E. J. FACE, JR.
COMMISSIONER OF
FINANCIAL INSTITUTIONS

COMMONWEALTH OF VIRGINIA

1300 EAST MAIN STREET
SUITE EIGHT HUNDRED
P.O. BOX 640
RICHMOND, VIRGINIA 23218-0640
(804) 371-9657
FAX (804) 371-9416
TDD (804) 371-9206
www.scc.virginia.gov

STATE CORPORATION COMMISSION
BUREAU OF FINANCIAL INSTITUTIONS

September 28, 2012

TO: The Honorable Senator John C. Watkins
The Honorable Delegate Terry G. Kilgore

As required by Title 6.2, Chapter 17, Section 6.2-1720 E of the Code of Virginia, the Bureau of Financial Institutions of the State Corporation Commission respectfully submits the attached report on the operations of the State Regulatory Registry LLC and the Nationwide Mortgage Licensing System.

For the reasons noted in my letter to you of July 3, 2012[1], the release of the 2011 audited financial statements for the Conference of State Bank Supervisors and its affiliate the State Regulatory Registry were delayed this year, resulting in a subsequent delay in our completion and delivery of this report.

Sincerely,

E. J. Face, Jr.

Cc: Members Senate Commerce and Labor Committee
Members House of Delegates Commerce and Labor Committee
Angela Bowser, State Corporation Commission

[1] The Internal Revenue Service retroactively approved an application by the Conference of State Bank Supervisors involving a change in tax exempt status from a 501(C) 6 to a 501(C) 3 organization; and the State Regulatory Registry became party to a lawsuit seeking to recover a payment received by the Registry as a result of a settlement between a mortgage company and certain state mortgage regulators. The Registry elected to record a contingent liability for an anticipated settlement and related expenses of $1.3 million.

Report on the Operations
of the
State Regulatory Registry LLC

Prepared by the Bureau of Financial Institutions
State Corporation Commission

September 28, 2012

CONTENTS

This Report was prepared pursuant to Title 6.2, Chapter 17, Section 6.2-1720 E of the Code of Virginia, which directs the Bureau of Financial Institutions of the State Corporation Commission to:

1. Annually review the proposed budget, fees, and audited financial statements of the State Regulatory Registry LLC (SRR).

2. Annually, to the extent practicable, report to the House and Senate Committees on Commerce and Labor on the operations of the SRR, including compliance with its established protocols for securing and safeguarding personal information in the SRR.

3. The extent practicable, prepare, publicly announce, and publish a report, by no later than May 1 of each year, that summarizes statistical test results and demographic information to be prepared by the SRR or its test administrator.

Introduction - In accordance with the Code of Virginia, the Bureau of Financial Institutions (Bureau) offers the following report of its review of the State Regulatory Registry LLC (SRR) and the Nationwide Mortgage Licensing System (NMLS).[1]

Background - NMLS was initiated by state mortgage regulators in 2004 in response to the increased volume and variety of residential mortgage loan originators. SRR was formed in 2006 and is a nonprofit corporation based in Washington, D.C. [2] SRR is a wholly owned subsidiary of the Conference of State Bank Supervisors (CSBS)[3], and it owns and operates NMLS. SRR is directed by a Board of Managers consisting of seven state regulators. NMLS was developed by the Financial Industry Regulatory Authority (FINRA)[4].

NMLS is a Web-based application which enables mortgage lenders, mortgage brokers, and mortgage loan originators (MLOs) to apply for, amend, update, and renew state licenses online with participating regulatory agencies using a single set of uniform applications. NMLS also offers the public an on-line public access/inquiry which discloses licensing information and regulatory enforcement history of mortgage firms and MLOs.

NMLS launched with seven states on January 2, 2008, and the Bureau went live on NMLS (with MLOs only) on August 3, 2009. Title V of the *Housing and Economic Recovery Act of 2008*, entitled The Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act), mandated that all

[1] The 2011 SRR Annual Report is dated May 1, 2012 and was publically released May 15, 2012. The 2011 audited financial statements for SRR and CSBS were publically released August 15, 2012 and September 7, 2012, respectively.

[2] SRR has been ruled by the Internal Revenue Service to be a single member domestic limited liability company and is therefore disregarded as a separate entity for tax purposes.

