Low mortgage volume and large underserved segments of market create opportunity;
- Zoning: NIMBY preventing affordable supply
Thanks to NIMBY-ism, people can’t afford to live here

A study released last week by three Boston University professors puts hard data behind something we have long assumed: NIMBYism is real, and it’s driving up housing costs and keeping a generation of families mired in economic insecurity. The report should be required reading for anyone sitting on a city council, board of selectmen, planning board or zoning board of appeals. Researchers Katherine Levine-Einsein, Maxwell Palmer and David Glick analyzed three years of meeting minutes from 97 cities and towns in Massachusetts, and used Census data and other public records to get an idea of who was doing the talking.

About two thirds of residents who spoke at housing-related public meetings were against new developments, the trio found. By contrast, only 14 percent spoke in favor. These numbers are out of whack with local and statewide polling, which shows a clear majority of citizens recognize the need for adding affordable housing.

To be sure, public meetings are often an important tool for city and town officials to hear from the public. But those having their say represent just a sliver of the citizenry — where a mere 3 percent of the housing stock is deemed affordable, a local record exceeded only by Boxford, which has less than 1 percent. A small handful of townspeople have done all they can to oppose efforts by the Harborlight Community Partners and the Hamilton Affordable Housing Trust to address the problem, even in a modest fashion. The NIMBYs have been frustratingly effective — not a single affordable house or apartment has been added in the past three years, according to state Housing and Community Development records.

Even those housing projects that do gain approval are often delayed by months and smaller in scale that what was originally proposed.

Make no mistake, the region needs more affordable housing. Near-record low vacancy rates in the Greater Boston area have pushed single-family home prices to record highs. Median prices in Essex County increased about 6 percent from a $415,000 in 2017 to $439,900 through July 2018, according to the Warren Group. Working-class communities aren’t immune. Peabody’s median home price has gone up 6 percent over the last two years, according to the Boston Foundation. Lawrence saw a 14.2 percent jump.

To be sure, not all affordable housing projects are created equal. And the more affluent members of our communities have a right to be heard. But their voices can’t drown out those of their neighbors.
Qualified Mortgage (QM)

Substantially all mortgages 2014-2017

Best practice product guideline

Presumption of compliance with Ability-to-Repay rules
Ability to Repay (ATR)

Good faith determination (8 UW factors)

Review credit history; verify employment; verify income/assets; calculate all debt, child support/alimony, and mortgage-related payments, taxes and insurance; determine DTI

Qualified Mortgage (QM) Safe Harbor Rules
Non-Qualified Mortgages (NQM)

Service large subsets of population which cannot be serviced by agency and gov’t loans

Target non-traditional income streams (self-employed, retiree, investor, foreign national)

Provide leniency for those who are just outside of agency UW standards

Allows for common sense lending and compensating factors

Largely Non-Prime
FICOs as low as 500
No Seasoning for Bankruptcy/Foreclosure
Mortgage Lates
DTI up to 55%
LTV up to 95%
Bank Statements
Asset Depletion
Interest Only
No PMI
### Securitization A

#### LTV Summary

<table>
<thead>
<tr>
<th>FICO</th>
<th>Purchase</th>
<th>Rate/Term</th>
<th>Cash Out</th>
</tr>
</thead>
<tbody>
<tr>
<td>680+</td>
<td>80%</td>
<td>80%</td>
<td>75%</td>
</tr>
<tr>
<td>660-679</td>
<td>80%</td>
<td>80%</td>
<td>70%</td>
</tr>
<tr>
<td>580-659</td>
<td>75%</td>
<td>75%</td>
<td>70%</td>
</tr>
<tr>
<td>540-579</td>
<td>70%</td>
<td>70%</td>
<td>65%</td>
</tr>
</tbody>
</table>

#### Averages:

- Origination Balance: $410,550.82
- Mortgage Rate: 7.021%
- LTV: 68.45%
- Credit Scores: 708

