



Financial Services & Products ADVISORY ■

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Mortgage Servicing Transfers: A Significant Concern to the CFPB

On August 19, 2014, the Consumer Financial Protection Bureau (CFPB) issued a new compliance bulletin and policy guidance, Bulletin 2014-01, (the "bulletin"), putting mortgage servicers on notice of the CFPB's heightened scrutiny of mortgage service transfers. The bulletin supersedes the CFPB's prior guidance found in CFPB Bulletin 2013-01, released in February 2013, and warns that additional guidance may be forthcoming. The new bulletin outlines areas of particular interest to the CFPB in servicing transactions, which the CFPB defines to cover transfers of servicing rights and transfers of servicing responsibilities through subservicing or whole loan servicing arrangements.

In light of the bulletin, servicers need to be aware of the following:

- The CFPB will carefully scrutinize pre- and post-servicing transfer policies and procedures to determine whether servicers, in particular servicers engaging in high-value transfers, are complying with the new servicing rules;
- With high value servicing transfers, servicers should consider implementing a written mitigation plan to minimize compliance risks; and
- Servicers should ensure that they have in place a strong Compliance Management System (CMS) to identify and mitigate compliance risks and ensure compliance with the myriad consumer laws applicable to servicing.

Background

The recent rise in servicing transfers and concomitant risks from those transfers has gained the attention of both federal and state regulators. Earlier this year, the New York Department of Financial Services halted a large servicing transfer. The Federal Housing Finance Agency (FHFA), the regulator of Fannie Mae and Freddie Mac, and the FHFA's Office of Inspector General have issued several recent reports on the operational and financial risks to the government-sponsored enterprises related to servicing transfers, including a June 11, 2014, advisory bulletin¹ setting forth supervisory expectations for risk management in connection with servicing transfers. The FHFA has also announced that additional guidance will follow later this year.

¹ Federal Housing Finance Agency, Advisory Bulletin AB 2014-06 Mortgage Servicing Transfers, June 11, 2014, <http://www.fhfa.gov/SupervisionRegulation/AdvisoryBulletins/AdvisoryBulletinDocuments/2014%20AB-06%20Mortgage%20Servicing%20Transfers%20Advisory%20Bulletin.pdf>

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While FHFA's focus is on liquidity and operational risks, the CFPB's guidance focuses on legal and compliance risk. In addition to providing specific guidance on servicing transfers, the CFPB reminds servicers that the bureau expects all servicers under its jurisdiction to maintain a robust CMS to ensure compliance with all servicing rules and applicable federal consumer finance laws, such as the Truth in Lending Act, the Fair Credit Reporting Act (FCRA) and the Dodd-Frank Wall Street Reform and Consumer Protection Act's prohibitions on unfair, deceptive or abusive acts or practices (UDAAP).

As the CFPB, FHFA and other regulators are looking to establish a more complete regulatory regime for transfers of servicing, the CFPB's bulletin provides the groundwork.

The CFPB's Recommended Pre- and Post-Servicing Transfer Policies and Procedures

In future reviews of servicers for compliance with the new servicing rules, CFPB examiners will consider several pre- and post-servicing transfer policies and procedures that contribute to a servicer's compliance with the information transfer and loss mitigation objectives of the new servicing rules.

Prior to completing a servicing transaction, servicers should consider implementing the following policies and procedures:

- Include in the transfer contract provisions requiring the transferor to provide all necessary documents and information at loan boarding.
- Provide tailored transfer instructions for each deal and conduct meetings to discuss and clarify key issues with counterparties in a timely manner; for large transfers, this could be months in advance of the transfer. Key issues may include descriptions of proprietary modifications, detailed descriptions of data fields, known issues with document indexing and specific regulatory or settlement requirements applicable to some or all of the transferred loans.
- Implement specifically tailored testing protocols to evaluate the compatibility of transferred data with the transferee servicer's systems and data mapping protocols.
- Engage in quality control reviews after the transfer of preliminary data in order to validate that the data on the transferee's system matches the data submitted by the transferor.
- Recognize when the transfer cannot be implemented successfully in a single batch and implement alternative protocols, such as splitting the transfer into several smaller transactions, to ensure that the transferee can comply with its servicing obligations for every loan transferred.