[3] CSBS is the nationwide, non-profit organization for state bank regulators, representing state regulators of the 50 states, the District of Columbia, and U.S. Territories which supervise state-chartered financial institutions. The majority of state banking departments also oversee mortgage providers and other financial service providers.

[4] FINRA is the largest independent regulator for all securities firms conducting business in the United States.

MLOs be either federally registered or state-licensed through NMLS[5]. From August 3, 2009 through June 18, 2012, the Bureau had received 11,309 MLO license applications. As of June 18, 2012, there were 6,827 MLOs approved and licensed in Virginia through NMLS, of which 6,277 licenses were active. Existing Virginia mortgage lender and broker licensees began transitioning onto NMLS on January 3, 2011. As of June 18, 2012, Virginia license transitions totaling 947 had been approved and were active.[6]

All state mortgage regulatory agencies utilized NMLS to manage MLO licenses for the first time in 2011. In addition, under federal mandate the NMLS Federal Registry became fully operational in 2011 and by year-end contained active registrations for 11,081 federal institutions with 375,654 registered MLOs. SAFE Act requirements were also met last year by adding functionality for the submission of mortgage "Call Reports" by state-licensed companies, as well as adding regulatory and enforcement actions of state regulators in the NMLS.[7] As these major SAFE Act mandates were met, SRR was able to focus on improving NMLS functionality for regulator and industry users, as well as begin expanding the NMLS to voluntarily allow states to manage non-mortgage financial service licensees in NMLS.

<u>Notable Activity in 2011 and 2012</u> - Effective July 21, 2011, the federal Dodd-Frank Act transferred the Department of Housing and Urban Development's SAFE Act oversight authority (as a regulator of the NMLS and as the arbiter of state law consistent with the mandates of the SAFE Act) to the Consumer Financial Protection Bureau (CFPB).

[5] Title V of The Housing and Economic Recovery Act of 2008 (H.E.R.A.), "the SAFE Act", became effective July 30, 2009 and mandated that state-licensed MLOs meet certain minimum requirements for licensure. States were required to enact laws that brought MLOs into compliance with the SAFE Act no later than December 31, 2010 or lose state oversight of MLOs to the federal government.

[6] This data is from the NMLS Statistical Report June 18, 2012.

[7] The Mortgage Call Report collects quarterly mortgage activity and either quarterly or annual financial data from all state-licensed companies.

In 2011 there were four major System releases, which occurred in January, April, August and October. State regulators were given the ability to post in NMLS public disciplinary and enforcement actions taken by regulators against mortgage companies and individual professionals. To further the effort to provide state regulators a complete application at the time of submission, NMLS was enhanced to allow regulators to prevent submission of a license application in NMLS until the candidate had successfully completed the SAFE Testing and Education requirements. System functionality was also added to allow or require individuals associated with a company or branch to submit a request to generate a credit report for distribution to the appropriate state regulatory agencies. Lastly, mortgage "Call Report" functionality was added to NMLS to fulfill SAFE Act requirements as well as build on state regulator efforts to create uniform financial and activity reporting requirements across state lines.

In 2012, there are no new statutory requirements, licensees, or registrants mandated for inclusion in NMLS. SRR's long-range plan forecasts a significant reserve to fund the ongoing development and maintenance of NMLS as mandated by the SAFE Act, as well as to position SRR to ensure continued operations in the event of variations in revenue given the cyclical nature of the mortgage industry. SRR will expand NMLS to allow state regulators to license non-depository financial services providers using NMLS. While the cash flow for development of this new service will be required in 2012, participation by the states is voluntary. Five states have started managing additional license authorities on NMLS, and an additional eight and twelve state agencies are scheduled to transition non-depositories onto the NMLS later in 2012 and 2013, respectively. Virginia has not committed to transition non-depository institutions onto NMLS.

Additional functionality to be added in 2012 includes data quality checks for Mortgage Call Report submissions, public availability of state regulatory actions against licensed and registered entities through NMLS Consumer Access, and enhanced credit report functionality.

Budget, Fees, Audited Financial Statements - As of December 31, 2011, SRR reported audited total assets of $48.5 million (compared to $29.4 million at the end of 2010), owner's equity of $40.0 million[8] (compared to $19.3 million at the end of 2010), and net income of $20.7 million (compared to $16.4 million for 2010). The certified public accounting firm of Tate & Tyron, Washington, D.C. issued a "Clean" or Unqualified Opinion of CSBS and its affiliates, including SRR. The Bureau's review of the financial statements did not reveal any significant concerns. The financial statements appear to be reasonable, including the amounts, estimates, and assumptions used.

