



Legal Counsel to the
Financial Services Industry

New and Evolving Mortgage Servicing Requirements in Light of Recent OCC and CFPB Activity

Jeffrey P. Naimon
Jonice Gray Tucker
Joseph J. Reilly

Disclaimer

The information contained herein is for informational purposes only; do not constitute legal advice; and, do not necessarily reflect the opinions of BuckleySandler LLP or any of its attorneys or clients. This presentation is not intended to create, and does not create, an attorney-client relationship between you and BuckleySandler LLP, or any of the presenters, and you should not act or rely on any information in this presentation without consulting legal counsel. The information contained in this presentation may or may not reflect the most current legal developments; accordingly, information in this presentation is not promised or guaranteed to be correct or complete, and should not be considered an indication of future results. BuckleySandler LLP expressly disclaims all liability in respect to actions taken or not taken based on any or all the contents of this presentation.

Regulatory and Enforcement Environment

- Foreclosure documentation crisis has triggered nationwide, multi-jurisdictional scrutiny of entire default servicing process
- Federal Prudential Banking Regulators
 - Horizontal Review leading to Consent Orders
 - OCC's June 30, 2011 Guidance
- CFPB Servicing Exams
- State Attorneys General

Regulatory and Enforcement Environment

- State regulators coercing servicers to enter into “voluntary” agreements consistent with banking agency consent orders
- CFPB has issued its exam guidelines and has started sending information requests to bank servicers it examines
- Enforcement actions are driving national servicing standards and compliance expectations

Presentation Overview

- We will focus on
 - Brief update on Multi-State AG settlement negotiations and other AG activity
 - OCC Bulletin 2011-29 and other bank regulator guidance on servicing
 - The new CFPB Servicing Supervision and Examination Manual published in October 2011
 - Compliance with the “rules” and expectations that stem from new examination procedures, recent regulatory guidance, and enforcement actions related to mortgage servicing

Multi-State Attorney General Group

- Investigation by Multi-State Attorney General Group is ongoing and focused on five largest servicers
 - Working with the DOJ, Dept. of Treasury, and CFPB
- Term sheet has been subject of months of negotiations
 - Clear attempt to set more detailed national servicing standards through enforcement action
- Original proposal very aggressive, but more modest reforms in counterproposals
- Addresses wide range of matters, including
 - Foreclosure information and documentation
 - Governance of loss mitigation functions
 - Permissible fees
 - Payment posting
 - Lender-placed insurance

Multi-State Attorney General Group

- Settlement has been “imminent” for months
 - General agreement on servicing “standards”
 - Latest sticking points include extent of liability release to be provided to the financial institutions, focus on MBS and MERS related claims
 - Exacerbated by FHFA lawsuits against 17 institutions
 - Influential AGs dropping out of group (CA, MA, NY, NV) and moving forward with separate investigations
 - Refinancing assistance back on the table for underwater borrowers
- NY & DE working together to investigate possible “criminal acts” by financial institutions tied to foreclosure crisis

Multi-State Attorney General Group

- On November 1, 25 Members of Congress sent letter to Attorney General Holder urging him to ensure that:
“[A]ny settlement reached between the states and the mortgage servicers reflects the gravity of the harm done to American homeowners”
- Multi-state settlement still possible, but difficult without CA & NY
 - Resolution will set detailed *de facto* servicing standards via enforcement action
 - Mandated changes likely to substantially increase time and cost associated with default servicing

Federal Banking Regulators – Horizontal Review Findings

- All foreclosed borrowers seriously delinquent notwithstanding process errors
- Generally adequate documentation of loan ownership
- Notwithstanding, weaknesses found in critical areas, described in the *Interagency Review* of April 2011
 - Foreclosure governance policies and procedures lacking; inadequate staffing to handle volume
 - Signing and notarization of affidavits deficient
 - Undercharging and overcharging of fees
 - Inadequate third-party vendor management
 - Quality control and audit deficiencies

