
**Sunset Review: Evaluation of the
Office of the Commissioner of Financial Regulation,
the State Collection Agency Licensing Board, and
the Banking Board**

**Presentation to the
House Economic Matters Committee**

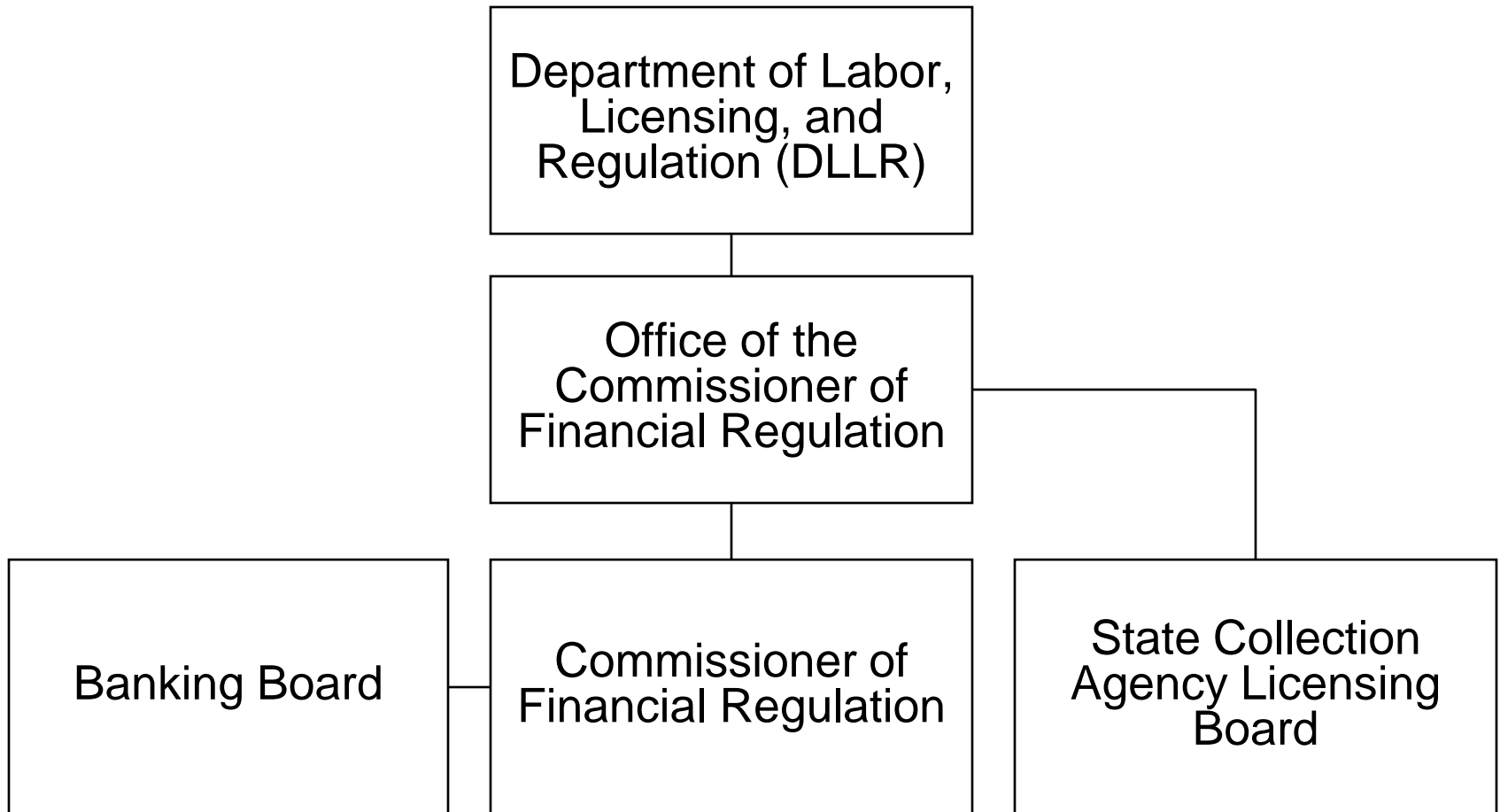
**Department of Legislative Services
Office of Policy Analysis
Annapolis, Maryland**

