JULY–AUGUST 1998
VOL. 32 ■ NOS. 3–4

CLEARINGHOUSE REVIEW
JOURNAL OF POVERTY LAW

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Guarding Against Servicer Abuses

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One of the most important skills an advocate can impart to a client homeowner is the ability to predict, recognize, and guard against some very common mortgage loan servicer abuses./1/ These abuses can range from refusing to answer homeowners' questions, to overcharging customers, to misleading borrowers about their intentions to foreclose. Even though extended default and subsequent foreclosure can be very costly to the mortgage industry, many large mortgage servicers refuse to work with homeowners who have fallen behind in their mortgage payments. This lack of communication makes it difficult for even sophisticated borrowers to participate in the workout options offered by many major lenders./2/ Advocates can help ease such difficulty by teaching homeowners how to communicate with lenders and avoid servicer abuses and by advocating changes in the law and regulations which govern loan servicing.

I. Recognizing and Guarding Against Servicer Abuses

The mortgage industry is no longer designed to allow borrowers direct and easy access to lenders. Years ago a customer borrowed money most likely from a bank that had a branch office in the neighborhood. If a financial problem arose, the customer would go into the branch office and work something out. Today lenders sell loans frequently and often hire large mortgage companies, usually located in some other part of the country, to service them. In many cases those servicers do not understand the local conditions that lead to financial problems and push people over the edge.

Many of these loan servicers refuse to work with borrowers who have fallen behind. Even when homeowners, invoking their rights under the Real Estate Settlement Procedures Act, send certified written requests for information, many *p140* servicers refuse to send the requested information to them./3/ Alternatively servicers send inaccurate information or information that does not address the their questions. Some servicer representatives deceive customers about their intentions to foreclose, even when the customers have enough equity for them to sell at a substantial profit./4/ Other common servicer abuses include the following: refusing to explain complex information coherently to customers; refusing to provide answers to commonly asked questions; regularly overcharging customers and adjusting those customers' accounts only when asked to do so; failing to disclose pertinent information about mortgage accounts or adequately explain account adjustments when asked; losing information and checks sent by customers; failing to disclose vital and timely information about the foreclosure process and time line; failing to work with customers, particularly those who have low income and/or high equity; pushing borrowers into workouts they cannot afford; and closing deals with customers in a way that is clumsy, confusing, and inefficient and which often results in cancellation of the deal.

II. Communicating Effectively with the Lender

Many of the larger loan servicers still run inefficient, unfriendly foreclosure prevention departments. When calling these departments, also called loss-mitigation departments, borrowers almost never reach a human voice. When they do, they rarely speak to the same person twice. Advocates can help homeowners learn the secrets to navigating the voice-mail sea of loss mitigation. When a homeowner falls behind on his or her mortgage, important recommendations an advocate can make include the following:/5/

> 1. Develop a new budget that reflects your current income and expenses and maximizes the amount of money you can contribute to the mortgage each month. If you know your financial situation will change again soon, prepare another budget to reflect the change. This will enable you to determine how much you can afford to contribute to your mortgage, both now and over the long term.
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> 2. Call your servicer. Explain your hardship, and ask for information about your workout options. Let the servicer know if you are working with the lender directly or with a counselor. If you are able to work out payment arrangements over the phone, make sure they concur with your present and ongoing budgets. Get the agreement in writing!
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> 3. Seek counseling in your community. Some servicers have lists of community-based counseling agencies that perform default- and delinquency- or foreclosure-prevention counseling.
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> 4. Keep a file for your mortgage, including copies of all mortgage-related correspondence, your budgets, and a log of mortgage-related phone conversations with dates and times.
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> 5. Find out who owns your loan and call the company about possible workout options and the eligibility requirements for those options. A few mortgage insurers will also help homeowners make their loans current by advancing insurance funds (usually in the form of a no-interest-bearing balloon) or by encouraging the servicer to work with the homeowner.
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> 6. Back up all of your phone correspondence with certified letters, and save your records of receipt. These letters **p141** should restate the results of your conversations and clearly ask for any additional

information you may require to proceed. Put copies of these letters and the records of receipt in your mortgage file.

