

InfoBytes Special Alert:

Federal and State Officials File Settlement with Nation's Five Largest Mortgage Servicers

March 15, 2011

On March 12, 2012, Federal and state officials filed documents in the United States District Court for the District of Columbia formalizing a previously announced settlement (the Settlement) of various government probes into alleged mortgage-related violations by the five largest residential mortgage servicers (collectively the Servicers). The Settlement, which was first announced on February 9, 2012, resolves investigations and inquiries by numerous federal regulators and 49 state Attorneys General (AGs). The federal agencies that have signed on to the settlement include: the Department of Justice, the Department of Housing and Urban Development, the Department of Treasury, the Department of Agriculture, the Department of Veterans Affairs, the Federal Trade Commission, the Consumer Financial Protection Bureau, and the U.S. Trustee.

With the filing of a consolidated complaint and a separate consent judgment for each Servicer, the details of the Settlement have been made available, including its provisions regarding: (i) restitution and other relief, (ii) new servicing standards, (iii) the scope of its releases, and (iv) implementation and enforcement.

RESTITUTION AND OTHER RELIEF

In its entirety, the settlement totals approximately \$26 billion dollars. The Servicers have agreed to provide roughly \$20 billion dollars in financial relief to distressed borrowers and an additional \$5 billion in direct payments to the signing states and the federal government. Of the \$20 billion dollars devoted to financial relief for distressed borrowers, up to \$3 billion will be directed toward refinancing eligible borrowers and up to \$17 billion will be directed toward providing loan modifications, principal reductions, and other relief for eligible borrowers.

The \$5 billion in direct payments to state and federal governments will be divided in the following manner: (i) \$500 million will be used to fund a loan modification program for certain Countrywide borrowers, (ii) \$1.5 billion will be used to create a Borrower Payment Fund to compensate up to 750,000 borrowers who lost their homes to foreclosure between January 1, 2008 and December 31, 2011, and (iii) the remaining \$3 billion will be used by state and federal governments to repay public funds lost as a result of alleged Servicer misconduct and to fund housing counseling, legal aid, and other similar public programs.

The Settlement also incorporates more than \$766.5 million in monetary sanctions [assessed by the Federal Reserve Board](#) as well as a \$1 billion False Claims Act settlement related to alleged wrongful origination and underwriting of Federal Housing Administration-insured mortgage loans by one of the Servicers. Each Servicer's financial responsibilities under the Settlement are summarized in a [Fact Sheet](#), and specific settlement amounts are available in each Servicer's consent judgment.

NEW SERVICING STANDARDS

In addition to providing the monetary relief described above, the Servicers have agreed to adhere to a new set of standards in connection with servicing activities. These standards will set a baseline for servicing expectations across the mortgage servicing industry and cover eight topics, which are discussed in further detail below:

- Foreclosure & Bankruptcy Information and Documentation;
- Third-Party Provider Oversight;

- Bankruptcy;
- Loss Mitigation;
- Protections for Military Personnel;
- Restrictions on Servicing Fees;
- Lender Placed Insurance; and
- General Servicer Duties and Prohibitions.

1) Foreclosure and Bankruptcy Information and Documentation

In an effort to address alleged deficiencies in the Servicers' business practices related to so-called "robo-signing" activities, the Settlement establishes standards for factual assertions made in foreclosure and bankruptcy proceedings, and outlines a process for executing documents used in those proceedings. To this end, the Settlement requires that the Servicers:

- (a) Have sufficient evidence to support the factual assertions made in bankruptcy or foreclosure proceedings;
- (b) Ensure that any sworn statements made in those proceedings are properly executed and are based on the personal knowledge of the affiant;
- (c) Implement minimum standards for the qualifications, training, and supervision of employees; and
- (d) Conduct regularly scheduled independent quality assurance reviews assessing the adequacy of the Servicers' internal controls and procedures related to loan, bankruptcy, and foreclosure documentation.

2) Third-Party Oversight

Under the Settlement, the Servicers must adopt policies and processes to oversee and manage third-party vendors (Third-Party Providers), such as law firms, foreclosure trustees, subservicers, and other independent contractors. These policies and processes must, among other things, include procedures for reviewing and addressing customer complaints lodged against Third-Party Providers.

The Settlement requires that the Servicers periodically review both the performance of their Third-Party Providers and the adequacy of their own internal controls against a number of metrics outlined in the Settlement. These reviews must be conducted by employees of the Servicers who are independent of employees who prepare foreclosure or bankruptcy documentation. To the extent a periodic review identifies a compliance issue, the Servicers must take appropriate remedial action.

