Enhancing the Escrow Payment Ecosystem with Integrated Platforms

Abstract

Business transactions in real estate are fraught with challenges. Disputes are arduous and time-consuming, making it imperative for both parties—the borrower and the servicer—to avoid them at all costs. Escrow-based payment mechanisms have been used in real estate to help redefine security and enable safe and seamless transactions.

Servicers bear the responsibility of compliance and provision of superior escrow services amid several challenges. These include exhaustive regulatory guidelines, varying borrower circumstances, geographical spread of counties and delays in processing, all of which impact customer satisfaction. A simple window between borrowers and other parties including investors, tax collection agencies, hazard and MI agencies, and home owners' associations (HOAs) can empower servicers to manage expectations effectively.

This paper outlines the compliance requirements for escrow management and examines the challenges faced in implementing them. The paper further proposes a technology-led integrated platform that will ensure superior compliance management and help enhance customer satisfaction.

The Implications of Non-compliance with Escrow Guidelines

The Real Estate Settlement Procedures Act (RESPA) and its implementing regulation, Regulation X, impose requirements for maintaining escrow accounts. Under the regulation, auditors will attempt to ascertain acts or practices that increase the risk of violations. Consequences of non-compliance could include:

Tax defaulted property sales

Failure to pay county taxes can result in the lender losing the property to a scheduled foreclosure sale. These sales are generally held to recover delinquent taxes on the property. To fulfill outstanding tax dues against the borrower's property, the agency affirms the claim through a tax lien. The prescribed process followed by the agency to do this is called a notice of federal tax lien (NFTL).

Figure 1 shows the annual NFTL filings for the past five fiscal years. NFTL filings increased by 33% from FY 2018 to FY 2019 (410,220 to 543,604).[1]

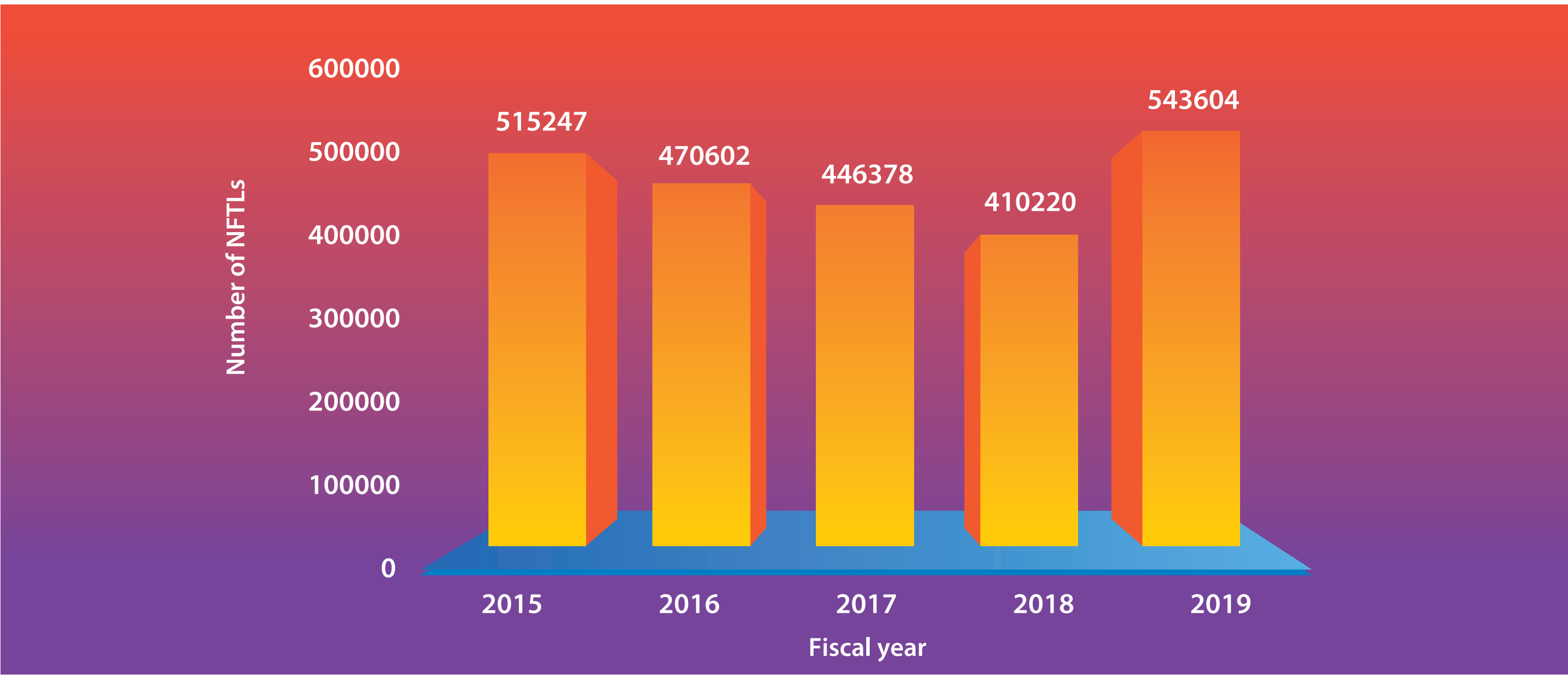

Figure 1: Number of NFTLs filed for Fiscal Years 2015 through 2019

Occasionally, borrowers too may be subjected to penalties by tax authorities due to non-timely payments of taxes by servicers.

