

What is portfolio cleansing?

A look at process, risk and how to be proactive

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The [mortgage servicing industry landscape](#) is shifting. For over a decade, the industry has experienced growth from two primary sources.

The first, and more traditional source, is organic growth through new loan originations.

The second method, which has become increasingly more common, is growth through either loan portfolios or company acquisitions. This shift is happening because of the increased willingness of private investors to invest in servicing and the government sponsored enterprises' focus on reducing their footprint.

This can cause problems for servicers in instances where loans are acquired with unknown, pre-existing property tax delinquencies missed in the due diligence phase.

What risks are incurred through the acquisition of a loan portfolio?

Under the second method mentioned above (growth through acquisitions), loan portfolios change hands, where one party acquires a set of loans while the other transfers ownership. With this exchange, there is an element of risk transfer for the new servicer after acquiring the new loan portfolio. Some of these risks include:

- Minimum due diligence on a new loan population incurred from the previous servicer
- "Pre-existing" conditions (e.g. tax sale critical items) within the loan portfolio that can lead to unrecoverable or lost properties, or large penalty/interest payments
- Borrower dissatisfaction and erosion of confidence
- Limited time to collect or recover loss from the prior servicer

What is portfolio cleansing?

The challenge for the portfolio buyer is to identify the "high-risk" loans at the time of the ownership change so they can mitigate these operating risks. To resolve this industry challenge, a new approach has been identified to address these concerns— portfolio cleansing. Under the new approach, tools are provided to support servicers' needs. This includes:

- Pinpointing high-risk accounts based on loan history and attributes
- Identifying and resolving ownership and delinquency issues at the time of the portfolio onboarding
- Remedying existing delinquent property taxes, thereby improving the borrower experience
- Reducing the risk of unrecoverable properties and decreasing penalty and interest accrued
- Securing quicker delinquency payments to recover loss from the prior servicer

What does the portfolio cleansing process look like?

Upon the transfer of loans, a comprehensive property tax dataset is used to identify if there were any known delinquencies on the accounts at the last time the tax records were updated. At that point, potential delinquencies can have taxes procured and paid so the accounts are proactively remedied. This approach helps portfolio buyers get paid sooner rather than waiting for the borrower inquiry to respond or until the next tax cycle.

To illustrate the power of the approach, CoreLogic tracked the process of a national prime lender use case for the portfolio cleansing methodology.

Step 1 – The full population from the portfolio transfer was run through CoreLogic’s databases to check the property tax status.

Step 2 – For any ‘Delinquent’ or ‘Unknown’ records, a redemption statement was ordered on behalf of the client so that payoff information could be obtained for any outstanding taxes. (Any ‘Paid’ status items were removed from the process at this point.)

Step 3 – On any procurement information showing a past due property tax amount, research tasks were initiated on behalf of the client to remedy the delinquencies. Since CoreLogic’s redemption statements provide a ‘criticality’ around the delinquency, high-risk loans with multiple year delinquencies and those in jeopardy of tax sale could be triaged first in the process.

Step 4 – CoreLogic remitted payment, notated accounts, and closed the tasks associated with portfolio cleansing. This proactive action enabled the lender to address these issues shortly after the loans were acquired.

By utilizing portfolio cleansing, this national prime lender was able to perform a higher level of due diligence around an acquired population of loans. As such, there were outstanding delinquencies that were proactively addressed.

In addition, penalty/interest charges were minimized as this process caught these delinquencies shortly after the loans were boarded. But perhaps the greatest source of loss mitigation was associated with uncovering ‘critically delinquent’ acquired loans and bringing the property taxes current. This reduced the lender’s exposure to ‘loss of collateral’ on these properties.

When it comes to loan servicing, a proactive ounce of prevention can be worth a pound of cure.

To learn more about portfolio cleansing, visit [CoreLogic.com](https://www.corelogic.com)