CFPB Mortgage Industry Reforms – Rulemaking and Guidance

Katalina M. Bianco, J.D. — Senior Attorney-Editor
Richard Roth, J.D. — Senior Attorney-Editor

Wolters Kluwer
Law & Business

CFPB Mortgage Industry Reforms – Rulemaking and Guidance

INTRODUCTION

The Consumer Financial Protection Bureau was created by the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act with the intention of improving consumer financial protection by consolidating in one agency rulemaking, supervision and enforcement authorities relating to consumer financial laws, including many of those relating to mortgage lending.

Before the financial crisis, many bank and nonbank mortgage lenders weakened their underwriting standards and made mortgage loans to homebuyers who could not afford them or engaged in abusive lending practices. After many homeowners were unable to make their mortgage payments, many of these mortgages went into default and led to widespread foreclosures. To address these consumer financial protection failures, the Dodd-Frank Act created the CFPB.

Mortgage-Related Bureau Activities

Even before its official start date of July 21, 2011, the CFPB began to focus on the mortgage industry, launching its "Know Before You Owe" initiative in May 2011 to request consumer and industry feedback on integrated mortgage disclosures.

Beginning with Richard Cordray's appointment as director of the bureau in January 2012, the CFPB has exercised its rulemaking authority under Sec. 1022 of the CFPA (12 USC 5512) to issue an avalanche of mortgage-related consumer compliance rules, all of which were adopted as final in January 2013.

Complementing the mortgage rules was guidance issued by the bureau in 2012, including the Mortgage Servicing Examination Procedures, as well as guidance directed to consumers on mortgage-related issues published on the bureau's website.

RULEMAKING

The weeks of January 7 and 14, 2013, saw the Consumer Financial Protection Bureau, in conjunction with the other federal financial regulatory agencies, adopt a series of new rules that will remake the mortgage lending industry in the United States. The rules, which will apply to mortgage originating, underwriting and servicing, all are required by the Dodd-Frank Act's amendments to the Truth in Lending Act, Real Estate Settlement Procedures Act and Equal Credit Opportunity Act. The rules take effect in January 2014, except that a rule on escrow accounts will be effective June 10, 2013.

The seven separate rules cover:

- mortgage underwriting standards, including borrowers' ability to repay;
- permissible practices and homeownership counseling requirements for high-cost mortgages;
- escrow account requirements;
- appraisals for higher-risk mortgages under TILA;
- appraisals for all mortgages secured by dwellings under ECOA;

- loan originator compensation and character and fitness standards; and
- mortgage loan servicing.

Underwriting Standards

The CFPB's ability-to-repay rule is intended to protect consumers from entering into mortgages they cannot reasonably afford to repay. It specifies factors that lenders are expected to consider when deciding whether a consumer qualifies for a loan, and creates two categories of "qualified mortgages"—mortgage loans that are presumed to meet the ability-to-repay standards and thus permit only limited subsequent challenges by borrowers. One consequence of the rule will be the elimination of low- or no-documentation loans—pejoratively called "liar loans"—according to the bureau.

Ability to Repay—While the rule does not mandate that mortgage lenders must use any specific underwriting model, it does impose minimum standards for ability-to-repay determinations. In general, lenders must consult reasonably reliable third-party records to determine a loan applicant's:

- current or reasonably expected future income and assets;
- employment status;
- expected monthly loan payment;
- monthly payments on any other loans on the same property;
- other monthly mortgage-related obligations;
- current required payments for debt, child support and alimony;
- monthly debt-to-income ratio or monthly residual income; and
- credit history.

The rule also imposes duties on how these factors are to be applied. For example, monthly payments are to be calculated based on the assumption that the loan will be repaid by equal monthly payments over the term of the loan; if the loan has an adjustable interest rate, the payments are to be calculated based on the higher of the fully-indexed rate or an introductory rate. However, special calculation assumptions apply if the loan has a balloon payment, or if it allows interest-only payments or negative amortization.

Qualified Mortgages—Under the Dodd-Frank Act, a lender that makes a qualified mortgage enjoys a presumption that it properly carried out the ability-to-repay analysis. However, the bureau noted that the act did not specify whether this was a rebuttable presumption, or a conclusive presumption (a "safe harbor"). As a result, the rule offers both—a safe harbor for most loans, but only a rebuttable presumption of compliance for higher-priced loans. This is intended effectively to provide separate treatment for prime loans and subprime loans, according to the CFPB.

In the case of a subprime, or higher-priced, loan a consumer could show a violation of the rule by proving that his income and debt obligations did not leave enough money to cover his living expenses at the time the loan was made. However, the longer the consumer has been able to stay current on the loan, the less likely he will be able to show a violation, the bureau noted.

It will be harder, but not impossible, for a consumer to show that a qualified mortgage prime loan violated the ability-to-repay rule. To challenge such a loan, the consumer would need to show that the loan actually did not meet the definition of a qualified mortgage.

The rule adopts the Dodd-Frank Act criteria for what constitutes a qualified mortgage. Many of those criteria are negative, focusing on features the loan may not have. A qualified mortgage cannot:

- permit negative amortization;
- allow interest-only payments;
- require a balloon payment;
- have a term of longer than 30 years;
- be a no- or low-documentation loan; or
- require the payment of points and fees that exceed 3 percent of the total loan amount (with an exception for bona fide discount points paid on prime loans).

Included in the rule are some underwriting standards for qualified loans. In general, monthly payments must be calculated based on the highest payment that could be required during the first five years of the loan. Also, the borrower cannot have a debt-to-income ratio of less than or equal to 43 percent.

The ability-to-repay rule also addresses three other issues:

The CFPB noted that some borrowers can manage a debt-to-income ratio of higher than 43 percent. However, these situations should be examined under an individual ability-to-repay analysis instead of under a presumption, the CFPB said.

