

New Jersey Expands Regulation of Mortgage Servicers

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Recently, New Jersey passed Assembly Bill A-4997, dramatically expanding the state's regulation of residential mortgage servicers. The law requires nonbank finance companies that specialize and focus almost exclusively on mortgage servicing, and that are not already licensed in New Jersey as residential mortgage lenders, to be licensed as mortgage servicers. The law also subjects mortgage servicer licensees and other mortgage servicing entities to various regulatory obligations, restrictions, and prohibitions. The author of this article summarizes key provisions of the Act.

New Jersey Governor Phil Murphy on April 29, 2019, signed into law a bill, A-4997 (the "Act"), that requires entities that engage in mortgage servicing to be licensed and subjects them to supervision by the New Jersey Department of Banking and Insurance ("Department"). The governor's action brings New Jersey in line with several of its neighboring states, including Connecticut, New York, and Pennsylvania, and with many other states around the country, which already license and regulate mortgage servicers.¹

The Act seems intended to capture as licensees those nonbank mortgage servicers that do not already hold a New Jersey residential mortgage lender license and thus enable the Department to expand its watchdog role. Banking institutions and licensed residential mortgage lenders do not appear to be

subject to this licensing requirement. While neither the Act nor any statement attached to the bill indicates what exactly triggered development of this legislation, it can be surmised that reports of servicing abuses or nonresponsiveness on the part of specialty mortgage servicers played a significant role. The Act appears to give the Department new weapons and powers to police most mortgage servicers. A brief summary of the key provisions of the Act is set forth below.

Scope

The Act applies generally to "mortgage servicers." It defines a mortgage servicer broadly as a person, "wherever located," who, on behalf of itself or other mortgage loan holders, "services" consumer-purpose loans made to a natural person that are secured by a first

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lien on a one to six family dwelling constructed or to be constructed on real property located in New Jersey (“N.J. Loans”). “Services” means collecting monthly mortgage payments, recording those payments on its books and records, and performing the “other administrative functions as may be necessary to properly carry out the mortgage holder’s obligations under the mortgage loan agreement.” These “other administrative functions” can include receiving funds to be held in escrow for payment of real estate taxes and insurance premiums, and paying funds from escrow to the taxing authority and insurance company. The Act indicates that persons who make payments to mortgagors in accordance with the terms of a home equity conversion or reverse mortgage fall within the definition of a mortgage servicer.

Licensing

Licensing Requirement and Exemptions

The Act prohibits “mortgage servicers” from acting as such “on or after the [Act’s] effective date” without first obtaining a license from the Department,² but exempts from this licensing requirement all federally insured banks and credit unions, their wholly owned subsidiaries, their operating subsidiaries (provided all of the owners of the operating subsidiary are wholly owned by the same bank or credit union), the New Jersey Housing and Mortgage Financing Agency (“NJHMFA”), and persons licensed as residential mortgage lenders under the New Jersey Residential Mortgage Lending Act (“RMLA”)³ that fulfill the Act’s supplemental surety bond, fidelity bond, and errors and omissions insurance coverage requirements (“Exempt RMLAs,” and collectively, “Exempt

Entities”).⁴ Also exempted from licensing are persons who service no more than five N.J. Loans within any period of 12 consecutive months (“De Minimis Servicers”), and any agency of the federal government, any state or municipal government or any quasi-governmental agency servicing residential mortgage loans under the specific authority of the laws of any state or the United States (“Government Entities”).⁵ Therefore, the key targets of the Act’s licensing provisions are nonbank, nonmortgage originator finance companies that specialize and focus almost exclusively on mortgage servicing.

Licenses

Those mortgage servicers that are required to be licensed under the Act must obtain a license for their designated main office and each branch office in which servicing business will be conducted. Initial licenses will generally expire at the end of the year in which approved, unless approved on or after November 1, in which case they will expire at the end of the following year, and renewal licenses will be valid for three years.⁶

License Qualifications

Generally, to qualify for a license under the Act, an applicant must demonstrate to the Department’s satisfaction that it, as well as its “control persons,” “qualified individual” and “branch managers,” possess the financial responsibility, character and general fitness to warrant a determination that the applicant will operate the business honestly, fairly and efficiently within the purposes of the Act.⁷ “Control person” refers to any individual who directly or indirectly exercises control over any director, general partner, or executive officer

of the applicant, any 10 percent or greater owner of a corporate or partnership applicant or any managing member of a limited liability company applicant. “Qualified individual” and “branch manager” refer to the individual designated by the applicant to have supervisory authority over servicing activities conducted at, respectively, the applicant’s main office or a branch office.

