COMMENTS
to the
Consumer Financial Protection Bureau

Docket No. CFPB-2013-0018
RIN 3170-AA37
78 Fed. Reg. 39901 (July 2, 2013)
Amendments to the 2013 Mortgage Rules
under the Real Estate Settlement Procedures Act (Regulation X) and
the Truth in Lending Act (Regulation Z)

by the
National Consumer Law Center
on behalf of its low income clients

as well as

Center for Economic Justice
National Association of Consumer Advocates

July 22, 2013

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The **National Consumer Law Center**[1] ("NCLC") submits the following comments on behalf of its low-income clients, as well as the **Center for Economic Justice**[2] and the **National Association of Consumer Advocates.**[3]

These comments address three topics: mortgage servicing, loan originator regulations, and the prohibition on financing of credit insurance. We suggest substantial changes to the servicing and loan originator regulations to ensure that the new rules adequately protect consumers and promote market function. We generally support the credit insurance proposals, with some additional recommended changes.

I. Further Changes to the Bureau's Mortgage Servicing Proposals are Needed To Ensure Reasonable Access to Loss Mitigation

A. Further Clarifications and Amendments Are Needed to Allow Borrowers to Exercise Their Rights. [Sections 1024.35(c) and 36(b) - Contact Information for Borrowers To Assert Errors and Information Requests]

The CFPB is proposing to amend comments 35(c)-2 and 36(b)-2 regarding its mortgage servicing regulations. The amendments would clarify that if a servicer establishes a designated address for receipt of notices of error or information requests, the servicer must provide that designated address to a borrower in any communication in which the servicer provides the borrower with an address for assistance from the servicer. Further clarification is needed to avoid confusion by borrowers. In addition, the proposed amendments underscore the need for the transfer of servicing notice to inform borrowers of their information and dispute rights under RESPA.

Borrowers' information and dispute rights under RESPA are both important and complex, and have been the subject of significant changes in recent years. The 2013 RESPA Servicing Rules substantially revised the former qualified written request procedure by creating two separate processes: one for resolving errors on a borrower's account and the other for requesting information regarding the account. The new procedures have extended error resolution to include matters such as loss mitigation and expanded the scope of information requests to include any information

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[1] Since 1969, the nonprofit **National Consumer Law Center® (NCLC®)** has used its expertise in consumer law and energy policy to work for consumer justice and economic security for low-income and other disadvantaged people, including older adults, in the United States. NCLC's expertise includes policy analysis and advocacy; consumer law and energy publications; litigation; expert witness services, and training and advice for advocates. NCLC works with nonprofit and legal services organizations, private attorneys, policymakers, and federal and state government and courts across the nation to stop exploitive practices, help financially stressed families build and retain wealth, and advance economic fairness. NCLC publishes a series of consumer law treatises including Mortgage Lending, Truth in Lending and Foreclosures. These comments are written by NCLC attorneys Alys Cohen, Andrew Pizor, John Rao, Diane Thompson and Geoff Walsh, as well as Birny Birnbaum of the Center for Economic Justice. NCLC attorneys provide assistance on a daily basis to the attorneys and housing counselors working with distressed homeowners across the country. These comments are based on the information from these advocates as well as our knowledge and expertise in RESPA and TILA specifically and consumer law in general.

[2] The **Center for Economic Justice** ("CEJ") is a non-profit organization that works to increase the availability, affordability and accessibility of insurance, credit, utilities, and other economic goods and services for low-income and minority consumers. CEJ joins only in the credit insurance portion of these comments.

[3] The **National Association of Consumer Advocates** ("NACA") is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

concerning the borrower's mortgage loan. At the same time, new limitations have been added related to overbroad, duplicative, confidential, and unduly burdensome requests.

Despite these significant changes, servicers are not required to notify borrowers of their information and dispute rights. None of the mandatory contacts with borrowers required by the CFPB in the 2013 RESPA and TILA Servicing Rules require disclosure of these rights. Neither the periodic billing statement proposal (§ 1026.41) or the early intervention notice (§ 1024.39) require the servicer to inform the borrower of the right to dispute errors or obtain account information. The one notice under current law that did provide this information to borrowers, the transfer of servicing notice under RESPA § 2605(c)(1), will no longer include this information.

Consequently, borrowers will not have any context in which to evaluate information about designated addresses provided under comments 35(c)-2 and 36(b)-2. Borrowers will be provided a designated address but not be aware of its significance, or even that there is formal procedure that must be followed for sending written information requests and notices of error.[4]

Section 1024.33(b)(4) requires that the transfer of servicing notice include the name, address, and toll-free number for the borrower to obtain answers to servicing transfer inquiries. Under comments 35(c)-2 and 36(b)-2, the servicer will also need to include the designated address for information requests and notices of error, if one has been established by the servicer. Without a brief explanation of the borrower's dispute and information rights or the importance of using the designated address, providing two different servicer addresses (one for servicing transfer inquiries and another for information requests and notices of error) will be confusing to borrowers and potentially prevent them from exercising their rights under RESPA.

For example, assume that the first periodic statement the borrower receives from a new servicer shows that the borrower has missed a payment, and the borrower believes that the new servicer has failed to credit a payment to the account that was sent during the transfer period. If the transfer notice does not explain the difference between the two addresses, the borrower may mistakenly send a notice of error to the transfer inquiry address. Under the CFPB's construction of the designated address rule, the servicer can ignore the notice of error and it would not be legally compelled to provide a response in accordance with RESPA § 2605(e)(2) or Reg. X § 1024.35(e).

Two changes are needed to allow borrowers to exercise their rights. First, the model form transfer notice (MS-2) should be revised to include language describing the significance of the designated address and how it is different from other addresses provided by the servicer, such as the servicing transfer inquiry address. Servicers should be required to use this language if a designated address has been established. Similar language should also be required on the notice of designated address itself under § 1024.35(c) and § 1024.36(b). Second, the CFPB should reestablish the requirement that the transfer of servicing notice include information about the borrower's information and dispute rights under RESPA. This information should also be required on the early intervention notice and whenever delinquency information must be provided on a periodic statement under § 1026.41(d)(8).

[4] When the CFPB initially proposed to delete the disclosure of error resolution rights from the servicing transfer notice, it was also proposing to permit notices of error and requests for information to be submitted orally. However, the final rule retained the writing requirement. It is therefore critical that borrowers be informed that notices of error and requests for information will only be effective if they are submitted in writing.

B. The Servicer's Obligation to Respond Should Terminate with the Security Interest, Not with the Debt. [Sections 1024.35(g) and 36(f) - Requirements Not Applicable]

The CFPB is proposing to replace the references to the date a mortgage loan balance is paid in full in § 1024.35(g)(1)(iii)(B) and § 1024.36(f)(1)(v)(B) with the date the mortgage loan is discharged. More precise language referring to the termination of the security interest should be used.