Additionally, for law firms that provide residential mortgage foreclosure and bankruptcy services on a periodic basis, the Settlement requires that the Servicers establish a certification process that will ensure that: (i) the firm's attorneys are licensed to practice in the relevant jurisdiction and have the experience and competence necessary to perform the services requested by the Servicers, and (ii) the firm's services comply with applicable law and regulations (including state prohibitions on fee splitting).

3) Bankruptcy

The Settlement requires that the Servicers provide specialized training to employees who regularly engage in servicing mortgage loans in bankruptcy. Additionally, with respect to Chapter 13 cases, the Settlement requires that, within 180

days of any bankruptcy filing, the Servicers must file and serve on the debtors, the debtors' counsel, and the trustees a special notice disclosing all fees, expenses, or outlays charged by the Servicers. Should any information contained in this notice change, the Servicers must file and serve a new notice on the debtors, the debtors' counsel, and the trustees 21 days before a payment is due under the new amount. If a Servicer fails to satisfy these requirements, it may be required to waive the charges or provide some other form of appropriate restitution.

4) Loss Mitigation

The Settlement includes a substantial number of loss mitigation provisions covering a wide range of topics, including, among others, (i) dual tracking, (ii) single points of contact, (iii) borrower communications, (iv) loan portals, (v) modification timelines, and (vi) loss mitigation staffing.

a. Dual Tracking

The Settlement establishes an extensive framework regulating how, and when, the Servicers may foreclose on borrowers if those borrowers have pending modification requests. The Servicers must send borrowers facing foreclosure a statement outlining any loss mitigation efforts undertaken with respect to their loan before referring the loan to foreclosure. If no loss mitigation solutions were offered to the borrower, the Servicer must indicate whether it attempted to contact the borrower and, if applicable, why the borrower was ineligible for a loss mitigation option.

If a borrower sends a Servicer a modification request at any point prior to or during a foreclosure proceeding, the Servicer must respond to the borrower's request before advancing to the next stage of foreclosure and must provide the borrower a specified amount of time to accept the terms of a modification, if one is offered, or to appeal the result.

b. Single Point of Contact

Servicers must establish an easily accessible and reliable single point of contact (SPOC) for each potentially-eligible borrower for whom it is servicing a mortgage in the first lien position.^[1] Additionally, if a borrower is in bankruptcy, he or she must receive a SPOC specifically trained on bankruptcy servicing.

This SPOC is responsible for communicating to the borrower, among other things, (i) the loss mitigation options available to the borrower, (ii) the actions the borrower must take to be considered for these options, and (iii) the status of Servicer's evaluation of the borrower for these options. Additionally, the SPOC must coordinate receipt of all modification documents and loss mitigation activities and must maintain a working knowledge of the borrower's current status in the default process.

In addition, the Servicers must provide management level SPOCs for AGs, federal and state regulators, and U.S. Trustees for communication regarding complaints and inquiries from individual borrowers in default or who have applied for loan modifications. Servicers must provide written acknowledgment of all such inquiries within 10 business days, and substantive written responses to all such inquiries within 30 days.

c. Borrower Communications

Pursuant to the terms of the Settlement, the Servicers must communicate loss mitigation options for first lien mortgage loans to all potentially eligible delinquent borrowers in accordance with HAMP borrower solicitation guidelines. Such steps must be undertaken without regard for whether a borrower is eligible for a HAMP modification. Likewise, the Servicers must conduct affirmative outreach efforts to inform borrowers who are delinquent on loans in the second lien position to contact servicers about the availability of payment reduction options.

The Settlement further provides that the Servicers must cease all collection efforts while a borrower is making timely payments under a trial loan modification plan as well as between the time that the borrower has submitted a complete modification request and the time that a final decision on that request is rendered.

Within five business days of a foreclosure referral, the Servicers (or their attorneys or trustees) must send a written communication to the borrower which includes the following statements:

- (a) The Servicer previously sent the borrower solicitation communications;
- (b) The borrower can still be evaluated for foreclosure alternatives and should contact the servicer to obtain a loss mitigation application package;
- (c) The borrower must submit a loan modification application to be considered for a foreclosure prevention alternative; and
- (d) If the borrower is contemplating or has pending an appeal of an earlier denial of a loan modification application, he or she may submit a loan modification application in lieu of his or her appeal within 30 days of the date of the letter.