In order to encourage mortgage lending, the rule establishes an additional temporary category of qualified mortgages. A mortgage that satisfies the general criteria for qualified mortgages and also the underwriting criteria of one of a number of federal agencies, including Fannie Mae and Freddie Mac, will be deemed to be a qualified mortgage but will enjoy more flexible underwriting requirements. This category will exist for no longer than seven years and could end sooner if the various agencies issue their own qualified mortgage rules.

Loans with balloon payments can be qualified mortgages if they are originated and held by a defined category of small lenders that concentrate their operations in rural or underserved areas. Such a loan must have a term of at least five years and a fixed interest rate, and it must satisfy basic underwriting standards set by the rule.

Other Rule Provisions—The Dodd-Frank Act also imposes several other mortgage lending restrictions that are implemented by the new rule. Prepayment penalties generally are prohibited, although they will be allowed for some fixed-rate qualified mortgages. Creditors will be required to maintain records showing their compliance with the ability-to-repay and prepayment penalty provisions for at least three years. Also, lenders are prohibited from attempting to evade the rule by structuring noncomplying loans as open-end credit.

Proposed Amendments—When the CFPB announced the new rule it simultaneously proposed amendments it said would "address potential adverse consequences of certain narrowly-defined categories of lending programs." One amendment would exempt from the rule some non-profit lenders, homeownership stabilization programs and federal or government-sponsored enterprise refinancing programs that already are subject to their own specialized underwriting criteria.

The second proposed amendment would establish a category of qualified mortgages for loans without balloon payments that are originated and held by small lenders. While this category would be similar to the rural balloon-payment qualified mortgage category, the CFPB said, it would not be limited in scope to rural or underserved areas. This proposal also would increase the permissible amount of points and fees that separate prime from subprime qualified mortgages.

Dates and Deadlines—The ability-to-repay rule will take effect on Jan. 10, 2014. If adopted, the proposed amendments will have the same effective date.

The ability-to-repay and qualified mortgage rule was published at 78 *Federal Register* 6408 on January 30, 2013. The proposed ability-to-repay amendments were published at 78 *Federal Register* 6622 on January 30, 2013.

High-Cost Mortgages

The CFPB's rule on high-cost mortgages implements expansions to the coverage of the Home Ownership and Equity Protection Act. HOEPA was amended by the Dodd-Frank Act to cover more loans and protect homeowners from certain loan features the bureau referred to as "risky." The rule also is intended to encourage, and in some cases require, consumers to obtain homeownership counseling through amendments to both Reg. Z—Truth in Lending (12 CFR 1026) and Reg. X—Real Estate Settlement Procedures (12 CFR 1024).

As amended, HOEPA now applies to most types of mortgage loans secured by a consumer's principal dwelling, including purchase-money mortgages, refinances, closed-end home-equity loans and open-end credit plans, the CFPB said. With some exceptions, such as reverse mortgages, a high-cost mortgage is one for which:

- the annual percentage rate exceeds the applicable average prime offer rate by more than 6.5 percent for most first-lien mortgages, or by more than 8.5 percent for a first mortgage if the dwelling is personal property and the transaction is for less than $50,000;
- the APR exceeds the applicable average prime offer rate by more than 8.5 percentage points for subordinate or junior mortgages;
- the points and fees exceed 5 percent of the total transaction amount or, for loans of less than $20,000, the lesser of 8 percent of the total transaction amount or $1,000; or
- the creditor can charge a prepayment penalty more than 36 months after the loan closing or such fees or penalties can total more than 2 percent of the amount prepaid.

The applicable average prime offer rate is an APR derived from the average interest rates, points and other loan pricing factors currently offered to consumers by a representative sample of lenders who make either fixed or variable-rate closed-end loans with low-risk characteristics. A table of such rates for a broad range of types of closed-end transactions is to be published by the CFPB on the Internet and updated at least weekly.

Lenders' Duties—The rule imposes a number of new consumer protection duties on lenders making high-cost loans:

- Balloon payments are generally, but not always, banned.
- Creditors cannot finance points and fees.
- Creditors cannot charge prepayment penalties.
- Late fees are restricted to 4 percent of the overdue amount.
- Fees for payoff statements are restricted.
- Fees for loan modifications or payment deferrals are banned.
- A creditor that originates a home equity line of credit must assess the borrower's ability to repay the loan.
- Creditors and mortgage brokers are prohibited from encouraging a consumer to default on a loan that will be refinanced by a high-cost mortgage.
- A creditor must obtain certification from an appropriate counselor that the borrower has obtained homeownership counseling before the loan can be made.

The rule also requires the lender to give most loan applicants a list of counseling organizations in the applicant's area within three business days of the loan application. The list must be either from a website the bureau will develop or from information furnished by the bureau or the Department of Housing and Urban Development, and the information can be up to 30 days old. The bureau intends to develop a web portal that will allow lenders to generate a list based on each applicant's zip code. Home equity lenders are not covered by this requirement, as they already are subject to other counseling-related obligations.

In its description of the rule, the CFPB noted that the statute said the list should comprise counselors "located in the area of the lender." However, the agency has chosen to interpret the law as referring to "the location of the applicant being served by the lender."

Counseling is a prerequisite if a first-time borrower is applying for a mortgage that will permit negative amortization.

The rule takes effect Jan. 10, 2014.

The Reg. Z high-cost mortgage and homeownership counseling amendments and Reg. X homeownership counseling amendments were published at 78 *Federal Register* 6856 on January 31, 2013.

Escrow Accounts

The rule on escrow accounts has three main features, the CFPB said:

1. Regulations that currently require creditors to establish and maintain an escrow account for one year after the loan closing will be extended to require the account be maintained for five years.

2. Some small creditors that operate predominately in rural or underserved areas will be exempt from escrow account requirements if they intend to hold the loans in their portfolios rather than sell them.

3. The current exemption for escrow accounts that cover insurance on condominiums will be expanded in situations when there is a master insurance policy in place.

The rule takes effect June 1, 2013.