#### Documentation Type

<table>
<thead>
<tr>
<th>Documentation Type</th>
<th># of Mortgage Loans</th>
<th>Average Interest Rate</th>
<th>Average LTV</th>
</tr>
</thead>
<tbody>
<tr>
<td>24 Months Bank Statement</td>
<td>172</td>
<td>6.621%</td>
<td>69.02</td>
</tr>
<tr>
<td>Standard</td>
<td>179</td>
<td>6.895%</td>
<td>71.98</td>
</tr>
<tr>
<td>Asset Depletion</td>
<td>5</td>
<td>6.404%</td>
<td>62.45</td>
</tr>
<tr>
<td>12 Month Bank Statement</td>
<td>5</td>
<td>6.524%</td>
<td>75.03</td>
</tr>
<tr>
<td>Foreign National</td>
<td>4</td>
<td>7.132%</td>
<td>65.05</td>
</tr>
</tbody>
</table>
## Securitization Credit Distribution

<table>
<thead>
<tr>
<th>Range of Original Credit Scores</th>
<th>Number of Mortgage Loans</th>
<th>Percentage of Pool</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Provided</td>
<td>72</td>
<td>12.1%</td>
</tr>
<tr>
<td>481-520</td>
<td>3</td>
<td>.5%</td>
</tr>
<tr>
<td>521-560</td>
<td>11</td>
<td>1.86%</td>
</tr>
<tr>
<td>561-600</td>
<td>14</td>
<td>2.4%</td>
</tr>
<tr>
<td>601-620</td>
<td>9</td>
<td>1.5%</td>
</tr>
<tr>
<td>621-640</td>
<td>11</td>
<td>1.9%</td>
</tr>
<tr>
<td>641-660</td>
<td>48</td>
<td>8.1%</td>
</tr>
<tr>
<td>661-680</td>
<td>71</td>
<td>12%</td>
</tr>
<tr>
<td>681-700</td>
<td>68</td>
<td>11.5%</td>
</tr>
<tr>
<td>701-720</td>
<td>98</td>
<td>16.6%</td>
</tr>
<tr>
<td>721-740</td>
<td>65</td>
<td>10.98%</td>
</tr>
<tr>
<td>741-760</td>
<td>35</td>
<td>5.9%</td>
</tr>
<tr>
<td>761-780</td>
<td>39</td>
<td>6.6%</td>
</tr>
<tr>
<td>781-800</td>
<td>36</td>
<td>6.1%</td>
</tr>
<tr>
<td>801-820</td>
<td>11</td>
<td>1.86%</td>
</tr>
<tr>
<td>821-850</td>
<td>1</td>
<td>.17%</td>
</tr>
<tr>
<td><strong>Total:</strong></td>
<td><strong>592</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>
FIGURE 1: HISTORICAL NON-AGENCY RMBS ISSUANCE

Source: Bank of America Merrill Lynch.
Back to the Future 2018-19

Non-QM Is Here

• Factors and Conditions Which Supported a Return of Non-QM
  1. Market Conditions (RE / MO)
  2. Economy
  3. Low Unemployment
  4. Policy Intervention

• Factors Which Will Support an Expansion of Non-QM
  5. Success of Current NQM Products
  6. Greed
  7. Confidence in Lack of Regulatory Accountability
Key Risk Indicators

• Product-level
  • Loosening underwriting standards
  • Risk layering
  • Fraud
  • No borrower skin in the game
  • Questionable appraisal practices

• Distorted incentives for MLOs and Lenders

• Third party complacency (gov’ts, rating agencies, investor due diligence)
Massachusetts Trends – First Mortgage Originations

Loan Originations By Credit Score

- I350 - Equals 600 or less
- I351 - Greater than 600 but less than or equal to 650
- I352 - Greater than 650 but less than or equal to 700
- I353 - Greater than 700 but less than or equal to 750
- I354 - Greater than 750
Equity Sharing/Shared Appreciation

- Provide down payment assistance / access to equity
- No monthly payments or accrued interest
- Repayment includes % of home value appreciation
QUESTIONS ??

References / Summer Reading:

Too Big to Fail ~ Sorkin
The Big Short ~ Lewis
After the Music Stopped ~ Blinder
Chain of Blame ~ Muolo
Age of Turbulence ~ Greenspan

Massachusetts Division of Banks

AARMR Summer 2019
Multi-State Mortgage Committee (MMC) Update
MMC Priorities

• Efficiency in exam operations
  • Exam metrics
  • Enforcement protocol

• Improved job aids
  • Examination Practices Working Group

• Examiner education
  • Education and Training Working Group

• Use of technology
  • Risk Profile Working Group
  • RegTech
MMC Exam Operations

• There are nine MMC examinations scheduled in 2019. Five of these are coordinated with the CFPB and four are MMC only exams.
• There are 37 states that are participating in at least one MMC exam.
• Goal to improve MMC exam turn-around times. There is improvement as evidenced in the year over year data since 2016...

