

New Pa. Mortgage Servicer Law Raises A Host Of Questions

By **Costas Avrakotos, Daniel Pearson and Patty Mesa**

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To welcome in the new year, mortgage loan servicers in Pennsylvania were greeted by a new licensing obligation. On Dec. 22, 2017, Pennsylvania Gov. Tom Wolf signed legislation into law imposing a licensing obligation for residential mortgage loan servicers. With the enactment of Senate Bill 751, Pennsylvania became the latest state to join the majority of states that license mortgage servicers.[1] The date by which a license needs to be obtained will be determined by the Pennsylvania Department of Banking and Securities by regulations that will be promulgated in 2018.[2] Prior to adopting such regulations to govern the licensing and regulation of mortgage loan servicers, Pennsylvania regulators have indicated that they are working on issuing a customary “secretary’s letter” to provide some preliminary guidance regarding the new licensing obligations for mortgage loan servicers.



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In the interim, questions have been raised as to who qualifies as a mortgage servicer, who is exempt from licensing, what servicing practices must be followed, and what requirements must be met to obtain a license. Herein, we discuss the mortgage service licensing provisions imposed by SB 751 that have engendered the questions raised.



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Who Needs to Be Licensed?

Rather than create an entirely new law, SB 751 amends the existing Pennsylvania Mortgage Licensing Act (the “Mortgage Act,”) to add servicer-specific provisions.[3] The Mortgage Act regulates activities involving first- and subordinate-lien residential mortgage loans and licenses mortgage lenders, mortgage brokers, mortgage loan correspondents and individuals acting as mortgage originators. SB 751 adds mortgage servicers to the list of licensed entities, providing that “no person shall engage in the mortgage loan business in this Commonwealth without being licensed as a mortgage broker, mortgage lender, mortgage servicer, mortgage loan correspondent or mortgage originator as provided under this chapter.”[4] The definition of “mortgage loan business” was amended to include a mortgage servicer as a separate component of the definition of “mortgage loan business.” Entities falling within the definition of “mortgage servicer” will be required to obtain a newly created mortgage servicer license as of the deadline to be set by the Department of Banking and Securities. SB 751 does not amend the Mortgage Act to expressly license entities that merely purchase and/or hold residential mortgage loans. Nevertheless, an entity merely purchasing closed mortgage loans could still

be subject to licensing, as discussed herein.

The legislation defines the new term “mortgage servicer” as “[a] person who engages in the mortgage loan business by directly or indirectly servicing a mortgage loan.”[5] Moreover, SB 751 broadens the existing definition of “service mortgage loan” to mean “[a] collecting or remitting payment or the right to collect or remit payments of principal, interest, tax, insurance or other payment under a mortgage loan,” without limiting the licensable servicing activity to that conducted “for another,” as now worded in the Mortgage Act.[6] The amended definition is typical of the manner in which mortgage loan servicing is defined under the laws of other states.

Thus, an entity that collects and remits mortgage payments will need to obtain the new mortgage servicer license in Pennsylvania unless otherwise exempt. Further, by deleting the phrase “for another” from the definition of “service mortgage loan,” the licensing obligation also will apply to an entity that services mortgage loans held in portfolio. Therefore, with limited exception, discussed below, a company that holds a Pennsylvania mortgage lender license most likely will need to obtain the new mortgage servicer license to service its own loans, unless otherwise exempt from the licensing obligation.

SB 751 provides that a mortgage lender that acts as a mortgage servicer can do so without a separate mortgage servicer license only for mortgage loans it “originated, negotiated and owns.”[7] This language could severely limit the extent to which a licensed mortgage lender can service the mortgage loans it makes without also being licensed as a mortgage servicer. SB 751 does not define the clause “originated, negotiated, and owns,” or each of its terms, or limit how the clause should be applied. Much will depend on how the department will define those terms. Will a lender be considered to have originated a mortgage loan only if the lender took the application for the loan, or also if the lender closed the mortgage loan in its name? Assuming “originated” is defined narrowly and is based on taking an application, then a mortgage lender that makes a loan that was brokered to it by a licensed or exempt mortgage broker would not have authority to service the loans it made without also being licensed as a mortgage servicer.

