

## Pennsylvania Licenses Residential Mortgage Loan Servicers

The New Year greeted mortgage loan servicers in Pennsylvania with a new licensing obligation. On December 22, 2017, Pennsylvania Governor Tom Wolf signed legislation into law imposing a licensing obligation for residential mortgage loan servicers. With the enactment of Senate Bill 751 (“SB 751”), Pennsylvania became the latest state to join the majority of states that license mortgage servicers.<sup>1</sup> The date by which a license needs to be obtained will be determined by the Pennsylvania Department of Banking and Securities (the “Department”) according to regulations that will be promulgated in 2018.<sup>2</sup> Prior to adopting such regulations to govern the licensing and regulation of mortgage loan servicers, Pennsylvania regulators are expected to issue a customary “Secretary’s Letter” to provide guidance regarding the new licensing obligations for mortgage loan servicers.

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. This Legal Update discusses what we know and raises some questions that SB 751 does not answer, but which Pennsylvania regulators should address in the regulations or the Secretary’s Letter. We will monitor developments as Pennsylvania regulators move forward with the regulatory process.

### 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.<sup>3</sup> The Mortgage Act regulates activities involving first and subordinate-lien residential mortgage loans and provides for the licensing of 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.”<sup>4</sup> 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 issued mortgage servicer license as of the deadline to be set by the Department. SB 751 does not amend the Mortgage Act to expressly license entities that merely purchase and/or hold residential mortgage loans.

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.”<sup>5</sup> 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.<sup>6</sup>

Thus, an entity that conducts the typical mortgage loan servicing activities of collecting and remitting 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, as discussed below, a company that holds a Pennsylvania mortgage lender license 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.”<sup>7</sup> This language severely limits the extent to which a mortgage lender can service the mortgage loans it makes without also being licensed as a mortgage servicer. A mortgage lender that makes a loan that was brokered to it by a third party would not be able to rely on this provision to service the loans it made without a license if it did not “negotiate” the loan. A lender also could not service the loans it made and sold to others without being licensed as a mortgage servicer. Similarly, a purchaser of loans would need to be licensed as a mortgage servicer to service the loans it acquires and holds in portfolio. In such cases, an entity making and servicing loans for others will need to hold more than one license, as an entity “only licensed as a mortgage servicer may only perform the services of a mortgage servicer.”<sup>8</sup>

SB 751 does not directly address mortgage servicing rights or expressly impose a licensing obligation merely to 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.<sup>9</sup> Many 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 ...”<sup>10</sup> To date, the Department has not given any indication of how broadly it will apply the mortgage servicer licensing obligation.<sup>11</sup> 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.<sup>12</sup> 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.<sup>13</sup> 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.<sup>14</sup> 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 “exempt affiliates.”<sup>15</sup> The pre- and post-amended Mortgage Act does not define the terms “subsidiary” and “affiliate.” Certain predecessor statutes to the Mortgage Act essentially applied a 25 percent or more test to determine a subsidiary or affiliate. 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.

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.”<sup>16</sup>

## What Servicing Practices Must Be Followed?

In enacting SB 751, Pennsylvania legislators clearly intend 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).”<sup>17</sup> With the enactment of SB 751, the Department is required to promulgate these servicer regulations immediately.<sup>18</sup> If the aforementioned federal regulations are altered, the Department must promulgate regulations making the appropriate incorporation.<sup>19</sup> 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.<sup>20</sup>

## 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 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.<sup>21</sup> Requiring an entity to be approved by a GSE or a federal

agency, which would include Fannie Mae, Freddie Mac, Ginnie Mae, HUD and the VA, is a requirement that is found in a very small number of state mortgage loan servicing licensing laws. Such a condition to obtaining a mortgage loan servicer license may be difficult for small non-FHA 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.

Additional requirements are likely to appear as the Department issues guidance and promulgates regulations interpreting the legislation. In the meantime, entities engaging, directly or indirectly, in mortgage servicing activities in Pennsylvania should evaluate what, if any, consequences SB 751 will have on their compliance obligations and, if necessary, follow the Department’s promulgation of its mortgage servicer regulations to stay ahead of when a license may be needed. Should you have any questions about this legislation or require assistance in preparing a license application when the time comes to need a license, please do not hesitate to contact us.

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*For more information about the topic presented in this Legal Update, please contact Costas Avrakotos.*

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## Endnotes

<sup>1</sup> In 2017, 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.

<sup>2</sup> SB 751 provides that certain mortgage servicer regulations governing the manner in which mortgage loans will be serviced must be promulgated by the Department immediately after the enactment of SB 751 and that those regulations and the licensing obligations for a mortgage servicer “shall take effect upon the effective date of regulations promulgated under 7 Pa. C.S., § 6141.” See SB 751, § 9.

<sup>3</sup> 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.

<sup>4</sup> 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 the “mortgage loan business” (see 7 Pa. 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.*

<sup>5</sup> SB 751, § 1; 7 Pa. Con. Stat. Ann. § 6102.

<sup>6</sup> *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.

<sup>7</sup> SB 751, § 2(b)(1)(ii); 7 Pa. Con. Stat. Ann. § 6111(b)(1)(ii).

<sup>8</sup> SB 751, § 2(b)(4); 7 Pa. Con. Stat. Ann. § 6111(b)(4).

<sup>9</sup> SB 751, § 1; 7 Pa. Con. Stat. Ann. § 6102.

<sup>10</sup> *Id.*

<sup>11</sup> 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 the issue would be addressed by regulations that would be promulgated. However, 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.

<sup>12</sup> SB 751; 7 Pa. Con. Stat. Ann. § 6101. (“This chapter does not apply to a banking institution....”) 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.

<sup>13</sup> SB 751, § 2; 7 Pa. Con. Stat. Ann. §§ 6102, 6101.

<sup>14</sup> See SB 751, § 3(7); 7 Pa. Con. Stat. Ann. § 6112(7).

<sup>15</sup> *Id.*

<sup>16</sup> SB 751 § 3; 7 Pa. Con. Stat. Ann. § 6112(3).

<sup>17</sup> SB 751, § 8; 7 Pa. Con. Stat. Ann. § 6141(a)(1).

<sup>18</sup> See SB 751, § 9.

<sup>19</sup> See SB 751, § 8; 7 Pa. Con. Stat. Ann. § 6141(a)(2).

<sup>20</sup> See SB 751, § 8; 7 Pa. Con. Stat. Ann. § 6141(b).

<sup>21</sup> See SB 751, § 6; 7 Pa. Con. Stat. Ann. § 6131 (k).

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