The Act also specifies that the Department may only issue a license if the applicant:

1) identifies a qualified individual for its main office and a branch manager for each branch office, each of whom must have at least three years’ experience in the mortgage servicing business within the five years immediately preceding the date of application;

2) files with the Department a surety bond covering its main and branch offices in the amount of \$100,000 per office, a fidelity bond and an errors and omissions (E&O) insurance policy, each in a prescribed minimum amount and that carries a prescribed minimum deductible; and

3) has not made a material misstatement on its application, and has met any other requirements as determined by the Department.

In addition, the Department may not issue a license if the applicant, its qualified individual or any of its control persons or branch managers have been convicted of or pled guilty or nolo contendere, at any time in the past, to a felony involving fraud, dishonesty, breach of trust or money laundering, or, during the seven years preceding the application, any other felony, unless pardoned or expunged. The Department is authorized under the Act, and

can be expected, to require the submission of fingerprints and to conduct criminal history background checks to confirm that this qualification has been met.

Fees

The license fee set forth in the Act is \$1,000 for an initial license and \$3,000 for a renewal license.⁸

Notification of Adverse Events

The Act requires licensees to notify the Department, in writing, within five business days after the licensee has reason to know of the occurrence of a significant adverse event, such as: 1) a material change in the licensee’s financial condition, a bankruptcy filing or the consummation of a corporate restructuring, 2) the filing of criminal charges against applicant, or any of its officers, directors, members, partners or other significant individuals, and 3) notification of a license denial, suspension or revocation, or other regulatory enforcement action, etc.⁹

Requirements, Restrictions, Prohibitions, and Questions About Their Scope

Sections 5 and 9-12 of the Act, which are summarized immediately below, set forth certain requirements, restrictions and prohibitions that appear to be applicable not only to licensees but to Exempt Entities as well. But the Act includes considerable ambiguities, also discussed below, regarding the scope of these sections.

Annual Reports

Section 5 requires “mortgage servicers” (which, as defined, includes both licensees

and Exempt Entities) to file annual reports with the Department, including a schedule of the ranges of costs and fees it charges mortgagors for its servicing-related activities, the number, types and characteristics of the residential mortgage loans it is servicing, the number of loans in default for 30, 60, or 90 days, a description of its loss mitigation activities (including details on workout arrangements undertaken) and the number of foreclosures commenced.¹⁰

Recordkeeping

Section 9 provides that licensees and Exempt RMLAs must maintain adequate records of each mortgage loan they service, retain those records for at least two years after the final payoff date or the date servicing was transferred to another servicer, whichever occurs first, and make those records available for inspection by the Department.

Servicing Transfer Disclosure

Section 10 requires any “mortgage servicer,” following the transfer to it of servicing rights on a N.J. Loan, to provide the mortgagor with 1) a servicing transfer notice required by the federal Real Estate Settlement Procedures Act (“RESPA”),¹¹ and 2) a schedule of the ranges and categories of fees that it charges for its servicing-related activities (which goes beyond the required content of the RESPA notice).

Federal Law

Section 11 incorporates by reference all applicable federal laws and regulations that relate to mortgage servicing, including but not limited to RESPA and Regulation X¹² and the Truth in Lending Act (“TILA”)¹³ and Regulation Z,¹⁴ and requires “mortgage servicers” to

comply with those laws and regulations as a matter of state law.

Servicing Fees

Section 12 requires “mortgage servicers” to maintain, keep current, and make available to their mortgagors, upon request, a schedule of its servicing-related fees that identifies each fee, provides a plain English description of the fee and states the amount or range of amounts of the fee or how the fee is calculated. In addition, Section 12 imposes restrictions on late fees, including that they cannot be 1) based on an amount greater than the past due amount, 2) collected from the mortgagor’s escrow account or from a surplus in that account absent the mortgagor’s approval, or 3) deducted from any regular payment.

Coverage Questions

Notwithstanding the apparent applicability of Sections 5 and 9 through 12 to entities other than mortgage servicer licensees, and the existence of Section 3c, which states that “sections 9 through 12 . . . shall apply to any person, including [an Exempt Entity], who acts as a mortgage servicer in this State on or after the effective date of this act,” the scope of these sections is unclear. This lack of clarity derives primarily from Section 19 of the Act, which expressly exempts the following persons and entities from the provisions in Sections 3-12: 1) Exempt RMLAs while servicing N.J. Loans “made pursuant to the exemption,” 2) De Minimis Servicers, 3) Government Servicers, and 4) Exempt Entities other than Exempt RMLAs and the NJHMFA.