Similarly, the authority of a licensed mortgage lender to service the mortgage loans it makes will depend on how broadly or narrowly the term “negotiated” is defined. Will negotiation of any terms of the mortgage loan be sufficient to constitute “negotiated,” or will the lender need to be involved in negotiating all of the terms of the mortgage loan it makes. A lender also could not service the loans it made and sold to others without being licensed as a mortgage servicer. Moreover, a purchaser of loans would need to be licensed as a mortgage servicer to service the loans it acquires and holds in portfolio. Additionally, an entity servicing loans for others may need to hold more than one license to modify mortgage loans, as an entity “only licensed as a mortgage servicer may only perform the services of a mortgage servicer,”[8] which term does not expressly include modifying a mortgage loan.

SB 751 does not directly address mortgage servicing rights, or expressly impose a licensing obligation merely to acquire or hold mortgage loan servicing rights, or to hold mortgage loans with the servicing rights. Notably, the legislation defines a mortgage servicer as one who “directly or indirectly” services a mortgage loan.[9] Many, but not all, other states that employ a similar definition interpret the “indirect” servicing of mortgage loans to reach an entity that merely holds mortgage servicing rights and contracts with third parties to conduct actual servicing operations. Moreover, as indicated above, SB 751 defines “service mortgage loan” to include the mere “right to collect or remit payments,”[10] which could further support an interpretation that licensing applies to the holders of mortgage servicing rights. If the department adopts such an interpretation in its mortgage servicer rules, an entity that holds mortgage

servicing rights may need to obtain the new mortgage servicer license even if it engages a third party to conduct all of the actual servicing activities on its behalf. To date, the department has not given any indication of how broadly it will apply the mortgage servicer licensing obligation.[11] Most likely, we will not have a sense of the department's position until regulations are promulgated.

Who Is Exempt From Licensing?

The amended Mortgage Act does not repeal any of the existing exemptions from licensing. A "banking institution," which includes, among others, a national bank or a state chartered bank, continues to be exempt from the entire Mortgage Act, including the new servicer licensing and practice provisions.[12] As a subsidiary of such a bank is considered a banking institution, a subsidiary of a national bank or of a state-chartered bank also is exempt from the entire act and the new servicer provisions.[13] Affiliates of banking institutions, and of certain other entities, are exempt from licensing upon registering with the department and complying with other requirements of the Mortgage Act.[14] As affiliates of banking institutions are exempt from licensing upon registering, they will be exempt from mortgage servicer licensing when the amendments take effect, but will remain subject to certain compliance obligations of the Mortgage Act, some of which have always applied to such "exempt affiliates." [15]

The pre- and post-amended Mortgage Act does not define the terms subsidiary or affiliate. Certain predecessor statutes to the Mortgage Act essentially applied a 25 percent or more test to determine a subsidiary or affiliate, and certain other provisions of the Pennsylvania Banking Code recognize the definitions of subsidiary or affiliate under the Federal Bank Holding Company Act, which essentially apply a 25 percent or more ownership or control test to determine a subsidiary of a bank, or a 25 percent or more common ownership or control test to determine an affiliate of a bank. As the Mortgage Act has exempted those entities since the Mortgage Act was enacted, there should be no change in the entities that qualify as a subsidiary or affiliate of a banking institution. Nevertheless, we believe Pennsylvania regulators should provide clear regulatory guidance as to the basis upon which an entity will be considered a subsidiary or affiliate of a banking institution.

The legislation further adds a de minimis exemption from mortgage servicer licensing for a person who "services ... less than four mortgage loans in a calendar year, unless determined to be engaged in the mortgage loan business by the department." [16] This de minimis exemption may benefit a lender that may service no more than three loans during an interim period, or that may service a few loans made and sold, but otherwise has no practical significance.