Federal Banking Regulators – Consent Orders

- The Orders “require major reforms in mortgage servicing operations” – *Acting Comptroller Walsh*
- Orders require servicers to undertake comprehensive risk assessments and make prospective changes
 - Single-point of contact/Dual-tracking
 - MIS improvements
 - Expanded compliance responsibilities
 - Greater third-party oversight
- Look-back loan file review also required
 - Aimed at remunerating borrowers who suffered “financial injury” as defined by the regulators
- Complaint procedure commencing for borrowers with loans serviced by entities subject to Consent Decrees.
 - Generally covers foreclosures 1/09 through 12/10
 - Millions of loans in potential pool

OCC 2011-29

- Consent Orders set baseline for national servicing standards
- Major themes carried forward in OCC 2011-29 guidance to all OCC-regulated servicers issued June 2011
 - Aimed at ensuring that all mortgage servicers under OCC supervision “adhere to appropriate foreclosure management standards”
- Requires banks and thrifts under OCC supervision to conduct self-assessments in at least six areas and make changes going forward
- Banks also required to conduct foreclosure “file reviews”

Default Servicing Standards – Significant Themes

- Media, regulators, and consumer advocates remain focused on issues related to default servicing – keeping politicians focused on these issues
- Compliance with major themes embodied in Consent Orders advisable even if not under Consent Order, subject to OCC Guidance, or otherwise the subject of enforcement action

Default Servicing Standards – Significant Themes

- Six Major Compliance Themes in Consent Orders and *Interagency Review* Become “Foreclosure Management Standards” in OCC 2011-29:
 1. Foreclosure process governance
 2. Dual track processing
 3. Affidavit and notarization practices
 4. Documentation practices
 5. Legal compliance
 6. Third-party vendor management

Standard #1 – Foreclosure Process Governance

- **Concept** - Foreclosure policies must be well documented and contain adequate controls to manage operational compliance, legal, and reputation risk associated with foreclosure activities. Employee compliance with written policies must be monitored
- **How to Comply** - Review and revise/rewrite written policies and procedures for all key functions and install mechanisms to ensure the appropriate management, reporting and board oversight of compliance at all levels

Standard #2 – Dual Track Processing

- **Concept** - Foreclosures cannot proceed for borrowers who have been approved for and have not defaulted on loss mitigation plans
- **How to Comply** - Discontinuation of practice
 - Requires significant coordination among internal groups and third-party service providers
 - Quality control and data integrity checks paramount

Standard #3 – Affidavit and Notarization Process

- **Concept** - Affidavit attestations must be based on personal knowledge of the affiant and supported by documentation. Notaries and signatories must comply with state notary requirements.
- **How to Comply** - Review and revise/rewrite written procedures on standards for personal knowledge, use of business records and adherence to notarization formalities
 - Which states' laws apply?

Standard #4 – Documentation Practices

- **Concept** - Documents supporting foreclosure proceedings must be maintained, properly endorsed/assigned, and their accuracy must be verified
- **How to Comply** - Implement processes sufficient to ensure
 - Ability to locate and access all pertinent documents (document retention and transmission checklists recommended for outside counsel)
 - Create audit trail of all facts asserted in affidavit
 - Understand exactly when non-bank employees can sign for the Bank, and the documentation of their authority to do so – powers of attorney or appointment as non-employee officers
 - Timely and appropriate documentation of legal standing to foreclose

Standard #5 – Legal Compliance

- **Concept** - Banks must comply with all laws and regulations relating to foreclosure, with special focus on SCRA and bankruptcy protections
- **How to Comply**
 - Acquire detailed understanding of state foreclosure laws and regulations
 - Actively monitor regulatory changes
 - Timely implement changes and audit processes to ensure compliance
 - Ensure that internal departments are communicating effectively with one another and outside counsel
 - Active monitoring of data sources for bankruptcy filings or changes in military status

Standard #6 – Third Party Vendor Management

- **Concept** - Management must ensure that third-party vendors are qualified to undertake the roles for which they are hired and must oversee and monitor vendors closely, including outside foreclosure counsel (See OCC Bulletin 2001-47 or OTS Bulletin TB-82a)
- **How to Comply**
 - Ensure that vendors comply with bank procedures, legal standards, and *emerging* industry best practices
 - Review current relationships and retention agreements with all third party vendors – especially outside law firms assisting with default servicing
 - Implement a careful due diligence process when selecting and renewing vendors
 - Provide ongoing oversight, including periodic reviews

