Servicing Remains An Enforcement Target

The number of government enforcement and litigation actions focused on mortgage servicing grew significantly during and immediately after the financial and foreclosure crisis. Then, as servicers adapted to new regulations and major servicers adopted the requirements of the National Mortgage Settlement, the volume of such actions began to decrease. ¶ Many believe that key perceived problems in the mortgage industry have been solved, and that federal and state agencies have felt less need to bring actions as we move past the crisis.

But new enforcement and litigation actions have not disappeared, and enforcement agencies are clearly still paying close attention to mortgage activities, bringing actions on a variety of mortgage-related issues.

And while most of the highly publicized actions taken against mortgage lenders over the past two years have concerned mortgage origination—from False Claims Act lawsuits over lenders' underwriting of Federal Housing Administration (FHA)-insured loans to settlements resolving allegations that lenders engaged in prohibited redlining—servicing practices have not escaped the grasp of federal and state agencies.

This should not be surprising. During the crisis, the volume of foreclosures and the ongoing awareness of borrower distress greatly heightened the public's and agencies' perceptions of deficiencies in servicers' processes and oversight. Subsequently more stringent servicing regulations were promulgated by the Consumer Financial Protection Bureau (CFPB). They were designed to provide more transparency for borrowers and ensure that many of the alleged servicing shortcomings were not repeated.

The result has been ongoing careful monitoring of servicing issues. Thus, as an example, the CFPB's April 2016 *Monthly Complaint Report* noted that more than a quarter of the complaints it received from consumers over the last five years concerned mortgages (the second most-complained about financial product or service). More than 80 percent of those mortgage-related complaints are about servicing—e.g., difficulties making payments, confusion over servicing transfers or a lack of responsiveness to requests for information, according to the CFPB's April complaint report.

As agencies terminate (often with accompanying penalties) consent orders that imposed restrictions and systemic changes on mortgage servicing practices, they continue to focus on other servicing practices or purported deficiencies. As a result, agencies have seen a need to bring actions covering a wide variety of other servicing issues, including:

- foreclosure, loan-modification and loss-mitigation practices;
- loan servicing transfer requirements, including following through on loan-modification promises or application processes after a transfer of loan servicing, and ensuring systems compatibility between the old and the new servicer;
- vendor management practices, including monitoring the