7. Prepare a hardship letter for the lender, servicer, or any counselor who may be helping you resolve the default. The letter should explain why you fell behind, the nature of your hardship, whether it was an involuntary hardship, and how the hardship has been or will be resolved.

8. Obtain documentation of your hardship, verification of your income, and documentation of any foreseen changes in your financial situation (e.g., doctor's note documenting illness, insurance report documenting a fire, or letter from an employer verifying a salary increase).

9. If you have equity, you may consider putting your home on the market. If you are later able to work out a plan to reinstate your mortgage and keep your home, you do not have to sell your property. If the mortgage company or lender denies any proposal that you can afford, you may have the opportunity to sell your home at a profit before the foreclosure is complete.

10. Talk to an attorney about your legal rights in the foreclosure process and whether there may be legal defenses to the foreclosure.

III. Advocating Consumer-Friendly Reform

Another critical component of the advocate's role is to help promote consumer-friendly reform of servicer practices. Before reform is likely, communities must be educated about the abuses suffered by low- and moderate-income homeowners, particularly those in default. There is no shortage of written material for advocates on this topic./6/

In addition to creating and enacting original regulations to protect homeowners, advocates should look to existing consumer-protection statutes for inspiration. The following are suggested reforms and examples of consumer-friendly creditor regulations and behavior that should be used as models for drafting protections for homeowners.

1. Upon Default, Right to Immediate Disclosure of Loan Status and Line-Itemized Charges as They Accrue. Through the enactment of consumer-protection laws governing the extension of unsecured debt and the practices of unsecured creditors, consumers who use credit cards have achieved important rights to fair disclosure of information and standardized procedures for challenging what they believe may be unfair charges./7/ Consequently most credit card company bills are readable and disclose pertinent information. For example, late charges and interest are clearly itemized on bills, and unpaid balances are clearly marked.

In contrast, details about loan status are often impossible to understand from looking at many mortgage loan servicers' monthly bills. Consumers often cannot tell when and where payments have been allocated, exactly how much is owed, and how much has been paid toward principal, interest, taxes, and escrow. Consequently many delinquent homeowners make poor decisions about how to cure their defaults or about when and whether to refinance. Consumer protection laws offer a model for regulation of disclosure of mortgage loan status and charges. These laws should be replicated in order to protect homeowners from further servicer abuse. **p142**

2. Upon Lender's Decision to Initiate Foreclosure Activity, Right to Full Disclosure of Intended Foreclosure Activity and the Estimated Time Line to Foreclose. Consumers who use credit cards are protected also by statute from abusive debt collection practices. When a credit card company's collection agency intends to take legal action to collect a debt, it usually makes this very clear to customers. In fact, much of the Fair Debt Collections Practices Act is geared toward restricting collection practices on this front./8/ Specifically the Act enjoins collectors from threatening to do either more than they are legally allowed to do or than what they actually intend to do./9/

In contrast, some mortgage companies or their foreclosure attorneys, when attempting to collect arrears on behalf of mortgage holders, often mislead or ignore customers when they fall behind on their mortgage payments. They do not tell customers when foreclosure proceedings begin, how long the proceedings will take, or how expensive they might be. In order to understand and implement their options in avoiding foreclosure, homeowners need immediate disclosure of the mortgage company's anticipated time line for foreclosure. Consumer protection laws that have been successful in protecting credit card users should be used as models for legislation to preserve homeowners' rights during foreclosure.

3. Standardization of a Readable and Easy-to-Understand Escrow Analysis. Many servicers offer an escrow analysis only when asked. These analyses often reveal that customers have been overcharged, and even double charged, in their escrow accounts. In fact, some mortgage servicers allegedly systematically double-charge customers who close loan modifications. When questioned about a particular account, servicers then remove the extra charges. However, they do not indicate any intention to change their formulas and remove the automatic double charge for their other customers. In the area of escrow analyses, standardization of the disclosure requirements of mortgage lenders would resolve much of the undue customer expense and other mayhem caused by inaccurate, unclear, and inconsistent reporting mechanisms.