File Assessment – Foreclosure File Review

- Key component of the Consent Orders has been a review of files in some state of foreclosure in 2009 and 2010
- Other servicers undertaking such reviews pursuant to OCC 2011-29 or otherwise outside of Consent Order context
 - Regulatory expectations for non-Consent Order reviews are uncertain
- Key concepts for file reviews
 - Data integrity
 - Appropriate sampling – special considerations for high risk populations
 - State-specific checklists
 - Appropriateness of default fees

File Assessment – Foreclosure File Review

- File collection process
- Require detailed checklists of all state laws and regulations for each state being reviewed
- Also need separate checklists for
 - Default servicing fees
 - SCRA
 - Bankruptcy
 - Loss mitigation activity
- Checklists should be in format that minimizes reviewer discretion

MICHIGAN
FORECLOSURE REVIEW CHECKLIST¹

Yes	No	Description of Item or Requirement	Citation
NON-JUDICIAL FORECLOSURE (known as "Foreclosure by Advertisement")²			
<input type="checkbox"/>	<input type="checkbox"/>	Does the security instrument (usually called a "mortgage") contain a power of sale clause?	Mich. Comp. Laws ("MCL") § 600.3201
<input type="checkbox"/>	<input type="checkbox"/>	Is there evidence in the file that all of the following conditions have been met: (1) a default in the condition of the mortgage occurred, by which the power of sale became operative; (2) an action or proceeding was not instituted to recover the debt secured by the mortgage, or if an action or proceeding has been instituted, the action or proceeding was discontinued, or an execution or judgment rendered in an action or proceeding was returned unsatisfied, in whole or in part; (3) the mortgage containing the power of sale was properly recorded; AND (4) the party foreclosing the mortgage is either the owner of the indebtedness or of an interest in the indebtedness secured by the mortgage or the servicing agent of the mortgage?	MCL § 600.3204(1)(a)

¹ A servicer or lender cannot foreclose on a mortgage judicially or non-judicially if that mortgage is held by the Michigan state housing development authority. MCL §§ 600.3101 and 600.3201.

² Michigan has both a judicial and non-judicial foreclosure process. Therefore, the first question asked for any file reviewed with this checklist should be whether it proceeded within the non-judicial or judicial process.

Yes	No	Description of Item or Requirement	Citation
<input type="checkbox"/>	<input type="checkbox"/> N/A	<p>Initial Notice – Is there evidence in the file that:</p> <p>(1) the Notice of Sale was first published ON or AFTER July 5, 2009 and BEFORE January 5, 2012;³ AND</p> <p>(2) the property is claimed as a principal residence exempt from tax under MCL § 211.7cc ("Homestead Property")?⁴</p> <p>(If neither of these two requirements is met, circle N/A and skip this section.)</p> <p>(NOTE: MCL §§ 600.3204(4) and (5) and MCL §§ 600.3205a through MCL § 600.3205d relate to requirements regarding loan modification rights. They apply only to Homestead Properties. The foreclosing party is required to notify the borrowers⁵ of the right to meet to discuss loan modifications, to apply a statutory analysis, and to make loan modifications with borrowers if certain conditions, as set forth in the questions in this section, are satisfied. A loan modification that has been, or could be, made under these statutory provisions will be referred to in this checklist as a "Loan Modification.")</p>	MCL §§ 600.3204(4)(a) and (5) and 600.3205a(1)
<input type="checkbox"/>	<input type="checkbox"/> N/A	<p>Is there NO evidence in the file that the borrower previously entered into a Loan Modification?</p> <p>(If there is evidence in the file that the borrower previously entered into a Loan Modification, circle N/A. If there is NO evidence that the borrower previously entered into a Loan Modification, select YES and skip the next question.)</p>	MCL § 600.3205a(6)
<input type="checkbox"/>	<input type="checkbox"/> N/A	<p>Is there evidence in the file that the borrower complied with the terms of the previous Loan Modification for at least one year after the date of the previous Loan Modification?</p> <p>(If there is evidence in the file that the borrower did NOT comply with the terms of the previous Loan Modification for at least one year after the date of the previous Loan Modification, circle N/A and skip the rest of this section and proceed to the Notice of Sale section.)</p>	MCL § 600.3205a(6)

³ Michigan's foreclosure mediation program, MCL §§ 600.3205a-d, is set to expire on January 5, 2012. MCL § 600.3205e. Pending legislation proposes the extension of this expiration date (see Appendix).