After a servicing transfer is completed, servicers should implement the following policies and procedures:

- Implement a post-transfer process for validating data to ensure it transferred correctly and is functional, and develop procedures for identifying and addressing data errors for inbound loans.
- Implement a plan to effectively organize and label incoming information and ensure that the transferee servicer uses any transferred information before seeking information from borrowers.
- Conduct regularly scheduled calls with transferor servicers to identify any loan level issues and to research and resolve those issues within a few days of being raised.

In loss mitigation matters, servicers should implement the following policies and procedures:

- As a transferor, specifically flag all loans with pending loss mitigation applications (complete and incomplete), as well as approved loss mitigation plans (including trial modification plans), through a previously agreed upon means and assist in ensuring that the transferee's systems can process the loss mitigation data upon transfer.

- As a transferee, require the transferor servicer to supply a detailed list of loans with pending loss mitigation applications and approved loss mitigation plans.
- As a transferee, require that appropriate documentation for loans with pending loss mitigation applications, as well as approved loss mitigation plans, be transferred preboarding (for example, provide advance access to a web portal containing loan documentation for such loans 45-60 days before transfer).
- As a transferee, ensure receipt of information regarding any loss mitigation discussions with borrowers, including any copies of loss mitigation documents. The CFPB provides the following additional guidance on this issue:
 - The transferee servicer's policies and procedures must address how to obtain any such missing information or documents from a transferor servicer before attempting to obtain such information from borrowers.
 - The CFPB expects transferee servicers to ensure that they review transferred documents to determine if the documents may be used in loss mitigation efforts.
 - A transferee, following a transfer, that requires borrowers to resubmit loss mitigation application materials is unlikely to have policies and procedures that comply with 12 C.F.R. § 1024.38(b)(4).
 - A transferee, following a transfer, that fails to identify documents and information that borrowers are required to submit to complete loss mitigation applications is unlikely to have policies and procedures that comply with 12 C.F.R. § 1024.38(b)(2)(iv).
 - A transferee, following a transfer, that fails to properly evaluate borrowers who submit loss mitigation applications is unlikely to have policies and procedures that comply with 12 C.F.R. § 1024.38(b)(2)(v).
- As a transferee, monitor newly transferred loans and determine if partial payments received are actually payments pursuant to trial or permanent modification agreements.

Policies and Practices That Will Draw CFPB Scrutiny

In the bulletin, the CFPB notes that examiners may consider the following practices, among others, as indications that a servicer's policies and procedures are not reasonably designed to achieve the objective of the Real Estate Settlement Procedures Act (RESPA) and its implementing regulation, Regulation X, to facilitate the transfer of information during mortgage servicing transfers or properly evaluating loss mitigation applications:

- Failure to have policies and procedures that properly identify loans that were in a trial or permanent modification with the prior servicer at time of transfer.
- Failure to honor trial or permanent modification offers unless the servicer could independently confirm that the prior servicer properly offered a modification or that the offered modification met investor criteria.
- Failure to obtain all of the information the servicer needed from the transferor servicer and, as a result, requiring borrowers to submit additional paperwork or provide copies of financial documents they had already submitted to the transferor servicer.
- Subjecting borrowers to substantial delays while re-underwriting their loans and providing borrowers modifications with inferior terms.
- Waiting until after loan boarding to transfer information that a transferor had in its possession prior to boarding.

It is important to note that the CFPB in prior examinations has considered these practices to be UDAAP violations.