<table>
<thead>
<tr>
<th>Year</th>
<th>Days from On-Site to Exit</th>
<th>Days from On-site to ROE Submission to MMC</th>
<th>Days from ROE Submission to MMC Approval</th>
<th>Days from MMC Approval to ROE Issued</th>
<th>Days from On-Site to ROE Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>2016</td>
<td>242</td>
<td>317</td>
<td>25</td>
<td>24</td>
<td>365</td>
</tr>
<tr>
<td>2017</td>
<td>130</td>
<td>195</td>
<td>16</td>
<td>16</td>
<td>227</td>
</tr>
<tr>
<td>2018</td>
<td>43</td>
<td>107</td>
<td>16</td>
<td>13</td>
<td>136</td>
</tr>
</tbody>
</table>
NDSC Multistate Mortgage Enforcement Protocol

• The Non-Depository Supervisory Committee (NDSC) will review recommendations from the MMC, a state regulator, or the American Association of Residential Mortgage Regulators (AARMR), as applicable, for possible enforcement action.

• The protocol is intended to separate mortgage examination processes, administered by the MMC, from enforcement processes.

• MMC enforcement recommendations will be derived from multistate mortgage examinations rated seriously or critically deficient or from examinations with systemic issues that would be best addressed in a multistate context.
NDSC Multistate Mortgage Enforcement Protocol

• Recommendations for enforcement matters will be developed through collaboration with the examiner in charge (EIC), participating states, the MMC, NDSC, and AARMR.

• If the case is elevated to multistate enforcement status, the NDSC, in consultation with AARMR, will facilitate the selection of a lead state(s) as an Enforcement Liaison for the enforcement case and may designate an individual to serve as lead investigator or assigned legal counsel for the specific matter.

• A Legal Pool, comprised of enforcement attorneys, has been established to support and counsel the MMC, NDSC, AARMR and regulators in the administration of an enforcement case.
Examination Practices Group

- The Examination Practices Group (EPG) shall ensure the MMC Manual is accurate (including the laws and regulations cited throughout the manual), identify new modules that should be included in the Examination Manual, coordinate the development of new modules, approve developed modules, and recommend the adoption of newly developed modules to the MMC.
MMC Manual

• The MMC Manual was updated in May 2019 and is published online at [https://www.csbs.org/mortgage-examination-supplements](https://www.csbs.org/mortgage-examination-supplements).

• This link also contains MMC examination procedures for servicing, origination, financial condition and compliance management system as well as supplemental origination and servicing documents and onboarding documents (i.e. MMC exam templates).

• Additional content for the MMC Manual will be added, as necessary.
  • Future anticipated updates include chapters on BSA/AML and cybersecurity.
Education and Training Group

• The Education Training Group (ETG) is responsible for overseeing and coordinating the development and maintenance of a comprehensive training program for mortgage examiners and ensures the program provides training on regulatory changes, developments, and current requirements.

• The goal is to create complete examiner training programs and training paths from new examiners to senior examiners. The ETG has outlined this training path and is working on content development for new examiner training.
Risk Profile Group

- The Risk Profile Group (RPG) is responsible for identifying and maintaining the list of Multi-State Mortgage Entities (MMEs) and developing and maintaining Mortgage Call Report (MCR) Analytics for risk profiling MMEs.
- The RPG leverages MCR data analytics to create reports for the MMC that consider risk factors pertaining to a MME’s loan origination and/or servicing portfolio and financial condition. These reports may be used by the MMC to evaluate MMEs for examinations and to monitor the mortgage marketplace for trends or emerging issues.
RegTech – Front End LOS v. Back End CMS

• The MMC and CSBS have been working diligently to resolve the issues of the loan examination file transfers from our licensees to ComplianceEase (aka ComplianceAnalyzer, ComplianceTool, LogicEase). Depending upon the LOS, Document Management Companies, and Compliance Management Systems you use, the results vary.
  • The MMC has taken five companies and walked through the process to find multiple fails in the transmission of data. In particular,
    • Loan information is not transferred from the LOS (loan origination system)
    • Loan information is transferred but in the incorrect field or format (column)
    • However, manual entry of the loan information resulted in a PASS or Minimal
• How does this affect our examiners? Examiner requests files to be submitted through CE > Examiner receives results which show multiple failures on almost 100% of loans > Examiner requests a sample of loans to be reviewed manually > Doesn’t come to the same conclusion of CE > Defeats the Purpose and examiner is frustrated with the whole process.
What is happening right to improve this process?