⁴ Per local counsel, MCL § 211.7cc governs Michigan's homestead exemption for principal residences. Local counsel further provides that approximately 85 percent of referrals to his firm have been homestead properties.

⁵ Per local counsel, although the statute uses the term "borrower," MCL § 600.3205(a) defines "borrower" as meaning "mortgagor," and there might be mortgagors who are not borrowers or borrowers who are not mortgagors.

File Assessment – Foreclosure File Review

- Purpose(s) of file review
 - Identify financial injuries to borrowers – and remunerate/remediate
 - OCC/FRB recently provided guidance on remediation to those subject to Consent Orders
 - No public guidance available yet to other banks
 - Identify technical errors in process – and fix going forward
 - Use checklists that allow for a yes/no/could not be determined construct
 - Determine problem foreclosure firms – and sever ties or fix problems
 - Document retention checklists

CFPB Exam Guidelines – Background

- In October 2011, the CFPB released its initial examination guidelines, including guidelines for servicing examinations
 - Much more extensive on consumer issues in servicing than prior examination guidance from the OCC
 - Until a Director is confirmed, CFPB exam authority only extends to banks that are over \$10 billion
 - Appears to require consultation with headquarters prior to making determination that there has been a fair lending violation
 - Banks are beginning to receive detailed information requests from the CFPB in preparation for a mortgage servicing examination

CFPB Exam Guidelines – Background

- Acting Director Date has stated that mortgage servicing is going to be one of the CFPB's initial priorities
- General CFPB exam guidance states that “every examination must include a review” of
 - Compliance management
 - Potential UDAAPs
 - Regulatory compliance matters presenting “risks” to consumers
 - Discrimination