The CFPB has correctly noted that use of the date a mortgage loan balance is paid in full would not cover situations in which the mortgage loan is terminated through foreclosure or a deed in lieu of foreclosure. These situations should also trigger the one year period for termination of the servicer's obligation to respond to notices of error and information requests. However, the language proposed is too broad in that it refers to the discharge of the borrower's indebtedness. Language that refers to the termination of the mortgage creditor's security interest would more accurately reflect the legal obligations between the parties. Discharge of indebtedness may occur long before the security interest is released, as in the case of a bankruptcy, or long after, in the case of a post-foreclosure deficiency judgment.

The proposal adds the phrase "the date the mortgage loan is discharged" to § 1024.35(g)(1)(iii)(B) and § 1024.36(f)(1)(v)(B). This language would include the situation in which a borrower files a chapter 7 bankruptcy, is current on the mortgage, fully intends to continue payments on the mortgage, and has not entered into a reaffirmation agreement with the creditor. Although the borrower's personal indebtedness on the mortgage loan is discharged in the bankruptcy case, the creditor's mortgage lien remains intact and is fully enforceable against the property. It is not uncommon in this situation for servicers to continue to accept payments from the borrower and to continue to service the loan in ordinary course of business. In fact, section 524(j) of the Bankruptcy Code contemplates this situation by clearly stating that a servicer does not violate the bankruptcy discharge injunction by engaging in such practice. The CFPB has also appropriately recognized this practice by refusing to include a bankruptcy exemption to the periodic statement requirement in the 2013 TILA Servicing Rules.[5]

Servicers may construe the proposed language to mean that they are not required to respond to a notice of error and information request sent more than one year after the borrower may have received a discharge in bankruptcy, even though the mortgage loan is continuing to be paid by the borrower. To avoid this problem, we believe that the replacement language should be: "the date the lien securing the mortgage loan is discharged, released, or avoided." This would cover situations in which the mortgage loan is terminated through foreclosure or a deed in lieu of foreclosure, but not simply when the borrower's personal liability on the mortgage loan is discharged in bankruptcy. Moreover, it would terminate a servicer's obligations to respond upon the conclusion of a

[5] The final rule allows servicers to make changes to periodic statements as they believe are necessary when a borrower is in bankruptcy, so as to reflect the payment obligations of the debtor as a result of the bankruptcy proceeding. A sample message servicers may add to the statement to avoid conflict with the automatic stay and discharge injunction was provided. *See* Section-by-Section Analysis, § 1026.41(d)(2), 78 Fed. Reg. 10,966, note 125 (Feb. 14, 2013) ("For example, servicers may include a statement such as: 'To the extent your original obligation was discharged, or is subject to an automatic stay of bankruptcy under Title 11 of the United States Code, this statement is for compliance and/or informational purposes only and does not constitute an attempt to collect a debt or to impose personal liability for such obligation. However, Creditor retains rights under its security instrument, including the right to foreclose its lien.' ").

foreclosure, even if a deficiency judgment remained against the borrower.

C. Submission of an Initial Application Should Trigger Dual Track and Appeal Protections. [Section 1024.41(b) - Receipt of a Loss Mitigation Application; Section 1024.41(b)(2) - Review of Loss Mitigation Application Submission; Section 1024.41(b)(2)(i) – Requirements]

Section 1024.41 imposes a number of duties on a servicer once it receives a borrower's application for loss mitigation review. Because the concept of a "complete" loss mitigation application is central to implementation of the loss mitigation rule as currently drafted, the CFPB is proposing three provisions to address concerns related to circumstances in which a servicer initially treats an application as complete but later determines that additional information is required. Before addressing the three specific proposals, we urge the CFPB to reconsider its general approach to the role of the loss mitigation application, particularly with respect to its interplay with the dual tracking provisions and other borrower protections. Reliance on submission of a "complete" application has confounded attempts to address dual-tracking and wrongful foreclosures.[6]

1. The CFPB Should Define the Elements of an Initial Submission of a Loss Mitigation Application.

The CFPB should define the minimum requirements in all cases for the initial submission of a loss mitigation application, similar to the proposal put forward by the California Monitor for the National Mortgage Settlement.[7] Servicers would, of course, be permitted to request additional information intended to satisfy any investor requirements after an initial application is submitted. However, § 1024.41 should provide that once the borrower has submitted documentation that satisfies this initial showing, the dual tracking restrictions under § 1024.41(g) should apply even if the servicer determines that the loss mitigation application is not "complete." This is the only approach that provides servicers with an incentive to process applications in a timely manner and avoids potential manipulation of the process based on a servicer's subjective determination of a "complete" application. It also obviates many of the concerns addressed by the proposed rule amendments in this docket.

To implement this proposal, the CFPB would define in § 1024.41 the elements of an initial submission of a loss mitigation application, similar to the "Initial Package" referred to under the HAMP Handbook. Chapter II, Part 4 of the HAMP Handbook provides that the Initial Package includes:

- A Request for Mortgage Assistance (RMA) Form, which includes a homeowner hardship affidavit, rental property certification, and Dodd-Frank certification
- IRS Form 4506-T or 4506T-EZ, which authorizes the release of a transcript of the borrower's tax return, and

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[6] *See, e.g.,* Shahien Nasiripour, *National Mortgage Settlement Review Prompts Dual-Tracking Discussions with Banks*, Huffington Post (June 19, 2013), http://www.huffingtonpost.com/2013/06/19/national-mortgage-settlement-dual-tracking_n_3468307.html.

[7] *See* "The 'Complete' Application Problem: A Solution to Help Homeowners and Banks Work Together," available at: http://californiamonitor.org/wp-content/uploads/2013/06/FINAL-June-19-Complete-App-Monitor-Report.pdf.

- Documentation to verify the borrower's income

By submitting this information and these documents, which is no simple task, the borrower is clearly demonstrating a commitment to the loss mitigation process. There is a strong likelihood that the borrower will respond and follow through with requests for additional information to complete the application. It is therefore appropriate at this point for the borrower to be protected from dual tracking while the initial application is being evaluated.

We are not suggesting a complete restructuring of § 1024.41. All of the current timelines and procedural requirements in § 1024.41 would remain unchanged. These timelines and the related borrower protections, however, should be aligned with the submission of an initial loss mitigation application (an Initial Package) as defined by the CFPB rather than a complete loss mitigation application. Current provisions that require a servicer to evaluate the borrower for all available loss mitigation options and that deal with duplicative requests would continue to apply only to a complete loss mitigation application.

We agree with the CFPB that a loss mitigation "application" should be viewed "expansively."[8] The CFPB's comments when promulgating the loss mitigation rule emphasize that an application need not be in any particular form, and that it may be made verbally.[9] The borrower's actions need only meet two broad criteria in order to be construed as an "application." First, the borrower must express an interest in seeking any form of foreclosure avoidance. Second, the borrower must provide some information that a servicer would normally use in determining whether a borrower qualified for a loss mitigation option.[10] We continue to believe that this approach is correct. To give full import to these general principles, borrowers who submit, within the applicable timelines, sufficient information to the servicer to constitute an initial application should gain the dual tracking and appeal protections afforded under the loss mitigation rule.