What Servicing Practices Must Be Followed?

In enacting SB 751, it clearly is the intent of the Pennsylvania legislators that the mortgage servicing rules of the Consumer Financial Protection Bureau become the law of the commonwealth, as the measure directs the department "to promulgate regulations which effectively incorporate the Consumer Financial Protection Bureau's mortgage servicing regulations at 12 CFR, Pt. 1024 (relating to mortgage servicing) other than 12 CFR 1024.30 (relating to scope)." [17] With the enactment of SB 751, the department is required to promulgate these servicer regulations immediately.[18] If the aforementioned federal regulations are altered, the department must promulgate regulations making the appropriate incorporation.[19] If an alteration of such federal regulations results in a complete lack of federal regulations in this area, the version of Pennsylvania servicer regulations in effect at the time of the alteration shall remain in effect for two years, during which time the department must promulgate replacement regulations.[20] Given the uncertainty that exists with the future of the CFPB and many of the regulations it has promulgated, these provisions related to servicing practices are likely

to cause confusion, unless the department is clear in its regulations as to the practices that should be followed.

What Requirements Must Be Met to Obtain a Mortgage Servicer License?

To be eligible for a mortgage servicer license, SB 751 requires that an applicant: (1) meet the eligibility criteria for approval as a residential mortgage loan servicer of a federal government-sponsored entity (GSE), government corporation or federal agency; (2) have a \$250,000 minimum net worth; (3) maintain as a licensee fidelity bond coverage as required by Fannie Mae or Freddie Mac; (4) obtain a \$500,000 surety bond under the conditions set forth in the legislation; and (5) designate a “qualifying individual” for the applicant’s principal place of business.[21] Requiring an entity to be approved by a GSE or a federal agency, which would include Fannie Mae, Freddie Mac, Ginnie Mae, the U.S. Department of Housing and Urban Development or the U.S. Department of Veterans Affairs, is a requirement that is found in a very small number of state mortgage loan servicing licensing laws. [22] Such a condition to obtaining a mortgage loan servicer license may be difficult for small non-Federal Housing Administration or VA-approved mortgage lenders to meet. If they cannot readily obtain a mortgage servicer license because they do not have the requisite “federal approval,” and they can only service mortgage loans they originated, negotiated and own, such small mortgage lenders will be squeezed out of any third-party servicing activities.

Additional requirements are likely to be added as the department issues guidance and promulgates regulations interpreting the legislation. Although an entity licensed as a mortgage lender under the Mortgage Act most likely will also need to hold a mortgage servicer license to service mortgage loans for others, it is unclear if such a licensed mortgage lender (1) will need to submit a full application, or (2) can be issued a servicer license under some abbreviated process. It also is unclear as to how much time a mortgage servicer will have to apply for a license once the regulations are issued, or whether the submission of an application will provide some temporary authority to service mortgage loans until a license issued.

Given the uncertainties as to how the new mortgage servicer law will be applied, it is imperative that servicers and lenders closely follow the department’s promulgation of its mortgage servicer regulations and comment once the regulations are proposed.

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[1] Every state does not license residential mortgage loan servicers. Each year, a few more states enact legislation to do so. In 2017, in addition to Pennsylvania, the Oregon Legislature enacted a new mortgage loan servicer licensing law, the Oregon Mortgage Loan Servicer Practices Act, and legislators in Maine enacted amendments to the Maine Consumer Credit Code to require mortgage loan servicers to be licensed as supervised lenders.

[2] SB 751 provided that, immediately after its enactment, the department must promulgate regulations that would govern the manner in which mortgage loans will be serviced, and that those regulations and the licensing obligations for mortgage servicers “shall take effect upon the effective date of regulations promulgated under 7 Pa .C.S., § 6141.” See SB 751, § 9.

[3] 7 Pa. Con. Stat. Ann. §§ 6101 et seq. As SB 751 amends the Mortgage Act, citations are to SB 751 and/or to the provisions of the amended Mortgage Act, as applicable.

