Changing Lender Process in the name of Consumer Protection
In the first white paper in this series, we focused on consumer protection as the new mandate handed down to the industry from the new federal regulator, the Consumer Financial Protection Bureau (CFPB or Bureau). While consumer protection has always been a concern for lenders and regulators, there was a difference in the way the government delivered its oversight and its ultimate objectives. In the past, regulator efforts to protect consumers were prioritized by the risks these consumers could pose to the safety and soundness of the institution if they took action, such as filing a class action lawsuit. The government was concerned, first and foremost, with the safety and soundness of the regulated institution and the banking system at large.

Under the new regulatory scheme, the Consumer Financial Protection Bureau puts mortgage lenders and third-party settlement service providers on notice: Compliance will be judged by the extent to which consumers have access to financial products and services and that such offerings are fair, transparent, and competitive. Today, it’s the consumer the government is out to protect, not the institution it regulates.
As the mortgage industry moves into this new era of consumer protection, executives face a new question: How is fairness, transparency, and competitiveness to be measured? For many lenders and their vendors, customer satisfaction has been a standard reporting and compliance measure. But is this old standard sufficient now that the regulatory pendulum has swung away from business as usual?

Ultimately, how will lenders balance the need to comply with the government’s consumer protection regulations with the business imperative of profit? In this paper, we will discuss the operational changes that mortgage lenders must consider in this environment if they hope to achieve this balance. In the final paper in this series, we’ll discuss how IT plays a major role in meeting this objective.

Customer Satisfaction is on the rise! Or is it?

From the moment the CFPB began organizing itself into what would become one of the federal government’s largest bureaus, their focus has been squarely on the consumer. The organization’s name, in hindsight, should have provided some clue to the industry as to the types of rules that the new bureau would be writing. Unfortunately, the industry was so preoccupied with complying with consent orders, defending repurchases, driving volume in an extremely tight credit environment and maximizing federal subsidies to mortgage credit for programs like HAMP and HARP, that it could afford little if any attention to the actions of its newest regulator. Despite this, some lenders were able to create transparent, consumer-friendly and consumer-safe business models. The result: at least one survey found consumers to be more satisfied with their mortgage lenders than they’ve been in years.

In a recent survey by J.D. Power & Associates (2012), customers’ overall satisfaction with mortgage lenders “has reached its highest level in the past six years,” according to the authors. (See Chart) The survey further reports that, on a 1,000-point scale, overall customer satisfaction has increased to 761 in 2012, up from 747 in 2011, and 734 in 2010. The survey cites improvements in both transparency and communication as primary factors in these improvements.¹

A more recent survey of loan servicing customers by the same firm (J.D. Power, 2013), finds that overall satisfaction with primary mortgage servicers has increased to 733 (on a 1,000-point scale) from 725 in 2012.² Like the 2012 mortgage origination survey, some of these gains are attributed to new rules promulgated by the consumer bureau.

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Let’s take a moment to put this good news into perspective.

In its 2012 mortgage loan originator consumer survey, JD Power looked at and provided awards in five areas of the business: application/approval process, loan representative, closing, contact and overall satisfaction. Only a single lender scored 5 out of 5 on the surveyor’s scale, and that institution scored only 817 out of 1,000, barely a B grade. Every other financial institution surveyed, including the nation’s largest institutions, performed worse, some far worse. While the industry’s overall performance at 761 is the highest we’ve seen in more than half a decade, it’s only a 1.5% improvement over last year and a 2.7% improvement from 2010.

One need not look at J.D. Power for an analysis of how the mortgage servicing industry performed in 2012, for this was the year of the historic servicing industry settlement. The second largest civil settlement ever obtained by the state attorneys general, second only to the tobacco settlement, will cost the nation’s five largest mortgage servicers, which control about 60 percent of the mortgage servicing market, an estimated $25 to $32 billion, according to the Office of Mortgage Servicing Oversight.³

Anyone operating in the U.S. home finance industry that puts their faith in a headline promising increasing satisfaction on the part of American homebuyers or owners is cautioned to think twice. Not only is the improvement small by any standard, J.D. Power & Associates is likely to be the last place the new federal regulator will look for signs of verifiable improvement. The first place the CFPB will look will be its own database.

The CFPB Customer Complaint Database

When George Orwell gave us his novel 1984, he envisioned a government obsessed with observing its citizens. It was a brilliant and prophetic work, but not even Orwell could have imagined a world in which the governed were equally eager to see the inner workings of their government. We live in such a world today. A glance at the increasing number of Freedom of Information requests since that program was enacted in 1966 is evidence of this as are the millions of social media-connected citizens who have “linked up” or “friended” their elected leaders.