• CSBS organized three LEF Summits where ComplianceEase, Regulators, LOS Providers, Lenders, Law Firms, and Associations were represented to air “grievances” or “complaints” about the LEF transfer. (25-40 attendees). One was in Orlando in February and the other in Fort Worth in March. The third is being held at this AARMR Conference.

• During the first two Summits, the MMC expressed its concern about the current process, and the amount of time loan review takes on an examination. States need to utilize RegTech to facilitate loan review, which will improve the examiner’s ability to use their resources more efficiently.
RegTech Working Groups

• Working Groups have been formed to review the following issues regarding loan file transfers:
  • LEF Gap Analysis Work Group – identify specific data gaps, failures, and potential improvements to the LEF data file and batch upload.
  • The MMC has taken this a step further and we have met one on one with a LOS provider.
  • LEF to MISMO Work Group – compare the LEF and MISMO data fields and see if they could work together.
  • Minimization of LEF – can the LEF be trimmed down in response to the findings of the GAP Analysis or can the method of transferring information be modified.
RegTech Goal

• The MMC’s goal is to have a proposal to the NDSC by the end of 2019.

• With this proposal, the MMC wants to have training material ready for examiners so that they can easily understand “fails” and how to request specific documentation instead of entire loan files, to satisfy or verify the failure.

• The MMC will not force the use of the LEF transfer until we have tested the process with market leaders in a sandbox environment.
RegTech

In addition to improving exam efficiencies through use of the LEF, CSBS is also developing the State Examination System (SES) to improve exam scoping and state cooperation.
MORTGAGE CALL REPORTS – UTILIZATION OF METRICS FOR
OFFSITE SUPERVISION AND EXAM SCOPING

Kevin Byers, CPA
CSBS Nonbank Supervision & Enforcement Section

AUGUST 2019
Mortgage Call Report Overview

• Requirement for MCR filing created by the SAFE Act

• Data collected and maintained by CSBS

• Access and user authorization provided to state regulatory personnel via NMLS

• Submitted by companies 45 days after quarter end

• Expanded filers (GSE seller/servicers, Ginnie Mae issuers):
  – Required to file activity and financial data every quarter

• Standard filers (non-agency originators and servicers):
  – Requirement to file activity quarterly and financial data annually
Mortgage Call Report Data: Common Uses

• Individual company review by examiners before/during/after exams

• Risk scoping by MMC and Risk Profiling Group for establishing examination priorities

• Market monitoring and analysis by state supervisory personnel

• Preparation of internal policy papers, reports and updates to Commissioners

• Preparation of external policy papers and reports to stakeholders outside state regulatory system
Regulator Access through NMLS

Single Sign-on through NMLS

Click the **MCR Analytics Beta** thumbnail (see *Figure 1*).

*Figure 1: Application Selection Screen*
MCR Analytics: Dashboard

The Dashboard allows a side-by-side comparison of two sets of information.

The user can manipulate the two charts independent of one another.

Use the Dashboard to compare:

- Forward and reverse loan type
- Forward and reverse loan amt
- Forward and reverse loan count
- Total loan amount
- Total loan count
- Number of MLO’s
MCR Analytics: Analysis

The Analysis tab shows risk levels among companies in rank order by various factors.

The user can adjust thresholds for each category of the risk profile.

**Analyze Company Risk Based On:**

- Market share of loans originated
- Flagged filings within MCR
- Avg loans per MLO
- Buybacks
- States licensed
- Non-QM % of total originations
- % of servicing retained

**Analysis screen example:**

1) Risk Profile Chart   2) Risk Threshold Controls   3) Risk Level Legend
MCR Analytics: The Analysis Tab – Servicer Risk Profile

Use the Analysis Tab – Servicing to generate a Servicer Risk Profile based on risk threshold settings.