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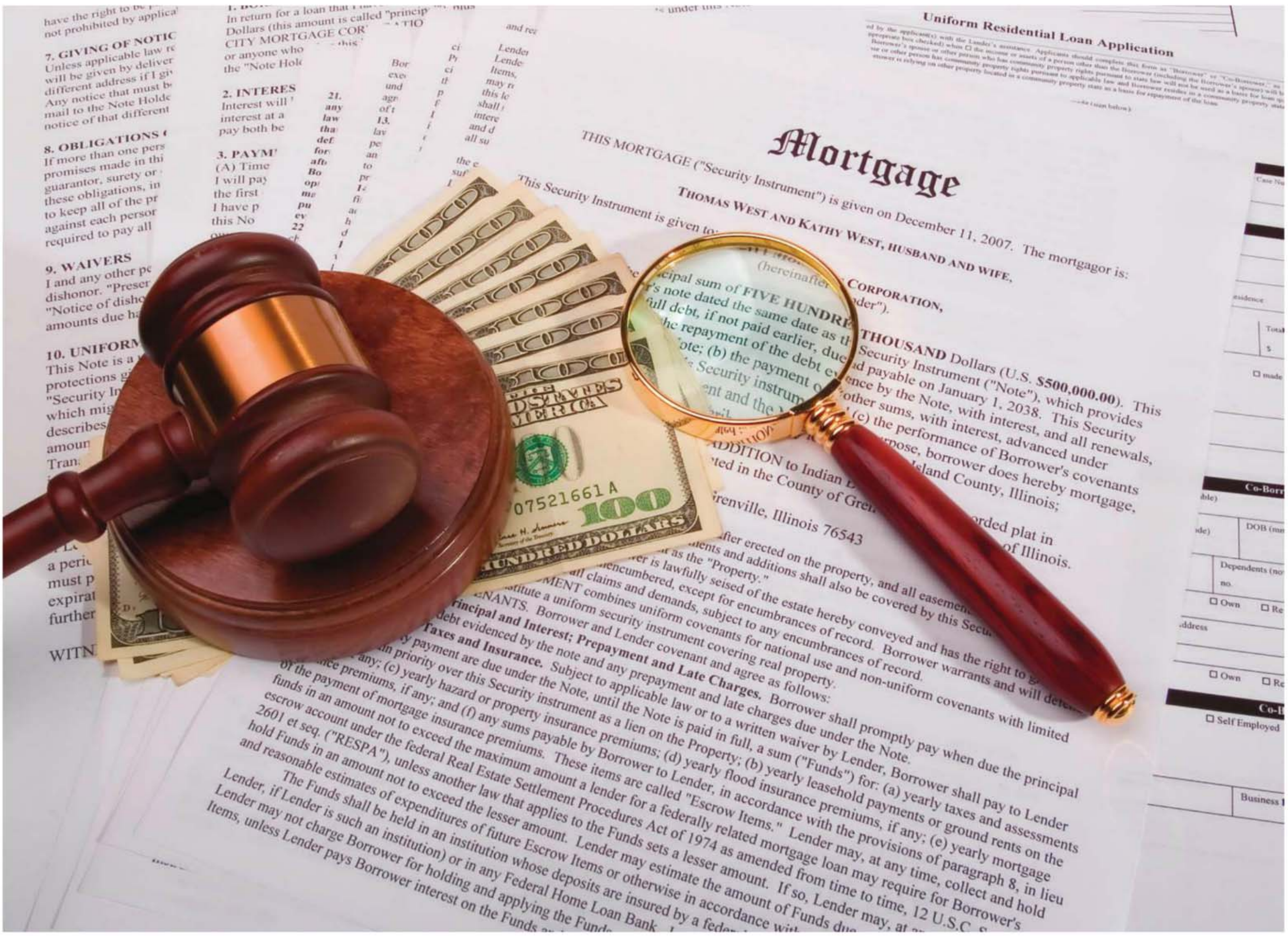
Given regulatory scrutiny, mortgage servicers must remain vigilant in implementing, operating and overseeing servicing processes.



representations made by a vendor to consumers;
- data security systems;
- Servicemembers Civil Relief Act (SCRA) requirements;
- responsiveness to agency information requests; and
- certifications and submissions to government agencies.

This article will examine recent key servicing-related government enforcement and litigation actions. It will both identify the areas where agencies have brought actions, and provide suggestions on the particular conduct targeted.

The National Mortgage Settlement and financial crisis-era enforcement actions

Mortgage servicers continue to settle enforcement actions stemming from the 2008 financial crisis. The Office of the Comptroller of the Currency (OCC) and other enforcement agencies have strictly enforced consent orders reached in 2011 and 2012 as part of the National Mortgage Settlement and similar actions taken against the largest mortgage servicers.

In February 2016, a mortgage servicer that did not participate in the National Mortgage Settlement—New York–based HSBC Bank USA and its affiliates—reached a $470 million settlement with the Department of Justice (DOJ), Department of Housing and Urban Development (HUD), CFPB and 49 states, based on allegations that HSBC engaged in abusive foreclosure-related practices such as robo-signing and failing to consider customers for loss-mitigation opportunities.

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Under the terms of the settlement, which are similar to those of the National Mortgage Settlement, HSBC is required to evaluate customers for loss-mitigation opportunities prior to foreclosure, postpone foreclosure proceedings while conducting its evaluation, review documents such as complaints and affidavits before filing them in court, and better manage third-party vendors used in the foreclosure process.

Meanwhile, other federal agencies have begun terminating crisis-era servicing and foreclosure-related consent orders while imposing substantial penalties in the process:

- In January 2016, the OCC imposed a $48 million penalty on New York–based JPMorgan Chase, alleging that between December 2011 and November 2013, JPMorgan Chase filed thousands of payment change notices in bankruptcy court that were untimely, signed by individuals who no longer worked at JPMorgan Chase or did not work in its bankruptcy division, or contained the wrong amount or date. In March 2015, JPMorgan Chase paid $50 million to the DOJ to resolve similar allegations.
- Also in January 2016, the OCC imposed a $1 million penalty on Jacksonville, Florida–based EverBank, alleging that between January 2011 and March 2015, EverBank "improperly charg[ed] fees related to MERS® assignments, property inspections, and post-acceleration late fees to approximately 47,833 borrowers" that were prohibited by earlier consent orders.
- In February 2016, the OCC terminated consent orders with Minneapolis-based U.S. Bank and Boston-based Santander Bank, but executed new consent judgments with each concerning alleged noncompliance. The OCC imposed a $10 million penalty on U.S. Bank, alleging that between October 2014 and August 2015, U.S. Bank had failed to establish appropriate deadlines for responding to loss-mitigation communications; identify a single point of contact for customers; and establish procedures governing complaints, prompt crediting of payments, and responses to foreclosure-related communications.

  The OCC also assessed a $3.4 million penalty against Santander Bank for its failure, between October 2014 and December 2015, to comply with a previous consent order's vendor-oversight provisions. Specifically, the OCC found that Santander failed to ensure that its policies and procedures for outsourcing foreclosures included due-diligence review of third parties and continuity and contingency plans in the event of long- or short-term disruptions in its vendor network.
- In May 2016, the OCC terminated its consent order with Sioux Falls, South Dakota–based Wells Fargo Bank, imposing a $70 million penalty based on allegations that, between October 2014 and August 2015, Wells Fargo either filed an untimely payment change notice or failed to file one at all on 84,480 accounts, causing further arrearages for 42,756 borrowers. The OCC also penalized Wells Fargo for making alleged escrow calculation errors on 76,720 accounts caused by an error in its proprietary loan software, resulting in 184 incorrect loan-modification denials.

The termination of these consent orders is not a signal that these issues are no longer of interest to federal agencies. To the contrary, the penalties imposed show that agencies are actively following up on prior consent orders and looking closely at how well servicers build out sustainable, compliant processes.

Servicers should assume that this type of follow-up—looking to see if processes are properly designed and implemented, and then if those processes are sustainable and maintained—will be a continued focus. In August, as this article went to press, the CFPB announced its Principles for the Future of Loss Mitigation, which sets forth principles—accessibility, affordability, sustainability and transparency—and more specific recommendations that servicers should review carefully.

Servicing transfers

Servicing transfers have long been in the crosshairs of federal and state agencies. Today we are seeing the CFPB target transfer-related issues such as successor servicers honoring in-process modifications, trying to determine whether these issues arise from systems incompatibility.

Servicing transfers was one of the issues discussed in the CFPB's June 2016 *Supervisory Highlights Mortgage Servicing Special Edition* report.

The CFPB found that "at one or more servicers, incompatibilities between servicer platforms led, in part, to transferees failing to identify and honor in-place loss mitigation after receiving the loans."

In addition to technological incompatibility, "one or more servicers failed to honor the terms of in-place trial modifications after transfer," and "[s]ome borrowers who completed trial payments with the new servicer nevertheless encountered substantial delays before receiving a permanent loan modification," the *Supervisory Highlights Mortgage Servicing Special Edition* reported.

This is a "growing point of emphasis" for the CFPB, according to the CFPB's *Supervisory Highlights Mortgage Servicing Special*

Edition, as evidenced by two recent enforcement actions.

In April 2015, the CFPB entered into a consent order with Green Tree Servicing LLC arising from allegations that Green Tree, according to the consent order, routed borrowers requesting loss mitigation to debt collectors; told borrowers that they had to make loan payments before they could be considered for a Home Affordable Modification Program (HAMP) modification; failed to respond to borrower requests to approve a short sale within the 30–45 days required by the Home Affordable Foreclosure Alternatives (HAFA) program; failed to recognize loan modifications that were in-process when Green Tree acquired the servicing rights, often because "[d]etailed loss-mitigation data is not part of the standard servicing data extract that Green Tree acquires from prior servicers"; and refused to investigate complaints concerning the validity of borrower data received from prior servicers.

The consent order imposed a $15 million penalty and required Green Tree to provide $48 million in redress to affected borrowers. In addition, Green Tree was required to honor loss-mitigation agreements entered into by prior servicers and adopt a "comprehensive data integrity program reasonably designed to ensure the accuracy, integrity and completeness of the data and other information about accounts that [the] defendant services, collects or sells, including any accounts acquired by or transferred to [the] defendant."