January 20, 2011

Sunset Process

- Conducted full evaluations of the Office of the Commissioner of Financial Regulation, the Banking Board, and the State Collection Agency Licensing Board during the 2010 interim
- Reviewed relevant literature, conducted interviews and surveys, reviewed documents, and attended board meetings
- All three entities are set to terminate on July 1, 2012
- Final report includes five recommendations

Organizational Overview



Office of the Commissioner of Financial Regulation

Commissioner of Financial Regulation

Deputy Commissioner

Depository
Corporate
Activities

Depository
Supervision

Nondepository
Institutions

Enforcement
& Consumer
Services

Internal
Policy

Nondepository
Licensing

Nondepository
Supervision /
Compliance

State-chartered Financial Institutions

- The Maryland banking industry comprises:
 - Maryland State-chartered banks
 - other-state chartered banks that operate in Maryland
 - federally chartered national banks and savings banks
- The Commissioner's Office is the primary regulator of:
 - 48 Maryland State-chartered banks
 - 9 State-chartered credit unions
 - 6 State-chartered trust companies
- 2004 – 62 State-chartered banks
- 2010 – 48 State-chartered banks

Oversight and Regulation of Nondepository Licensees

- In addition to State-chartered financial institutions, the Commissioner's Office licenses and regulates over 9,300 nondepository licensees, including:
 - mortgage lenders, brokers, servicers, and originators
 - sales finance companies
 - consumer loan companies
 - money transmitters and check cashers
 - installment loan lenders
 - credit services businesses
 - debt collection agencies
 - debt management service providers

Decline in Mortgage-related Licensees

- The office is responsible for licensing mortgage lenders and loan originators that are not employed by, or affiliated with, banking institutions (which are exempt)
- From fiscal 2008 to 2010:
 - 60% decline in the total number of licensed mortgage lenders (3,714 in fiscal 2008 to 1,478 in fiscal 2010)
 - 55% decline in the total number of licensed mortgage loan originators (11,171 in fiscal 2008 to 5,007 in fiscal 2010)
- Attributable to the residential real estate crisis and the tightening of banks' lending standards in the wake of the credit crunch in 2008 and 2009

Office Has Reorganized to Strengthen Nondepository Oversight

- The full evaluation anticipated examining the “needs of the enforcement unit to effectively respond to constantly evolving threats to State consumers, as predatory lending activities shift to loan modification and other schemes”
- Prior to and during the full evaluation, the Commissioner’s Office implemented significant changes to enhance supervision of nondepository institutions:
 - appointed a new assistant commissioner to coordinate mortgage licensing and compliance activity
 - added a staff attorney and paralegal to combat mortgage fraud (grant funded)