[4] See SB 751, § 2; 7 Pa. Con. Stat. Ann. § 6111(a). Under the Pennsylvania Mortgage Act, the licensing obligation formally applies to one engaged in “mortgage loan business” (see 7Pa. Con. Stat. Ann. § 6111(a), which, prior to the amendments to the Mortgage Act, was defined as “the business of advertising, causing to be advertised, soliciting, negotiating or arranging in the ordinary course of business or offering to make or making mortgage loans.” See id. § 6102. The definition of mortgage loan business is written more broadly than the definition of mortgage broker or mortgage lender under the Mortgage Act. See id.

[5] SB 751, § 1; 7 Pa. Con. Stat. Ann. § 6102.

[6] Id. Until the amendments go into effect, the Mortgage Act regulates certain servicing activities conducted for others, but does not license mortgage loan servicers. Under the pre-amended Mortgage Act, the term “service mortgage loan” means “[a] collecting or remitting payment for another, or the right to collect or remit payments for another, of principal, interest, tax, insurance or other payments under a mortgage loan.” Id. § 6102 of the pre-amended Mortgage Act.

[7] SB 751, § 2(b)(1)(ii); 7 Pa. Con. Stat. Ann. § 6111(b)(1)(ii), as amended. We have not researched the legislative history to understand the intent in restricting the mortgage loans that can be serviced by a licensed mortgage lender to those mortgage loans that a mortgage lender “originated, negotiated, and owns.”

[8] SB 751, § 2(b)(4); 7 Pa. Con. Stat. Ann. § 6111(b)(4).

[9] SB 751, § 1; 7 Pa. Con. Stat. Ann. § 6102.

[10] Id.

[11] We do not want to be presumptuous of the department’s view, as regulators in different states view this licensing issue from their own perspective. For example, with respect to the other new servicer licensing laws in 2017, Oregon regulators preliminarily have indicated that those who only hold mortgage servicing rights will not need to be licensed as mortgage servicers, unless the servicing activity is conducted in the name of the entity holding the servicing rights, or if such “master servicer” has an “ongoing obligation” to advance funds, and that the issue would be addressed by regulations that would be promulgated, whereas Maine regulators have indicated publicly that the amended supervised lender licensing obligations will not be applied to license those who only hold mortgage loan servicing rights.

[12] SB 751; 7 Pa. Con. Stat. Ann. § 6101. Section 6112 (1) provides that a banking institution is exempt from licensing, as are certain other institutions, but the department has recognized Section 6101 as governing the exemption for a banking institution.

[13] 7 Pa. Con. Stat. Ann. §§ 6102, 6101.

[14] See SB 751, § 3(7); 7 Pa. Con. Stat. Ann. § 6112(7), as amended.

[15] Id.

[16] SB 751 § 3; 7 Pa. Con. Stat. Ann. § 6112(3), as amended.

[17] SB 751, § 8; 7 Pa. Con. Stat. Ann. § 6141(a)(1), as amended.

[18] See SB 751, § 9.

[19] See SB 751, § 8(a)(2); 7 Pa. Con. Stat. Ann. § 6141(a)(2), as amended.

[20] See SB 751, § 8(b); 7 Pa. Con. Stat. Ann. § 6141(b), as amended.

[21] See SB 751, § 6; 7 Pa. Con. Stat. Ann. § 6131 (k), as amended.

[22] To date, being "federally approved" as a condition of being issued a license to service residential mortgage loans is required under the California Residential Mortgage Lender Act and the Oklahoma Secure and Fair Enforcement for Mortgage Licensing Act. In Texas, such a "federally approved" entity can register as a mortgage banker under the Texas Residential Mortgage Loan Company and Residential Mortgage Loan Originator Licensing and Registration Act to make mortgage loans, and be exempt from needing to be registered as a mortgage loan servicer under the Texas Residential Mortgage Loan Servicers Act.