The Reg. Z escrow account amendments were published at 78 *Federal Register* 4726 on January 22, 2013.

Appraisals for Higher-Risk Mortgages

The federal financial regulatory agencies—the CFPB, Federal Deposit Insurance Corp., Office of the Comptroller of the Currency, Federal Reserve Board, National Credit Union Administration and Federal Housing Finance Agency—have jointly adopted amendments to several of their real estate lending consumer compliance regulations that implement amended appraisal requirements for higher-risk mortgages. The amendments principally will affect Reg. Z—Truth in Lending (12 CFR 1026), but also will apply to the agencies' other real estate appraisal rules.

A higher-risk mortgage is defined by the rules as a residential mortgage loan that is secured by a consumer's principal residence and that has an annual percentage rate that exceeds the defined average prime offer rate:

1. by at least 1.5 percent in the case of a first-lien loan with an original principal of no more than the limit for a home of the same size that is set under the Federal Home Loan Mortgage Corporation Act (a "conforming mortgage loan");
2. by at least 2.5 percent in the case of a loan that is comparable to the first category except that the original principal exceeds the limit (a "jumbo mortgage loan"); or
3. by at least 3.5 percent in the case of any subordinate-lien loan.

Several types of loans will be excluded from the rule's coverage. Excluded loans will include qualified mortgages as defined in the ability-to-repay rule; qualified reverse mortgages; loans secured by new manufactured homes, mobile homes, boats or trailers; and construction loans and bridge loans with maturities of less than a year.

Lenders' Duties—The amendments will impose several obligations on a lender that originates a covered loan. The lender will be required to:

- obtain a written appraisal by a certified or licensed appraiser who has physically inspected the interior of the property;

- at the time of application, inform the consumer of the purpose of the appraisal, the consumer's right to a copy of any written appraisal and the consumer's right to hire another appraiser; and
- give the consumer a copy of all written appraisals the lender has obtained at least three business days before the closing.

Additional Appraisals—Additionally, the lender will be obligated to obtain an additional written appraisal from a different appraiser without an additional charge to the consumer if the consumer will use the loan to buy a principal residence that was the subject of a prior sale, at a lower price, during the previous 180 days. The additional appraisal will be required if either of two thresholds is reached:

1. The seller is reselling the property within 90 days of acquiring it and the resale price exceeds what the seller paid by more than 10 percent; or

2. The seller is reselling the property within 91 to 180 days of acquiring it and the resale price exceeds what the seller paid by more than 20 percent.

This additional appraisal will be required to include an analysis of the price difference, any changes in market conditions and any improvements made by the seller.

An appraisal obtained in connection with the seller's purchase of the property cannot be used to satisfy the additional appraisal requirement; in other words, two new appraisals are needed.

In their description of the rules, the agencies explained that the use of *appraisal* rather than *second* appraisal was intentional. The intent was to avoid the implication that the two appraisals had to be ordered sequentially. A lender is free to order both appraisals at the same time.

The agencies also noted that the two-appraisal requirement may present a dilemma for lenders—if the two appraisals yield different values, which should be used to make the credit decision? The agencies explicitly declined to answer that question. Rather, they said that under other sections of TILA, a lender was obligated to use its discretion to select what it considered to be "the most reliable valuation."

There are a number of exceptions to the two-appraisal requirement. These include purchases from a seller who acquired the property: from a government agency; through a foreclosure or comparable means; as an inheritance or through the dissolution of a domestic relationship; from some described non-profit agencies; from a seller that acquired the property as part of an employee relocation; or from a servicemember who was deployed or relocated after purchasing the property. Properties in described disaster areas or rural counties also are exempt.

The rule will take effect Jan. 18, 2014.

The interagency notice was published at 78 *Federal Register* 10368 on February 13, 2013.

Appraisals for All Mortgages

The CFPB supplemented the rule on appraisals for higher-priced mortgages with another rule covering all mortgages that are secured by a first lien on a dwelling. The rule jointly adopted with the other financial services regulatory agencies implemented Dodd-Frank Act amendments to TILA, while the second implements amendments to ECOA. A joint rulemaking was not required by the ECOA amendments, the bureau noted.

The bureau described four main points of the rule:

1. Creditors must, within three business days of when a loan application is received, tell the applicants of their right to receive copies of all appraisals.
2. Creditors must provide copies of all appraisals or other written valuations as soon as they are completed or at least three business days before the loan closes, whichever is earlier. In the case of open-end credit, the appraisal must be provided at least three days before the account is opened.
3. An applicant may waive the delivery deadlines; however, in that case, the appraisals or written valuations must be delivered no later than when the loan closes or the account is opened. If the creditor denies the application, the copies still must be provided, but the deadline is 30 days after the creditor's decision.
4. Creditors may charge consumers a reasonable fee for obtaining appraisals if doing so is permitted by other laws, but they may not charge for providing the written copies.

The notice of the right to copies of written appraisals required by the TILA rule can be combined with the notice required by this rule, the CFPB added.

Prior to the ECOA amendment, a lender was obligated only to inform consumers that they had a right to a copy of an appraisal if they requested it. However, creditors could alternatively provide all consumers with copies. The ECOA amendment requires that copies must be given in all cases.

The rule takes effect Jan. 18, 2014.

The CFPB rule was published at 78 *Federal Register* 7216 on January 31, 2013.

Compensation, Qualifications, Arbitration

A rule intended to prevent mortgage lenders from steering borrowers into risky and high-cost loans also was adopted. The rule operates through compensation restrictions and character and fitness standards for loan originators. Due to a broad definition of what a loan originator is, the rule has broad applicability.

The rule also generally prohibits the use of mandatory arbitration clauses in both mortgage and home equity loan agreements.

According to the CFPB, the rule clarifies the existing prohibition on basing a loan originator's compensation on the terms or conditions of the loan transaction. A "term of a transaction" is defined as "any right or obligation of the parties to a credit transaction." Interest rates and the purchase of title insurance from an affiliate of the broker were given as examples of terms.