2. The Proposed Changes Under Consideration Should Be Revised To Better Protect Homeowners Wrongly Informed of the Status of Their Application.

With respect to the proposed amendments, the CFPB is first proposing new comment 41(b)(2)(i)(B)-1 to clarify that a servicer must request from a borrower any additional information required to complete an application, even if it had previously informed the borrower that an application is complete. We agree that a servicer should not rely upon an inaccurate determination that an application is complete, as this would likely result in a denial of loss mitigation options for the borrower. Servicers in this situation should be required to request from the borrower any additional necessary information.

We are concerned, however, with the consequences of a switch from a complete to an incomplete application in this situation. The CFPB is proposing new comment 41(b)(2)(i)(B)-2, to clarify that except as provided in § 1024.41(c)(2)(iv), the provisions and timelines triggered by a complete loss mitigation application in § 1024.41 are not triggered by an incomplete application. This would mean that the borrower would lose the dual tracking protections if the application is

[8] *See* Official Bureau Interpretation, Supplement 1 to Part 1024, ¶ 41(b)(1)-2.
[9] *See* Section-by-Section Analysis, § 1024.41(b), 78 Fed. Reg. 10825 (Feb. 14, 2013).
[10] *See* Official Bureau Interpretation, Supplement 1 to Part 1024, ¶ 41(b)(1)-3.

effectively converted to an incomplete application. The CFPB is proposing to mitigate this impact on borrowers by adding new § 1024.41(c)(2)(iv). This would require the servicer to treat the application as complete for certain purposes if the servicer creates a reasonable expectation that a loss mitigation application is complete but later discovers information is missing, at least until the borrower has been given a reasonable opportunity to complete the loss mitigation application.

While the new § 1024.41(c)(2)(iv) is helpful, the language used in the proposed regulation is ambiguous, may invite spurious arguments concerning servicer compliance, and will multiply litigation. The borrower protections under this provision are triggered if the "servicer creates a reasonable expectation" that an application is complete. Whether a "reasonable expectation" has been created is likely to be a fact-specific and fact-intensive inquiry. Does a letter incorrectly informing the borrower that an application is complete create a reasonable expectation (the proposed comment suggests it does)? What about a phone call? What if multiple letters are sent, containing different information? The regulation should be redrafted to make clear that the borrower protections apply whenever a § 1024.41(b)(2)(i)(B) letter incorrectly informs the borrower that an application is complete, in addition to any other actions by the servicer that may create a reasonable expectation that an application is complete. The proposed provision should be redrafted to state: "If a servicer has sent a § 1024.41(b)(2)(i)(B) notification incorrectly informing the borrower that a loss mitigation application is complete, or has otherwise given the borrower reason to believe an application is complete, …"

The proposed provision also states that the servicer must treat the application as complete "as of the date the borrower has reason to believe the application was complete…." This is inconsistent with how other timelines in § 1024.41 are applied. The dual tracking protections under § 1024.41(f)(2) and (g) are invoked when the borrower "submits" a complete loan application, not when the borrower has reason to believe the application was complete. The wording of the proposed regulation, if read without consideration of proposed comment 41(c)(2)(iv)-1, would permit a servicer to evade the dual tracking provisions. For example, if a servicer mails a § 1024.41(b)(2)(i)(B) notice to the borrower on the 40th day before a scheduled foreclosure sale that incorrectly states the loss mitigation application is complete, but the borrower does not receive the letter until the 36th day before the sale, the servicer may argue that the borrower did not have reason to believe the application was complete until the 36th day before the sale. Under the proposed regulation as drafted, the servicer is permitted to treat the application as complete as of the 36th day before the sale, rather than the date the application was submitted and the servicer determined it to be complete, and the servicer would not violate § 1024.41(g) if it proceeded with the foreclosure sale. This interpretation of the proposed regulation may not be consistent with proposed comment 41(c)(2)(iv)-1(i), though the second sentence of the comment is also ambiguous in that it refers to both the "receipt of the notice that the application was complete" and the "date the application was submitted." Again, this language introduces needless ambiguity and fact-specific inquiries. We urge the CFPB to use language in the regulation that is unambiguous.

Relying on the "date the borrower has reason to believe the application was complete" can be beneficial to the borrower in the situation in which the borrower receives a § 1024.41(b)(2)(i)(B) notice that information is needed to complete the application, and the borrower then provides the requested information and believes the application is complete. But we believe clarity, uniformity, and consequent ease of application and enforcement are better served by eliminating this language from the regulation. The key factor in the proposed regulation is the creation by the servicer of a reasonable expectation that an application is complete. The CFPB has confirmed in proposed comment 41(c)(2)(iv)-1(ii) that a reasonable expectation is created when the borrower provides all of the information requested a § 1024.41(b)(2)(i)(B) notice. Thus, in order to avoid any unnecessary arguments about the application of the proposed regulation, we recommend that new § 1024.41(c)(2)(iv) be redrafted as follows:

> (iv) *Servicer creates reasonable expectation that a loss mitigation application is complete.* If a servicer has sent a § 1024.41(b)(2)(i)(B) notification incorrectly informing the borrower that a loss mitigation application is complete, or has otherwise given the borrower reason to believe an application is complete, but the servicer later discovers that the application is incomplete, the servicer shall treat the application as complete for purposes of paragraphs (f)(2), (g) and (h) of this section as of the date the servicer created the reasonable expectation that the application is complete, until the borrower has been given a reasonable opportunity to complete the loss mitigation application.

Proposed comment 41(c)(2)(iv)-1 is consistent with the above language and would not require any amendments. We support adoption of proposed comment 41(c)(2)(iv)-1.

In addition, proposed § 1024.41(c)(2)(iv) is limited to providing the borrower with the protections under § 1024.41(f)(2) and (g) when there has been a switch by the servicer from a complete to an incomplete application. The new provision should be expanded to include § 1024.41(h), as a borrower's appeal rights are also dependent upon the timely receipt of a complete loss mitigation application. A borrower should not be denied the right to appeal a servicer's denial of loss mitigation options if a servicer has sent the borrower 95 days before a scheduled foreclosure sale a § 1024.41(b)(2)(i)(B) notification incorrectly informing the borrower that the loss mitigation application is complete, but later realizes 85 days before the sale that the application is in fact incomplete. As reflected in the above redraft of § 1024.41(c)(2)(iv), the application should be treated as complete "… for purposes of paragraphs (f)(2), (g) and (h) of this section…."

Finally, the CFPB should include in the regulation specific guidance regarding the content and timing of the notice a servicer provides to a homeowner informing the homeowner that the application was erroneously identified as complete. Proposed comment 41(c)(2)(iv)-2 provides simply that the borrower should be given a "sufficient" time to complete the application, and that the "amount of time that is sufficient for this purpose will depend upon the facts and circumstances." Servicers should be required to provide homeowners with the same amount of time for completing the application upon receipt of such notice as they would have received if they received the usual letter informing them that their application is incomplete. The regulation should provide that servicers must comply with § 1024.41(b)(2)(ii) when notifying the borrower of the prior erroneous notice and that additional information is needed.

