Date of Hearing: April 22, 2013

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Roger Dickinson, Chair
AB 1169 (Daly) – As Amended: April 1, 2013

SUBJECT: Consumer credit reports: escrow agents: real estate.

SUMMARY: Revises the definition of a consumer credit report to include information regarding a proprietary database and rating evaluation. Specifically, this bill:

1) Provides that a "consumer credit report" includes specified information that would be used in establishing a consumer's eligibility for a proprietary database and rating evaluation.

2) Defines "proprietary database and rating evaluation" as a report prepared for a fee and provided to a furnishing of credit for the purpose of evaluating a consumer in the consumer's capacity as an escrow agent, or as a person performing in the business of title insurance, or as a real estate broker, or his or her employees.

3) Specifies that information stored or retained that is used to prepare a proprietary data base and rating evaluation constitutes a "file" under existing law, which is defined as all information on that consumer recorded and retained by a consumer reporting agency, regardless of how the information is stored.

EXISTING LAW

1) Regulates consumer credit reporting agencies via the Consumer Credit Reporting Agencies Act. [Civil Code, Section 1785.1 et seq. All further references are to the Civil Code].

2) Defines consumer credit report as any written, oral, or other communication of any information by a consumer credit reporting agency (CRA) bearing on a consumer's credit worthiness, credit standing, or credit capacity, which is used or is expected to be used, or collected in whole or in part, for the purpose of serving as a factor in establishing the consumer's eligibility for: (1) credit to be used primarily for personal, family, or household purposes, or (2) employment purposes, or (3) hiring of a dwelling unit, as defined in subdivision (c) of Section 1940, or (4) other purposes authorized in Section 1785.11. [Section 1785.3].

3) Requires that every (CRA) shall, upon request and proper identification of any consumer, allow the consumer to visually inspect all files maintained regarding that consumer at the time of the request. [Section 1785.10]

4) Specifies the circumstances under which a CRA shall furnish a consumer credit report. [Section 1785.11]

FISCAL EFFECT: None

COMMENTS:

On April 13, 2012 the Consumer Financial Protection Bureau (CFPB) issued Bulletin 2012-03 (Bulletin) designed to clarify provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) relating to appropriate third party vendor risk management by supervised banks and nonbank entities. In California these non-bank entities would include mortgage lenders consumer finance lenders, credit unions, warehouse lenders, and other entities licensed to originate loans securing real property.

The provision of the Dodd-Frank Act inspiring clarification in section 1002(26) concerning the definition of "service provider" which is defined as "any person that provides a material service to a covered person in connection with the offering or provision of such covered person of a consumer financial product or service." The CFPB Bulletin acknowledges that supervised entities may need to use the services of third party service providers, but that such use, does not absolve the covered entities from their responsibility for complying with Federal consumer protection laws. Furthermore, CFPB urged supervised banks and nonbanks to have effective procedures for managing the risk of service provider relationships. The Bulletin provides several steps that could be taken to minimize risks, including, but not limited to,

a) Conducting thorough due diligence to verify that a service provider understands and can comply with Federal consumer financial law;

b) Request and review the service providers policies, procedures, controls and training materials;

c) Include in contracts with service providers clear compliance expectations;

d) Establish internal controls and ongoing monitoring; and

e) Taking prompt action to address any problems discovered from the monitoring process.

Subsequent to the release of the Bulletin a new type of entity emerged to handle the due diligence review process. Companies describing themselves as risk management providers (RMPs) emerged to provide a layer of protection for supervised entities when they use third parties for settlement services such as escrow agents.

How do these RMPs work? For a fee, a settlement provider, such as an escrow agent, sign up to be included on a database managed by the RMP that generates a low, medium or high risk index score that is made available to lenders and others in the mortgage industry. Settlement service providers are told that they will receive preference by lenders for the use of their services because of the special vetting process. The fee for each settlement service provider is several hundred dollars per year to maintain "accreditation." A failure to maintain "accreditation" could lead a provider to lose business from lenders as these RMPs use information on settlement providers to create lists of vetted agents that is made available to supervised entities. As one company advertises, "These lenders and underwriters utilize the…list as their key source of closing professionals…" The implication here appears to be that either through a bad review or no review at all, a settlement service provider runs the risk of being pushed out of their industry.