4. Creation of Incentives for Servicers to Work with Borrowers. Borrowers who have fallen behind in their payments rarely receive quality assistance from servicers, who often refuse to work with such borrowers at all. On other occasions servicers initially work with customers; servicers appear to understand the customers' hardship but then present the customers with a foreclosure date at the last minute. This practice seems particularly common when customers have substantial equity. When mortgage servicers do work with borrowers, they often propose workouts that borrowers cannot afford. Although they are sometimes willing to negotiate down to something a little more affordable and realistic, many servicers rarely make any earnest effort to help lower-income customers make payment arrangements that make sense for their income and budget constraints, even when they can do so without a loss to the investor. Even when borrowers hold the majority of their arrears, including legal fees, in hand, some servicers will accept nothing less than 100-percent payment of all arrears to cancel foreclosure.

Lack of control over servicers and their practices is another problem faced by borrowers. Customers currently have little choice or knowledge about who invests in or services their loans. Thus the market competition that may influence borrowers' initial choice of a bank has little chance of preventing or mitigating the egregious behaviors and errors of servicers once the loan is sold. For this reason banks and investors, at a minimum, should take greater responsibility for the **p143** loss-mitigation practices and standards of the companies they hire to service their loans. They should do this on behalf of their borrowing customers and investing clients, who benefit from reduced foreclosures but have little control over servicer practices.

Some borrowers are able to negotiate workouts with their lenders directly. The Federal Home Loan Mortgage Corporation, or Freddie Mac, for example, runs a loss-mitigation department that welcomes calls from homeowners and counselors and will often work with eligible borrowers to develop long-term foreclosure alternatives./10/ Other lenders and mortgage holders often can be helpful to homeowners, and some demonstrate the desire and need to help homeowners avoid foreclosure. The most likely explanation for this helpfulness is that lenders, mortgage holders, and their investors bear all or most of the costs of foreclosing unless sufficient equity in the property covers these costs.

Even though they face no direct loss by foreclosing, servicers should still help homeowners avoid that end. Reduced foreclosures can generate sustainable homeownership and more financially secure borrowers. Stable housing adds to the economic strength of communities and, at the same time, increases lenders' and investors' customer bases and profit levels. Just as lenders are encouraged, through legislation such as the Community Reinvestment Act, to foster prosperity in low-income communities through the extension of credit and homeownership opportunities, servicers should be urged to improve their communities./11/ Servicers should be strongly encouraged to approve workouts for customers who can afford them, even when they have lower incomes or substantial equity, and particularly when refusing to do so has a disproportionate impact on protected classes./12/ In order to protect both homeowners facing financial crises and the investment of the mortgage holder, servicers should be required also to make a demonsrated effort to determine whether homeowners facing foreclosure have the income to support a mortgage. This effort might include early disclosure of counseling programs and all options offered by the investor to help homeowners avoid foreclosure.

IV. Preventing Foreclosure with Specific Reforms

All borrowers should regularly receive standardized bills that indicate how payments are allocated to principal, interest, **p144** escrow, and suspense accounts; full and immediate disclosure of the status of their mortgages, including a breakdown of arrears and fees; and a standardized, detailed, and simplified escrow analysis.

Borrowers in default are particularly vulnerable to a lack of knowledge about their rights and options during the foreclosure process. Because of their vulnerability, these borrowers should receive additional information from servicers. Any borrower who has defaulted should immediately receive timely and accurate disclosure of all workout options offered by the lender or investing corporation; all available counseling options for budget counseling and workout preparation assistance; and an anticipated time line to foreclosure, including a breakdown of anticipated fees and costs associated with foreclosure.

Borrowers and counselors who are making a concerted and informed effort to resolve a default need full cooperation from lenders and servicers. All borrowers who submit a proposal to their loan servicer or lender should receive timely notification of decisions concerning workout proposals and documentation of nondiscriminatory reasons for the refusal of denied workout plans. Two important disclosures during the period after the foreclosure process has been initiated might be notification of borrowers' legal rights both during foreclosure and after a foreclosure auction and, in the event of a foreclosure, an accounting of loan sale proceeds with a breakdown of the lender's claim.

Reforms are necessary to protect homeowners from servicer abuse. The absence of protections such as those proposed above may be perpetuating the accrual of unfair fees, confusion on the part of mortgagors, and the unnecessary acceleration of many mortgages into foreclosure. Many homeowners come dangerously close to foreclosure when the servicer clearly can help them cure the default weeks before the foreclosure attorney becomes involved.

