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CFPB Order Offers Insight Into Pandemic Mortgage Servicing

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The U.S. Consumer Financial Protection Bureau in December issued a consent order based on alleged violations of its 2014 mortgage servicing regulations.

The consent order, which also bootstraps claims of unfairness and deception to alleged technical violations of the servicing regulations — principally adopted under Section 6 of the Real Estate Settlement Procedures Act — creates a remediation framework that financial institutions servicing mortgage loans should consider as they navigate the COVID-19 pandemic and prepare to work through the likely backlog of loans awaiting foreclosure once federal and state moratoria end.

The CFPB's Mortgage Servicing Consent Order

The violations at the heart of the consent order stem from what the bureau said was "widespread failure" in how Seterus Inc., a mortgage servicer, allegedly handled loss mitigation applications from borrowers seeking to avoid foreclosure. The order focused on alleged errors in acknowledgement notices that Seterus sent to the borrowers.

These notices — prescribed by Title 12 of the Code of Federal Regulations, Section1024.41(b)(2) — are critical for borrowers because they indicate the documents a borrower must deliver to a servicer to receive an evaluation for loss mitigation options.

RESPA's implementing regulation, Regulation X, generally prohibits a mortgage servicer from offering a loss mitigation option on the basis of an incomplete loss mitigation application, and borrowers who receive inaccurate information regarding what and when they must submit are effectively stymied.

The order required Seterus' successor, Kyanite Services Inc., to set aside approximately $5 million for consumers harmed by the violations described in the order. Consumers who initially received a faulty acknowledgement notice but subsequently received an accurate one more than 60 days before the foreclosure sale, were not included in the remediation population.

Within the remediation population, the consent order set aside an average of $175 for the 10,743 affected consumers who were not foreclosed on, and an average of $2,500 for 1,121 affected consumers who were. It also set aside $250,000 for two borrowers who submitted the requested documents, were approved for a loan modification, but who ultimately went to foreclosure while the offer was pending.

Pandemic Relief Through Reg X

Under Regulation X, a servicer may define what documents and information a borrower must submit to create a complete loss mitigation application, but not what constitutes a loss mitigation application, complete or otherwise. Rather, the CFPB took the liberty to define that for servicers, stating that it is "an oral or written request for a loss mitigation option

that is accompanied by any information required by a servicer for evaluation for a loss mitigation option."[1]

On April 3, 2020, the prudential banking regulators, the Conference of State Bank Supervisors and the CFPB issued guidance making it clear that when a borrower requests assistance due to a COVID-19-related hardship and affirms the existence of that hardship that request constitutes a loss mitigation application.

That brought all subsequent servicer communications with these borrowers under the ambit of Section 1024.41, which sets forth a host of timing, disclosure and evaluation requirements for assisting borrowers with hardships.

While the agencies indicated some flexibility in how servicers complied with these technical requirements, such forbearance does not apply to private litigants, who have a right of action against servicers for violations of Section 1024.41.

RESPA and Reg X Limitations on Damages Available for Violations

One of the persistent challenges in enforcing consumer financial protection laws is that there is often a disconnect between the violation, and whether there was any harm as a result of the violation.

The enforcement of Section 1024.41, which governs default servicing, is particularly fraught because the issue at hand is whether a borrower keeps or loses their house. Clearly, foreclosures may carry economic and emotional harm or pain, but whether a specific violation constitutes causation is a separate question.

Servicers should be mindful that there are strict limits on their liability for a violation of RESPA and Regulation X. Section 1024.41 contemplates only two types of damages: actual damages and statutory damages of up to $2,000, when there is a "pattern or practice of noncompliance."[2] Actual damages are defined as those that "compensate the injured party for the injury sustained, and nothing more."[3]

A borrower must "present specific evidence to establish a causal link between" the violation and the damages alleged. In other words, actual damages can only be awarded to compensate for harms caused by RESPA violations, and "not harms generally resulting from a plaintiff's default and the foreclosure of his or her home."[4] In addition, costs incurred before the violation occurred cannot serve as the basis for actual damages.

Servicers that can differentiate actual harm of the technical violation from emotional difficulties of the foreclosure process are best equipped to challenge regulators' claims of unfairness and deception likely to accompany such charges.

Mitigating Risk and Harm From Technical Violations

Mortgage servicing since last March has been extremely complicated. As the country slid into its pandemic-induced lockdown, servicers mobilized suddenly remote workforces to help borrowers.

What began as a straightforward effort focused on borrower forbearance turned into a regulatory labyrinth as the pandemic wore on, with servicers mandated to follow ever-changing federal and state laws and regulations and navigate repeatedly updated investor guidelines.

Given that technical violations may have occurred during the rush to provide assistance, servicers should now consider taking steps to get in front of scrutiny likely to arise when the foreclosure process restarts, including:

- Confirming that communications sent out during the pandemic clearly articulated to borrowers their rights and remedies as part of the loss mitigation process;
- Verifying that letters sent by print vendors were accurate and printed as intended;
- Strengthening the preforeclosure referral process to ensure that consumers were invited to apply for loss mitigation and, if they eventually requested assistance, were provided the process set forth in Section 1024.41; and
- Conducting a root-cause analysis where issues are identified to catch other borrowers within their population who may have been affected by similar issues.

Institutions undertaking such efforts should be mindful of the potential for litigation and enforcement actions arising from remedial activities.

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[1] 12 C.F.R § 1024.31.

[2] Lage v. Ocwen Loan Servicing LLC, 839 F.3d 1003, 1011 (11th Cir. 2016) (citing 12 U.S.C. § 2605(f)(1)).

[3] Bray v. Green Tree Servicing, LLC, 2016 U.S. Dist. LEXIS 130940, at *8 (N.D. Tex. Sept. 26, 2016).

[4] Smith v. Specialized Loan Servicing, LLC, 2017 U.S. Dist. LEXIS 67782 (S.D. Cal. May 3, 2017).