



CLIENT ALERT: State Consent Orders

Independent mortgage companies have been increasingly subject to scrutiny by state regulatory authorities and examiners. Many states have stepped up their enforcement activities in recent years, including California, Arizona, Washington, and New York. In particular, mortgage companies doing business in California and New York have been hit with hefty fines recently for a variety of compliance issues.

Perhaps most notably, California has been very active in assessing fines and penalties on mortgage companies doing business in that state. One of the most common issues we have seen recently is the calculation of per diem interest on loans originated in California. The state has cited numerous companies for incorrectly calculating per diem interest charged to borrowers, alleging that companies charged borrowers interest for more days than the note was actually outstanding in the first month of funding. Similarly, the state of California has imposed penalties for collecting appraisal fees from borrowers in excess of the amounts shown in appraisal fee invoices and not issuing refunds to borrowers for the difference.

In addition to penalties assessed by the state of California, there are often other expenses incurred directly by companies as a result of findings, including refunds to borrowers of overpaid interest, legal expenses, and the costs associated with tying up internal human resources. In some instances, the state has required companies to hire an independent accountant to review not only current loan files, but every file for loans originated (as far back as 2010 in one case). Additionally, in some cases the state has required that quarterly reviews of future loan files be performed by an independent third party. All of this can obviously be extremely burdensome and expensive for independent lenders.

California has also been focused recently on the commingling of escrow cash. The state requires that all deposits held for borrower escrows and servicing payments be separated from a company's operating cash.

To ensure compliance with applicable rules and regulations, we recommend that companies perform an internal review of their per diem interest calculations, refund any borrower overpayment for appraisal fees within 30 days of loan funding, and verify that all borrower escrow funds are deposited into a separate trust account within one day of funding.

In addition to the enforcement actions taken by California, it has recently been reported that the state of New York has focused at least some of its examinations on whether lender credits and discount points are being properly applied. Specifically, the state has looked into whether any excess lender credits are being applied toward reducing the interest rate, reducing the principal balance of the loan, reducing the down payment required to be made by the borrower, or otherwise being refunded to the borrower at settlement or closing.

We recommend that companies periodically review discount points and lender credits to ensure that they are being properly applied and, where necessary, refund excess credits to the affected borrowers.

If you are doing business in California or New York, we strongly suggest that you review your practices in these areas to ensure compliance with all state regulations.

Our firm has performed numerous engagements to provide assurance to regulators that companies are complying with the terms of consent orders. Please reach out to your Richey May contact or email us at info@richeymay.com with any questions or for further information on this topic.

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