The amount of credit extended is not deemed to be a term of the transaction, as long as the compensation is based on a fixed percentage of that amount.

The rule generally bans basing compensation on the profitability of a loan or of a pool of loans. However, provisions are included to permit the consideration of profitability in retirement and profit-sharing plans.

Evasion—Several provisions are included in the rule that are intended to prevent evasion. First, an originator's compensation cannot be based on a proxy for any term of the transaction. A proxy is a factor that varies consistently with a transaction term over a significant number of loans and that the originator can add, drop or change when originating a loan. Compensation also cannot be reduced to offset the cost of a change in transaction terms. An exception to this prohibition allows originators to reduce their compensation to reduce the effect of unexpected settlement cost increases.

Comments to the rules list a number of compensation methods that will not be deemed to be proxies. These include methods such as basing compensation on the total value or number of transactions delivered by a loan originator, the long-term performance of the loans, an hourly rate that reflects hours actually worked, the quality of the originator's files or the percentage of loans submitted that are consummated.

Dual Compensation—The rule continues the existing prohibition on dual compensation, saying that a loan originator who is paid by a consumer cannot receive compensation from anyone else for the same transaction. An exception to the prohibition allows brokers to pay employees or contractors commissions, as long as the commissions are not based on a transaction term.

Another exception permits borrowers to pay upfront points and fees to the originator even when the originator receives compensation from another person. A prohibition on this practice was included in the Dodd-Frank Act, but so was the authority for the CFPB to allow the payment of points and fees if doing so would benefit consumers and be in the public interest. The CFPB said the current exemption will give it an opportunity for further research into the issue, so the exemption may be modified or ended in the future.

Originator Qualifications—Loan origination companies will be required to ensure that their individual originators are licensed or registered as required by the Secure and Fair Enforcement for Mortgage Licensing Act or any other applicable law. Banks and other organizations that are not subject to the SAFE Act registration requirements must ensure that their originators meet character, fitness and criminal record standards comparable to those of the act and must provide them with appropriate training.

The rule also incorporates the obligation for originators to include their unique Nationwide Mortgage Licensing System and Registry identifiers, and their names, on loan documents.

Prohibited Loan Terms—Dodd-Frank Act prohibitions on several specific loan terms also are part of the rule:

- Mandatory binding arbitration clauses are prohibited for mortgage loans and home equity credit lines.
- Terms that would prevent a consumer from suing over an alleged violation of federal law are prohibited.
- Premiums or fees for credit insurance in connection with a loan secured by a dwelling cannot be financed; however, monthly premiums are permissible.

Most provisions of the rule take effect Jan. 10, 2014; however, the provisions relating to prohibited loan terms take effect June 1, 2013.

The CFPB rules were published at 78 *Federal Register* 11279 on February 15, 2013.

Compliance Guidance

As part of its Supervision and Examination Manual, the CFPB established mortgage loan originator examination procedures. These procedures were the first step in extending federal supervision of mortgage lending to lenders, brokers and others who were not affiliated with federal financial institutions. The bureau noted at the time that these companies included many of the largest subprime mortgage lenders before the housing market collapse.

The bureau also adopted procedures to examine for SAFE Act compliance. These procedures cover registration requirements, the use of unique identifiers, and criminal background checks.

In addition, the CFPB made clear its intent to continue vigorous enforcement of the ECOA through use of the disparate impact doctrine (see CFPB Bulletin 2012-04). This long-standing legal doctrine, also referred to as the “effects test,” allows an enforcement agency or consumer to prove that a lender has engaged in discriminatory conduct in the absence of overt evidence of discrimination or evidence of disparate treatment on a prohibited basis. Instead, a practice that has a disproportionately negative effect on a prohibited basis can be found to be illegal unless it meets a legitimate business need that cannot be met by another method that has a less disparate effect. It is irrelevant that the lender has no intent to discriminate or that the practice appears neutral on its face.

Mortgage Servicing

The last of the rules establishes duties that are intended to protect consumers from mortgage servicer practices the bureau deems abusive or detrimental. The provisions are contained in amendments to Reg. Z and Reg. X. The CFPB said that the rules include reduced duties for companies that service 5,000 or fewer mortgages that they or an affiliate originated or own, which will reduce the compliance burden for community banks and credit unions.

The rules cover nine general topics relating to mortgage servicing. Six of these have broad applicability, while the other three focus specifically on how servicers are to deal with consumers who are in default.

General Servicing Requirements—The mortgage servicer obligations that will apply across-the-board include:

Periodic statements—Consumers must be given a periodic statement for each billing cycle. The statement is to include information on payments, fees, transaction activity, how previous payments were applied and any delinquencies. Contact information for the servicer and for housing counselors also must be included. If the loan is a fixed-rate loan, the servicer has the option of providing a coupon book, but the book also must meet specified requirements. The rules provide sample forms that servicers may use to comply with their duties.

Small servicers are exempt from the periodic statement requirements.

Interest rate adjustments—Two notices that must be given to consumers who have adjustable-rate notices are described. One notice must be given between 210 and 240 days before the first payment is due after the first interest rate adjustment, and this notice must provide an estimate of the new rate and new payment. A different notice must be given between 60 days and 120 days before a payment is due if an interest rate adjustment causes the payment amount to change. The CFPB noted that servicers no longer will need to provide annual notices if the payment does not change.

Crediting payments and payoff statements—The rules define a "periodic payment" as the total of principal, interest and any required escrow amounts, and require servicers to credit periodic payments to a consumer's account as of the day of receipt. A payment of a lesser amount does not qualify as a periodic payment and can be held in a suspense account until the total in the suspense account equals a periodic payment. At that time, the periodic payment must be credited to the consumer's account.

A consumer must be given an accurate payment statement within seven business days of the servicer's receipt of a written request.