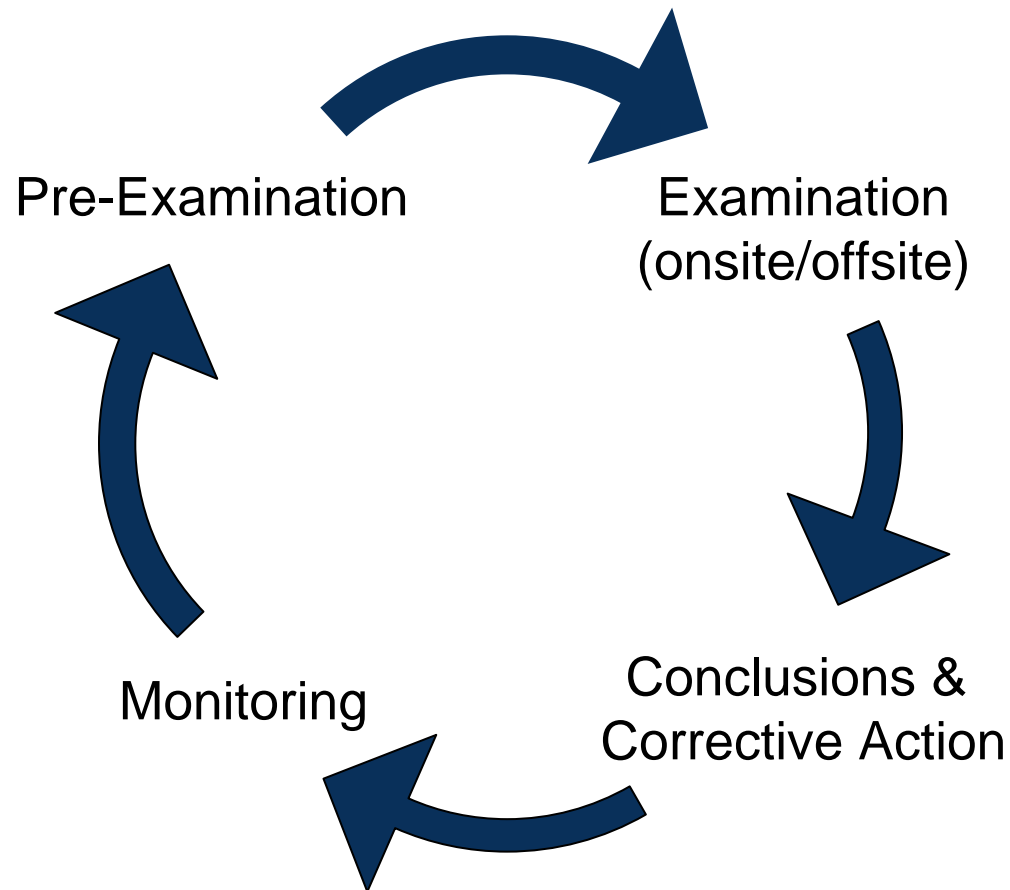
CFPB Exam Guidelines – Background

- State Attorneys General
 - Joint Statement of Principles with NAAG addressing coordination of investigations and enforcement actions and information sharing
 - AGs as deputies – can enforce Dodd-Frank consumer protection provisions and CFPB regulations in federal court
 - Working together on mortgage servicer settlement
- Fair lending MOU with FTC, HUD, and DOJ
- MOU with FTC on broader enforcement remains under negotiation

CFPB Exam Guidelines – Background

- Focus on gathering information and complaints directly from consumers
- Agreement with FTC on access to Sentinel consumer complaint database
- Information-sharing MOUs and agreements with various federal and state agencies including banking regulators, FFIEC, FinCEN, NAAG, and Conference of State Bank Supervisors

CFPB Exam Guidelines – Background Ongoing Supervision Process



CFPB Exam Guidelines

- Nine modules
 - Module 1: Servicing and Ownership Transfers and Escrow Disclosures
 - Module 2: Payment Processing and Account Maintenance
 - Module 3: Customer Inquiries and Complaints
 - Module 4: Maintenance of Escrow Accounts and Insurance Products
 - Module 5: Credit Reporting
 - Module 6: Information Sharing and Privacy
 - Module 7: Collection and Accounts in bankruptcy
 - Module 8: Loss Mitigation
 - Module 9: Foreclosure

CFPB Exam Guidelines – Module 1

- Servicing Transfers
 - Federal statutory requirements under RESPA, FDCPA and new TILA ownership transfers
 - Special focus
 - Data integrity upon transfer
 - Transfer of defaulted loans and related transfer of loss mitigation agreements and discussions

CFPB Exam Guidelines – Module 2

- Payment Processing and “Account Maintenance”
 - Federal statutory requirements under TILA, ECOA, EFTA and Fair Credit Billing
 - Basic payment processing
 - Specific discussion of reviewing customer complaints
 - Accurate and documented assessment of fees to protect the interest in the collateral
 - Scrutiny of all policies and practices around default-related services that give rise to fees, including loan-level documentation
 - Account statement accuracy
 - Query – will you face systems limitations in providing all “material” information

CFPB Exam Guidelines – Module 3

- Customer inquiries and complaints

CFPB Exam Guidelines – Module 4

- Escrow 101 – compliance with RESPA
- Focus on lender-placed insurance
 - “Determine whether the servicer or any of its affiliates imposes mark-ups, or received commissions or other payments, related to any force-placed insurance products”
 - Does this mean that such payments are illegal? Show inadequate compliance management even if not illegal? Or is it just interesting information?
 - “Any” affiliates would seem to include both insurance agencies receiving commissions to place insurance and captive reinsurers taking premiums
 - Disclosure and placement cycle

CFPB Exam Guidelines – Module 5

- Credit reporting
 - FCRA furnisher requirements
 - Process to handle complaints

CFPB Exam Guidelines – Module 6

- Information Sharing and Privacy
 - GLB Privacy notices
 - Affiliate sharing
 - Reference to existing exam guidance on these issues