As mentioned earlier, all of these revisions would be unnecessary if the CFPB adopts an approach to loss mitigation that does not rely upon the concept of a "complete" loss mitigation application and instead looks to the submission of an initial application.

D. The Bureau Should Not Permit a Servicer To Use an Estimated Date for a Foreclosure Sale in Setting the Completion Date in the Time Period Disclosure. [Section 1024.41(b)(2)(ii) - Time Period Disclosure]

In order to address the problems occasioned by determining when an application is complete, the CFPB is proposing to amend the § 1024.41(b)(2)(ii) time period notice requirement, which requires a servicer to provide a date by which a borrower should submit any missing documents and information to complete a loss mitigation application. The current regulation requires the servicer to provide in the § 1024.41(b)(2)(i)(B) notice the earliest remaining of four specific dates: (1) the date by which any document or information submitted by a borrower will be considered stale or invalid pursuant to any requirements applicable to any loss mitigation option available to the borrower; (2) the date that is the 120th day of the borrower's delinquency; (3) the date that is 90 days before a foreclosure sale; and (4) the date that is 38 days before a foreclosure sale. The significance of three of these dates is that they determine the level of protection a borrower is afforded under § 1024.41. The CFPB is proposing to permit servicers to include a "reasonable date," as more fully defined in related comment 41(b)(2)(ii)-1. The proposed changes provide servicers with more flexibility in suggesting an appropriate completion deadline.

We do not object to the proposed amendment to § 1024.41(b)(2)(ii). However, proposed comment 41(b)(2)(ii)-1 should not permit a servicer to use an estimated date for a foreclosure sale in setting the completion date. If a foreclosure sale has not been scheduled by the time the letter is being sent, the servicer should not be permitted to schedule a foreclosure sale. If the CFPB relied on the initial application rather than the complete application as the trigger date, this level of complexity would be avoided. With a focus on the initial application rather than the complete application, there would be no need to suggest completion dates based on the greatest set of protections available to the borrower; that would be determined not by when the application is complete but rather when the initial application is submitted.

E. Borrower Protections Should Vest with Certainty, Even if a Foreclosure Sale Is Later Rescheduled. [Section 1024.41(b)(3)-Timelines]

The CFPB is proposing to add a new provision in § 1024.41(b)(3) addressing the timelines for determining borrower protections in relation to a scheduled foreclosure sale, in the situation in which a foreclosure sale has been rescheduled or when no foreclosure sale is scheduled as of the date a complete loss mitigation application is received. We support this proposed change, which would clarify that the timelines should be determined as of the date a complete loss mitigation application is received (though we again urge the CFPB to instead use the date an initial application is received). More importantly, though, we strongly support: 1) proposed comment 41(b)(3)–1 that would clarify that if a foreclosure sale has not yet been scheduled as of the date that a complete loss mitigation application is received, the application shall be treated as if it were received at least 90 days before a foreclosure sale; and 2) proposed comment 41(b)(3)–2 that would clarify that such timelines remain in effect even if at a later date, a foreclosure sale is rescheduled.

The availability of borrower protections under the loss mitigation rule should be established with certainty on the date a complete (or initial) loss mitigation application is received. Any alternative to this approach, such as by varying the timelines based on the proximity of the rescheduled or new foreclosure sale date to the receipt of a complete application, will make the rule overly complex and confusing to borrowers. It would also encourage servicers to immediately schedule (or reschedule) a foreclosure sale for the earliest possible date after receipt of a complete application, in the hope that the borrower may lose the right to appeal the loss mitigation decision or some other borrower protection. The CFPB's loss mitigation rules should not provide incentives to servicers to speed up the foreclosure process. A procedure in which the timelines are calculated based on a servicer's estimate of a scheduled foreclosure sale date is also highly problematic due to the inaccuracy of estimated dates and the potential for abuse of the process.

F. Consolidation of Notice Requirements Would Improve Ease of Compliance.[Section 1024.41(c) - Evaluation of Loss Mitigation Applications; Section 1024.41(c)(1) - Complete Loss Mitigation Application; Section 1024.41(c)(1)(ii)]

The CFPB is proposing to amend § 1024.41(c)(1)(ii) to provide explicitly that the notice required by that subsection must state the deadline for accepting or rejecting a servicer's offer of a loss mitigation option. The CFPB notes that it had intended that the § 1024.41(c)(1)(ii) notice would specify the time and procedures for the borrower to accept or to reject the servicer's offer, and that this is reflected in the requirement in § 1024.41(e)(2) that the servicer may deem the borrower to have rejected an offer if the borrower does not respond within the timelines specified under § 1024.41(e)(1).

The problem the CFPB is proposing to fix occurs in part because § 1024.41 does not have one subsection that deals exclusively with the requirements for notification of the servicer's decision with respect to a loss mitigation application. The servicer is required under § 1024.41(c)(1)(ii) to provide the borrower with a written notice stating the servicer's determination of which loss mitigation options, if any, are being offered to the borrower. However, this section appears not to address a servicer's determination that loss mitigation options will not be offered to the borrower. If the servicer denies a loan modification option, a different section, which is now re-codified as § 1024.41(d), applies and requires that notice be sent detailing the specific reasons for the denial of each modification option. Moving the requirements in § 1024.41(d)(2) to the § 1024.41(c)(1)(ii) notice is helpful; greater clarity would be provided by having one subsection that covers all of the evaluation notice requirements.

In addition, the § 1024.41(c)(1)(ii) evaluation notice requirement currently refers only to the loss mitigation options being offered to the borrower. Another provision in § 1024.41 that deals with dual tracking refers to the notice under § 1024.41(c)(1)(ii) as stating that the borrower is not eligible for any loss mitigation options. To avoid any ambiguity on this issue, we urge the CFPB to clarify, in § 1024.41(c)(1)(ii), that servicers are required to provide in the evaluation notice the specific reasons for the servicer's determination for any loss mitigation options that are not being offered to the borrower.

G. Limitations on the Duplicative Request Rule Would Clarify Servicers' Authority to Offer Short-Term Forbearance Agreements. [Section 1024.41(c)(2) - Incomplete Loss Mitigation Application Evaluation; Section 1024.41(c)(2)(iii) - Payment Forbearance]

The CFPB is proposing to modify the requirement in § 1024.41(c)(2) to allow servicers to offer certain short-term forbearances to borrowers, notwithstanding the prohibition on servicers offering a loss mitigation option to a borrower based on the review of an incomplete loss mitigation application. Specifically, the Bureau is proposing to add § 1024.41(c)(2)(iii) to provide that a servicer may offer a short-term payment forbearance program to a borrower based upon an evaluation of an incomplete loss mitigation application. Proposed comment 41(c)(2)(iii)-1 states that a short-term forbearance program allows the forbearance of payments due over periods of no more than two months. We support these changes, but only because they are necessitated by the duplicative request provision in § 1024.41(i). We urge the CFPB to place practical limitations on the duplicative request provision. If such limitations were adopted, there would be no compelling need for a special rule dealing with requests for short-term forbearances.