Force-placed insurance—A servicer cannot charge a consumer for force-placed insurance unless the consumer has been given specified notices and the servicer has a reasonable basis to believe that the consumer has not kept the property insured as required. The first notice is to be sent at least 45 days before the charge is imposed, and the second notice is to be sent at least 30 days after the first notice and at least 15 days before the charge is imposed. If the consumer proves that insurance was in place, the servicer must cancel any policy it obtained and refund any premiums that were charged for the time that the consumer's policy was in effect.

In most cases, the rules require that force-placed insurance charges must be for a service that actually was performed and be reasonably related to the servicer's cost of providing the service. The rules also provide that, if there is an escrow account to cover insurance, the servicer must continue the consumer's policy rather than force-placing insurance, even if the servicer needs to advance funds to the escrow account to do so.

Small servicers are subject to a less restrictive rule. A small servicer may charge a borrower for force-placed insurance if the cost to the borrower is less than what the servicer would need to disburse from the escrow account to keep the consumer's policy in effect.

Error resolution and information requests—The rules set requirements for how servicers must respond to consumers' requests for information or claims of servicing errors. In general, a servicer is to acknowledge the consumer's communication within five days. Within 30 to 45 days, the servicer is to investigate any claimed error and either correct the error and notify the consumer or complete its investigation and inform the consumer why there was no error. The same time periods apply to information requests.

Policies and procedures—Each servicer must have policies and procedures reasonably designed to meet the rules' goals. These policies and procedures are to be appropriate for the servicer's size and scope and the nature of its operations, but they must enable a servicer to compile specified documents into a "servicing file" within five days.

Small servicers are not required to create specific servicing policies and procedures.

Protections for Distressed Consumers—In explaining the rules, the CFPB observed that the mortgage servicing industry "was built to handle large volumes of loans for which only limited service was required." As a result, the industry as a whole was not equipped to deal with the large volumes of delinquencies and foreclosures that resulted from the financial crisis, and many consumers "suffered substantial harm." The new rules address three aspects of this problem.

Early intervention—If a borrower becomes delinquent, a servicer has 36 days to make a good faith effort to establish "live contact" and tell the borrower that loss mitigation options may be available. A written notice giving information about loss mitigation options must be given within 45 days of the beginning of the delinquency.

Small servicers are exempt from the early intervention requirements.

Continuity of contact—A servicer's written policies and procedures must be reasonably designed to ensure that specific personnel are assigned to the borrower's account by the time the written delinquency notice is given. The borrower is to be able to speak to the assigned persons by telephone, and the assigned persons must be able to give the borrower information on loss mitigation options, applications and timelines. The rules require that the assigned personnel must have access to all of the information they need to be able to answer the borrower's questions, and they also must be able to pass the information on to anyone who is evaluating the borrower's eligibility for loss mitigation options. The bureau noted that these requirements will be enforced only by the federal regulatory agencies; consumers will have no right to sue servicers for violations.

Small servicers are not required to comply with the continuity of contact requirements.

Loss mitigation—Specified loss mitigation procedures will be required if a mortgage loan is secured by the borrower's principal residence, but the rules do not require that any specific loss mitigation options be offered. A borrower's application must be acknowledged within five days of its receipt. The acknowledgment is to either tell the borrower that the application is complete or, if it is not, tell the consumer what additional information is required. If a complete application is received more than 37 days before a scheduled foreclosure sale, the servicer has 30 days to evaluate the borrower for all loss mitigation options offered by the servicer for which the borrower might be eligible. This includes both options that would allow the borrower to keep the home and options such as short sales. The borrower must be given a written decision and, if the application is denied, the reasons for the denial must be stated. A borrower can appeal a denial if he filed a complete application at least 90 days before a scheduled foreclosure sale.

The rules also restrict a servicer's ability to evaluate a borrower for loss mitigation options and move toward foreclosure simultaneously. The initial notification or filing in the foreclosure process cannot take place until the loan is at least 120 days delinquent and, if a loss mitigation application is filed before that first step is taken, the servicer must complete its evaluation before it moves toward foreclosure. However, these restrictions do not apply if the borrower has been informed that he does not qualify for any loss mitigation options and any appeal has been resolved, loss mitigation options have been offered to the borrower and rejected, or an option has been accepted by the borrower but the borrower has failed to comply with its terms. Moreover, if a borrower files a complete application for loss mitigation after the foreclosure process has started but more than 37 days before the scheduled sale, the servicer may not move forward until at least one of the same criteria has been met.

Borrowers will have the right to sue servicers for violations of these parts of the rules, the CFPB said.

Small servicers are exempt from some parts of the rule requirements that are intended to protect consumers in danger of foreclosure. However, they may not start a foreclosure process until a loan is at least 120 days delinquent, and they may not move forward on a foreclosure in any way as long as a borrower is in compliance with a loss mitigation agreement.

The rules will take effect Jan. 10, 2014.

The Reg. X amendments were published at 78 *Federal Register* 10695 on February 14, 2013. The Reg. Z amendments were published at 78 *Federal Register* 10901 on February 15, 2013.

Compliance Guidance

The CFPB also has adopted mortgage servicer examination procedures, which are included in its Supervision and Examination Manual. These procedures cover servicers' obligations under RESPA, TILA, the ECOA, the Fair Debt Collection Practices Act, the Fair Credit Reporting Act and the Electronic Fund Transfers Act.

Specific guidance was issued jointly with the other regulatory agencies addressing the problems of servicemembers who have received permanent change of station orders (see Federal Reserve Board CA 12-8 and Federal Deposit Insurance Corporation FIL-28-2012, June 22, 2012). This guidance was intended to ensure that servicemembers were given timely and accurate information about their options and were not improperly asked to waive their rights under the Servicemembers Civil Relief Act or other consumer protection laws.

New Guidance on Mortgage Servicing

The bureau in early February tackled problems that were reported to be arising from the transfer of mortgage servicing rights. The CFPB said that it was going to begin to look closely at servicing transfers and warned that in some cases it would require servicers participating in "significant servicing transfers" to file informational plans that would describe how the resulting risks to consumers would be managed. Servicing transfers-related issues would be made a focus of supervisory activities, the bureau announced in CFPB Bulletin 2013-01.

