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U.S. Consumer Financial Protection Bureau Proposes Mortgage Servicing Reforms

The mortgage finance system in the United States is under radical reconstruction as a result of the events of 2007-2009. The Dodd-Frank Act (Dodd-Frank) impacts mortgage origination, servicing and securitization through a wide range of new requirements. It creates ability to repay requirements, risk retention requirements and mortgage origination compensation restrictions, among other things. At the same time, federal and state regulators have been reformatting the mortgage servicing business through enforcement proceedings in addition to instituting notice and comment rulemaking proceedings. Still unaddressed is the future of Fannie Mae, Freddie Mac and federal support of affordable housing finance.

Reminiscent of the activism of the 1970s when our current federal consumer protection laws were first established, the Consumer Financial Protection Bureau (CFPB) has issued two proposed rules under the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA) to comprehensively modify the practices of residential mortgage servicers. The proposals would impact how servicers (i) credit borrowers for their mortgage payments; (ii) notify borrowers of changes in the status of their mortgages; (iii) respond to borrower inquiries; and (iv) provide early intervention and loss mitigation programs to delinquent borrowers.

The CFPB inherited responsibility for rulemaking under TILA and RESPA as part of Dodd-Frank, and the proposed amendments are intended to implement Congress' direction in Dodd-Frank to correct practices and conflicts of interest in mortgage lending and servicing that many believe contributed to the foreclosure crisis. The proposed rules would affect lenders that retain mortgage servicing rights, third-party mortgage servicers and issuers of and investors in mortgage-backed securities. In many instances, model forms or model language is provided. The comment period on the proposed rules will remain open until October 9, 2012, and final rules are expected to be adopted no later than January 21, 2013.

Key Features of the Proposed Rules

The proposed rules would revise Regulation Z under TILA and Regulation X under RESPA in nine major areas.

Periodic Billing Statements

Content, format and timing requirements for periodic billing statements are established, and model forms are provided. Entities that service no more than 1,000 mortgage loans, all of which they originated or own, are exempt.

ARM Adjustment Notices

When an adjustment in an interest rate causes a change in a borrower's payment obligations, the servicer must notify the borrower of the adjustment between 60 and 120 days before it takes effect. Prior to the first such adjustment, the servicer must give the borrower between 210 and 240 days' notice.

Prompt Payment Crediting and Payoff Information

Servicers generally must credit borrowers for payments on the day of receipt, but they may place insufficient payments in a suspense

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account and, when a sufficient payment is accumulated, credit it to the oldest outstanding payment owed.

Force-Placed Insurance

The ability of servicers to arrange for property insurance is restricted. Among other things, the servicer must have a reasonable basis to believe that the required insurance is not being maintained, and any force-placed insurance must be cancelled and unearned premiums must be refunded to a borrower's account after the borrower provides proof of coverage.

Error Resolution

For specific types of complaints, servicers generally must correct or respond to a complaint and provide requested information or explain why such information is not available within 30 to 45 days.

Information Management

Servicers must establish policies and procedures for information management, including document retention and information retrieval goals, that are consistent with the size, scope and nature of their operations.

Early Intervention

Servicers must make good faith efforts to notify delinquent borrowers of the foreclosure process and of available loss mitigation options, including how to obtain additional information regarding those options.

Borrower Contact

Servicers must make dedicated personnel available to assist borrowers regarding their loss mitigation options, no later than five days after providing early intervention notice.

Loss Mitigation

Servicers that offer loss mitigation options must implement procedures to ensure that complete applications for loss mitigation are reasonably evaluated in a timely manner before proceeding with a scheduled foreclosure sale.

Timing Considerations

Title XIV of Dodd-Frank includes several substantive amendments to TILA and RESPA. It also authorizes the CFPB to adopt any other servicer obligations that it finds by regulation to be appropriate to carry out the consumer protection purposes of Dodd-Frank. Any provision of Title XIV for which a final regulation is adopted before January 21, 2013 shall not take effect until the date on which its implementing regulation takes effect. However, if a final regulation is not adopted by January 21, 2013, the statutory provision will take effect on that date.

The CFPB has stated that it intends to adopt final regulations before January 21, 2013. In order to help it to meet this target, the CFPB has set a 60-day comment period that began on August 10, 2012, the date on which the proposed rules were released, and will close on October 9, 2012, rather than following the customary practice of waiting to begin the comment period until the date on which the proposed rules are published in the Federal Register. The proposed rules are lengthy and include numerous detailed requirements, which dictate that persons interested in submitting comments on the proposed rules should review them promptly.

While the adoption of final rules before January 21, 2013 should avoid causing related provisions of Title XIV to take effect automatically on that date, the effective date of any final rules must be established. The CFPB has specifically requested comment on the appropriate implementation schedule for the proposed rules, in view of the remedial nature of Title XIV, the difficulty and costs of compliance with the proposed requirements and the possible interaction between the requirements of the proposed rules and the requirements of other Dodd-Frank rulemaking. The CFPB also has specifically requested comment regarding the impact on consumers and servicers of having various servicing requirements take effect simultaneously or in a staggered sequence.

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