The current administration has embraced this. Never before in the history of our democratic government have we seen an administration so open to connecting with its constituents. The American people have been invited into the virtual Oval Office and their comments are receiving responses, if not by the President himself, at least by members of his social media savvy staff. Consumers are being trained to expect transparency and access through digital networks.

Of all of the government agencies, the Consumer Financial Protection Bureau has been the best example of this type of transparent, socially available agency. The first thing the new bureau did was to set up a website and create social media connections that would allow it to communicate directly with the consumers it was charged with protecting. And this has had a profound impact on the banking industry, but not an unforeseen one.

In the Accenture Banking 2020 Consumer Survey report, data clearly pointed to a growing acceptance and even demand on the part of consumers for information delivered electronically. It should come as no surprise that consumers have responded favorably to the government’s attempts to connect with them online. But this also points to an opportunity for banks, as the data clearly indicates that digital banking has become essential. Consumers view online banking as the single most important area in which banks should invest and develop.

Far from a casual overseer, the CFPB came out with heavy fines against the credit card industry early on and then began collecting consumer complaint information to use as a prod to keep the mortgage industry moving down the path to a better consumer experience.

The CFPB officially began taking mortgage complaints on its website in December 2011. By June 30, 2013, the CFPB had received approximately 176,700 consumer complaints, forty-eight percent of which, about 85,000, concerned mortgage transactions, according to the consumer bureau’s most recent semi-annual report.

More than 144,800 (82 percent) complaints received as of June 30, 2013 have been sent by Consumer Response to companies for review and response. The vast majority of consumers’ complaints dealt with matters relating to loan modifications, collections, or foreclosures (62 percent). Other common types of mortgage complaints, according to the report, involved issues related to making payments, such as loan servicing payments or escrow accounts (24 percent). Few dealt with mortgage origination complaints.

One result of this data collection effort has been the revelation that the things mortgage customers loathe about the mortgage origination and servicing processes today are pretty much the same things they have loathed for years. Chief among them, being denied the credit they feel they deserve.

In the past, lenders dealt with this country’s over-developed sense of entitlement by developing new loan products, many of them with requirements so lax that most borrowers could not help but qualify. The NINA loans with the drive-by closings spring to mind. At least this allowed the industry the opportunity to profit handsomely for removing this source of borrower frustration. That ended poorly.

In the past, regulators used more carrot than stick to get the industry to move in the direction it wanted. The best example of this was the availability of low-cost funds to those institutions that helped the government reach its goal of high homeownership rates. Those institutions that failed to fall into line found themselves competing on a less than level playing field when it came to home finance.

Today’s regulator uses both carrot and stick to keep lenders in line and one of its sticks is its public complaint database. By promising to share information on the “bad” banks with consumers, the CFPB becomes a source of reputational risk to any bank that has ever dissatisfied a consumer. This, of course, is a majority of banks.

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Adjudications from the CFPB

Another revelation provided by the public CFPB complaint database is that the most common mortgage complaints arise among consumers having difficulty keeping up with their mortgage payments. This should come as no surprise; collection efforts, judicial and non-judicial remedies such as loan modifications, short sales, deeds-in-lieu of foreclosure are often contentious. As such, aggrieved borrowers are more likely to file a complaint with the CFPB than are borrowers with performing loans.

The Consumer Complaint Database allows the public to know what is being complained about and why, according to the Consumer Bureau. Still, the public can’t really do much with the information. There is no mechanism that allows a consumer to use information gleaned from the database to secure a redress of alleged wrongs.

“Each and every time we hear from American consumers about their troublesome transactions with financial products, it gives us important insight,” said CFPB Director Richard Cordray. “The information helps us and it should be available to help others too. By making our data publicly available... we hope to improve the transparency and efficiency of this essential consumer market.” 5

Lenders didn’t seem to agree with the Director’s assessment, at least when the database was announced in January, 2012, and then expanded in March 2012 to include, among other things, mortgage related complaints. Initially, trade groups worried that their member companies’ trade secrets would be exposed and customer privacy would be at risk, according to an article in BusinessWeek.6 Additional industry concerns included posting company names without verifying the accuracy of complaints, unfairly casting reputable businesses in a bad light.

The median amount of monetary relief reported was approximately $410 for the 600 mortgage complaints where companies reported relief. Where the database becomes a source of serious risk to the industry is when the information it contains is used by the CFPB itself. The bureau uses this information to prompt what it calls a “Target Review.”7 So far, the Administrative Adjudications CFPB has pursued against institutions with complaints in the database have led to hundreds of millions of dollars in restitution and fines. Lenders are well-advised to pay close attention to consumer complaints, regardless of the claims’ voracity, to reduce or even avoid these targeted reviews.

