

Dodd-Frank 2014 Part Two: New Federal Rules for Consumer Mortgage Loan Servicing and Loss Mitigation

[On behalf of Dornish Law Offices, PC](#) | May 21, 2014 | [All, Real Estate Practice](#)

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In addition to the new rules for loan applications which went into effect this January, (covered in part one of this article) the Consumer Financial Protection Bureau promulgated a new set of rules governing the servicing of existing consumer mortgage loans by creditors and their mortgage servicers. Some of the changes in these rules affect all mortgage servicers, while others have exemptions for certain small servicers. The changes appear in the Code of Federal Regulations, abbreviated here as C.F.R. The code is available online at eCFR.gov.

Many of the changes dictate how servicers must deal with all of their consumer borrowers, while other changes only affect consumer borrowers who are in default. Certain provisions have exemptions for Small Loan Servicers, which are defined as servicers of fewer than 5,000 mortgage loans as of January 1 of the applicable year. We will review the changes affecting all consumers first, and note which provisions exempt small servicers.

1. **A. Periodic Billing Statements and Other Information to be Provided to Borrowers.**

Mortgage servicers, including both original creditors and assignees, now must give borrowers billing information in writing. Borrowers are entitled to a written mortgage statement each billing cycle, showing what the borrowers owe on the current bill, how it is applied to principal, interest and escrows, payments made since the last billing, and how they were applied, and any transaction activity including fees charged to the account (12 C.F.R. §1026.41).

Additionally, this section requires lenders to give borrowers a free copy of all appraisals it obtained on the borrower's property, contact information for the servicer, and late payment information as well as information on how to contact a housing counselor if the borrowers fall behind on their loan. All of this information must be provided at least three days before loan closing.

Note that there is an exemption to these requirements for small loan servicers, and borrowers under fixed rate mortgages may be sent a coupon book with all the same information, instead of monthly statements. 12 C.F.R. §1026.41(e)(3).

1. **B. Interest Rate Adjustments for Adjustable Rate Mortgages.**

Special new rules for notice apply to adjustable rate mortgages. For the first time an interest rate adjusts under such a loan, the servicer must give notice of the change between 240 days (8 months) and 210 days (7 months) prior to the date the first payment is due after the rate adjusts. 12 C.F.R. § 1026.20(c). Any time an ARM has a rate adjustment resulting in a new payment amount, the servicer must give at least 60 days' notice to the borrower. 12 C.F.R. §1026.20(d).

1. **C. Prompt Payment Crediting**

Mortgage Servicers must promptly credit borrowers' payments. Servicers have to give borrowers credit for their full payments as of the day they are received by the servicer. 12 C.F.R. §1026.36(c)(1).

If borrowers pay only part of what they owe, the servicer may hold their partial payment(s) in a special suspense account, but the servicer must tell borrowers about this on their monthly statement. When multiple partial payments add up to a full payment, the servicer has to credit that payment to the borrowers' account.

Mortgage Servicers must also respond quickly when borrowers ask about paying off their loan. See 12 U.S.C. § 2605(k)(1)(C); 12 C.F.R.

§1026.36(c)(3). The servicer generally has seven business days after receipt of a written request to provide a complete and accurate pay-off statement.

This rule should prove very beneficial to real estate investors waiting for payoff information to close on purchases from owner occupants who have outstanding mortgage loans. Unfortunately, the rule does not apply to commercial loans when investors are selling a property with a mortgage, or buying a property with a non-consumer mortgage loan outstanding.

1. **D. Restrictions on Force Placed Insurance**

Mortgage Servicers must not charge borrowers for insurance they don't need, or over-charge borrowers for force-placed insurance. See 12 U.S.C. § 2605(k)(1)(A); see also 12 C.F.R. §1024.37. Servicers must warn borrowers at least 45 days before charging them for a force-placed insurance policy, thus giving borrowers time to buy their own policy. The servicer must then warn borrowers again between 30 days and 15 days before it changes borrowers for such coverage. If the servicer has to purchase force-placed insurance; it can't over-charge borrowers for it. See 12 U.S.C. § 2605(l)(1)(A)-(C); see also 12 C.F.R. §1024.37.

If a borrower provides proof of hazard insurance to the Servicer, it must cancel the force placed insurance and refund any premiums paid for overlapping periods when both policies were in place. 12 C.F.R. §1024.37(g)(1)-(2). The rule also provides that charges related to force placed insurance must be for services actually performed and must bear a reasonable relationship to the servicer's actual cost of providing such services. 12 C.F.R. §1024.37(h)(1)-(2).

