Consumer Finance Monitor (Season 3, Episode 11): The CFPB's Winter 2020 Supervisory Highlights: Takeaways for Payday Lenders and Mortgage Servicers

Speakers: Chris Willis, Jason Cover, and Reid Herlihy

Chris Willis:

Welcome to the Consumer Finance Monitor Podcast, where we explore important new developments in the world of consumer financial services and what they mean for your business, your customers, and the industry. I'm your host, Chris Willis. And I'm the chair of our Consumer Financial Services Litigation Group here at Ballard Spahr, and I'll be moderating today's program. For those of you who want even more information, don't forget about our blog, consumerfinancemonitor.com. We've hosted the blog since 2011, so there's a lot of relevant industry content there. We also regularly host webinars on subjects of interest to those of us in the industry. So to subscribe to our blog, to get on the list for our webinars, or for our mortgage banking update, visit us at ballardspahr.com. And if you like our podcast, please let us know. Leave us a review on Apple Podcasts, Google Play, or wherever you get your podcasts.

Chris Willis:

Today. I'm joined by two of my colleagues, Jason Cover. Who's an associate in our consumer financial services regulatory group in Philadelphia. And my partner Reid Herlihy who is here in Atlanta with me. And who's a partner in our mortgage banking group. And we're going to be talking together about the most recent edition of the CFPB supervisory highlights, which contains items that we thought would be of interest relating to both payday lending and mortgage servicing. So Jason and Reid are going to cover those, respectively.

Chris Willis:

So Jason, let's start with you. The supervisory highlights is something that we pay a lot of attention to in sort of taking the temperature of the CFPB and seeing what its priorities are and in advising clients. And so with respect to payday lending, what are some of the issues that the CFPB highlighted in its most recent edition or relating to that industry?

Jason Cover:

Thanks, Chris. I think some of the most interesting, or maybe the most interesting thing about the supervisory highlights is the relative lack of interesting notes that are here. These are really garden variety violations that I don't think would surprise anyone to have the CFPB have findings about. These aren't the circle of debt and some of the... just somewhat shocking things that the CFPB used to do in the past. So we have violations for an inaccurate APR for loan renewals, where there was no documentation of the loan renewal, and the charge itself wasn't included in the APR. We have a failure to apply payments to a borrower's account. So the borrower makes a payment of a hundred dollars to pay down their account, and it's never applied, and they continue to charge interest in late fees on it.

Jason Cover:

I don't think anyone would find that to be something that the CFPB shouldn't be interested in. Failure to disclose finance charges for the refinancing of delinquent loans. Again, it's something that wasn't documented. It wasn't very disclosed when the customer made the refinance. And again, this is just something that is another garden variety violation. Failure to comply with reg Zs record retention requirements. Again, this is a black letter type of violation. Inaccuracies and adverse action notices. I know this is something many of our clients struggle with due to the system limitations, system problems. But again, it's black-letter violation. It's nothing exotic or shocking. And finally, unauthorized collection fees. Again, this is maybe a little bit of a FDCPA import to the payday lending sphere. But once again, this isn't something that I think anyone would be surprised to find in supervisory highlights.

Chris Willis:

So, Jason, I mean, the things you've talked about, as you noted, look like kind of garden variety, black letter law issues, nothing adventurous, so to speak. In terms of the CFPB creating a new legal theory or surprising the industry or us with the kinds of things that is brought up. So what does the presence of this type of issue being highlighted in supervisory highlights tell us about the CFPB current behavior?

Jason Cover:

I think, first of all, this really is a continuation of what former director Mulvaney had to say when he took over that the CFPB would fulfill its statutory responsibilities. But it wasn't going to go farther. So I think we've seen this in enforcement as well. There's plenty of things that plenty of financial institutions get wrong and are... have statutory obligations that they fail. But the CFPB doesn't seem to be overstepping its bounds, particularly on what it deems a disfavored industry like payday lending and creating novel theories that no one can comply with an advanced, because we don't know about them. I think it gives us some comfort to being comfortable with the laws as they are and putting a good faith effort into complying with them. So I think that's one takeaway. I think another takeaway here is that the CFPB continues to have interest with payday lenders, I think, in payments.

Jason Cover:

And I think you can see that from some of the things they were looking at here, whether it's payment application or how we're processing payments. And you see that in the continued interest in those provisions of the small-dollar rule. And then also collections. These are... some of these APR or reg Z violations, but they're ostensibly about a refinance fee and a delinquency or an unauthorized fee in collections. So I get the impression that examiners are still putting a lot of attention into both payment processing, payment application. And also how these lenders are conducting their collection activity.