The reports done by RMPs are prepared using a combination of public and private data, including credit reports, civil cases, arrest records, bankruptcy, unlawful detainer actions and more.

On December 5th, 2012, the Commissioner of the Department of Corporations issued Commissioner's Bulletin No: 001-12. The Commissioner's Bulletin addressed the rise of concerns relating to RMPs. The Commissioner's Bulletin, among other things, stated the following:

> The Department has learned that some third-party risk management companies are requiring that potential service providers pay a fee in order to be screened by the companies, and to appear on a list of "approved" service providers. In addition, some supervised banks and nonbanks have been advising potential service providers that the service providers must be on the third –party risk management company's "approved list" in order to receive business.
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> Lenders subject to the Department's jurisdiction should be cautious of delegating their responsibility to vet service providers to third parties, and are reminded that they are responsible for such companies' compliance with the law. Escrow agents should be cautious of subscribing to the vetting services of third party companies for a fee, in order to get on a list provided to lenders, as these actions may lead to violations of law. All parties should take necessary precautions prior to sharing personal and confidential information with third parties.

AB 1169 attempts to address the issue of RMPs by ensuring that these entities must comply with California's credit reporting laws. A major issue of concern raised by settlement service providers is that the RMPs use credit information in addition to other sources of information in order to evaluate the settlement service provider for risk. Among the Frequently Asked Questions on the website of Secure Settlements is the following, "Attorneys and settlement agents must pass a list of credentialing criteria that covers everything from E&E coverage, proven industry experience, valid licensing and bonding where required, clean credit, criminal and litigation backgrounds, trust account safety, and other proprietary criteria." Clearly this company is evaluating and reviewing credit information and "other proprietary criteria."

AB 1169 does not propose to limit how these entities collect data, or how they charge for membership to their data base. Instead, AB 1169 ensures that proprietary databases and rating evaluations prepared by RMPs are covered under California's Consumer Credit Reporting Agencies Act, Civil Code section 1785.1 *et seq*. This inclusion would allow those persons subject to review by RMPs various remedies, including notice and opportunity to be heard in response to an adverse report. This would allow the settlement service provider to request the correction of any errors that show up in their report with the RMP. Effectively, a RMP that operates a proprietary database or rating evaluation would be considered a CRA.

As evidenced by the Commissioner's Bulletin, the use of RMPs raises many questions concerning the use of a pre-approved, or pre-screened exclusive list, that requires payment of a fee, for the purpose of choosing a mortgage settlement service provider. Specifically, the Commissioner's Bulletin states:

> *Among other things, one purpose of this bulletin is to remind escrow agents of the prohibition in Financial Code section 17420 against the payment of referral fees for soliciting escrow accounts…The payment of fees to be on a referral list appears to fall within this prohibition, and consequently may be a violation of the Escrow Law*.

The author and sponsors may want to consider, moving forward, additional clarifications in the Escrow law and other places that will provide guidance for licensees on the use of RMPs. At several hundred dollars per year to register with RMPs, mortgage settlement service licensees should clearly know if they are utilizing a service that is not prohibited under existing law. The Commissioner's Bulletin raises the prospect that these arrangements raise significant legal and regulatory issues. While committee staff does conclude that these services and arrangements are in violation of laws or regulations, this grey area raises enough significant concern that additional efforts may be necessary to provide further clarity for the sake of all parties.

REGISTERED SUPPORT / OPPOSITION:

Support

California Escrow Association (CEA) – Sponsor
California Land Title Association
National Notary Association

Opposition

None on file.

Analysis Prepared by: Mark Farouk / B. & F. / (916) 319-3081