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In July 2015, the CFPB entered into a similar consent order with Fort Worth, Texas–based Residential Credit Solutions Inc., resolving claims that the servicer engaged in unfair and deceptive acts by failing to honor loan modifications agreed to by borrowers' previous servicers; provided incorrect information to borrowers about their modifications or payment information; sent incorrect escrow statements to borrowers; and illegally required borrowers to waive legal rights as a condition of receiving a modified payment plan.

To settle these allegations, Residential Credit agreed to pay $1.5 million in redress to affected borrowers and a $100,000 penalty to the CFPB. The CFPB also required Residential Credit to stop in-process foreclosures for certain borrowers, make temporary loan modifications permanent, and honor loss-mitigation agreements made between the borrower and previous servicer.

It is apparent that the CFPB looks to servicing transfer issues as part of its increased interest in servicing matters. As with the other issues discussed in this article, building viable, long-term transfer processes that are compliant with servicing rules is essential.

Vendor management

Vendor management has continued to draw agencies' attention. A clear example is the July 2015 CFPB settlement with Virginia Beach, Virginia–based LoanCare LLC and a mortgage payment processor. LoanCare was required to pay a $100,000 penalty (and the processor to refund $33.4 million to borrowers and pay a $5 million penalty) for deceptively advertising an electronic payment system that purported to allow borrowers, for an enrollment and per-usage fee, to reduce their interest payments and change their payoff schedule.

The CFPB found that only a small percentage of customers achieved the promised savings, and the savings were caused not by the electronic payment system but because customers ended up making higher annual mortgage payments.

This settlement indicates strongly that the heightened vendor management expectations now extend to marketing and advertising of service providers. Servicers must conduct due diligence of representations made by their vendors to borrowers and realize they may be held responsible for any vendor misrepresentations.

Data security

In the wake of several highly publicized data breaches, federal and state enforcement agencies have started targeting the data security practices of financial institutions like mortgage servicers.

Last November, the New York Department of Financial Services (DFS) released voluntary (for now) cybersecurity guidelines for financial institutions, recommending that they adopt strict data security protocols, including "standards reasonably designed to ensure the security of all applications utilized by the entity" and "policies and procedures to ensure the security of sensitive data or systems that are accessible to, or held by, third-party service providers," according to a Nov. 9, 2015, letter to Financial and Banking Information Infrastructure Committee members from Anthony J. Albanese, DFS acting superintendent of financial services.

The California Department of Justice's February 2016 *Data Breach Report,* while proposing fewer concrete recommendations, also highlighted the need for "reasonable" data security procedures and vendor management.

In March 2016, for the first time, the CFPB took action on a data security issue, entering into a consent order with Des Moines, Iowa–based Dwolla Inc. related to security misrepresentations. The CFPB asserted that Dwolla misled customers about the quality of its data security system, even though no data security breach had occurred.

The CFPB maintained that Dwolla's misrepresentations amounted to deceptive acts or practices in violation of the Consumer Financial Protection Act. The CFPB found that Dwolla had assured customers that their transactions were "safe" and "secure," that their information was stored "in a bank-level hosting and security environment," and that Dwolla's data security practices "exceed[ed] industry standards."

The CFPB alleged that Dwolla had not adopted or implemented written, "reasonable and appropriate" data security policies, had failed to identify "reasonably foreseeable security risks," did not adequately train employees about security risks, stored or transmitted unencrypted data and failed to implement secure software development practices. To settle these charges, Dwolla agreed to pay a $100,000 penalty and adopt 10 "reasonable and appropriate" cybersecurity measures.

While some mortgage servicers like Fort Worth, Texas–based Roundpoint Mortgage Servicing Corporation and Winston-Salem, North Carolina–based BB&T Mortgage Servicing have reported data security breaches, in light of the CFPB's actions, mortgage servicers cannot assume that a lack of data breaches insulates them from an enforcement action.

Servicers should verify the security representations they and their vendors make to borrowers and engage in proactive and ongoing testing, oversight and risk management of their and their vendors' data security systems. In the event that these cybersecurity audits fail to prevent a data breach of servicers' or their vendors' systems, servicers should obtain a cybersecurity assessment from a third party, and comply with all federal and state reporting requirements.