According to the CFPB, it has received complaints that servicing transfers have interrupted loss mitigation efforts, either because the transferor has failed to transfer relevant documents or because transferees have not taken necessary steps to identify consumers who are engaged in trial loan modifications.

Three specific areas of examiner attention were described in the bulletin:

1. Servicing transferors will be expected to prepare for a transfer by ensuring that they transfer information in a way that is compatible with the transferee's systems. They will need to have systems in place before the transfer to ensure that the transferee is given enough information to continue servicing the loans properly and without interruption, and they must know in advance of the transfer how they will respond to subsequent consumer inquiries.
2. Transferees must have plans to ensure they provide complete and accurate information to consumers after the transfer. They must establish procedures to identify loans that were in loss mitigation plans at the time of the transfer. Also, transferees must have servicing platforms that accurately reflect information on the transferred accounts and they must train their employees in how to use those platforms properly. Finally, examiners will look at what post-transfer audits the transferee has performed.
3. The transferee must be given information on all loans that are in any loss mitigation program, including all relevant documents. The transferee must be prepared to continue any existing loss mitigation efforts as well as consider appropriate additional accounts for mitigation.

Significant Servicing Transfers—The CFPB did not give any guidance on what would constitute a significant servicing transfer, but it did set out what information it would require servicers to include in their plans. The bureau did not specify whether such a plan would be required of the transferor or the transferee, or whether it would be submitted jointly.

The required information usually will be:

- the total number of loans;
- the total unpaid principal balance of the accounts;
- the name and a description of the platform used by the transferor and information on its compatibility with the transferee's platform;
- information on the testing to be done to ensure that necessary information was transferred accurately;

- a description of how the transferee will identify and correct errors, including the relevant time period for doing so;
- a description of the transferee's employee training plan, including the training materials to be used; and
- a description of how the transferee will identify which accounts are subject to current loss mitigation efforts and respond to consumer inquiries.

OTHER MORTGAGE INITIATIVES

The Consumer Financial Protection Bureau has undertaken a number of mortgage-related initiatives since its inception. Some of these initiatives were in preparation for the mortgage rules the bureau proposed in 2012 and adopted as final in January 2013.

The bureau's projects also were in fulfillment of various objectives and functions enumerated in Sec. 1021 of the Consumer Financial Protection Act (12 USC 5511), such as ensuring that consumers receive understandable information in a timely fashion and providing financial education to assist consumers in making better financial choices.

Integrated Mortgage Disclosures

The Dodd-Frank Act requires the bureau to combine Truth in Lending Act and Real Estate Settlement Procedures Act disclosures. In preparation for rulemaking that would implement this requirement, the CFPB began to design prototype forms for testing in February 2011.

The goal of the testing was to create forms that contain clear and conspicuous disclosures about the consumer financial product or service, as required by the Consumer Financial Protection Act Sec. 1032(b)(2) (12 USC 5532(b)(2)).

In May 2011, the CFPB unveiled its "Know Before You Owe" initiative, an online program that provides information to consumers on a variety of topics relevant to consumer finances. The bureau posted the first two prototype loan estimates and asked consumers and mortgage industry members to examine them and comment on what aspects work for them as well as those that do not work well. The feedback was intended to help ensure that the disclosure actually helps consumers understand features of competing loan products, from the overall loan amount to estimates of taxes and insurance costs.

The bureau continued to post updates to its "Know Before You Owe" project as it refined the prototypes and began testing.

Testing of the prototypes was done in a number of cities across the country as the CFPB asked consumers and industry participants to respond to:

- graphic design approaches;
- prototypes with lump sum closing costs and itemized closing costs;
- closing disclosures;
- loan estimate forms; and
- sample federal disclosures documents.

To supplement the testing, the bureau issued a series of comment requests on disclosures, seeking to gather further input from the public, and convened a Small Business Review Panel to gather information from small businesses that make mortgage loans and conduct mortgage closings.

Once the bureau gathered information on the prototypes from the public and completed testing, it issued its proposed rule to implement the combined mortgage disclosures on July 9, 2012, published at 77 *Federal Register* 51116 on August 23, 2013.

Monthly Mortgage Statement

In February 2012, the CFPB sought public input on a draft monthly mortgage statement intended to assist homeowners in understanding their loans and avoiding unnecessary costs and fees.

The Dodd-Frank Act requires that most mortgage borrowers receive periodic statements containing specified information. Periodic statements generally must be provided by the creditor, assignee of the loan or the mortgage servicer that manages the loan. Most borrowers are to be informed monthly of:

- the loan principal balance;
- the current interest rate;
- the date on which the interest rate could reset, if applicable;
- late payment and penalty fees;
- how to obtain housing counseling; and
- how to contact the servicer.

As with its integrated mortgage disclosures prototypes, the CFPB tested a prototype monthly statement with consumers to make it as user-friendly as possible. The bureau also posted the prototype on its website to solicit general feedback.

After gathering information and refining the prototype in response to comments, the CFPB incorporated the statement into its proposed rule, published at 77 *Federal Register* 57318 on Sept. 17, 2012. Eventually, the monthly statement requirement became part of the mortgage servicer rules described above.

Reverse Mortgages

On June 28, 2012, the CFPB published a report to Congress highlighting consumer confusion in the reverse mortgage market and issued a request for information on consumer use of reverse mortgages.

"Reverse mortgages are complex and have the potential to become a much more pervasive product in the coming years as the baby boomer generation enters retirement," said CFPB Director Richard Cordray when the report was released. "With one in ten reverse mortgages already in default, it is important that consumers understand what they are signing up for and that it is the right product for them."

The reverse mortgage market study, required by the Dodd-Frank Act, found that the realities of the market greatly differ from what the intended purpose. Findings include the following:

- While consumers are largely aware of reverse mortgages, few completely understand them.