The CFPB May Require Written Mitigation Plans for High Value Servicing Transfers

The CFPB will be placing particular focus on significant servicing transactions and, in appropriate cases, will require servicers to prepare and submit written plans to the CFPB that detail how they will manage the risks related to the transfer of borrower information. While servicers do not need approval from the CFPB to move forward with servicing transfers, unless required to do so by a consent order or other provision, servicers should be aware of this potential request for a written plan from the CFPB; the CFPB will use such plans to assess consumer risk from the transaction and inform further examination planning. If the CFPB requests a written plan, it will likely request information regarding the following:

- The number of loans involved in the transfer;
- The total servicing volume being transferred (measured by unpaid principal balance);
- The name(s) of the servicing platform(s) in which the transferor stored all relevant account-level information for transferred loans prior to transfer and information about compatibility with the transferee's systems;
- A detailed description of how the servicer will ensure that it is complying with the new servicing rule provisions on transfers;
- A detailed description of the transaction and system testing to be conducted to ensure accurate transfer of electronic information and a description of the summary report resulting from the transferee or transferor's testing;
- A description of how the transferee will identify and correct errors identified in connection with the transfer, including a specified time period for reviewing files and resolving errors;
- A description of the training plan and materials for staff involved in reviewing, assessing, utilizing or communicating information regarding the transferred loans; and
- A customer service plan, specific to the transferred loans, that provides for responding to loss mitigation requests or inquiries and identifies whether a loan is subject to a pending loss mitigation resolution or application.
- Even if the CFPB does not require a written plan, servicers should consider this information a tool to evaluate and mitigate any potential compliance risk from their servicing transactions.

Servicers Must Implement a Strong Compliance Management System

There are a number of new servicing rules and federal consumer laws applicable to servicing transfers. As noted earlier, the CFPB expects all servicers under its jurisdiction to maintain a strong CMS. According to the CFPB, a "robust CMS must, among other things, both ensure that violations of Federal consumer financial law do not occur during a transfer and must contain mechanisms for promptly identifying and remediating any violations of Federal consumer financial law that do occur." To establish a strong CMS, an entity must have strong policies and procedures, effective board oversight, regular and properly directed training, internal monitoring, external audits and compliance reviews.

In addition, servicers should also be mindful of the following rules and laws in the context of servicing transfers:

- Error Resolution Procedures (12 C.F.R. § 1024.35) and Requests for Information (12 C.F.R. § 1024.36)
- Force-placed Insurance (12 C.F.R. § 1024.17(k) and 12 C.F.R. § 1024.37)
- Early Intervention (12 C.F.R. § 1024.39)
- Continuity of Contact (12 C.F.R. § 1024.40)
- Loss Mitigation (12 C.F.R. § 1024.41)
- Fair Credit Reporting Act (15 U.S.C. §§ 1681i, 1681s-2)
- Fair Debt Collection Practices Act (15 U.S.C. §§ 1692a, 1692d, 1692e, 1692f, 1692g)

Alston & Bird Observations

Given the continuing high volume of servicing transfers and the attendant risks to borrowers, the CFPB has been closely monitoring servicing transactions. While the bulletin covers a number of regulations relevant to servicing transfers, its focus is on revised Regulation X, which implements the Real Estate Settlement Procedures Act that took effect January 10, 2014. The provisions of Regulation X at issue are found in 12 C.F.R. § 1024.38 and require servicers to, among other things, maintain policies and procedures that are reasonably designed to achieve two objectives: (1) the accurate transfer of mortgage servicing information; and (2) the proper evaluation of loss mitigation applications from borrowers.

The accurate transfer of mortgage servicing information is governed by Regulation X as well as many other consumer financial laws and regulations. Servicers must be careful to comply with all of the foregoing regulations and statutes (and, of course, those not stated but nonetheless could be deemed a UDAAP). Failure to do so will invite CFPB scrutiny, and the CFPB will take appropriate supervisory or enforcement actions to address violations and seek all appropriate corrective measures, which could prove quite costly to servicers.

To ensure compliance with Regulation X, the bulletin provides practical policies and procedures that transferors and transferees should implement to mitigate the potential for noncompliance with the regulation. We encourage you to review these policies and procedures carefully and to implement them to the fullest extent.

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