These written communications also must provide the applicable Servicer's contact information, including its address for modification applications and its toll-free number.

d. Loan Portals

Servicers are required to develop an online portal linked to their primary servicing system. The portal must (i) allow borrowers to check, at no cost, the status of their first lien loan modifications, (ii) enable borrowers to submit loan modification-related documents electronically, (iii) provide an electronic receipt for any documents submitted, (iv) provide information and eligibility factors for loss mitigation programs, and (v) inform borrowers of any outstanding required documentation.

Additionally, the Servicers must participate in the development of a nationwide loan portal system to communicate with housing counselors. This system must be linked to the Servicers' primary servicing systems.

Both the borrower and housing counselor portals must be updated with the borrower's pending loan modification information at least every 10 business days.

e. Modification Timelines

The Settlement establishes timelines to which the Servicers must adhere when processing modification applications. For example, for first liens, the Servicers must acknowledge the receipt of a borrower's loan modification application documentation in writing within three business days and must notify the borrower of any known deficiency in his/her initial submission within five business days of receipt. The borrower then will have 30 days from the time of this notification to supplement his/her submission. Once a loan modification application is complete, the Servicers must process and provide the borrower with a determination within 30 days, absent compelling circumstances beyond the Servicers' control.

f. Loss Mitigation Staffing

The Settlement requires the Servicers to assess loss mitigation staffing levels periodically to ensure that they are adequate, especially with respect to the number of document processors, SPOCs, and customer representatives. The Servicers also must ensure that their loss mitigation employees meet reasonable minimum experience, educational, and

training requirements and that they are not compensated in a manner which incentivizes foreclosures over loss mitigation alternatives.

5) Protections for Military Personnel

a. Provisions Relating Specifically to Military Servicemembers

The Settlement contains a number of requirements relating specifically to military servicemembers. First, any borrower identified as a servicemember within the last nine months must be routed to a customer service representative and/or SPOC specializing in issues related to the Servicemembers Civil Relief Act (SCRA). That specialist then will determine whether the borrower is eligible for SCRA benefits. Second, the Servicers must accept letters from a servicemember's commanding officer as evidence of a servicemember's active duty military status.

In addition, the Settlement also establishes a number of prohibitions relating specifically to military servicemembers. First, whenever a servicemember is suffering financial hardship or is otherwise eligible for loss mitigation, the Servicers must not require that servicemember to be delinquent in order to qualify for short sales, loan modifications, or loss mitigation relief. Second, the Servicers may not make inaccurate reports to credit reporting agencies in cases where a servicemember, who had not defaulted before relocating under military orders to a new duty station, obtains a short sale, loan modification, or other form of loss mitigation relief. Finally, unless they first obtain a court order or an agreement from the servicemember, the Servicers are prohibited from foreclosing on any servicemember, regardless of his/her SCRA eligibility, who within the last nine months was eligible for Hostile Fire/Imminent Danger Pay and was serving at a location that was either: (i) more than 750 miles from the location of the secured property or (ii) outside the United States.

b. General Provisions

The Settlement contains several provisions relating to SCRA compliance that are applicable to all borrowers. First, the Servicers must engage an independent consultant to review their foreclosures from January 1, 2009 to December 31, 2010 for compliance with SCRA, and provide remediation where appropriate. Second, the Servicers must notify all customers who are 45 days delinquent that, if they are servicemembers, they may be entitled to SCRA benefits and can receive housing counseling services. Finally, the Servicers also must conduct Defense Manpower Data Center searches on all borrowers (i) before referring a loan for foreclosure, (ii) within seven days of a foreclosure sale, and (iii) promptly after a foreclosure sale or within three days before the end of a regularly scheduled redemption period, whichever is later.

6) Restrictions on Servicing Fees

The Settlement requires that all fees charged by the Servicers must be bona fide, reasonable, and disclosed in detail. In addition, the Servicers must maintain current schedules of common non-state specific fees on their servicing websites. These fee schedules also must be made available to borrowers upon request.

The Servicers may collect default-related fees only if they are for reasonable and appropriate services actually rendered and (i) the fees are expressly or generally authorized by the loan instruments and not prohibited by law or the Settlement, (ii) the fees are permitted by law and not prohibited by the loan instruments or the Settlement, or (iii) the fees are not prohibited by law, the Settlement, or the loan instruments and are reasonable fees for specific services requested by the borrowers that are collected only after clear and conspicuous disclosure of the fees are made available to the borrowers.