- Consumers are getting reverse mortgages at younger ages.
- Seventy percent of borrowers are taking out the full amount of proceeds as a lump sum rather than as an income stream or line of credit. This raises concerns that consumers who take out all of their accessible home equity upfront will have fewer resources available later in life.
- Older consumers may be receiving deceptive and misleading marketing materials about reverse mortgages. The bureau noted that it has seen examples of mailers that tout reverse mortgages as a government benefit or entitlement program like Medicare.
- The new array of product choices in the reverse mortgage market makes a housing counselor's job much more difficult. Counselors need improved methods for helping consumers better understand the complex tradeoffs they need to make in deciding whether to get a reverse mortgage.

To educate consumers on reverse mortgages, the CFPB posted questions and answers about reverse mortgages to its *Ask the CFPB* database, which can be found on the bureau's website. The bureau issued a request for information on consumer use of reverse mortgages to assist its study.

Consumer Complaints

A major undertaking by the CFPB has been the tracking of consumer complaints, many of which are mortgage-related. The most common type of mortgage complaints concerned mortgage loan modifications, collections or foreclosure. Other common types of mortgage complaints address payments, such as issues related to loan servicing, payment posting or escrow accounts. For example, consumers express confusion about whether making timely trial period payments will guarantee placement into a permanent modification. Issues related to applying for the loan, such as the application, the originator, or the mortgage broker, also are among the most common types of mortgage complaints.

In its Semi-Annual Report to Congress, released on July 30, 2012, the bureau noted that 43 percent of all complaints to date related to mortgages.

Appearing Sept. 13, 2012, before the Senate Banking Committee, CFPB Director Cordray said that mortgage-related complaints top the list of consumer grievances received by the CFPB, and their volume is expected to continue. Cordray said the number of complaints was not unexpected, but "it's hard work for us to keep up with it."

Consumer Complaint Database

The CFPA requires the bureau to establish procedures for timely responses by regulators to consumer complaints (Sec. 1034(a), 12 USC 5534(a)). These procedures must be "reasonable" and must be developed in consultation with the appropriate federal regulatory agencies.

To implement this requirement, the CFPB launched a public Consumer Complaint Database on June 19, 2012. Initially, the database included only data from credit card complaints. However, since the inception of the database, the CFPB expanded the data to complaints about other consumer financial products and services within CFPB jurisdiction, including mortgages.

The American Bankers Association called the database a "questionable—even misleading—resource," as it would include unverified data. The association asserted that complaint resolutions are best handled between the parties involved. Privacy and consumer groups, however, commented that the lack of verification presents only minimal risks to issuers because there are controls to ensure that complaints must come from actual account holders and creditors are given adequate time to dispute their identification. The CFPB says it "will allow the marketplace of ideas to determine what the data show."

According to the bureau, a company can respond to a complaint in four ways:

1. with monetary relief;
2. with non-monetary relief such as altered account terms, corrected submissions to a credit bureau or foreclosure alternatives;
3. with an explanation that substantively meets the consumer’s desired resolution or explains why no further action will be taken; or
4. without relief or explanation.

The Consumer Response Database prioritizes for review and investigation complaints in which the consumer disputes the response or in which companies fail to provide a timely response.

Consumer Response Team

The CFPB provided an overview of how its Consumer Response team handles complaints in an Oct. 10, 2012, report entitled “Consumer Response: A Snapshot of Complaints Received.”

In the report, the bureau explains that the Consumer Response team screens all complaints submitted by consumers based on several criteria. These criteria include whether the complaint falls within the CFPB’s primary enforcement authority, whether the complaint is complete, or whether it is a duplicate of a prior submission by the same consumer. Screened complaints are sent via a secure web portal to the appropriate company. The company reviews the information, communicates with the consumer as needed, and determines what action to take in response. The company reports back to the consumer and the CFPB via the secure company portal. The bureau then invites the consumer to review the response. Consumer Response prioritizes for review and investigation complaints in which the consumer disputes the response or where companies fail to provide a timely response.

Consumers can log onto the secure consumer portal available on the CFPB’s website or call the toll-free number to receive status updates, provide additional information and review responses provided to the consumer by the company. Throughout this process, the Consumer Response team is supported by CFPB colleagues who provide subject matter expertise and help monitor complaints involving certain groups.

Deceptive Practices

One of the stated objectives of the CFPB is to ensure that consumers are protected from unfair, deceptive or abusive acts or practices (Sec. 1021(b)), 12 USC 5511(b)). The bureau has taken steps to meet this objective by acting to halt mortgage-related actions it determines to be potentially deceptive or misleading.

Mortgage Modification Scams

One such area of deceptive practices targeted by the bureau in 2012 was mortgage modification scams. Specifically, the bureau targeted loan modification operations that attempt to disguise their false promises of relief for struggling homeowners with claims that they are performing legal work or are a law firm. The CFPB also is concerned with schemes that attract victims with false claims that they are endorsed by or represent the government. These tactics are used by mortgage relief scams to attract victims, add credibility to their schemes or exploit certain legal exemptions for the practice of law, according to the bureau.

In December 2012, the CFPB took steps to halt two alleged mortgage loan modification scams. The scams targeted financially distressed homeowners in danger of losing their homes, taking in $10 million by charging consumers for services that promised to prevent foreclosures, the bureau said.

The CFPB complaints allege that the defendants in both cases violated the Dodd-Frank Act and Regulation O, formerly known as the Mortgage Assistance Relief Services Rule. These laws prohibit unfair, deceptive or abusive acts or practices and protect distressed homeowners from mortgage relief scams.

The CFPB had requested that U.S. District Court Judges in California order a halt to both operations, the Gordon Law Firm and the National Legal Help Center, and freeze their assets while the bureau pursues cases against them.