SRR's largest revenue sources included NMLS processing fees and NMLS professional services (test administration fees, criminal background and fingerprinting fees, credit report fees, and education course fees). These sources contributed $57.7 million to the 2011 revenue base. Major operating expenses included NMLS professional services, system operations costs, and operation costs involving the NMLS Call Center. In 2011, SRR spent significant resources to implement the NMLS Federal Registry for bank-employed MLOs, to improve NMLS functionality for industry and state regulators, and to increase NMLS functionality to meet SAFE Act requirements.

Liabilities to net worth were 21.2% at year-end 2011 and continue to improve, compared to 52.5% at year-end 2010 and 453.9% at year-end 2009. SRR was considered liquid for 2011 according to the audited Statement of Cash Flow, with an increase in net assets for the year of $20.7 million.

With respect to fees, NMLS charges three basic fees to fund development, functionality, and operations. Section 1510 of the SAFE Act authorizes NMLS to "charge reasonable fees to cover the costs of maintaining and providing access to information from the Nationwide Mortgage Licensing System and Registry."

[8] $18.5 million of which has been designated as a reserve for the continued maintenance and upgrading of NMLS.

The initial license set-up fees are $100 per company, $20 per branch, and $30 per MLO each time NMLS is used to transition an existing entity to NMLS or to apply for a new license in NMLS. The $100/$20/$30 processing fees are also charged annually at the time of renewal when a company, branch, or MLO renews a license in a participating state. A $30 MLO transfer fee is charged each time NMLS processes a company's request to have a MLO's license affiliated with that company (i.e. each time a MLO changes employment to another company). These fees are unchanged since NMLS launched in January 2008.

NMLS test fees are charged to an individual who enrolls to take the MLO national and state tests or charged to a company which may enroll its MLOs for the national and state tests. The national test fee is $92, and the state test fee is $69 - both unchanged since 2010.

NMLS education fees are charged for the approval and renewal of education courses and course providers. The course provider application fee is $400, and the course provider renewal application fee is $400 (each valid for two years). A course application fee is $300 plus $20 per each course hour (valid for one year), and the course renewal application fee is $200 plus $20 per each course hour (valid for one year). All of the above course fees are paid by the course provider and are unchanged since 2010.

NMLS criminal background check and fingerprint fee is $39 for a live scan (electronic) and $49 for a paper card scan, also unchanged from 2010. NMLS credit report fee is $15. For more detailed information on all fees, refer to Pages 32-33 of the attached SRR 2011 Annual Report.

Securing and Safeguarding Information - Established protocols for securing and safeguarding information in NMLS can be found on the NMLS Resource Center Website[9]. NMLS complies with the

[9] http://mortgage.nationwidelicensingsystem.org/about/policies/Pages/SystemPrivacyPolicy.aspx

Federal Information Security Management Act (FISMA) standards and guidelines set by the National Institute of Standards and Technology (NIST). NMLS also meets the moderate baseline security controls contained in the NIST Special Publication 800-53, *Recommended Security Controls for Federal Information Systems*, and NMLS has been fully accredited by all six federal agencies.

SRR reports it did not experience any material issues related to security, privacy, or information breach in 2011. In 2008, 2009 and 2010, SRR also reported no material issues related to security, privacy, or information breach. As the developer of NMLS, FINRA biannually conducts an internal audit on parts of NMLS. FINRA's policy does not provide for the release of its internal audit reports.

Test Results - SRR periodically will release and post on the NMLS Website certain statistics regarding the development, delivery, and performance of the MLO national and state tests. The SAFE Act requires MLOs to pass written qualified national and state tests. The following data, released by NMLS, represents tests administered in 2010 and 2011. The chart below compares the total number of individuals who have ever taken the test component to the number of individuals who have passed the test component, regardless of whether they passed it on the first attempt or a subsequent attempt.

2010 - 2011 Pass Rates by Individual

	National Test	Aggregate State Tests
Total Candidates	147,586	246,657
Candidates Passed	122,945	230,757
Pass Rate	83%	94%

From July 2009 to June 15, 2012, the Virginia test was taken 11,010 times with an overall pass rate of 87%. NMLS reports that 84% of candidates who took the Virginia test also passed the national test. NMLS does not currently track or collect demographic test information.