Chris Willis:

So Jason, from a practical standpoint, for participants in the short-term small-dollar lending industry, what are the takeaways from this edition as supervisory highlights? What should we do or not do or be paying attention to as a result of reading the matters that you just went over with us?

Jason Cover:

Sure. I think another thing that's noted in almost every one of these was the lender either didn't have sufficient monitoring. Didn't have sufficient auditing process. Didn't have sufficient policies and procedures or didn't have sufficient training to conduct its operations and find the sort of garden variety of violations. So step one, I and this isn't anything new, but you can catch APR violations by double-checking the APR. So, some of these things can be cured by a lender by adopting some minimal level of monitoring and process in that sense. And I do wonder because we've had the impression lately that the CFPB has conducted several sweeps of the largest lenders in this space. And they've sort of moved on to the sort of smaller, mid-range, more regional lenders. So I think a lot of the largest lenders have realized they have to beef up their compliance management systems.

Jason Cover:

And I wonder if some of this isn't commentary now that the CFPB is getting into smaller and mid-range level, mid-level lenders that maybe haven't had an examination before. Maybe had paper some CMS-type procedures over, but really hadn't had that applied in an examination. So now, is this the CFP kind of letting everyone know, "Hey, we still care about the CMS, and you need to have these policies, procedures of CMS in place to catch these things in process." And then the final takeaway I had is record retention. I think this is a relatively new. And I don't recall seeing this at least in the recent supervisory highlights or enforcement. And I think this might be something that there's a fair amount of lenders out there in the space that maybe they haven't thought of because they've been so busy working on their actual CMS.

Jason Cover:

It's well enough to say the record retention... is two years for truth and lending. And then not have an actual record retention policy that documents that for all of the statutes, all of your documentation. And then it's an even bigger step to then implement that. So I think this would be an area we might urge lenders and clients to reach out to outside counsel because this is not an easy thing. And then if you're really going to do a record retention policy that has your employment records and everything else, not just your consumer-facing documentation. It's really a huge processed. I've done it a couple of times, and it's a bit of a bear. So it's not something that necessarily is a good idea to conduct internally.

Chris Willis:

Got it. Well, thanks a lot for sharing your thoughts on that portion of the supervisory highlights, Jason. And Reid, now I'd like to turn to you. It seems like mortgage servicing has been perpetually on the CFPB mind and at the top of its priority list ever since the inception of the agency, given its sort of birth in the subprime mortgage crisis. And this episode of supervisory highlights has even more about mortgage servicing. So tell us, Reid, what's going on from the CFPB standpoint in terms of the issues that raised in this most recent edition of supervisory highlights?

Reid Herlihy:

Yeah. Thanks, Chris. And that's absolutely right. The Bureau has always been focused within the mortgage industry on mortgage servicing as really the high-risk area that they want to drill down on it for these supervisory highlights at a minimum. And within mortgage servicing, it comes as no surprise that these... this edition of supervisory highlights focuses on loss mitigation findings. Now, similar to what you and Jason just discussed. The first couple of findings here really are very basic clear cut examples of violations. And these are issues of very basic requirement under Regulation X and the loss mitigation rules. So the third one though a little bit more interesting, and we'll get into some detail on that. But for thoroughness, I'll go ahead and get through them all. So the first finding, again, a pretty clear example of a Regulation X issue.

Reid Herlihy:

The Bureau simply found that one or more servicers fail to issue the loss mitigation acknowledgment letter within five days of receiving a loss mitigation application. That's one of the most basic requirements in 1024.41. The second finding similarly a clear violation. One or more servicers fail to issue the written notice of a loss mitigation evaluation within 30 days after receipt of a complete loss mitigation application. That's not going to surprise anyone or create any novel legal theories for enforcement. The third finding, as I mentioned, slightly more nuanced. We have issues here of loss mitigation in the context of disaster relief. We have the provision in Regulation X for the loss mitigation anti-evasion clause, which I'll describe in more detail and some concepts of what constitutes a loss mitigation application that are not always clear to servicers or to folks who haven't focused on this rule in a while.