1. The Duplicative Request Rule Should Be Reconsidered or Clarified.

The brief, one sentence provision currently in § 1024.41(i) provides:

> (i) *Duplicative requests.* A servicer is only required to comply with the requirements of this section for a single complete loss mitigation application for a borrower's mortgage loan account.

This language may be construed such that the exclusion applies only to a request related to an initial loss mitigation application, but not to a totally separate request coming at a different time and under different circumstances. The caption for the provision is: "Duplicative requests." The word "duplicative" suggests that the provision would not be referring to a loss mitigation request being made years after an earlier request, as the two requests could not possibly be viewed as "duplicates." The CFPB has repeatedly referred to the provision as dealing with "renewed applications."[11] Again, a "renewed" application is consistent with a request being made in close proximity to an earlier request and involving the same nucleus of facts. Surely a request made five years after an earlier request does not involve a resumption after an interruption of the earlier request. Thus, the phrase "single complete loss mitigation application" in § 1024.41(i) should refer to one application made during a particular time period, in order to exclude multiple overlapping and contemporaneous requests for loss mitigation based on the same or similar facts. This interpretation is certainly most consistent with the consumer protection purposes of RESPA.

But the lack of guidance allows for multiple interpretations. The CFPB has not expressly included a time or material change limitation in the final rule, noting that limiting the loss mitigation procedures to a "single complete loss mitigation application provides appropriate incentives for borrowers to submit all appropriate information in the application and allows servicers to dedicate resources to reviewing applications most capable of succeeding on loss mitigation options."[12]

As a result, servicers may use the duplicative request exclusion under § 1024.41(i) to deny borrowers the loss mitigation rights provided under § 1024.41 because the borrower requested years earlier a short, six-month payment forbearance agreement to deal with a temporary job layoff. Under the proposed changes, the borrower in this example must be evaluated for all loss mitigation options even though the borrower is requesting only a short-term forbearance agreement. Because the duplicative application exclusion is not limited to an application for a loan modification, this request for a forbearance would appear to be the borrower's one and only opportunity with that servicer to have access to the consumer protections under the Regulation X loss mitigation rules. Even if there were an economic crisis five or ten years later not unlike that which preceded the adoption of the HAMP program, any request by the borrower at that later time for loss mitigation assistance for that mortgage account apparently would not be subject to § 1024.41. The borrower would lose the regulation's minimum protections, such as the notification requirements for

[11] *See* Section-by-Section Analysis, § 1024.41(i), 78 Fed. Reg. 10836 (Feb. 14, 2013).
[12] *Id.*

incomplete applications and loan modification denials, evaluation and appeal rights, and protections from dual tracking.

In adopting the duplicative request rule, the CFPB may have been influenced by somewhat similar provisions in the HAMP guidelines and other loss mitigation programs. However, any comparison that may be drawn between these programs and Regulation X is misguided. HAMP and the National Mortgage Settlement are temporary measures designed to deal with a crisis. Although HAMP has been extended, it is scheduled to terminate on December 31, 2015. The servicing provisions of the NMS will expire on October 2, 2015. Unlike these programs, the provisions of Regulation X and § 1024.41 are intended to be in effect for years to come and to establish a permanent set of servicing standards that will regulate the industry in the future.

Moreover, none of these other programs have provisions as draconian as the CFPB's duplicative request rule. HAMP's one modification limitation only applies to homeowners who actually receive modifications (and this limit is itself ill-advised, unnecessarily penalizing homeowners with genuine additional hardship), not to the procedural mechanisms in the program. A homeowner under HAMP is permitted to reapply after previously being denied a loan modification, and the servicer would be required to evaluate the borrower based on any subsequent requests. Under the FHA's loss mitigation program, if a borrower fails to successfully complete a trial plan, mortgagees must still re-evaluate the borrower's eligibility for other loss mitigation options.[13] If there has been a change in circumstances, the borrower is eligible to reapply for FHA assistance and begin a second trial plan if found eligible. If the borrower received a permanent loan modification or FHA-HAMP, the borrower is permitted to reapply after a period of 24 months. Under the Fannie Mae loss mitigation program, a borrower that previously received and defaulted on a Fannie Mae HAMP Trial Period Plan or a permanent HAMP modification is still eligible to reapply for a Fannie Mae standard modification.[14]

In addition, HAMP, the FHA and GSE loss mitigation programs, and the NMS actually compel servicers to evaluate and offer loan modifications under certain circumstances. In contrast, § 1024.41 merely imposes procedural requirements when a servicer evaluates a borrower for loss mitigation options, if such options are available. This distinction between mere procedural rules and substantive requirements alone justifies a different approach to the duplicative request issue. Quite simply, a rule that will ban huge numbers of consumers from access to the Regulation X loss mitigation procedural rights is bad policy and should be reconsidered by the CFPB.

We strongly urge the CFPB to either 1) clarify that the rule is intended to apply only to true "duplicative" requests arising out of the same factual scenario or incidence of default, or 2) reconsider the duplicative request rule under § 1024.41(i) in its entirety. Some practical and meaningful limitations on its application should be expressly provided for in the regulation, and no request arising out of a change in circumstances should be considered a duplicative request. If the CFPB is concerned that a changed circumstance standard may be difficult to administer, a time limitation would provide a bright-line rule and some protection for borrowers. For example, §

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[13] *See* HUD Mortgagee Letter 2012-22, Revisions to FHA's Loss Mitigation Home Retention Options, Nov. 16, 2012, *available at:*
http://portal.hud.gov/hudportal/documents/huddoc?id=12-22ml.pdf.
[14] *See* Fannie Mae (GSE Servicing Alignment) protocol, p. 13, *available at:*
https://www.fanniemae.com/content/job_aid/loanworkoutfactsheet.pdf.

1024.41(i) could provide that a servicer is not required to comply with the requirements of § 1024.41 for a complete loss mitigation application received within one year of the evaluation of a prior complete loss mitigation application. Alternatively, the CFPB could provide, in a manner similar to § 1024.39(b)(2), that a servicer is not required to evaluate a loss mitigation application in accordance with § 1024.41 more than once during any one-year period. However, given the vast difference between a borrower's circumstances in facing a temporary reduction in hours and the death or permanent disability of a co-borrower, for example, we urge the CFPB to implement a change in circumstances exception, as well as a time limitation, to the ban on duplicative requests.

2. Additional Borrower Protections Are Needed to Prevent Borrowers from Inadvertently Entering into Short-Term Forbearance Agreements Instead of Permanent Loan Modifications.

Short-term forbearance agreements are seldom helpful for borrowers or investors, although they can provide economic benefits for servicers kicking the can down the road. Historically, servicers have diverted borrowers into short-term forbearance agreements at the expense of both borrowers and investors.[15] If borrowers waste their one chance at loss mitigation review with a short-term forbearance request, real harm is done. A re-interpretation of the duplicative request rule, as discussed above, would reduce the harm done by servicer steering of borrowers to inappropriate short-term forbearance agreements. In the absence of clearer guidance on what is and what is not a duplicative request, further protections are needed for borrowers.