The Settlement restricts late fees, forbidding Servicers from collecting such fees (i) in instances where the borrower is only delinquent due to a previous late fee, (ii) on amounts greater than the past due amount, (iii) from the borrower's escrow without approval from the borrower, (iv) if deducted from any regular payments, (v) while the borrower is under consideration for a modification or short sale, or (vi) while the borrower is making timely modification payments.

The Settlement also limits certain third party fees. For example, the Servicers are prohibited from charging unnecessary or duplicative property inspection, property preservation, or valuation fees. In addition, all default, foreclosure, or bankruptcy related services must be earned and must be charged at a reasonable market value, free from mark-ups. To determine what qualifies as a reasonable market value, the Servicers must perform an independent annual market review.

Finally, the Settlement bars the Servicers from collecting any attorneys' fees or other charges with respect to the preparation or submission of a proof of claim or a motion for relief from stay that is withdrawn or denied as a result of a substantial misstatement of the amount due by the Servicers. Likewise, the Servicers may not collect late fees on payments that the debtor timely makes to a Chapter 13 trustee.

7) Lender Placed Insurance

For escrowed accounts, the Settlement requires that the Servicers advance payments to maintain an existing policy. Otherwise, as long as the Servicer has a reasonable basis for believing that a borrower has failed to maintain insurance, it may initiate a lender placed insurance policy, but only after having sent the borrower two notices at least 30 days apart and only after having failed to receive a written confirmation of coverage from the borrower within 15 days of the second notice.

Insofar as a borrower submits evidence of existing coverage, the Servicer must terminate any lender placed insurance policy on that borrower's property within 15 days. The Servicer also must refund any premiums paid by the borrower while the borrower's own coverage was in effect.

8) General Servicer Duties and Prohibitions

Under the Settlement, the Servicers must develop and implement policies and procedures to prevent blight in their REO properties. In this regard, the Servicers must (i) enhance coordination with state and local anti-blight programs, (ii) inform borrowers that they must continue to maintain their property until title is transferred to the Servicers, (iii) present borrowers with foreclosure alternatives when they indicate that they are going to abandon their property, and (iv) with respect to first lien loans, notify the borrower and local authorities when the Servicers intend to charge-off a property.

Servicers also must develop and implement policies and procedures to comply with all applicable tenants' rights laws.

SCOPE OF RELEASES

The Settlement includes separate federal and state releases for each Servicer. Each release outlines its scope in detail, addressing the conduct covered under the release, the claims released, and any exceptions to the release.

1) The Scope of the Federal Releases

Each Servicer's federal release covers the activities of the Servicer as well as its affiliates, subsidiaries, officers, directors, employees, and agents. The Settlement releases the Servicer from certain civil claims relating to single-family residential mortgages that fall into the following three categories:

(a) Servicing Conduct - This category encompasses most claims related to the servicing of loans post-origination, including, for example, claims based on deficiencies in the Servicers' (i) loan modification practices, (ii) foreclosure processes, (iii) supervision of vendors and agents, (iv) collections activity, (v) escrow account management, (vi) handling of customer inquiries and complaints, (vii) lender placed insurance practices, (viii) property preservation practices, and (ix) HAMP administration.

(b) Origination Conduct - This category includes, for example, claims related to: (i) the submission of unqualified loans to FHA insurance programs, (ii) deficiencies in the processing, underwriting, closing, and funding of loans, (iii) deficiencies in loan advertisements and borrower solicitations, and (iv) deficiencies in the drafting and provision of loan disclosures.

(c) Bankruptcy Conduct - This category includes, for example, claims related to deficiencies in the Servicers' (i) servicing of mortgages for borrowers in bankruptcy, (ii) administration of loan modifications for borrowers in bankruptcy, and (iii) submissions to bankruptcy court.

The federal releases specifically do not extinguish existing or potential claims related to: (i) any liability under the tax code, (ii) any criminal liability for the Servicers or affiliated individuals, (iii) most activity involving the securitization of mortgages, (iv) liability under Section 8 of the Real Estate Settlement Procedures Act, (v) certain information security protections, (vi) liability for discriminatory conduct, including any violations of the Fair Housing Act, the Equal Credit Opportunity Act, and the Home Mortgage Disclosure Act, (vii) HUD administrative proceedings against individuals, (viii) environmental liability, and (ix) civil claims brought by individual borrowers on either an individual or a class basis. The federal releases also preserve specific claims on behalf of federal banking and housing regulators, as well as certain existing lawsuits. While the release covers the activity of third-party agents, such agents themselves are not released under the Settlement.