Additionally, it has become clear that the CFPB’s actions against institutions that receive consumer complaints are likely to go well beyond the single-transaction grievances. So far in 2013, the CFPB has entered Administrative Adjudication agreements with institutions covering a range of bank processes, including deceptive marketing tactics8, Truth-in-Lending violations9, illegal referral fees10 and misleading customers.11

The industry response to the new regulatory risk

The days of responding to consumer dissatisfaction by loosening underwriting standards and using a poorly or completely uninformed secondary market for a funding source through securitization are over. The pendulum has now swung back to the other end of the spectrum. Underwriting standards and the availability of loans, as well as interest rates pegged to the borrower, property, and credit risks associated with the loan transaction are the new reality. So too is the realization that any given customer’s level of satisfaction with her or his transaction experience isn’t enough to protect the lender from CFPB scrutiny.

Despite the apparent increase in borrower satisfaction with their lender, there needs to be a great deal more focus on those relatively few customers who voice dissatisfaction with their experience. This is exactly what the CFPB is doing with substantial help from its Customer Complaint Database.

Uncertainty about the final rules abounds. Discussions with mortgage lenders and third party settlement service providers suggest reluctance within the mortgage industry to launch extensive process re-engineering or technology initiatives that don’t relate directly to compliance concerns. These industry professionals suggest that lenders’ legal departments continue to assess the likely effects and true impact of the new regulations. In the meantime, a new industry of consultants and advisors are emerging to advise the mortgage industry on risk, reporting, and compliance in the post Dodd-Frank era.

Some of these firms are providing guidance and even mock audits in an effort to prepare institutions to answer to the new regulator as the rules go into effect. These firms aim to assist their clients to sift through the confusion and conjecture about where the CFPB fits into the existing regulatory structure and what the new regulatory environment might look like. No one knows exactly what to expect.

The CFPB is the newest member of the Federal Financial Institutions Examination Council (see chart), an interagency group representing five federal regulators that work together to lay down the standards by which financial institutions will be examined. It’s not yet clear to bank executives whether the CFPB will examine them separately or jointly with other FFIEC regulators.12

Members of the Federal Financial Institutions Examination Council (FFIEC)

- Board of Governors of the Federal Reserve System
- Federal Deposit Insurance Corporation
- National Credit Union Administration
- Office of the Comptroller of the Currency
- Consumer Financial Protection Bureau

Goal: interagency body empowered to prescribe uniform principles, standards, and report forms for the federal examination of financial institutions.

So, what is the best strategy for an institution to embrace in order to put it in good stead with the new regulator as the rules come online? Since much of the “letter of the law,” or the rules, have yet to be written, lenders will be best served by focusing on the “spirit of the law.” This requires us to carefully examine our processes and their ultimate impact on the consumer experience.

Adjusting our process to meet the new federal mandates

We recommend three process changes that institutions should consider at once in order to prepare effectively for more stringent regulator oversight. The first of these concerns actions taken in the planning and budgeting office. The second is an addition to the traditional QA/QC function. The third relates to re-engineering the customer service department.

Establish a separate budget for Customer Relationship Management

CRM in the financial services industry has largely been a case of failure to launch, especially in the mortgage department. As the industry implemented technologies designed to close loans faster, and to reduce costs, borrowers remained customers of the mortgage originator for a shortened period of time. As soon as the deal was closed, the loan was either sold or the servicing rights were transferred (or both). For all practical purposes, the borrower became someone else’s customer, and as the industry discovered, all too often their problem as well.

Until the historic refinance boom, mortgage loan borrowers came back to the closing table only once every 7 years or so. There was no CRM software available that could nurture a lead for that long. In most cases, those leads were never tracked. Instead, lenders turned to business partners, realtors and title agents, who could provide leads that would close much sooner.

By the height of the refinance boom that blossomed at the turn of this century, most of the mortgage loan originators working in the business had forgotten all about leads from business partners or any other source and were instead trying to answer the phone and capture as much of the bountiful business as they could in the time they had available. The industry’s sales staff had become a corps of order takers. For the most part, the majority of banks still capture their business this way. They answer the phone when a borrower needs a home loan.

While this may have been acceptable when there were no lasting, serious side effects of a dissatisfied borrower, it will not suffice in the post Dodd-Frank era. Lenders would do well to begin now by establishing a real CRM budget and making an executive within the institution accountable. This budget should not be part of the bank’s normal marketing budget, but a separate investment in software, systems and management tools specifically for engaging and tracking mortgage customers.

As lenders make these investments, analytical tools will be a critical consideration. Analytics represents a key component of the bank’s CRM process. Applying analytics will allow them to anticipate their borrower’s needs faster and more accurately. It will be the difference between proactive customer management, where the bank systematically deepens customer relationships and benefits from customer loyalty and a greater share of wallet, and reactive customer management, where the bank must chase its customers for new business.