Mortgage Advertisers

The CFPB also targeted mortgage advertisers for potentially misleading claims made to consumers. In conjunction with the Federal Trade Commission, the bureau in November 2012 sent warning letters to approximately 12 mortgage lenders and mortgage brokers advising them "to clean up potentially misleading advertisements, particularly those targeted toward veterans and older Americans."

The agencies warned of potential violations of the Mortgage Acts and Practices-Advertising (MAP) Rule, which targets misleading claims and statements in mortgage advertising as well as violations of the FTC Act.

Consumers were warned to be wary of ads that contain an official-looking seal or logo that implies some kind of government status. Promises of very low rates and assurances that a reverse mortgage will allow you to stay in your home payment-free are other warning signs to watch out for, as are announcements of pre-approval and offers of large amounts of available cash or credit, the agencies said.

The bureau also announced at that time that it had begun formal investigations of six companies that it thinks may have committed more serious violations of the law.

CONCLUSION

As the first federal agency tasked solely with the responsibility for regulating consumer financial protection in the United States, the CFPB has stated that its central mission is to make markets for consumer financial products and services work for Americans. In terms of the mortgage market, the CFPB has been active in taking steps that are intended to fulfill that mission.

In June 2012, Raj Date, then Deputy Director of the bureau, stated in a speech made during the American Bankers Association Annual Regulatory Conference that mortgage reform was "front and center" on the bureau's agenda. His statement clearly reflects the intense focus on mortgage-related consumer compliance that the CFPB has displayed through its promulgation of rules, issuance of guidance and consumer-driven initiatives intended to correct earlier failings in the regulation and supervision of the mortgage markets.

About the Authors

Katalina M. Bianco, J.D. — *Senior Attorney-Editor*

Katalina Bianco is a Banking Law Analyst at Wolters Kluwer Law & Business, a leading provider of banking information. She was the author of *Identity Theft: What You Need to Know* and a co-author of *Dodd-Frank Wall Street Reform and Consumer Protection Act, Law, Explanation and Analysis* and *Financial Services Modernization—Gramm-Leach-Bliley Act of 1999; Law and Explanation.* Bianco also authored *The Subprime Lending Crisis: Causes and Effects of the Mortgage Meltdown* and *Money Laundering and Mortgage Fraud: The Growth of a Merging Industry,* as well as several white papers for various banking trade associations. She is the lead editor of the *Consumer Financial Protection Bureau Reporter* and also contributes her editorial expertise to the *Federal Banking Law Reporter.*

Richard Roth, J.D. — *Senior Attorney-Editor*

Richard Roth also is a Banking Law Analyst at Wolters Kluwer Law & Business. He was a co-author of *Dodd-Frank Wall Street Reform and Consumer Protection Act, Law, Explanation and Analysis, Financial Services Modernization—Gramm-Leach-Bliley Act of 1999; Law and Explanation* and *Guide to Federal Privacy Rules for Financial Institutions.* Roth is the lead editor of the *Federal Banking Law Reporter* and the *Bank Compliance Guide.*

About Wolters Kluwer

Wolters Kluwer Law & Business, a unit of Wolters Kluwer, is a market-leading information services company providing research products and software solutions in key specialty areas for legal and business professionals, as well as casebooks and study aids for law students. Our markets include law firms, law schools, corporate counsel, health care organizations, and professionals requiring legal and compliance information.

Find Out More:
Global: wolterskluwer.com
Law & Business: wolterskluwerlb.com
Twitter: twitter.com/Wolters_Kluwer
Facebook: facebook.com/wolterskluwer
YouTube: youtube.com/user/WoltersKluwerComms

Dodd-Frank Act QuickCharts

Optional add-on tool for the ***Federal Banking Law Reporter*** and ***Federal Securities Law Reporter***—Internet

Wolters Kluwer
Law & Business

Understanding the Dodd-Frank Act and its ramifications

QuickCharts provide a clear, organized way to understand the numerous provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and keep track of ongoing new rule-making and regulations that arise from the new law.

The charts allow you to select and review key elements such as added, amended and/or repealed laws, effective dates and new agency guidance, opinions, rules and regulations.

Charts include links to the underlying primary source material contained in either the *Federal Banking Law Reporter* or the *Federal Securities Law Reporter.*

The charts in this comprehensive resource will continually be updated as new regulations are proposed and adopted to quickly guide you through the new law as it evolves. By analyzing, distilling and organizing this critical information in an easy-to-use format, you're assured of having critical information at your fingertips, saving hours of research time.

Every provision covered in the Dodd-Frank Act is organized by topic with a full menu of sub-topics for each—all with full analysis.

1. Introduction
2. Financial Stability Oversight
3. Orderly Liquidation Authority
4. Supervision of Depository Institutions
5. Private Fund Advisers
6. Insurance
7. Bank and Thrift Regulatory Improvements
8. OTC Derivatives
9. Clearing and Settlement
10. Investor Protection and Securities Regulation
11. Consumer Financial Protection
12. Strengthening the Federal Reserve
13. Access to Mainstream Finance
14. Pay It Back Act
15. Mortgage Reform and Anti-Predatory Lending
16. Miscellaneous Provisions

The charts feature:

- Links to full analysis of the Dodd-Frank Act
- Links to full-text of enacted law
- Links to laws added, amended or repealed
- Links to new rules, regulations and guidance
- Effective dates
- Results that may be exported to Excel or Word and also emailed
- Daily updates
- Highlighted updates (within the last 1, 7, 14, 30, 60, 90, or 120 days as selected)

A valuable add-on to your online subscription

There is a version of QuickCharts for the *Federal Securities Law Reporter* as well as the *Federal Banking Law Reporter*. A special bundle price is available for both versions of the Charts if you wish to see the Act's effects on both practice areas.

QuickCharts utilize our Smart Charts® technology and provide multiple features such as: quick custom chart creation, effective dates, links to primary source material and multiple export options

Wolters Kluwer Law & Business | 4025 W. Peterson Ave., Chicago, IL 60646 | 800 449-6435 | **http://store.wolterskluwerlb.com**