Further, when a Servicer maintains an escrow account through which it pays the borrower's hazard insurance premiums, the servicer is prohibited from obtaining force placed insurance if it can continue the borrower's homeowners' coverage, even if that payment exceeds the balance in the escrow account. 12 C.F.R. §1024.37(a). The provisions of this rule are likely to prevent a lot of snowballing defaults when borrowers lose their insurance coverage, and a lot of very expensive bills for force placed insurance.

1. **E. Time Requirements for Response to Error Resolution and Information Requests**

Mortgage Servicers must quickly resolve complaints and share information. See 12 U.S.C. § 2605(k)(1)(C); 12 C.F.R. §1024.35. When borrowers write to their servicer to ask for information or to complain about certain errors, the servicer generally has five days to acknowledge their letter. 12 C.F.R. §1024.35(d). The servicer then, generally, has 30 to 45 days to fix the error and provide notice of the fix to the borrower or to send borrowers information they requested or investigate and explain why no error occurred or why the information is not available. 12 C.F.R. §1024.35(e).

1. **F. Required General Servicing Policies and Procedures for All Loans**

Mortgage Servicers must have and follow good customer service policies and procedures. 12 C.F.R. §1024.38. Servicers have to set up their business so they can: access correct information about borrowers' loan, respond

promptly and correctly to borrowers' problems, pass along correct information about their account when the servicer sells borrowers' loan servicing to another company, properly evaluate an application for relief if borrowers are having difficulties paying their loan and keep records for at least one year after borrowers pay off their loan (or the loan is transferred). The reasonableness of the servicer's policies is considered in light of the size, scope and nature of the servicer's operations. The objectives which the servicing policies are to be designed to achieve include:

- i. Accessing and providing accurate and timely information to borrowers, investors and the courts. 12 C.F.R. §1024.38(b);
- ii. Properly evaluating loss mitigation applications in accordance with eligibility rules established by investors. 12 C.F.R. §1024.38(b)(2);
- iii. Facilitating oversight of and compliance by service providers. 12 C.F.R. §1024.38(b)(3); and,
- iv. Informing borrowers of the availability of written error resolution information request procedures. 12 C.F.R. §1024.38(b)(5).

Servicers are required by the rule to maintain certain documents and information for each covered mortgage loan in a manner which allows the servicer to compile it into its servicing file within five days. 12 C.F.R. §1024.38(c)(2). There is an exemption for this requirement for small servicers. 12 C.F.R. §1024.30(b).

Beyond the above rules for all consumer loans, the following new rules deal with loans in default, notices, time frames and mitigation procedures. These rules significantly affect the process and time frame for foreclosure of delinquent loans. Therefore, any investor looking to buy properties with delinquent consumer mortgages, "short sale buyers", and investors who buy at sheriff's sales should be very familiar with the following rules. Some of these rules should reduce the number of consumer properties going through foreclosure. Others will separate owners who can modify their mortgages and keep their homes from those who can't. Finally, I believe some of these rules will delay foreclosures.

1. **G. Early Intervention with Delinquent Borrowers**

Mortgage Servicers must establish or make good faith efforts to establish live contact with borrowers to help them when they're having trouble making their payments. When a payment is missed, borrowers' mortgage servicer must try to contact them to talk about the situation no later than 36 days after their payment was due. Where appropriate, contact should also advise that loss mitigation options may be available. The servicer has

to give borrowers written notice about mortgage workout options that may be available no later than 45 days after borrowers are late on the payment. See 12 C.F.R. §1024.39.

The servicer must assign personnel to a delinquent borrower and make available to such borrower, via telephone, the assigned personnel to respond to the borrower's inquiries and assist borrower with available loss mitigation options. See 12 C.F.R. §1024.40. Small servicers are exempt from certain requirements of this rule. 12 C.F.R. §1024.30(b).

1. Continuity of Contact with Delinquent Borrowers Required

Servicers must maintain reasonable policies and procedures for its personnel assigned to assist borrowers with loss mitigation options. Policies and procedures must be designed to ensure that a servicer assigns personnel to a delinquent borrower by the time it provides written notice for early intervention, by the borrower's 45th day of delinquency. 12 C.F.R. §1024.40(a)(1).

Assigned personnel should be available to the borrower by phone to assist in loss mitigation options, including assistance with mitigation applications and timelines. 12 C.F.R. §1024.40(a)(2)-(3). Assigned personnel should also be able to access all of the information provided by the borrower to the servicer and provide that information, when appropriate, to the persons responsible for evaluating the borrower's eligibility for loss mitigation options. 12 C.F.R. §1024.40(b)(1)-(4). Small servicers are exempt from these requirements. 12 C.F.R. §1024.30(b).