Responding to industry regulatory concerns associated with individual state test components and reviewing the magnitude of resources associated with state test maintenance, the SRR Board of Managers requested a feasibility study on the development of a uniform state test component. SRR is in the process of developing a uniform state test component with possible deployment in early 2013.

As test development wound down in 2011, the focus shifted to maintenance. Through test maintenance and other means, SRR will identify and remove questions that are no longer appropriate, resulting in a revised and republished test. In instances where candidates' results have been negatively impacted, SRR notifies candidates and corrects their NMLS testing records.

Other – It should be noted for the record that FINRA is utilized to provide significant development and support services for NMLS. As such, a disruption in the capabilities provided by FINRA could have a negative impact on CSBS/SRR. In addition, SRR reports a contingent liability involving Taylor Bean & Whitaker Plan Trust (TBW), which filed a complaint against NMLS seeking to recover a payment received by SRR and transferred to CSBS in the amount of $4.5 million as a result of a settlement between Taylor Bean & Whitaker Mortgage Company and certain state mortgage regulators. Neither SRR nor CSBS was a signatory to the settlement agreement. While other defendants have begun a mediation process, SRR has filed a motion for summary judgment with the Bankruptcy Court. At this time, SRR management considers it likely will be required to repay some portion of the payment; and for financial purposes, SRR has chosen to record a contingent liability and related expense of $1.3 million. This liability is reflected in the organization's 2011 audited financial statements. Management believes there is a high probability of settling the claim during 2012.

Summary – NMLS launched on January 2, 2008, and the Bureau went live on NMLS August 3, 2009. As of December 31, 2011, SRR reported audited total assets of $48.5 million and net income of

$20.7 million. The certified public accounting firm of Tate & Tyron issued a “Clean” or Unqualified Opinion of SRR. The Bureau’s review of the financial statements did not reveal any significant concerns.

SRR reports it did not experience any material issues related to NMLS security, privacy, or information breach in 2011. Testing data for 2010 and 2011 combined show that 147,586 national test components were administered with a total pass rate of 83% and 246,657 aggregate state test components were administered with a total pass rate of 94% (the Virginia state test was administered 11,010 times from 2009 to 2012 with a total pass rate of 87%). NMLS processing fees remain unchanged for the fourth straight year of System operations. SRR/NMLS does not currently track or collect demographic test information.

OTHER ITEMS OF INTEREST[10]

- NMLS is used by over 170,000 active state-licensed non-depository mortgage companies, over 10,500 banks and credit unions, and more than 475,000 individual MLOs to manage license and registration requirements under state and federal laws.

- NMLS managed 152,903 unique entities (companies, branches, and MLOs) which held 288,170 state licenses from 58 participating state agencies.

- In 2011, NMLS collected and disbursed approximately $71 million in state license and registration fees.

- NMLS administered more than 130,000 tests (national and state test components) in 2011, bringing the total administered since July 2009 to more than 525,000 tests.

- In 2011, since the passage of the SAFE Act, all state agencies required state-licensed MLOs to complete annual continuing education.

- Since July 2009, state-licensed MLOs have completed over 3,500,000 hours of pre-licensure and continuing education.

- By the end of 2011, 170 course providers and 1,200 pre-licensure and continuing education courses were approved by NMLS; and approximately 1.5 million hours of education were delivered through NMLS-approved courses.

- NMLS collected and disbursed approximately $71 million in state license and registration fees.

[10] Data is taken from the 2011 Annual Report of the SRR.

- NMLS Call Center answered more than 936,000 inquiries from users.

- NMLS Resource Center was viewed by over 2 million unique visitors.

- By year-end 2011, *NMLS Consumer Access* received over 1 million visitors who viewed over 56 million pages of information on licensed and registered companies and individuals.

- Almost 500,000 individual MLOs (state and federal), along with their license or registrations status, NMLS Unique Identifier, and employment history were made available to the general public on *NMLS Consumer Access*.

- SRR now offers a subscription service that provides a subset of *NMLS Consumer Access* data in a business-to-business format. This service gives compliance firms, government agencies, lenders, investors, and other eligible parties the ability to check a license or registration status in an automated manner.

- Eleven companies are using NMLS business-to-business access subscriptions to access NMLS Consumer Access data.

- SRR conducted more than 76 live industry and regulator user training sessions, instructing more than 11,600 professionals.