If § 1024.41(i) is kept in its current form, we urge the CFPB to make the following changes:

- Require servicers to notify the borrower of the consequences of the duplicative request rule under § 1024.41(i) in any § 1024.41(b)(2)(i)(B) notice sent to the borrower and in any written materials about loss mitigation that are made available to borrowers by the servicer;

- Proposed comment 41(c)(2)(iii)-1 should be revised to state that for purposes of the proposed exemption in § 1024.41(c)(2)(iii), a short-term payment forbearance arrangement may allow for the forbearance of payments due over periods of no more than six months.[16] Extending the allowable short-term forbearance to six months would keep the time period limited while allowing the many homeowners to need a few months of forbearance to still access the loss mitigation procedures another time.

- If the borrower makes an informed decision to be considered only for all forbearance programs offered by the servicer (even those extending beyond six months), and not to be considered for all available loss mitigation options, we propose that § 1024.41(c)(2)(iii) should provide that a servicer may offer a payment forbearance program to the borrower based upon an evaluation of an incomplete loss mitigation application and without considering the borrower for other loss

[15] *See generally* Diane E. Thompson, *Foreclosing Modifications: How Servicer Incentives Discourage Loan Modifications*, 86 Wash. L. Rev. 755 (2011).
[16] The example provided in proposed comment 41(c)(2)(iii)-1(i) would be inaccurate under our proposal as it precludes a three-month forbearance program.

mitigation options, and that the servicer is prohibited from treating the application as a complete loss mitigation application. Borrowers seeking forbearance should not be required to give up their procedural protections for all loss mitigation; under the Bureau's rubric, then, it is essential that the servicer not treat the request as a complete loss mitigation application. To avoid evasion of the requirement to evaluate a borrower's complete loss mitigation application for all loss mitigation options, we propose that the borrower's informed consent be documented in writing and verified by a third-party representative or agent of the borrower, such as an attorney or housing counselor.

Once again, these steps are from ideal but they are needed to counter the damaging impact of the duplicative request rule under § 1024.41(i).

H. The Servicer Creates a Reasonable Expectation that a Loss Mitigation Application is Complete When Providing Such Notice or Providing Notice of Missing Documents That Are Then Provided. [Section 1024.41(c)(2)(iv)]

As mentioned above, we support adoption of proposed comment 41(c)(2)(iv)-1 that would clarify that a servicer creates a reasonable expectation that a loss mitigation application is complete when the servicer notifies the borrower in the § 1024.41(b)(2)(i)(B) notice that the application is complete or when the servicer notifies the borrower in the § 1024.41(b)(2)(i)(B) notice that certain items are missing and the borrower provides all the missing documents and information.

I. Servicers Should Be Required to Disclose All Reasons for the Denial. [Section 1024.41(d) - Denial of Loan Modification Options]

The CFPB is proposing to amend § 1024.41(d) to require that a denial notice for loan modification options provided by the servicer must state the "specific reason or reasons" for the denial and also, where applicable, disclose that the borrower was not evaluated based on other criteria. Requiring servicers only to disclose the actual reasons the borrower was denied is helpful and sensible; servicers should be required to disclose, however, all of the reasons for the denial that were actually evaluated. This will simplify appeals, improve borrower understanding, and aid in compliance.

For example, if a borrower must meet qualifications A, B, C and D to receive a loan modification, and the servicer determines that the borrower fails qualifications A and C, proposed § 1024.41(d) suggests that the servicer need only disclose that the borrower has been denied a loan modification based on the failure of qualification A. In order to make the appeal process more efficient and meaningful, proposed § 1024.41(d) should make clear that the borrower should be notified that the loan modification was denied based on the failure of qualifications A and C.

Otherwise, the proposed amendment to § 1024.41(d) could provide a means for servicers to evade the requirement expressed in current comment 41(d)(1)-2 that if the servicer denies any loan modification option because of a net present value calculation, the notice must state this reason and include the inputs used for the calculation, for example. We are concerned that if qualification C in the above example were a net present value calculation that was actually performed, that a servicer may have an incentive to disclose only the denial based on qualification A so as to avoid disclosure of the NPV inputs and evade compliance with the comment 41(d)(1)-2 requirement. Our work with homeowners shows that borrowers are often given multiple and sequential bases for denial, which frustrates any attempt by borrowers to understand the actual basis for denial. Servicers should provide full and complete information to borrowers about the reasons for denial.

J. The Proposed Clarification Regarding Which Document Constitutes the Commencement of Foreclosure Is Helpful. [Section 1024.41(f) - Prohibition on Foreclosure Referral]

The Bureau is proposing new comment 41(f)–1 to clarify what servicer actions are prohibited during the 120-day pre-foreclosure review period. Proposed comment 41(f)–1 states that whether a document is considered the first notice or filing is determined according to applicable state law. A document that would be used as evidence of compliance with the foreclosure practices under state law is considered the first notice or filing, and a servicer is prohibited from filing or sending such a document during the pre-foreclosure period. However, other documents not used for this purpose are not considered the first notice or filing. Thus, a servicer is not prohibited from attempting to collect the debt, sending periodic statements, sending breach letters or any other activity during the pre-foreclosure review period, so long as such documents would not be used as evidence of complying with requirements under state law for initiating the foreclosure process (and are not prohibited by other applicable law such as the FDCPA or the Bankruptcy Code).

We support adoption of new comment 41(f)–1 as it provides helpful clarification of the 120-day pre-foreclosure review period.

K. In Order to Prevent Servicers from Evading the Intent and Letter of the Law, the Exceptions to the 120-Day Foreclosure Ban Must Be More Narrowly Drafted. [Section 1024.41(f)(1) - Pre-Foreclosure Review Period]

The CFPB is proposing to amend the foreclosure referral ban during the first 120 days of delinquency in two situations: when the foreclosure is based on a borrower's violation of a due-on-sale clause and when the servicer is joining the foreclosure action of a subordinate lienholder.

Our concern with the exception based on violations of the due-on-sale clause is that it is too broadly drafted and would allow foreclosure before the 120th day of delinquency in cases involving transfers of property protected by federal law. The Garn-St Germain Act provides that mortgages should be freely assumable between family members living in the home, whether they acquire title through death or divorce or devise. However, servicers routinely block modifications when family members seek to assume the mortgage. Servicers will usually not recognize the authority of a homeowner who is not on the note to modify a mortgage, even where there is a divorce decree or probate court order transferring responsibility for the mortgage to the homeowner who remains in the house. Until the homeowner has assumed the note and its responsibilities, servicers refuse to allow a modification. But, in a classic Catch-22, servicers will not allow assumption of the note while the mortgage is in default—and the only way to bring the mortgage out of default is through a loan modification. The result is often unnecessary and expensive foreclosures, at a loss to the investors as well as the homeowners. The CFPB's regulation prohibiting foreclosure starts during the first 120 days of delinquency is a positive step that could actually help align the interests of investors and widows, orphans, and divorcees.