1. I. Loss Mitigation Procedures

Mortgage Servicers must work with borrowers, if they are having trouble paying their mortgage, before starting or continuing foreclosure. To get help, borrowers must tell the servicer they are interested in a loan workout. The servicer will have borrowers submit an application that includes certain information. See 12 C.F.R. §1024.41(a)-(b); 12 U.S.C. §2605(f). Once complete, the servicer has five days to tell borrowers whether it needs more information and, if so, what information it needs. The Servicer must exercise reasonable diligence in obtaining documents and information to complete the application. Within 30 days after the completed application is submitted, as long as the application is received more than 30 days before the foreclosure sale, the servicer has to let borrowers know if there is an option to save their home. See 12 C.F.R. §1024.41(c).

Servicers' personnel must evaluate each borrower for all loss mitigation options available under the investor's guidelines including options for retention of the home (loan modification) and non-retention options (short sale or deed in lieu). 12 C.F.R. §1024.41(c)(i). The Servicer must provide the borrower with a written decision, including an explanation of the reasons for denying the borrower for any loan modification option offered by the investor. 12 C.F.R. §1024.41(c)(ii). The written explanation must include input used to make a net present value calculation if such input was a basis for denial of modification. See the official comments to 12 C.F.R.

§1024.41(d) for more of an explanation.

Borrowers must act fast. Once they're 120 days behind on their payments, the servicer can start the foreclosure process if borrowers haven't submitted a complete application. Mortgage Servicers must allow borrowers to seek review of the mortgage servicer's decision about borrowers' loan workout request. As long as borrowers sent in their loan workout application at least 90 days before their foreclosure sale, borrowers can seek review of the servicer's decision and the servicer has to assign the review to someone who was not involved in the initial decision. See 12 C.F.R. §1024.41(h).

The rule further restricts "dual tracking," where a servicer simultaneously evaluates a borrower for loan modifications or other mitigation alternatives while preparing to complete a foreclosure. The rule also specifically prohibits a servicer from making the first notice or filing required for a foreclosure process until a mortgage loan is more than 120 days delinquent. 12 C.F.R. §1024.41(f)(1)(i)-(iii). By contrast, Pennsylvania law allows the Act 6 and Act 91 notices to be sent when a loan is 2 months overdue, or at 60 days delinquency. 35 P.S. §1680.403(c).

Even if a borrower is over 120 days delinquent and the borrower submits an application for loss mitigation before the servicer has made the first notice or filing required for the foreclosure process, the servicer may not start the foreclosure process unless: i. The servicer informs the borrower that the borrower is not eligible for any loss mitigation options (and any appeal of the decision is exhausted). 12 C.F.R. §1024.41(f)(2)(i); or, ii. The borrower rejects all mitigation offers. 12 C.F.R. §1024.41(f)(2)(ii); or, iii. a borrower fails to comply with the terms of a loss mitigation option such as a trial modification. 12 C.F.R. §1024.41(f)(iii).

If the borrower submits a complete application for an available loss mitigation option after foreclosure has started but more than 37 days before the sale is scheduled to occur, the servicer may not, until one of the three

conditions listed above is met, commence a sale, move for a judgment, obtain an order for sale, or conduct a foreclosure sale 12 C.F.R. §1024.41(g). It is anticipated that these loss mitigation procedures will significantly slow the residential mortgage foreclosure process in both judicial foreclosure states like Pennsylvania and non-judicial states. However, Pennsylvania counties with foreclosure conciliation programs may consider abandoning those programs if the pre-judicial loss mitigation required by the rule makes the judicial procedures unnecessary.

The loss mitigation provisions have only a partial exemption for small servicers. Two loss mitigation requirements remain for small servicers. 12 C.F.R. §1024.41(j);

- i. Small servicers may not make the first notice or filing to commence foreclosure until the borrower is more than 120 days delinquent; and,
- ii. Small servicers may not proceed to foreclosure while a borrower is performing under the terms of a loss mitigation agreement.

If this article seems to you to be more technical and full of citations to the law than my usual articles, it is not your imagination. It is excerpted from materials I wrote for continuing education classes for lawyers on the subject. I taught these classes in Philadelphia, Harrisburg and Pittsburgh between February and May. The rules are complex, so my materials are somewhat complex, but worth learning if you buy distressed consumer mortgaged properties, or if you want to provide mortgage or installment land contract financing to consumers on properties they buy from you.

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