[1] IRS Data Book for FYs 2015 through 2019, Accessed November 2020, https://www.treasury.gov/tigta/auditreports/2020reports/202030068fr.pdf

Incorrect escrow estimations

Servicers need to accurately project the annual escrow amount that is to be paid to various parties and collect it from the borrower. Omitted escrow components, overblown estimations or incorrect cushions could result in a breach of regulatory guidelines, customer dissatisfaction and complaints to regulatory agencies.

Additional cost components

Escrow is a cost center for any servicer. Incorrect assessments and rectifications resulting from it could add unrecoverable supplemental costs to the company.

Less recovery in cases of property damage

Non-payment of insurance can jeopardize the insurance cover. In the event of a disaster, the insurance acting as a loss mitigation for the mortgage will be ineffective and the lender may not be reimbursed by the insurance company.

Cancellation of insurance policies

Occasionally, when the servicer does not pay the premium, the borrower may have to endure the costs of procuring a replacement homeowner's insurance policy. Untimely disbursements of premium may also lead to cancellation of insurance policies.

Loss of servicer contracts and reputation

Existing contracts with servicers may be terminated leading to loss of servicer goodwill and reputation.

Challenges in Implementing Escrow

By adding an extra layer of transparency in the ecosystem, escrow-based transactions help build trust. As the ingenuity of the technology continues to evolve, platforms will become more easily accessible and the service will become further democratized as a safe and secure one. Despite these obvious benefits however, escrow-based payment mechanisms are not without their difficulties. The most common challenges faced while implementing escrow include:

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Managing multiple local guidelines and scarcity of process experts

The regulations at the state level continue to change and evolve. Diverse local codes, laws, and municipal guidelines lead to dependence on hard-to-find process experts who are better equipped to understand local requirements.

As servicers struggle to efficiently manage their loans and escrow payments, superior customer service could provide the competitive advantage required to catalyze growth.

Collating data and documents manually

Servicers need to manually access county portals as well as hazard and insurance portals to ensure they are referencing the most current figures and updating employees' systems accordingly. Validating each account of the portfolio is a long-drawn, cumbersome and labor intensive process.

Certain documents such as insurance certificates need to be gathered from corresponding insurance portals. Manual activities are not only exhaustive but could also result in incorrect grouping of an escrowed account as a non-escrowed loan.

Handling exceptions arising from system limitations

Existing systems could have limited functionalities, which could in turn lead to a large number of exceptions, each of which will need to be individually managed. As a result, the number of manual overrides and interventions required also increase.

Processing multiple payment refunds

Accounts need to be manually reconciled and reviewed to identify surplus and overages. Inaccurate reviews lead to incorrect refunds, resulting in increased instances of borrower grievances.

Driving Adherence through Next-gen Technologies

An integrated platform connecting servicers, tax agencies, insurance agencies and home owners' associations can help servicers and other stakeholders leverage digital disruption and drive customer delight.

An integrated escrow platform can also provide a host of other benefits:

Support better integration between multiple sources

Escrow is a cost center that servicers are required to set up in order to comply with Regulations X and Z. Servicers are also required to sub contract vendors who can gather required details from multiple sources.

By investing in a country or enterprise level escrow platform that connects all affiliated tax offices, insurance agencies and HOAs, and/or federal agencies, servicers can simplify the data collection process. Details can be captured on a real-time basis, ensuring accurate estimations and avoiding lapses and corresponding penalties.

The centralized repository would also ease the process for escrow setup, file maintenance, batch runs, payments, research, returns and refunds. It can be used to conduct periodic reviews and ensure timely disbursements. By providing access to the latest regulations and demonstrated best practices, the platform enables superior knowledge sharing and training, and can therefore also be extended as an online portal for comprehensive e-learning.

Increase accuracy of annual escrow estimations with analytics

Escrow analysis is a mandatory annual requirement, with the frequency determined by state defined timelines. Generally, the volumes tend to increase nearer to the timeline. Moreover, these transactions require the tax, insurance and hazard lines to be manually validated, increasing the likelihood of errors. Further analysis through an aggregate or composite computing method would help project accurate estimations.

As shown in Figure 2, an integrated platform with real-time data on escrow lines interfaced with servicer systems can instantly conduct escrow analysis on applicable portfolios and simplify the treatment of cushions, surpluses, shortages, and deficiencies.