Reid Herlihy:

So as background, the so-called anti-evasion clause in 1024.41 of Regulation X requires that, "A servicer evaluate a borrower for all loss mitigation options based on a complete loss mitigation application for all of those options, but there are certain exceptions." And so here, one such exception. "Allows a servicer to offer a short-term forbearance or repayment plan based on the evaluation of an incomplete application." Now, if a servicer uses that exception to offer the short-term forbearance or repayment. Certain additional content has to be included in the offer letter, which essentially encourages the borrower towards the end of this short-term plan to complete the loss mitigation application so that he or she can be more fully evaluated for long-term loss mitigation options, like a loan modification, which could really ensure long-term affordability for the loan product.

Reid Herlihy:

Now, with that as background, getting back to the CFPB findings. The servicer at issue spoke with disaster-affected borrowers over the telephone, absent any written loss mitigation application. And then the servicer offered a short term forbearance without including that additional language I mentioned required under the regulation to encourage the borrower to complete the application later on. And the CFPB found here that those telephone discussions with the borrower did constitute in loss mitigation application. And so, the failure to include certain language in the offer letter violated Regulation X. But I know the supervisory highlight state that the findings did not result in any MRAs through the examination due to the overall circumstances of the disaster-related applications.

Chris Willis:

Reid, you said that the CFPB found that the borrower's conversations with the servicer alone constituted loss mitigation applications that triggered the rule. How does a phone call rise to the level of a loss mitigation application? I thought that was a lot more formal process.

Reid Herlihy:

Yeah, thanks, Chris. And as I mentioned, this is an issue that servicers can forget if they haven't really focused on this rule in a while. So Regulation X defines a loss mitigation application very broadly to include, "Any oral or written request for a loss mitigation option that is accompanied by any single piece of information required by a servicer for evaluation of a loss mitigation option." So, for example, an informal discussion over the phone where the borrower expresses some interest in a loss mid option, like a forbearance. And conveys any detail regarding any type of hardship that the borrower is experiencing could be interpreted as a loss mitigation application, albeit an incomplete one. So once that happens, the procedures under 12 CFR, 1024.41 kick in. And in light of that, we can see through this example how borrower outreach over the phone or a quality right party contact under agency or GSE requirements can develop into an oral loss mitigation application very easily.

Chris Willis:

You also mentioned that this finding was related to loss mitigation offered to borrowers affected by a natural disaster. Is there anything that mortgage servicers should be thinking about in conduction with the evolving coronavirus situation?

Reid Herlihy:

Yeah, Chris. So this topic actually came up earlier this week on a panel I was on at the MBA servicing conference. And it's an interesting thing to bring up. And I think timely in of this supervisory highlights finding. So servicers should always absolutely have an eye on procedures for disaster events. They're by definition hard to predict, and you should have procedures in place to assist these kinds of borrowers in various ways and which I'll get into in a second. And to be sure in that aim, the agencies, the GSEs, private investors, they have loss mitigation options available that are generally geared toward these events. So they may either be generally structured to address short-term hardships of any kind, including a... or loss of employment through disaster, or more specifically to disaster-affected borrowers with certain built-in procedures.

Reid Herlihy:

However, those programs for disaster effected borrowers are generally tied to a declared geographic disaster area. So a FEMA declared disaster area for a hurricane, for example. So in that scenario, one can simply bump up the property location to the declared area to confirm certain information, such as whether the borrower was actually affected by the disaster whether there was any property damage. And also, to identify borrowers to proactively offer assistance through outreach or streamlined loss mitigation options without a loss mitigation application. With this kind of viral pandemic, though, we kind of have different logistical issues to worry about. So the affected persons may be categorized by their employers, say if there's a large scale government shutdown or a shutdown of several major airports in the United States or other reasons. They could be simply a group of borrowers quarantine on their cruise line in a port somewhere. So we have different logistical considerations. And I think it's a good exercise and an opportunity to think that through for servicers to see how they can verify hardships in these scenarios or how they can identify effective borrowers and contact them regarding this kind of event.

Chris Willis:

Thanks, Reid, for sharing your views on that. And I think our audience will be very appreciative for both your and Jason's comments. So I want to thank both of you for participating in today's podcast. And thanks to our listeners for listening in on today's episode. Be sure to visit our website ballardspahr.com, where you can subscribe to the show in Apple Podcasts, Google Play, Spotify, or your favorite podcast platform. And don't forget to check out our blog consumerfinancemonitor.com for daily insights about the financial services industry. And of course, our mortgage banking update, which is specific of course to the mortgage banking industry. If you have any questions or suggestions for the show, please email us at podcast@ballardspahr.com, and stay tuned each Thursday for a great new episode. Thank you all for listening.