Thus, the CFPB's proposed exception to the foreclosure referral ban should be more narrowly drafted to exclude transfers that are protected by the Garn-St Germain Act. Servicers should be required to comply with the regulation when 1) there has been a transfer of the property following the death of the borrower; 2) any transfer of the property resulting from an order entered in a family court, divorce, or probate proceeding; and 3) any other transfer of the property to a member of the borrower's family.

The exception for joining the foreclosure action of a subordinate lienholder should be limited to the situation in which all of the servicers and lienholders with respect to the property are separate entities. If a senior lien and junior lien on the property are both held by the same entity, the senior lienholder and its servicer should not be permitted to evade the obligations under the loss mitigation rules by simply initiating a foreclosure on a small second mortgage and then joining that foreclosure proceeding in order to take advantage of this exception.

L. The Regulation Should Expressly Provide That the Appeal Determination Notice Must Also State the Amount of Time the Borrower Has to Accept or Reject an Offer of Loss Mitigation. [Section 1024.41(h) - Appeal Process; Section 1024.41(h)(4) - Appeal Determination]

The CFPB is proposing to amend § 1024.41(h)(4) to provide expressly that the appeal determination notice must also state the amount of time the borrower has to accept or reject an offer of a loss mitigation option after the notice is provided to the borrower. For the reasons discussed above with respect to § 1024.41(b)(2)(i)(B), we support this change.

M. The Cross-Reference Regarding Exceptions to the 120 Rule Should Be More Narrowly Drafted. [Section 1024.41(j) - Prohibition on Foreclosure Referral]

The CFPB is proposing to amend § 1024.41(j) with respect to small servicers, to allow foreclosure before the 120th day of delinquency when the foreclosure is based on a borrower's violation of a due-on- sale clause and when the servicer is joining the foreclosure action of a subordinate lienholder, by incorporating a cross-reference to § 1024.41(f)(1). We do not oppose the cross-reference, but request that the CFPB consider and adopt the suggestions we offered above with respect to § 1024.41(f)(1).

II. The Loan Originator Compensation Proposals Should Be Revisited to Avoid Further Weakening the Statutory Protections

The Bureau should revisit its proposal to clarify the regulations addressing loan originator compensation. Aspects of the latest proposal amplify problems with the Bureau's recently finalized loan originator rules. The proposal issued on July 2, 2013 and the final rules issued in recent months are contrary to Congressional intent: they narrow the scope of Dodd-Frank and create loopholes that will be easily exploited. Below we describe specific problems with the Bureau's pending proposal; we recommend corrections; and we propose additions. But to adequately explain and address these problems, we also refer to problems with rules the Bureau has already issued. Our original comments on those proposals are available on NCLC's website.[17]

Before discussing our proposed revisions, we first note that in proposed Official Interpretation § 1026.32(b)(1)-2 the Bureau clarifies that charges paid by parties other than the consumer may be included in points and fees. This is important because the cost of a loan should not depend on who pays. This commentary may also reduce attempts to use third-parties to evade the points-and-fees definition.

A. Consumers are targeted for more reasons than financial characteristics.

The Bureau has added the phrase "to that consumer selected based on the consumer's financial characteristics" in many places. This was apparently done to clarify the scope of conduct that could subject a person to the loan originator regulations. For example, the Bureau proposes amending the definition of loan originator by specifying:

> The term does not include:
>
> (A) A person who does not take a consumer credit application or offer or negotiate credit terms available from a creditor <u>to that consumer selected based on the consumer's financial characteristics</u>, but who performs purely administrative or clerical tasks on behalf of a person who does engage in such activities. [proposed 1026.36(a)(1)(i)]

As the Bureau states in the Federal Register:

> The Bureau intended the references to "credit terms" in these provisions to refer to particular credit terms that are or may be made available to the consumer in light of the consumer's financial characteristics. The Bureau believes that, when a loan originator's or creditor's employee . . . is offering or discussing particular credit terms selected based on his or her assessment of the consumer's financial characteristics, the person is acting in the role of a loan originator. However, this does not extend to a person's discussion of general credit terms that a creditor makes available and advertises to the public at large, such as where such person merely states: "We offer rates as low as 3% to qualified consumers."
>
> In light of inquiries from loan originators and creditors, the Bureau is concerned that the term "credit terms" could be construed too broadly and thus render any person that provides such general information a loan originator. This was not the Bureau's intent. Accordingly, the Bureau is proposing to revise § 1026.36(a)(1)(i)(A) and (B), and comments 36(a)-1 and -4 to . . . clarify that any such activity must relate to "particular credit terms that are or may be available from a creditor to that consumer

[17] http://www.nclc.org/images/pdf/foreclosure_mortgage/dodd-frank/comments-cej-nclc-credit-insurance-delay05242013.pdf (May 24, 2013).

selected based on the consumer's financial characteristics," not credit terms generally.[18]

The Bureau's intention--to exclude generic discussions of credit terms--is reasonable, but the method of implementing it will also exclude conduct that should be subject to the loan originator regulations. Particular credit terms are not only targeted to selected consumers based on the consumer's financial characteristics. Unfortunately, consumers are sometimes targeted with specific credit terms based on their race, gender, ethnicity, zip code, or perceived gullibility to accept more expensive credit than their creditworthiness requires. Particular credit terms may also be offered based on incentives offered by the creditor. For example, a bank may give tellers a bonus for each customer referred to the loan department for a certain type of loan.

Any employee conduct that can reasonably be predicted to influence a specific consumer to select a particular credit term or product should be subject to the loan-originator regulations. How the employee selected the consumer or the credit term is irrelevant; what is relevant is the assistance in accessing credit. Limiting the scope of the loan originator regulation to conduct related to the consumer's financial characteristics will inadvertently exempt pernicious activities, such as steering, from the reach of the loan originator compensation rules, surely an unintended consequence.

The Bureau should revise the reference to a "consumer's financial characteristics" to more accurately reflect the loan origination process and to avoid perverse incentives to select credit terms on bases other than the consumer's financial characteristics. Specifically, if a loan originator or creditor's employee offers or discusses particular credit terms that have been selected based on *any* of the consumer's characteristics, or based on incentives offered to the employee by anyone, the employee is acting in the role of a loan originator.

NCLC recognizes that there are some employees who may fall into a "gray area" between clearly administrative/clerical jobs and clearly loan originators. If the Bureau is concerned by the burden of subjecting the employees in the gray area to the loan originator rules, the Bureau should follow Congressional intent and err on the side of making the gray area subject to the loan originator rules. But if the Bureau remains reluctant to do so, an alternative to making the scope of the rule too narrow would be to exempt the gray-area employees from the SAFE Act requirements of the loan originator rules while leaving them within the scope of the substantive regulations on loan originator conduct and the points-and-fees calculation. This alternative will spare the industry from the cost and administrative burden of registering and training employees under the SAFE Act without exposing consumers to unregulated loan originator conduct.