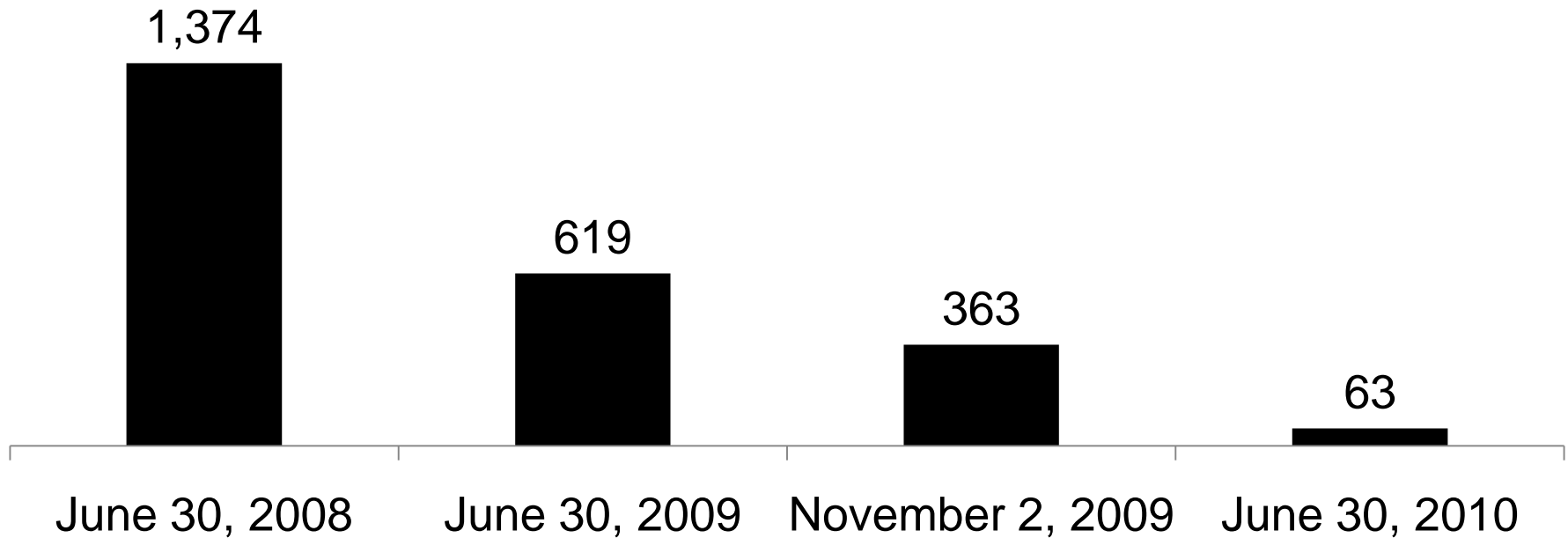
Nationwide Mortgage Licensing System and Registry

- 2008 federal legislation required all mortgage lenders and loan originators to be federally registered or state-licensed through the electronic Nationwide Mortgage Licensing System and Registry (NMLSR)
- NMLSR allows the Commissioner's Office to receive real-time updates of disciplinary actions taken in any state against any licensee
- As of January 1, 2011, all 50 states, the District of Columbia, and all U.S. territories utilize NMLSR

Calendar-based Mortgage Examination Schedule

- Pursuant to statute, the Commissioner's Office must examine each mortgage lender licensee at least once every 36 months and each new mortgage lender licensee within 18 months of initial licensure
- Meeting this statutory schedule proved difficult for the office from fiscal 1996 through 2007
- The Commissioner's Office greatly improved its timeliness in 2008 and has effectively eliminated its examination backlog as of January 1, 2011

Reduction of Overdue Mortgage Lender Examinations



Source: Commissioner of Financial Regulation, Response to Legislative Audit Report, July 2010

Implementation of a Risk-based Examination Approach

- Chapters 7 and 8 of 2008 required the commissioner to study the feasibility of scheduling mortgage lender examinations using a risk-based approach (one that categorizes licensees by the degree of risk to consumers that they pose, thereby warranting different examination frequency) rather than the statutory calendar-based schedule
- Relevant factors that could be used to evaluate a licensee's risk to consumers include:
 - loan volume, business model, and types of mortgage products offered
 - instances of noncompliance identified through self-reporting or industry stakeholders

Implementation of a Risk-based Examination Approach (Cont.)

