

# Dissecting Dodd-Frank's Loan Servicing Mandates

Implementing the new servicing requirements may take months of analysis.

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**S**ervicers, take heart - you are not alone trying to solve the riddle that is the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). While servicing is not the only part of the mortgage industry affected by Dodd-Frank, shops will have to assemble new

mandatory effective date beyond the January 2013 date.

Implementing the new requirements may take months of analysis. The following discussion identifies some of the issues that will have to be addressed.

## **ARM adjustments**

First on the list is compliance with adjustable-rate mortgage (ARM) adjust-

amount of the monthly payment that will be due after the adjustment and the assumptions on which the estimate is based;

- a list of alternatives the consumer may pursue before the adjustment and descriptions of what the customer must do to pursue these alternatives, which include refinancing, renegotiation of loan terms, payment forbearance and pre-foreclosure sale;

- the names, addresses, telephone numbers and Internet addresses of counseling agencies or programs available to the consumer; and

- the address, telephone number and Internet address for the appropriate state housing finance authority.

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resources, systems and policies to address all of the compliance nuances of the sweeping changes contained in the Dodd-Frank Act and the new regulations that are yet to come.

Dodd-Frank revised the Truth in Lending Act (TILA) and the Real Estate Settlement Procedures Act (RESPA) to impose a number of new requirements for servicers. Those new requirements are scheduled to go into effect no later than one year after final regulations are published (or no later than Jan. 21, 2013, if regulations are not published). The Consumer Financial Protection Bureau is responsible for publishing regulations to implement Dodd-Frank. So far, regulations have been slow in coming, and as a result, people are wondering whether Congress will push the Dodd-Frank Act's

ment notices under the terms of new Section 128A of TILA. Servicers will have to identify adjustable rate change dates on "hybrid adjustable mortgage loans" and provide new adjustment notices to the consumer seven months before the rate resets from its introductory rate to a new variable rate. If that rate change occurs within the first six months of the loan, the servicer will have to confirm that notice was given at the time of loan closing. The following must be included in the notice:

- the index or formula used in making the adjustment;
- an explanation of how the new interest rate and payment are determined, including an explanation of how the index was adjusted, such as by the addition of a margin;
- a good-faith estimate of the

## **Billing and payments**

Billing statements must also be updated to comply with the new Section 128(f) of TILA. Servicers will be required to provide a comprehensive billing statement to the borrower for each billing cycle of the mortgage loan. The billing statement must include the current interest rate, the date of the next rate adjustment, the amount of any prepayment fee to be charged, a description of any late-payment fee, a telephone number and Internet address to obtain information regarding the mortgage, and specific contact information for counseling agencies and programs. Regulators may eventually opt to require that servicers include more information. The information may be included in a coupon book on a fixed-rate loan.

Under new Section 129F of TILA, servicers must comply with prompt crediting of payments and new pay-

off statement requirements. A servicer must credit payments on the date the payment is received unless a delay in crediting does not result in a charge or a negative report to a consumer reporting agency. A servicer does not have to credit a payment on the date the payment is received if the servicer delivered written instructions explaining how and where the consumer must make payments and the consumer fails to follow those instructions.

If the servicer accepts a nonconforming payment, the servicer must post the payment within five days after it is received. New Section 129G of TILA requires a servicer to send an accurate payoff balance no more than seven business days after receipt of a written request from or on behalf of a borrower.

#### **Escrow administration**

New Section 129D of TILA will require new practices for escrow accounts. Creditors and servicers must establish and maintain escrow accounts for a minimum of five years for the payment of taxes, hazard insurance, flood insurance, mortgage insurance, ground rents, and any other required periodic payments or premiums relating to the property or the loan on a consumer credit transaction secured by a first lien on a consumer's principal dwelling in the following instances:

- state law or federal law requires escrow accounts;
  - the loan is made, guaranteed or insured by a state or federal government agency;
  - the original principal amount does not exceed the conventional loan limit, as of the date the interest rate is set, and the annual percentage rate (APR) exceeds the average prime offer rate by 1.5 or more percentage points;
  - the original principal amount exceeds the conventional loan limit, as of the date the interest rate is set, and the APR exceeds the average prime offer rate by 2.5 or more percentage points;
- or
- an escrow account is required by a yet-undefined "regulation."

