Texas Savings and Loan Department

MORTGAGE BROKER EXAMINATION OVERVIEW

I. INTRODUCTION

The Texas Savings and Loan Department (TSLD) promotes compliance with the Mortgage Broker License Act (MBLAct), Real Estate Settlement Procedures Act (RESPA), Truth in Lending Act (TILA), Equal Credit Opportunity Act (ECOA), and other State of Texas regulations through supervisory and outreach programs. The TSLD conducts three types of supervisory activities to review a mortgage broker's (broker) compliance posture: compliance examinations, investigations and visitations. Compliance examinations are the primary means the TSLD uses to determine whether a broker is meeting the responsibility to comply with the requirements and proscriptions of consumer protection laws and regulations. Investigations are conducted to follow up on particular consumer inquiries or complaints. Visitations are rare but conducted on occasion by the TSLD to review a broker's progress on corrective actions in the interval between compliance examinations. Visitations are usually targeted events aimed at specific operational areas or entire compliance management systems previously identified as significantly deficient.

This document provides a general overview of the TSLD compliance examination. The purposes of compliance examinations are to:

- Review compliance with relevant laws and regulations
- Assess the quality of the mortgage broker compliance management system for implementing state and federal consumer protection statutes and regulations
- Initiate effective supervisory action when elements of a broker's compliance management system are deficient or when significant violations of law are found

II. EXAMINATION APPROACH

The TSLD compliance examination scheduling is based on a risk-focused approach that incorporates items such as consumer complaints, inconsistent licensing information, inaccurate advertising or other sources, and the volume of production. Risk focusing involves using information gathered about the broker from these four primary criteria to direct TSLD examiner resources to those operational areas that present the greatest risk in compliance and to Texas consumers.

Determining Risk

Risk focusing involves a random selection of five loans per loan officer. Whenever possible, one of these files should be in process and one denied. Examiners will use their discretion to determine the need for expanding the scope of the review. For larger operations where more than nine active loan officers are sponsored by the same broker,

a smaller statistical sample will be taken. When a smaller sample is initiated, a minimum of fifty loans or at least one file per loan officer will be imposed.

Evaluating the Compliance Management System
Previous compliance examinations have revealed either the complete absence or significant deficiencies in many brokers' compliance management systems. The examiner considers the compliance risk profile for a broker using various sources of information about its business lines, organizational structure, operations, and past supervisory performance. Factors used in measuring adequacy include:

- Knowledge level and commitment of broker and personnel
- Broker's responsiveness to compliance deficiencies
- Broker information systems and proper settings
- Policies and procedures
- Training program

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Based on the results of this review, the examiner may conclude that weaknesses in the broker's compliance management system may result in current or future noncompliance with consumer protection laws, regulations, or policy statements. The TSLD expects a viable system in place to manage the sponsoring broker's compliance risk, consistent with size and product mix.

Unlicensed Activity
A reconciliation of TSLD office records for approved broker activities against field examination findings will sometimes reveal activity that is unlicensed. For example, a loan "processor" who is acting as a loan officer without having obtained a license is conducting unauthorized unlicensed activity. Another common example is a loan officer who originated loan applications prior to his/her licensing date or during a period of time when the license was allowed to expire before renewal.

III. ROLE OF THE MORTGAGE BROKER EXAMINER

Mortgage broker examiners play a crucial role in the supervisory process. The compliance examination, along with follow-up supervisory attention to a broker's compliance program deficiencies and violations, helps to ensure that consumers obtain the benefits and protections afforded them under state and federal law. To this end, an examiner's efforts should help brokers improve their compliance posture and prevent future violations.

Primarily, examiners will conduct transaction testing through the sample of five loans per officer, evaluate the broker's compliance management system and adjust the scope based on assessed risk areas.

As part of the examination process, examiners are expected to:

- Use a common sense approach to examining and use sound judgment when

making decisions
- Maintain ongoing communication with the broker
- Assist the broker to help improve performance by providing sound recommendations for enhancing its compliance management system
- Share experiences and knowledge of successful compliance management systems
- Provide guidance regarding the various consumer and fair lending laws and regulations

IV. EXAMINATION MANAGEMENT

Mortgage broker examinations primarily involve four stages: pre-examination planning and analysis, on-site examination, reaching conclusions, and communicating findings to the broker via meetings and a report of examination.