Establish routine monitoring of the CFPB’s complaint database

Traditionally, lenders have focused on monitoring a number of elements internal to the loans they process. They monitor their consumer’s credit through the process, the value of the collateral and the actions of their staff in order to avoid legal non-compliance. Now, we need to add another task to the teams monitoring the health of the institution and its borrowers.

Someone within the institution should be monitoring the CFPB’s complaint database on a regular basis. In the case where a complaint is lodged against the bank, steps should be taken at once to ensure and document that the fault, if there is one, is a unique circumstance and not a pattern of behavior.

The database is public in respect to the institutions that receive complaints, but it masks the information about the consumer filing a complaint, so it may not be possible for the bank to respond directly to the borrower filing the grievance. What it will do is highlight areas of the bank’s operation that may pose future risks of customer satisfaction. Moving forward on initiatives designed to prevent or reduce future customer dissatisfaction will stand in the bank’s favor during an audit.
Additionally, tracking and responding to CFPB complaints in a formalized way establishes a pattern of behavior geared to improve the customer’s overall experience. Integrating customer complaints lodged with the CFPB with the bank’s own customer complaint processing organization offers a holistic picture of the bank’s consumer satisfaction, consumer protection, and complaint feedback system. This is directly in line with the spirit of the CFPB’s consumer protection mandate.

The best banks will respond in this manner, but not all of them will apply human resources to this task. In many cases, banks will automate this monitoring function, embedding controls within their existing process that raise flags early and allow the bank to react in a proactive fashion without incurring the burden of additional full-time employees.

Enabling customer self service

Allowing the customer to interact with the bank’s technology in order to receive informational updates without waiting for bank personnel will be viewed by most as a technology initiative. In fact, there is a major technology component and we’ll deal with that in the next white paper in this series. In truth, the bank’s ability to offer self service to its customers starts with process re-engineering.

Regardless of what any technology vendor claims, banks cannot just present technology that opens up the door to their database of record; not without significant risk to data quality or consumer privacy. The institution must first carefully consider what information can be accessed, by whom and under what conditions. While technology vendors are quick to point out that business rules consulting is provided as part of the sale, these are considerations that the bank will consider internally before any specific technology tools are considered, most likely with the support of external consultants.

But the bank must take care not to consider this question only from the risk perspective. It must also be considered in regard to customer satisfaction. When Interactive Voice Response telephone systems were first made available, IVR was viewed by most industries as a godsend. It was expected that customers would embrace the ability to get all the information they wanted without ever having to wait on a human operator. Today, IVR is referred to as “voice mail hell” by many consumers. Just because a technology allows a consumer self service does not mean it will improve their overall experience. Changes made in this area must achieve customer satisfaction if the bank hopes to comply with CFPB regulations.
Avoiding the risks that come with change

In today’s mortgage business, mistakes are costly. Change is a process that opens up organizations to the possibility of making mistakes, by its very nature. Responding appropriately to change without making mistakes that will cause the firm to fall out of compliance with federal regulators is a key success factor in this environment, which seeks transparency and clear and regular communication, while encouraging innovation in bringing new products and services to market.

No better evidence for this can be found in the new products industry technologists have brought to lenders so far this year. Nearly every new innovation we have seen has been built around the intended or unintended consequences of the new compliance rules. Vendors know that these are the issues that drive the lenders’ “Actions Items” list, so new appraisal ordering technology, loan officer compensation models and LOS audit trail technologies are the newest shiny objects tempting bankers.

Best practices include careful advance planning, adequate project budgeting, thorough employee education, staggered rollout, ongoing training and managing to any new metrics in a visible way. Institutions are urged to view any silver bullet solutions with distrust until their efficacy has been thoroughly established.

Ultimately, successful change management is an occupation unto itself. The important thing to recall is that the changes discussed in this paper and the others in this series are not suggestions that banks may wish to implement for a competitive advantage, but rather represent change that is being forced upon our industry by new regulatory oversight. It is important for institutions to succeed in these efforts.

Conclusion

Both the letter and the spirit of the new Dodd-Frank legislation and the rules the CFPB is writing to define them are centered squarely on consumer protection. As the final wording of major rules are being finalized and amended, the industry’s best chance of staying compliant is to begin thinking in terms of improving the borrower experience. For now, at least, protecting the consumer is being treated as a synonym for pleasing the consumer. Customer satisfaction has become the metric by which the regulator measures fairness and transparency.

Improving customer service in our industry is a regulatory mandate and firms will be working to meet this goal in various ways. No firm will achieve success without changing their processes. Those that do this while opening themselves up the least to compliance errors will be most successful. In the next paper, we’ll talk about how technology can decrease this burden. ■
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