POINT OF VIEW

Reshaping Loan Servicing Compliance

by Abhishek Roy

Servicers in lending organisations are challenged with navigating economic headwinds that are pushing delinquency- and default-rate projections higher. This task has been complicated by increased global regulatory focus and dynamic customer expectations, which are further providing impetus for servicers to reassess existing strategies and processes from a compliance perspective while continuing to evaluate their impact on operational efficiency and resiliency.

Regulatory landscape impacting loan servicers

Key workflows typically within loan servicers' responsibilities are at the centre of recent regulatory updates, prompting a need for additional data collection and changes to operational processes and related controls.

In the United States, regulators have recently increased scrutiny and focus on data collection. The Consumer Financial Protection Bureau has updated mortgage servicing examination procedures to support continued account maintenance and loss mitigation practices[1] and has pushed to build a national auto-lending data set (e.g., a request for nine large auto lenders to provide data on lending portfolios around lending channels and loan portfolio trends, including days-past-due and payment trends prior to repossession).[2]

The Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation and the National Credit Union Administration have proposed a policy statement on commercial real estate loans highlighting the need for financial institutions to work closely with borrowers during financial stress, including areas like loan-loss accounting, loan modification, classification and reporting.[3]

1 "CFPB Releases Updates to Mortgage Servicing Exam Procedures," by Lorelei Salas, Consumer Financial Protection Bureau, January 18, 2023, www.consumerfinance.gov/about-us/blog/cfpb-releases-updates-to-mortgage-servicing-exam-procedures/.

2 "CFPB Seeks Data From Large Auto Lenders," ABA Banking Journal, February 23, 2023, https://bankingjournal.aba.com/2023/02/cfpb-seeks-data-from-large-auto-lenders/.

3 Interagency Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts, Federal Deposit Insurance Corporation, August 2, 2022, www.fdic.gov/news/financial-institution-letters/2022/fil22036.html.

The Financial Consumer Agency of Canada has proposed guidelines for loan servicers to support consumers with increasing hardships resulting from the current environment of higher interest rates, and those with high levels of household debt.[4] These guidelines establish the expectation for institutions to proactively monitor consumers vulnerable to mortgage delinquency due to these exceptional circumstances and offer them appropriate relief measures as applicable, implement effective policies and procedures, and maintain detailed recordkeeping and reporting so that they can be made available to the agency on request.

In the United Kingdom, the Financial Conduct Authority in March 2023 finalised guidance on how financial institutions can support mortgage borrowers impacted by the rising cost of living through automated processes and digital channels. The guidance highlights the importance of providing forbearance at scale and mortgage-contract variations for the purpose of forbearance.[5]

Call to action

To address this growing set of regulatory asks and sharpen their focus on operational efficiency and resiliency, servicers should take the following multipronged approach:

- Establish or reinforce a compliance focus within the cross-functional transformation task force
- Continually review and strengthen compliance key risk indicators and risk reporting
- Scan and leverage the right technology-enablement toolset.

Detailed discussion of these strategies follows.

Establish or reinforce a compliance focus within the cross-functional transformation task force

Small to midsize lending and servicing institutions typically do not have a centralised and focused transformation office or task force that can ensure that relevant compliance requirements are adequately considered across all initiatives. Servicers should establish a centralised and multidisciplinary (i.e., business, operations and technology) process transformation and data analytics task force, or strengthen their existing one, making compliance an explicit focus area. This task force and the enabling infrastructure components should ensure that the strategies for compliance readiness are also embedded within operational efficiency and resiliency mandates. These strategies include:

- Structured and intelligent regulatory mapping to impacted business functions and business or operational processes
- Performing an operational and regulatory compliance gap assessment to identify priority areas (e.g., parts of servicing, manually extensive but important processes, and collections) that may require deeper-dive analysis and remediation
- Defining and/or strengthening regulatory compliance-related responsibilities and ownership
- Enhancing or setting up a compliance change-management function to effectively integrate regulatory-compliance changes within ongoing initiatives across impacted processes
- Designing controls to monitor compliance (i.e., manual versus automated).

Continually review and strengthen compliance key risk indicators and risk reporting

Servicers should increase the frequency and coverage with which they review their loan portfolio and enhance regulatory compliance and loss-mitigation practices by strengthening proactive risk indicators and risk reporting. This action is especially important now, with several industry and market factors driving a potential increase in delinquencies and the focus on concentration risks, impacting servicing. Risk reporting should focus on areas such as:

- **Loss-mitigation options and processing time:** Substantial or significant disparities across processing time or loss-mitigation servicing options by specific customer-group characteristics
- **Noncompliant collection practices:** Collection practices not based on delinquency status
- **Delinquencies and workout options offered:** Options offered to customers, including forbearances and loan modifications

[4] Proposed Guideline on Existing Consumer Mortgage Loans in Exceptional Circumstances, Financial Consumer Agency of Canada, March 21, 2023, www.canada.ca/en/financial-consumer-agency/corporate/transparency/consultations/mortgage-loans/proposed-guideline.html.

[5] FG23/2: Guidance for Firms Supporting Existing Mortgage Borrowers Impacted by Rising Living Costs, Financial Conduct Authority, March 13, 2023, www.fca.org.uk/publications/finalised-guidance/fg23-2-guidance-firms-supporting-existing-mortgage-borrowers-impacted-rising-living-costs.