V. Conclusion

Under the current system, default resolution options are an alternative to foreclosure that most large servicers treat with disdain and pursue with incompetence. Lenders, homeowners, and their communities stand to benefit if foreclosure becomes a last-resort option, to be pursued only after homeowners have been clearly offered counseling about how to resolve their arrears; received full, detailed, broken-down, and well-explained information about the status of their accounts; and after every reasonable and feasible proposal to implement an alternative to foreclosure has been thoroughly reviewed and denied for good reason.

Working with large mortgage servicers can be frustrating and difficult, and many homeowners are not aware of their own rights as consumers. When homeowners receive adequate and timely information about the foreclosure process and their realistic options for avoiding foreclosure, however, many positive results follow. Foreclosures are reduced, homeownership--particularly new and low-income homeownership--is sustained, communities remain economically and culturally strengthened, and mortgage holders save money over costly foreclosure./13/ Advocates can assist borrowers by making sure that they receive the information and support that they need to make informed decisions about their mortgages, by giving them reliable advice about working with safe and reputable lenders, and by using their advocacy skills to promote the legal protections that all homeowners deserve and poor homeowners need desperately.

Footnotes¶

/1/ A servicer is a company which services a loan for a lender or a mortgage holder. Often these companies-not the actual lenders-collect mortgage payments. When pursuing a workout, clients and their advocates should contact the servicer to find out who holds and who insures the mortgage. See Nika Elugardo & Gary Klein, Sustaining Homeownership: Advocates Needed, in this issue.

/2/ For a more detailed discussion on workout options and preventing foreclosure see generally id.

/3/ 12 U.S.C. Secs. 2605(d), 2605(e). See Deanne Loonin & Elizabeth Renuart, Less Than Six Degrees of Separation: Consumer Law Connections to Your Practice (Part II), 32 CLEARINGHOUSE REV. 3, 7-10 (May-June 1998) for more information on the Real Estate Settlement Procedures Act with respect to preventing foreclosures.

/4/ This practice can disproportionately affect older borrowers, who may be able to afford their mortgages under workout plans but have lower incomes, more equity, and a greater need to stay in their homes than younger borrowers.

/5/ See NATIONAL CONSUMER LAW CTR., MASSACHUSETTS HOMEOWNERS: WHAT YOU SHOULD KNOW ABOUT PREVENTING FORECLOSURE (1996), for more foreclosure prevention tips. To order call NCLC Publications at 617.523.8089.

/6/ For detailed information on consumer credit legislation see generally NATIONAL CONSUMER LAW CTR., TRUTH IN LENDING (3d ed. 1995 & Supp. 1997).

/7/ Specifically the Truth in Lending Act, 15 U.S.C. Sec. 1637, prescribes certain disclosures that must be given to applicants and holders of credit cards. See generally TRUTH IN LENDING, supra note 6.

/8/ 15 U.S.C. Secs. 1692 et seq.

/9/ For more information see generally NATIONAL CONSUMER LAW CTR., FAIR DEBT COLLECTION (3d ed. 1996 & Supp. 1997). See also Deanne Loonin & Elizabeth Renuart, Less Than Six Degrees of Separation: Consumer Law Connections to Your Practice (Part I), 31 CLEARINGHOUSE REV. 584, 596-97 (Mar.-Apr. 1998).

/10/ For most workout options which keep the borrower in the home, the borrower will need enough income to support a reasonable mortgage for the area and other reasonable expenses. Freddie Mac does not typically approve a workout unless it saves the company money over foreclosure. This practice can make workouts more difficult when borrowers have substantial equity. Extreme and involuntary hardships usually are required before most high-equity proposals are considered.

/11/ 12 U.S.C. Secs. 2901 et seq.

/12/ The Equal Credit Opportunity Act, 15 U.S.C. Sec. 1691, and the Fair Housing Act, 42 U.S.C. Secs. 3601-31, protect individuals from discrimination on the basis of race, gender, or national origin. See generally NATIONAL CONSUMER LAW CTR., CREDIT DISCRIMINATION (1993 & Supp. 1997).

/13/ For an example of how lender collaboration has reduced foreclosures while mitigating lender losses through a statewide pilot program, see generally Elugardo & Klein, supra note 1.