- The office has employed these additional risk assessments only on an *ad hoc* basis; limited resources have prohibited the office from examining licensees according to the current 36/18-month statutory framework
- Successful implementation of a risk-based scheduling system largely depends on the availability of risk-based data
- The real-time information available to the office for potential risk assessments through NMLSR has significantly expanded

Enhanced Regulation of Mortgage-related Licensees

- In the near future, NMLSR will allow the Commissioner's Office to review mortgage lenders' annual call reports, which will include detailed financial statements and production activity volumes on a state-by-state basis
- **Recommendation 1 (pg. 19):** With the reduction of the mortgage lender examination backlog and the transition to NMLSR nearly completed, the Commissioner's Office should use its existing authority to implement a risk-based examination schedule to supplement the existing calendar-based statutory framework by January 1, 2012, and report on the status of implementation by October 1, 2012.

Investigations Increase with Limited Enforcement Personnel

- The enforcement unit's workload has tripled over the last five fiscal years while the number of investigators has fluctuated between five and eight

<u>Fiscal Year</u>	<u>Investigations</u>	<u>Investigators</u>
2006	123	5
2007	142	7
2008	247	8
2009	316	7
2010	373	6

- The significant increase in investigations is attributable to the mortgage foreclosure crisis and the comprehensive mortgage reform laws passed in the 2008 and 2009 sessions

Heightened Compliance and Enforcement Activity

- Fines and Penalties (general fund revenue)
 - Fiscal 2008: \$392,900 Fiscal 2010: \$1,622,895
 - Increased fines and penalties in fiscal 2009 and 2010 are a function of growing volume of consumer complaints and increased mortgage examinations and investigations
- Consumer Recoveries
 - Fiscal 2008: \$1,318,938 Fiscal 2010: \$2,463,899
 - Consumer recoveries include mortgage loan modifications achieved by the consumer services unit

Summary

- The Commissioner's Office has admirably confronted many challenges (including the stabilization of its mortgage-related special fund) and increased regulatory responsibilities while continuing to protect Maryland consumers
- The office has successfully transitioned to a nationwide mortgage licensing system and increased mortgage-related investigations with limited enforcement unit personnel
- The office has worked hard to reduce mortgage lender examination backlogs and continues to return millions of dollars per year to aggrieved consumers
- **Recommendation 2 (pg. 28): The Commissioner's Office should be continued, and legislation should be enacted to extend its termination date to July 1, 2022.**

Banking Board

- Operates as an advisory body to the Commissioner of Financial Regulation on matters relating to the regulation of Maryland banking institutions
- Established during the national banking crises of the 1930s
- Charged with providing the commissioner with “sound and impartial advice” on:
 - the approval or disapproval of certain bank applications
 - protecting the interests of the public, depositors, and bank stockholders
 - any another matter concerning banking in the State
- Meets at the discretion of the commissioner
- As an advisory body, the board’s recommendations are not binding on the commissioner

Banking Board – Membership

- Nine members:
 - State Comptroller (Chair)
 - Eight appointed members:
 - three representatives from the Maryland Bankers Association
 - one economist
 - one certified public accountant
 - one consumer representative
 - two public members
- Four of the nine seats on the board are vacant

Advice Required on Certain Matters

- Approval or disapproval of:
 - articles of incorporation
 - agreements of consolidation, merger, or transfer of assets
 - applications for bank service corporations
 - applications for the reorganization of a savings bank
- Changes to demand deposit and time deposit reserve requirements
- Before reporting to the Secretary of Labor, Licensing, and Regulation on the unsafe/unsound banking practices of a bank director or officer

Advice Required on Certain Matters (Cont.)

- Board members rarely respond to requests for advice
- Bank applications often are lengthy and complex
- Not clear why the commissioner is required to seek the board's advice on some applications but not on:
 - affiliate transactions
 - permits authorizing foreign bank offices in the State
 - branch applications
 - applications to operate ATM machines

Summary

- Board last met almost four years ago (February 27, 2007)
- Board did not convene during one of the greatest banking crises in recent history
- Board does not respond to requests for advice on bank applications
- **Recommendation 3 (pg. 32): The General Assembly should repeal the Banking Board.**