- **Gaps in disclosures:** Weak or nonexistent processes (e.g., disclosures) and controls (e.g., reporting) to ensure ongoing lending and servicing compliance
- **Complaints:** Consumer complaints alleging discrimination in servicing or loss-mitigation practices
- **Audit and regulatory findings:** Internal audits, compliance reviews or monitoring reports identifying significant weaknesses or violations in handling exceptions, fee waivers, credit reporting, agency reporting or compliance with bank policies and procedures.

To address regulatory examinations and facilitate operational excellence, servicers should be prepared to record, track and report the items highlighted above.

Scan and leverage the right technology-enablement toolset

The challenge for any regulated lending institution is effectively leveraging technology on an ongoing basis to track myriad regulations issued by different regulatory agencies and effectively map and integrate them within existing internal policies and processes. Lending organisations should explore data and analytics tools along with artificial intelligence. A set of leading use cases is highlighted in the table below.

Technology	Operational Efficiencies	Regulatory-Compliance Advantages
Cloud-based solutions	• Aggregate, store and analyse data • Automate and streamline workflows and manage customer engagement	• Easily structure, store and access data to fulfil increased volume of regulatory requests • Build automated monitoring to routinely measure compliance metrics such as flood lender-placed insurance and refunds • Use automated-testing tools to map and test servicing compliance, provide complete evidence of compliance and identify proactive risk mitigation process and policy gaps
Predictive analytics	• Drive lending decisions through intelligent credit scoring • Provide proactive customer support by identifying issues before they materialise (e.g., tying historic and current data to identify inherent risks) • Identify less-engaged customers at a higher risk of attrition	• Tie historic and current data to identify inherent risk, potentially identifying compliance concerns before they materialise • Zone in on areas with known issues (e.g., customer complaints) and analyse large sets of available data (e.g., debt-to- income, loan-to-value FICO)
Natural-language processing, chatbots and speech analytics	• Automate repetitive tasks, answer customer questions and process servicing transactions • Collect data related to customer interactions across multiple channels (e.g., chat, emails, speech, text) to build analytics using keywords, phrases, call emotions for automation in compliance testing and broader operational efficiency	• Monitor and notify the business regarding any changes to regulatory requirements • Ensure adherence to regulatory requirements (e.g., call disclosures, customer greetings) and reduce customer complaints and regulatory criticism (e.g., using speech analytics to test effectiveness of Fair Debt Collection Practices Act and Unfair, Deceptive, or Abusive Acts or Practices policies and procedures, and identify areas in need of improvements and training)
Optical character recognition	• Accelerate initial data upload and document indexing and classification • Accelerate document review and validation across the loan-servicing lifecycle to verify completeness and accuracy of loan documentation • Compare loan information in documentation with system of records	• Board critical data fields (e.g., payment instructions, fees and accrual schedules, escrow, and flood) to reduce manual-input error and provide more accurate reporting • Accelerate review of critical compliance-related data fields across documents • Produce evidence in support of compliance testing across documents

Conclusion

Now is the time for loan servicers to reevaluate their strategies for compliance readiness, which, along with an ongoing focus on operational efficiency, will drive greater resiliency. Servicers can immediately deploy a set of strategic levers, including a robust transformation office, enhanced risk reporting and a range of enabling technologies, to enhance customer loyalty, advance efficiency goals and manage regulatory expectations. These initiatives can serve as the foundation for broader, long-term investments and ensure a structured approach for growth and effectiveness.

About Protiviti's Credit Risk and Technology Solutions for Financial Services

Protiviti's Credit Risk team offers credit risk management consulting and internal audit services across the credit lifecycle, including risk appetite, policies and procedures, underwriting and originations, problem loan management, credit and loan review, regulatory and financial reporting requirements, lender and portfolio due diligence, and ongoing monitoring and reporting. Our Credit/Lending Operations team works closely with our Credit Risk team in supporting operations leaders' efforts to streamline their function. We work with lending operations teams in a range of areas, including business process review and automation, platform modernisation, cost optimisation, and managed business operations setup.

Additionally, our teams work closely with Protiviti's Technology Consulting practice when the need arises for broader end-to-end solutioning and technology enablement. Our experts leverage agile processes and are certified in the latest technologies and platforms to ensure that clients remain at the forefront of technology transformation. Their expertise includes technology strategy, technology risk management, cybersecurity and privacy, the cloud, and data and analytics.

Protiviti's Global Financial Services practice has served more than 75% of the world's largest banks and many of the largest and mid-sized brokerage and asset management firms, as well as a significant majority of life, property and casualty insurers.

About the Author

Abhishek "Abhi" Roy is a managing director in Protiviti's Risk and Compliance practice focused on lending operations and credit risk management services offerings. He has extensive experience structuring and driving digital banking and operating model transformations as key levers for growth and addressing operational, resiliency and technology risks. Roy has partnered with C-suite-level and senior business, operational and technology leaders across large global and North American banks, consumer and commercial lending institutions, credit union associations, and other financial services organisations. Roy has managed and delivered numerous consulting, regulatory remediation and digital transformation engagements, strengthening aspects of lending, credit, underwriting, origination, collections, and the underlying platforms and operating models. His recent engagements include a large-scale transformation of a regional bank's operations functions across organisational, process and technology and automation areas; strengthening the credit function for a global technology organisation; and setting up a highly efficient and effective managed delivery centre for lending operations across the U.S. and India.

Acknowledgments: Protiviti Directors Indre Anelauskas and Amit Garg contributed to this paper.

protiviti®