Pre-examination Planning and Analysis

Pre-examination planning involves gathering information available in TSLD records and databases such as SEMARCA and delivering prior notification to the broker of a pending examination. The prior notification begins with a telephone call to determine an examination date that is acceptable to both parties. The phone call is followed up with the notification cover letter from the Director of Examination and a form called "The Examination Process: What You Should Anticipate" **(Exhibit 1),** delivered via e-mail or fax to the broker. SEMARCA data that will be beneficial includes: list of offices, list of officers with initial approval date, and current expiration dates, as well as annual report data. Proper examination preparation and advanced planning maximizes the examiner's time and resources. The scope of an examination may be expanded based on discussion with the broker's or loan officer's views about compliance, a lack of necessary procedures or controls, or the presence of violations.

On-site Examination

An initial meeting with the broker should be scheduled as early as possible upon arriving on-site. The focus of this meeting should be an interview for the examiner's completion of the "Mortgage Broker Questionnaire" **(Exhibit 2).** **(a .pdf file)** The broker should provide a complete overview of the operation. Make a copy of the questionnaire and provide the original to the broker for his/her review and signature, then trade the copy for the signed original. During the on-site phase of an examination, the examiner thoroughly reviews a broker's loan application log to make a determination of the loan cut, assesses the quality and viability of the compliance management system, and documents system weaknesses and violations of consumer protection laws and regulations. The compliance review includes, among other things, an evaluation of the effectiveness of training.

Reaching Conclusions

At the conclusion of the on-site examination, an examiner:

- Defines and provides examples supporting violations and deficiencies.

- Summarizes all findings regarding the strengths and weaknesses of a broker's compliance, using the aggregation page for the "Application Compliance Worksheet" **(Exhibit 3). (a .pdf file)**

Communicating Findings
Examiners must discuss findings and recommendations with the sponsoring broker and, if needed, obtain a commitment for corrective action. This exit discussion will include delivery to the broker of the aggregation page for the Application Compliance Worksheet. The examiner will retain a copy signed by the broker acknowledging receipt. The results of the examination will also be communicated in the Report of Examination. The Report of Examination is a stand-alone document that details the following items:

- Scope of the examination
- Compliance rating
- Loan sample
- Summary and detail of significant violations
- Compliance program and management of the program
- Discussion summary of the exit meeting with the broker regarding the examiner's findings and conclusions
- Management's response to findings with proposed corrective actions (if needed)

V. COMPLIANCE PROGRAM

A sound compliance program is essential to the efficient and successful operation of the broker operation. It is expected that no two compliance programs will be the same, and that the formality of a program will be dictated by a variety of considerations, including the volume of business, number of branches, and number of sponsored loan officers, as well as the variety and types of products.

Policies and Procedures
Compliance policies and procedures generally should be described in a document, reviewed, and updated as the mortgage broker's business and regulatory environment changes. Policies should be established to include goals, objectives, and appropriate procedures for meeting those goals and objectives. Generally, the degree of detail or specificity of procedures will vary in accordance with the complexity of the issues or transactions addressed. A broker's policies and procedures should provide personnel with all the information needed to perform a business transaction. This may include applicable citations of regulations and definitions, sample forms with instructions, broker policies, and, where appropriate, directions for routing, reviewing, retaining, and destroying transaction documents.

Monitoring
Monitoring is a proactive approach to identify procedural or training weaknesses in an effort to preclude regulatory violations. An effective monitoring system includes

regularly scheduled reviews of:

- Disclosures and calculations for various product offerings
- Document filing and retention procedures (especially in branch situations)
- Posted notices, marketing literature, and advertising (particularly if officers advertise individually)

Monitoring also includes reviews at the transaction level during the normal, daily activities of employees in every operating unit. This might include, for example, verification of an annual percentage rate, or a second review of a loan application before the transaction is completed. Monitoring at this level helps establish management and staff accountability, and it identifies potential problems in a timely manner. The frequency and volume of employee turnover at a broker operation should be factored into the intensity of reviews.

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