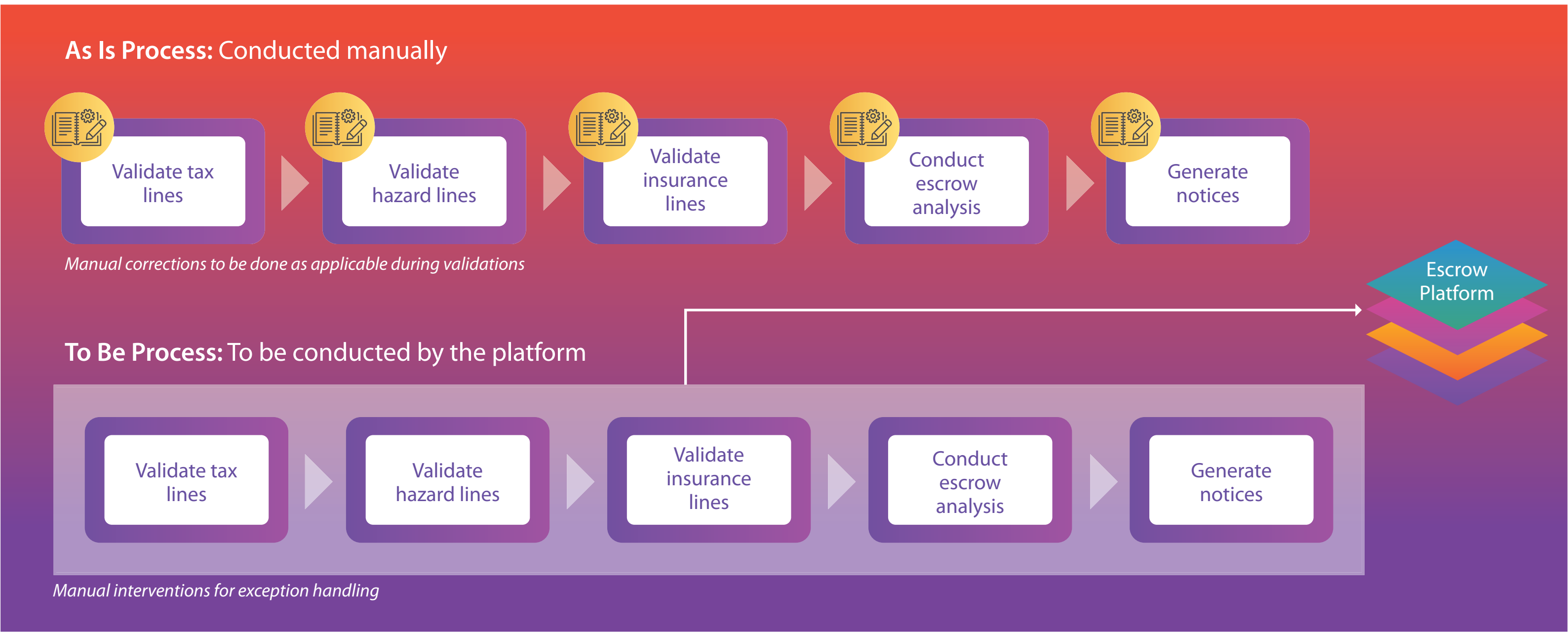

Figure 2: As-is and To-be Escrow Analysis

Generate regulatory notices intuitively

Digitizing various processes and workflows would increase the depth of metadata available throughout the process. This, in turn, can be leveraged to generate regulatory notices for disclosures of escrow transfers, escrow account cancellations, refund of surplus, escrow statements, escrow account adjustments, insurance termination, and so on.

Trigger preemptive compliance alerts

Timelines defined by regulatory guidelines, when integrated into the platform, can act as a compliance management system that preemptively averts potential slipups. Triggers can be set up for various parameters such as setting up of the escrow account, crediting the account for tax and insurance funds that are received as part of the borrower's monthly mortgage payment, making timely payments on the borrower's obligations, analyzing the account balance in relation to anticipated payments and reporting the account balance to the borrower annually. By providing alerts and reminders, the system can help reduce instances of missed timelines and associated penalties.

Document custodianship of all interested parties

As the document custodian, servicers must acquire, track and safekeep escrow documents for interested parties. Missing documents pose a grave operational risk. By serving as a document repository that safekeeps critical and non-critical escrow related documents related to individual loan files, an integrated platform eases the process of making revisions and deletions, improves overall access to requisite documents and enhances the record keeping process.

Staying Profitable in the Age of Online Payments

To stay profitable in this age of continuous digital disruption, an escrow compliance management platform is no longer a desirable addition to your business but an imperative. Servicers today must not only ensure that escrow accounts are managed within permissible limitations and investor procedures but facilitate integration between interested parties, ensure compliance with regulatory guidelines and offer escrow maintenance through advanced analytics.

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The decision to move to an integrated platform is no longer one that can be mulled upon. Instead, it is one that requires immediate implementation and action.

About The Author

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Rajesh Ramu Chhatriya is a domain expert with TCS' Banking, Financial Services, and Insurance business unit. He has over 13 years of experience in project delivery and has extensive expertise in developing training plans, policies, and procedures; reengineering process flows; implementing process enhancements and enabling transition management. Chhatriya holds a Post Graduate Diploma in Business Management in Marketing from the N. L. Dalmia Institute of Management Studies & Research, Mumbai University, India.

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