Regulation of the Debt Collection Industry

- The federal Fair Debt Collection Practices Act (which is enforced by the Federal Trade Commission (FTC)) and the Maryland Consumer Debt Collection Act generally prohibit debt collectors from engaging in abusive, unfair, or deceptive practices to collect debt
- These laws prohibit a person from using or threatening force or violence to collect debt, threatening criminal prosecution, or using a communication that simulates legal process or gives the appearance of being approved by a government agency
- Licensing law – Maryland Collection Agency Licensing Act

State Collection Agency Licensing Board

- Housed within the Office of the Commissioner of Financial Regulation
- Five members:
 - Commissioner of Financial Regulation (Chair)
 - two collection agency industry representatives
 - two consumer members
- Licenses more than 1,400 collection agencies doing business in Maryland and enforces the Maryland Consumer Debt Collection Act

Scope of Licensing Requirement

- State statute defines a collection agency as a third party that collects or attempts to collect consumer debt or sells a system used to collect a consumer debt
 - Most entities that collect their own debt are not considered collection agencies and, therefore, are not regulated by the State Collection Agency Licensing Board (Collection Agency Board)
 - A purchaser of consumer debt must be licensed by the board if the purchaser attempts to collect consumer debt through civil litigation

Collection Agency Board Revenues and Expenditures

- The Collection Agency Board is general funded
- The preliminary sunset evaluation noted concerns as to whether the licensing fees covered the costs of licensing and regulating collection agencies
- DLLR introduced departmental legislation in the 2010 session to resolve the funding imbalance
- Chapter 149 of 2010 requires the board to set the licensing fee at an amount that will cover the board's costs, up to a maximum of \$900 for a two-year license

Litigation-based Debt Collection

- Collection industry traditionally relied on phone calls and collection notices, with litigation as a final resort
- An emerging business model relies on purchasing consumer debt portfolios at a substantially reduced rate and immediately filing a large number of lawsuits in an effort to collect
- Law firms that file these claims often rely on specialized software that automatically produces paperwork needed to initiate a civil action
- Litigation-based debt collection practices may lead to mistakes and abuses of the judicial system

FTC Report on Litigation-based Debt Collection

- 2010 report of the Federal Trade Commission, *Repairing a Broken System: Protecting Consumers in Debt Collection Litigation and Arbitration*, raised the following concerns regarding litigation-based debt collection practices:
 - high rate of default judgments
 - lawsuits based on insufficient evidence
 - consumers receiving insufficient notice of lawsuits
 - the collection of time-barred debt

FTC Recommendations for States

- Adopt measures to make it more likely consumers will defend debt collection cases:
 - adequate notice
 - ensure court filing fees are not prohibitively high
- Require debt collectors to include more information about the debt in the complaint:
 - identify original creditor and account
 - identify current owner
 - include the amount owed, by principal, interest, and fees
 - include relevant contract terms

Measures Taken by Maryland Judiciary

- Letter from the Chief Judge of the District Court to judges and clerks provided an overview of litigation-based debt collection practices and highlighted common issues associated with the practice
- Office of the Attorney General and the Judiciary are engaged in preliminary discussions regarding potential changes to the Maryland Rules that would address issues associated with litigation-based debt collection

Monitor the Issue

- The Department of Legislative Services recommends that the Collection Agency Licensing Board and the General Assembly monitor issues associated with litigation-based debt collection practices
- **Recommendation 4 (pg. 44): The State Collection Agency Licensing Board, the Attorney General's Office, and the Judiciary should examine whether changes to the Maryland Rules of Procedure are necessary to protect Maryland consumers in debt collection cases and report their findings and recommendations to specified committees by October 1, 2011.**

Summary

- There is a continued need for the regulation of debt collection agencies to protect the public from harassment and illegal activity
- The board has taken proactive measures to respond to evolving industry issues and to resolve the board's funding imbalance
- **Recommendation 5 (pg. 44): Legislation should be enacted to extend the board's termination date to July 1, 2022.**