Servicers must maintain the escrow

accounts in a federally insured depository institution or credit union and must pay interest on the funds if required by federal or state law.

However, escrow accounts are not required in connection with open-end loans and reverse mortgages and some other circumstances, such as when the borrower has sufficient equity so that private mortgage insurance is no longer required, the borrower is delinquent, the borrower otherwise fails to comply with the loan agreement (as established by a yet-undefined "rule") or the underlying mortgage is terminated.

A servicer must make an escrow-waiver disclosure if the consumer elects to close an escrow account after one has been established. This escrow-waiver disclosure must include the following:

- the applicable fees or costs associated with not having an escrow account;
- a clear and prominent statement that the consumer is responsible personally and directly for paying the non-escrowed items, in addition to paying the mortgage payment, and that costs for taxes, insurance and related fees can be substantial; and
- a clear explanation of the consequences of failing to pay non-escrowed items, including the possible requirement for the forced placement of insurance and the potentially higher cost (including any potential commission payments to the servicer) or reduced coverage.

As is the case with several of the other new TILA and RESPA provisions ushered in by the Dodd-Frank Act, other information may be required under new regulations.

#### **Section 32 loans**

The Dodd-Frank Act also revises the rules for high-cost mortgages (i.e., Section 32 loans). Section 129 of TILA was revised to require the following in connection with Section 32 loans:

- limit the circumstances under which a late-payment fee could be imposed;
- prohibit acceleration unless the

borrower fails to make a payment, pursuant to a due-on-sale provision, or when the borrower defaults under some other material provision of the loan unrelated to the payment schedule;

- limit the circumstances under which the loan may be accelerated;
- prohibit modification or deferral fees;
- limit payoff statement fees; and
- impose new timing requirements for the delivery of a payoff statement to a borrower.

#### **Lender-placed insurance**

The Dodd-Frank Act added new rules affecting force-placed insurance to Section 6 of RESPA. A servicer will not be able to force-place insurance unless there is a reasonable basis to believe the borrower has failed to maintain required property insurance.

A servicer may not force-place insurance if a borrower provides any reasonable form of written confirmation of insurance coverage that either includes the insurance policy number and the contact information for the insurance company or agent or otherwise meets the requirements set out in any applicable regulations. If the servicer force-places insurance, the servicer must terminate that insurance and refund any premiums and related fees to the borrower within 15 days of receiving the evidence of coverage from the borrower.

Before imposing a charge for force-placed insurance, a servicer must send two written notices at least 30 days apart that explain the borrower's obligation to maintain hazard insurance. The notices must also state that the servicer does not have evidence of the required insurance and explain to the borrower in a clear and conspicuous statement how to provide such evidence to the servicer. Additionally, the notices must state that the servicer may obtain such coverage at the borrower's expense if the borrower does not provide evidence of coverage in a timely manner.

A servicer may not impose a charge for force-placed insurance until 15 days after the second notice and

then only if the fee is bona fide and reasonable.

### QWRs

The Dodd-Frank Act also amends Section 6 of RESPA to shorten the time frames to respond to a qualified written request (QWR). Specifically, the time period to acknowledge a QWR is shortened from 20 days to five, and the time period to make any corrections in response to a QWR or to provide the borrower with a written explanation is shortened from 60 days to just 30. The 30-day period may be extended by 15 days if the servicer notifies the borrower before the end of the 30-day period and provides the reason for the delay. Section 6 of RESPA was also amended to prohibit the following:

- charging fees to respond to a QWR;
- failing to respond timely to a borrower's request to correct errors related to allocation of payments, final payoff balances, or other standard servicer's duties;
- failing to respond within 10 business days to a borrower request for the name or contact information of the owner or assignee of the loan; and
- failing to comply with any other obligation prescribed by new regulations.

All of the servicers we have spoken with are working through the new compliance requirements and overall generally agree with this high-level analysis of the Dodd-Frank Act. However, further changes surrounding each servicer's current preemption strategy

and how that strategy may be impacted by legislation or regulations yet to come have created unique challenges. Executives in servicing organizations may need to rely heavily on their legal counsel and the vendors to support their operations. **SM**



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