2) The Scope of the State Releases

Each Servicer's state release covers the activities of the Servicer as well as its affiliates, subsidiaries, officers, directors, employees, and agents. The Settlement releases the Servicer from civil claims that fall into the following three categories:

(a) Residential Mortgage Loan Servicing Conduct - This conduct includes all actions, errors, or omissions of the Servicers, arising out of or relating to the servicing (including subservicing and master servicing) of residential mortgage loans from and after the closing of such loans, regardless of whether the Servicers own an interest in the residential mortgage loans or service them on behalf of another institution.

(b) Residential Foreclosure Services Conduct - This conduct encompasses all actions, errors, or omissions of the Servicers' arising out of, or relating to, foreclosures on residential mortgage loans, regardless of whether the Servicers own an interest in the residential mortgage loans or service them on behalf of another institution.

(c) Residential Mortgage Loan Origination Services Conduct - This conduct includes all actions, errors, or omissions of the Servicers arising out of, or relating to, the origination of, or the assistance in the origination of, residential mortgage loans, or the purchasing of residential mortgage whole loans.

The state releases specifically exclude from release: (i) claims related to the securitization of mortgages, (ii) claims against a trustee related to the pooling of residential mortgages in trusts and securities, (iii) claims relating to previously obtained assurances of compliance regarding pay option ARMs, (iv) claims against MERS; (v) tax liability claims, (vi) claims arising out of discriminatory conduct, (vii) criminal claims, and (viii) civil claims brought by individual borrowers on either an individual or a class basis. As in the federal release, the state parties also specifically preserve certain existing state lawsuits.

IMPLEMENTATION, MONITORING, AND ENFORCEMENT

1) Implementation

The Settlement provides detailed enforcement mechanisms and timelines for compliance. Former North Carolina Commissioner of Banks, Joseph A. Smith, will serve as the Independent Monitor for the Settlement and has been charged

with overseeing the implementation and enforcement of the Settlement over a period of three years. During the Settlement's implementation stage, government parties will be represented by a Monitoring Committee composed of representatives from the AG offices, state financial regulators, the U.S. Department of Justice, and the U.S. Department of Housing and Urban Development.

2) Monitoring

Within 90 days of March 12, 2012 (June 9, 2012), the Servicers and the Independent Monitor must develop work plans that establish metrics and testing methodologies for measuring compliance with the Settlement's servicing standards. The Servicers then must conduct quarterly compliance testing based on their work plans, delegating responsibility for testing under the plans to an internal quality control group (Internal Review Group) within their respective organizations. This Internal Review Group must be independent from the lines of business being reviewed and must report to a chief risk officer, chief audit executive, chief compliance officer or "another employee or manager who has no direct operational responsibility for mortgage servicing." In addition, the Internal Review Group must conduct yearly reviews of the Servicer's compliance with the Settlement's consumer relief provisions.

Periodically, the Independent Monitor also will issue his own reports on the Servicers' compliance. These "monitor reports" will address: (i) whether any of the Servicers have committed potential violations of the Settlement, (ii) whether these violations were cured, and (iii) the number of borrowers who have been assisted by the Settlement. The Servicers may submit written comments on these monitoring reports.

If at any time a Servicer becomes aware that it is engaged in a significant pattern or practice of noncompliance with a material aspect of the Settlement, it must notify the Independent Monitor promptly. Additionally, if the Independent Monitor becomes aware that a Servicer may be engaged in a pattern of noncompliance with a material term of the Settlement, the Monitor may conduct a review of the Servicer. When conducting this review, the Independent Monitor (i) may require access to all work papers prepared by the Servicer's Internal Review Group, (ii) may interview the Servicer's employees and agents regarding settlement compliance, and (iii) may request additional information from the Servicer in a format agreed upon by the Servicer and the Independent Monitor.

3) Enforcement

If the Independent Monitor finds that a Servicer is in serious noncompliance with the Settlement, he may petition the United States District Court for the District of Columbia for both equitable relief and civil penalties of up to \$1 million per uncured violation and \$5 million per repeat violation.

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For additional information concerning the Settlement, please contact any member of our [Mortgage Servicing Team](#).

[1] The phrases "potentially-eligible borrower," "potentially-eligible first lien mortgage borrower," "potentially eligible borrowers," and "potentially eligible delinquent borrowers" appear throughout the Settlement term sheet, but are not defined. [\[Back.\]](#)

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