Reading Sections 3c and 19 together leads to a conclusion that Sections 5 and 9-12 may only apply to Exempt RMLAs with respect to

N.J. Loans that they did not originate, which makes some sense since RMLAs are already subject to some of these same requirements under the RMLA when servicing their own loans. Hopefully, the Department will be able, by regulation, to provide some clarity in this regard.

Investigation and Enforcement

The Act appears to significantly expand the Department's enforcement jurisdiction. It authorizes the Department to pursue enforcement actions not only against mortgage servicer licensees but against mortgage servicers generally that commit servicing violations and impose heavy penalties upon them.

Prohibited Activities

Section 13 of the Act lists numerous activities in which "mortgage servicers" are prohibited from engaging. However, unlike Sections 5 and 9-12, there does not appear to be a question as to the applicability of the prohibitions in Section 13 to all mortgage servicers. Section 13 applies on its face to all mortgage servicers, and Section 19 only provides an exemption from Sections 3-12.

Section 13 prohibits:

- 1) Engaging in unfair or deceptive servicing practices, misrepresenting or omitting material information in connection with loan servicing;
- 2) Knowingly misapplying or recklessly applying loan payments to the outstanding balance of a residential mortgage loan or to an escrow account;
- 3) Force-placing hazard or flood insurance on a property when the servicer knows or has

reason to know that the mortgagor has an effective policy in place or requiring such insurance in an amount that exceeds the replacement cost of the improvements on the property;

- 4) Knowingly or recklessly providing inaccurate information to a consumer reporting agency ("CRA") or failing to report a mortgagor's favorable as well as unfavorable payment history to a national CRA at least annually (where the servicer regularly furnishes information to a CRA); and

- 5) A host of other activities.

Investigation and Examination Authority

Section 14 gives the Department wide-ranging authority to conduct investigations and examinations in connection with 1) license applications, and 2) complaints against and suspected violations committed by a licensee or "any other person subject to this [Act]" "as often as necessary in order to carry out the purposes of the [Act]." This same section also authorizes the Department to retain attorneys, accountants or other professionals and specialists (such as examiners, auditors or investigators) to conduct or assist in the conduct of any such investigations or examinations.¹⁵

Enforcement Authority

The Act authorizes the Department, if it finds that "any person" has engaged or is about to engage in acts or practices that violate any of the Act's provisions, to:

- 1) Suspend, revoke, refuse to renew or deny the person's license (if applicable);
- 2) Issue an order directing the person to

cease and desist from engaging in such acts or practices and/or to perform corrective actions;

3) Bring an action in court to enjoin the acts of practices and to enforce compliance with the Act's provisions;

4) Permanently bar from the residential servicing or lending business any person who has been found to have knowingly violated any of the Act's provisions and thereby causing harm to consumers; and

5) Impose a civil penalty of not more than \$25,000 for each violation of the Act.

Knowing violations are deemed to constitute crimes of the third degree.¹⁶

Section 18 of the Act also provides that the Act's rights, remedies and prohibitions are in addition to those contained in the New Jersey common law and the New Jersey statutes, including the New Jersey Consumer Fraud Act,¹⁷ which is enforceable by the attorney general and the Division of Consumer Affairs in the Department of Law and Public Safety,¹⁸ as well as by aggrieved consumers by means of individual and class actions.¹⁹

Effective Date

Finally, Section 22 of the Act provides that it

will become effective 90 days following enactment, which means that nonexempt mortgage servicers must obtain their licenses on or before July 28, 2019, or cease their servicing activities. This is an extremely tight time frame for the Department to be able to meet, and one that it may find itself compelled to extend.

NOTES:

¹See Conn. Gen. Stat. §§ 36a-715 to 36a-719 (effective Jan. 1, 2015); N.Y. Banking Law § 590(2)(b-1) (2009); 7 Pa. C.S. § 6101 et seq., as amended by P.L. 1260, No. 81 (Dec. 22, 2017).

²Section 3a.

³N.J.S.A. 17:11C-51 et seq.

⁴Section 3b.

⁵Section 19.

⁶Section 7a.

⁷Section 4.

⁸Section 7a.

⁹Section 6c.

¹⁰Section 8.

¹¹12 U.S.C.A. §§ 2601 et seq.

¹²12 C.F.R. Pt. 1024.

¹³15 U.S.C.A. §§ 1601 et seq.

¹⁴12 C.F.R. Pt. 1026.

¹⁵Section 14.

¹⁶Sections 15-17.

¹⁷N.J.S.A. 56:8-2 et seq.

¹⁸N.J.S.A. 56:8-3 to -18.

¹⁹N.J.S.A. 8-19.