Example of Servicer Risk Profile:

**Analyze Company Risk Based On:**
- States licensed
- % of loans 90+ DQ
- % change in loans 90+ DQ
- % loans in Foreclosure
- % change in loans in foreclosure
- % loans in REO
- % change in loans in REO
MCR Analysis Screen: Company-Specific Data
MCR Data Screen: Reports and Filtering Options

1) Current Selections        2) State        3) Peer Group*
4) Company Name & ID        5) Filing Year & Quarter
MCR Data Screen: Canned Reports Available
Data Quality

• Major and minor data errors are routinely identified by regulators and CSBS staff every quarter

• Macro level: incorrect conclusions about market conditions

• Micro level: incorrect conclusions about the licensee (and you will get a call eventually)
### Data Quality – Example #1

**Error summary:** Q1 2018 origination volume by UPB in one state for high LTV loans reported as $4.64 trillion for 23 loans.

**Impact:** Error vastly inflates loan origination volume in this category in state, district and nationwide.

<table>
<thead>
<tr>
<th>Heading</th>
<th>Line Item</th>
<th>Amount</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>First Mortgage Borrower’s FICO Score Distribution</td>
<td>I350 - Equals 600 or less</td>
<td>$3,145,904</td>
<td>19.0</td>
</tr>
<tr>
<td>First Mortgage Borrower’s FICO Score Distribution</td>
<td>I351 - Greater than 600 but less than or equal to 650</td>
<td>$1,633,005</td>
<td>8.0</td>
</tr>
<tr>
<td>First Mortgage Borrower’s FICO Score Distribution</td>
<td>I352 - Greater than 650 but less than or equal to 700</td>
<td>$1,119,010</td>
<td>6.0</td>
</tr>
<tr>
<td>First Mortgage Borrower’s FICO Score Distribution</td>
<td>I353 - Greater than 700 but less than or equal to 750</td>
<td>$825,644</td>
<td>3.0</td>
</tr>
<tr>
<td>First Mortgage Borrower’s FICO Score Distribution</td>
<td>I354 - Greater than 750</td>
<td>$181,050</td>
<td>1.0</td>
</tr>
<tr>
<td>Average FICO Score</td>
<td>I360 - Average FICO Score for First Mortgage Borrowers (s)</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>Average FICO Score</td>
<td>I365 - Average FICO Score for Second and HELOC Mortga</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>First Mortgage Loan-to-Value (LTV) Distribution</td>
<td>I370 - Equals 60% or less</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>First Mortgage Loan-to-Value (LTV) Distribution</td>
<td>I371 - Greater than 60% but less than or equal to 70%</td>
<td>$124,531</td>
<td>1.0</td>
</tr>
<tr>
<td>First Mortgage Loan-to-Value (LTV) Distribution</td>
<td>I372 - Greater than 70% but less than or equal to 80%</td>
<td>$126,400</td>
<td>1.0</td>
</tr>
<tr>
<td>First Mortgage Loan-to-Value (LTV) Distribution</td>
<td>I373 - Greater than 80% but less than or equal to 90%</td>
<td>$1,777,043</td>
<td>9.0</td>
</tr>
<tr>
<td>First Mortgage Loan-to-Value (LTV) Distribution</td>
<td>I374 - Greater than 90% but less than or equal to 100%</td>
<td>$4,642,296,444,330</td>
<td>23.0</td>
</tr>
<tr>
<td>First Mortgage Loan-to-Value (LTV) Distribution</td>
<td>I375 - Greater than 100%</td>
<td>$433,332</td>
<td>3.0</td>
</tr>
</tbody>
</table>
Error Summary: Seriously delinquent loan servicing volume by UPB overstated at least five-fold in two consecutive quarters and appears to be duplication of Subservicing for Others numbers.

Impact: Seriously delinquent loan servicing volume by UPB significantly overstated and potentially leading to regulator inquiry.
Data Quality – Example #3

Error Summary: Q4 2018 modified loan volume in one state overstated by 100.

Impact: UPB volume of loans modified over 1 year ago inflated in state, district and nationwide.
Data Quality: Takeaways for Industry and Regulators

• **For Industry:** QC your MCR data before filing!
  
  – See MCR resource page in NMLS if needed:
    • [https://nationwidelicensingsystem.org/slr/common/mcr/Pages/default.aspx](https://nationwidelicensingsystem.org/slr/common/mcr/Pages/default.aspx)

• **For Regulators:** Check your state’s Flagged Filings quarterly in MCR and follow up with licensees to review their filings and correct any errors!

THE END.