Servicemembers Civil Relief Act

While the bulk of recent Servicemembers Civil Relief Act enforcement actions—including actions initiated by the California attorney general and DOJ—have concerned banks' collection of credit-card and auto-lending debts, servicers should ensure that their mortgage servicing practices fully comply with the SCRA.

The OCC in July 2015 entered a consent order with JPMorgan Chase, imposing a $30 million penalty for its failure to comply with the SCRA in connection with foreclosure procedures. The OCC found that JPMorgan had "[f]ailed to have in place effective policies and procedures across the bank to ensure compliance with the SCRA."

Specifically, the consent order targeted JPMorgan's alleged practice of filing affidavits in federal court concerning a customer's military service without reviewing the borrower's records to verify active-duty status. JPMorgan also allegedly failed to adequately supervise third parties, including outside counsel, who falsely certified that they had completed SCRA-compliant investigations.

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Regulatory examinations

Agencies have also pushed for more information from servicers in order to perform adequate examinations and oversight. In January 2015, after threatening to suspend its servicer license, the California Department of Business Oversight (DBO) entered into a settlement with Orlando, Florida–based Ocwen Loan Servicing LLC concerning its failure to provide examination information requested by the DBO.

The consent order alleged that Ocwen failed to cooperate fully with the DBO's examination, including specifically failing to produce more than 1,300 loan files requested by the DBO.

In addition to paying a $2.5 million penalty, Ocwen agreed to permit the DBO to select an independent third-party auditor to conduct a comprehensive review of its servicing practices to determine compliance with state and federal laws. Ocwen was also barred from servicing new California loans until the DBO was satisfied that it was completely capable of responding to future regulatory examination requests.

In Ocwen Financial Corporation's February 2016 SEC Form 10-K, it disclosed that the DBO had taken the position that Ocwen was in material breach of the consent order due to deficiencies in its onboarding activities for new California originations.

False Claims Act

Servicers have also been targeted by the recent spate of False Claims Act litigation:

- In June 2016, Ocwen disclosed in its SEC Form 8-K filing that it would pay $30 million to settle two False Claims Act lawsuits alleging that it had falsely certified compliance with the requirements of the FHA insurance programs and HAMP. While the lawsuits were filed by private parties, the DOJ intervened in each and will receive $15 million of the settlement.
- In September 2015, the DOJ announced that it had reached a $30 million settlement with Tampa, Florida–based Walter Investment Management Corporation over claims that its servicing of reverse-mortgage loans violated the False Claims Act.

HUD's Home Equity Conversion Mortgage (HECM) program insures reverse-mortgage loans, and the DOJ alleged that a Walter Investment Management subsidiary submitted false claims for debenture interest by failing to disclose that it had not obtained appraisals of insured properties within the required 30 days of the loan becoming due and payable. The DOJ also alleged that the subsidiary had submitted false reimbursement claims for unlawful referral fees by describing them as sales commissions.

This threat of False Claims Act litigation is yet another reason for servicers to be certain to have comprehensive processes and strong quality control and procedures for any certifications or submissions made to federal agencies.

The underlying message for servicers

Following the financial and foreclosure crisis, servicing regulations were enhanced, and agencies put greater scrutiny on servicer activities and processes. The recent servicing enforcement actions and lawsuits highlight a number of factors servicers must consider as they face this stepped-up scrutiny.

First, while many recent enforcement actions and lawsuits concern mortgage originations, mortgage servicers should not conclude that enforcement agencies will not continue to scrutinize servicing matters. The actions discussed in this article show that government agencies remain attentive to servicing issues.

Second, it is clear that the servicing emphasis by enforcement agencies runs across a wide range of servicing issues—from foreclosure and loss mitigation to vendor management and data security. Thus, servicers must look to maintain compliant functions across the entire servicing spectrum.

Third, in looking at servicer processes, agencies will not simply focus on whether a process or procedure is designed in a compliant manner. More and more, they are focusing on the longer-term sustainability of compliant processes—are the oversight and management controls around the process designed to ensure that the process and procedures remain complaint and functional on an ongoing basis?

Finally, agencies will not simply focus on direct customer-touching processes. As the data security and vendor management matters discussed here reveal, the back-office or second-layer processes that create risks for borrowers will be closely examined. MB

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