CFPB Exam Guidelines – Module 7

- Collections

- FDCPA compliance
- When is a loan “in default” when acquired by the servicer, making it subject to the FDCPA
 - Footnote 6 in exam guidance highlights that default is not defined in the statute but notes further that “**the standard mortgage note states that the debt is in default if the payment is even one day late**”
 - This is consistent with FTC’s official position for the past several years but is not a position that courts have accepted in the mortgage context due to absurdity of the implication that a substantial majority of US mortgage loans are in default

CFPB Exam Guidelines – Module 8

- Loss Mitigation
 - Major focus on fair servicing
 - Disparate treatment
 - Disparate impact
 - Other Issues
 - Adequate outreach
 - Operational concerns

CFPB Exam Guidelines – Module 8

- Other Loss Mitigation Risks to Consumers
 - Outreach to defaulted borrowers
 - Numerous operational concerns
 - Adequate ability of consumers to contact the servicer and communicate accurate information
 - Does not appear to require SPOC
 - Providing accurate information throughout process
 - How do you tell consumers that they would not qualify for loss mitigation unless they are in default without “advising customers to stop payments to qualify for loss mitigation relief”
 - Information regarding potential negative consequences of loss mitigation
 - Referring loans to loss mitigation from customer service and collections and properly following loss mitigation waterfall from HAMP
 - Timely and accurate processing of applications

CFPB Exam Guidelines – Module 9

- Foreclosure
 - Is default information contained in affidavits and other court papers accurate
 - Is the borrower actually delinquent
 - Have all foreclosure protections been considered (e.g., SCRA or state mediation requirement)
 - Discrimination – disparate treatment and disparate impact stemming from loss mitigation processing
 - Dual tracking – has servicer foreclosed when
 - The consumer was meeting the terms of a trial mod or other forbearance
 - Loss mitigation agreement reached but first payment not due yet
 - Consumer was not given options for loss mitigation or had a request pending
 - Consumer ability to “game” if standard for a halt is “pending request”

Fair Servicing

- Consumer advocacy groups claim race disparities in workouts and treatment of REO properties
 - NCRC study of **just over 100 borrowers** selected by NCRC local affiliates suggested that among HAMP eligible borrowers 36.4% of white borrowers received loan modification approvals in contrast to 32.3% of Hispanic and 24.3% of African-American borrowers
 - But more recent Federal Reserve Bank of San Francisco study of over **100,000 loans** shows that minority borrowers were more likely to receive a loan modification, and less likely to re-default after the modification
 - NFHA “investigation” alleges disparities in maintenance and marketing of REO properties based on predominate race in census tracts
- Substantial public pressure to ensure that borrowers who are members of minority groups have fair opportunity to prevent foreclosure

Fair Servicing

- Fair Servicing issues have now become a focal point of both enforcement efforts and in the examination process
- As a result, regulators are engaging in heightened scrutiny of servicing issues, with unprecedented attention and access to loan-level servicing data
 - Foreclosure disparities between protected classes and others
 - Consumer complaints alleging discrimination in loan servicing
 - Poorly documented or undocumented servicing decisions
 - High levels of litigation alleging loan servicing discrimination
- Fair Lending Unit within DOJ Civil Rights Division analyzing potential discrimination in loan modifications
 - Demographics at census tract level likely to be an analytical driver

Contact Information

Jeff Naimon

jnaimon@buckleysandler.com

Jonice Gray Tucker

jtucker@buckleysandler.com

Joe Reilly

jreilly@buckleysandler.com

BuckleySandler LLP
1250 24th Street NW, Suite 700
Washington, DC 20037
(202) 349-8000
www.buckleysandler.com

Disclaimer

The information contained herein is for informational purposes only; do not constitute legal advice; and, do not necessarily reflect the opinions of BuckleySandler LLP or any of its attorneys or clients. This presentation is not intended to create, and does not create, an attorney-client relationship between you and BuckleySandler LLP, or any of the presenters, and you should not act or rely on any information in this presentation without consulting legal counsel. The information contained in this presentation may or may not reflect the most current legal developments; accordingly, information in this presentation is not promised or guaranteed to be correct or complete, and should not be considered an indication of future results. BuckleySandler LLP expressly disclaims all liability in respect to actions taken or not taken based on any or all the contents of this presentation.