B. Adopt commentary to avoid abuse of the exemption for employees providing application forms from their employer.

The proposed Official Interpretation of § 1026.36(a)(4)(i) [proposed 1026.36(a)(4)(i)-4(i)] says "[t]he definition of loan originator does not include a loan originator's or creditor's employee (or agent or contractor) who provides a credit application form <u>from the entity for which the person works</u> . . . ." (emphasis added). For example: If Richard Receptionist, a salaried employee of Poisonwood Mortgage Brokerage, gives a new customer a blank loan application form with Poisonwood's name printed at the top, that action alone does not make Richard a loan originator.

[18] 78 Fed. Reg. 39901, 39924 (July 2, 2013).

Nevertheless, even though this is reasonable, additional clarification is necessary to ensure that this exception is not exploited.

Imagine that Poisonwood often brokers loans for Snakeroot Finance, a high-cost lender. If Richard gave the same new customer a Snakeroot loan application, Richard would be a loan originator because he is referring the customer to Snakeroot. But if Snakeroot had previously arranged for Richard to sign an employment contract specifying that he is an authorized agent of Snakeroot for the salary of $ X per month, Richard would no longer be a loan originator because--according to proposed OI 1026.36(a)(4)(i)-4(i)--he would be a creditor's agent who provided a credit application form from one of his employers--i.e. Snakeroot.

Limiting this exception to those employed by one organization might address this loophole and prevent the resurgence of bird-dogging by home improvement contractors and property flippers.

The Bureau should adopt additional commentary to prohibit creative schemes that abuse the exception described in the proposed interpretation.

C. Add commentary clarifying that "compensation" includes "anything of value."

Reg. Z § 1026.36(a)(3) (eff. 1/10/14) defines the term "compensation" as "includ[ing] salaries, commissions, and any financial or similar incentive." We compliment the Bureau for adopting a broad definition of compensation. But the commentary on the definition is inadequate and should be expanded. The Bureau should add commentary specifying that the term "compensation" is not limited to cash and equivalents. Compensation may include merchandise, services, trips, and anything else of value.

The proposed commentary to another aspect of the regulations already indicates that the Bureau accepts such a broad definition of "compensation." Proposed OI § 1026.36(b)-3(v)(D)[p160], for example, specifies that the cash value of non-cash compensation paid to a loan originator must be included when calculating the 10-percent cap on compensation. For clarity, the Bureau should add the list of examples found in proposed OI § 1026.36(b)-3(v)(D) to the commentary on § 1026.36(a)(3). The Bureau should also expressly state that compensation includes anything of value.

D. Abolish loopholes in compensation rules, or at least prohibit evasion.

The proposed and finalized regulation of loan originator compensation should be revised because it guts Dodd-Frank, is contrary to Congressional intent, and exceeds the discretion granted to the Bureau.

Dodd-Frank amended the Truth in Lending Act by adding provisions designed to eliminate harmful practices involving loan originator compensation. Congress decided to do so based on a well-developed body of research demonstrating conclusively that dual compensation and compensation based on the terms of a loan lead to higher pricing for homeowners across all categories,[19] rampant racial discrimination,[20] and, ultimately, the extension of unaffordable and unsustainable credit.[21]

Congress adopted Dodd-Frank after extensive and heated debate, ultimately deciding that abolishing abusive practices was an essential public policy. In doing so, Congress weighed arguments that Dodd-Frank would harm the financial services industry and reduce access to credit. But Congress ultimately decided that the need to protect consumers from predatory lending and to protect the financial system from unsafe and unsound practices outweighed those risks. Dodd-Frank charged the CFPB with implementing Dodd-Frank and gave the Bureau substantial discretion to do so, but nowhere did Congress condone regulations that would undermine the democratically adopted decision to value safe lending practices over protecting the financial services industry.

Nevertheless, the Bureau has adopted regulations that substantially weaken Dodd-Frank's protections, disregarding a clear Congressional mandate, and doing so based on arguments that Congress already rejected. There are two particular loopholes that we believe are most likely to be abused:

- The weak rules for deferred compensation and bonus plans; and
- The general loophole for compensation calculated in the aggregate.

1. Close the loophole for bonuses and deferred compensation.

The recently finalized provisions regarding deferred compensation and bonus plans are a gaping loophole in Regulation Z's limits on loan originator compensation. Rather than implementing the ban mandated by Dodd-Frank, the new regulations do little more than change compensation practices from a per-loan basis to an aggregate basis. This is nothing more than a mathematical sleight of hand. All forms of compensation should be subject to the same rules--without exception.

If the Bureau does not abolish the loopholes for bonuses and deferred compensation, it should at least adopt additional commentary to avoid abuse of these compensation plans. Specifically, the Bureau should explicitly state the general principal that no compensation plan may be structured in a way that intentionally or consequentially encourages loan originators to act against a borrower's best interests or to steer borrowers to loans based on anticipated compensation or other incentives. Making this guidance explicit will deter attempts to evade the spirit of Dodd-Frank. Importantly, it will also give regulatory examiners clear authority to look at the consequences

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[19] *See, e.g.,* Office of Pol'y & Dev., Dep't. of Hous. & Urban Dev., RESPA: Regulatory Impact Analysis and Initial Regulatory Flexibility Analysis, FR-5180-P-01: Proposed Rule to Improve the Process of Obtaining Mortgages and Reduce Consumer Costs, 2-24 - 2-43 (2008).

[20] *See, e.g.,* Debbie Gruenstein Bocian, Keith S. Ernst & Wei Li, Ctr. For Responsible Lending, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages 21-23 (May 31, 2006), *available at* http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf (discussing evidence and analysis that links pricing disparities with broker activity and incentives); *see also* Press Release, Office of the New York State Attorney General, Countrywide Agrees to New Measures to Combat Racial and Ethnic Disparities in Mortgage Loan Pricing (Dec. 5, 2006), *available at* http://www.oag.state.ny.us/press/2006/dec/dec05a_06.html (pricing disparities between whites and minorities highest for broker originated loans).

[21] *See, e.g.,* Rick Brooks & Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy: As Housing Boomed, Industry Pushed Loans to a Broader Market,* Wall St. J., Dec. 3, 2007, at A1 (61% of subprime borrowers in 2006 were prime eligible).

of compensation policies that may be superficially compliant, and to order changes if a compensation policy is found to have a negative impact on borrowers.

2. Close the loophole for aggregate compensation.

Under section 1026.32(b)(1)(ii), loan originator compensation is only included in the points and fees if it can be "attributed to the transaction at the time the interest rate is set." Proposed OI 1026.32(b)(1)(ii)-5. This rule will be easy to evade by designing forms of compensation that are calculated on an aggregate basis and cannot be determined on a per-loan basis when the rate is set. Retirement compensation and bonuses are examples of aggregate compensation, but any compensation not calculated on a per-loan basis (other than an hourly wage or salary) also falls within this loophole. Limiting the rule to compensation that can be calculated at the time the interest rate is set may simplify compliance but it also allows the financial services industry to continue abusive compensation practices.

If compensation is calculated based on factors that cannot be linked directly to an individual loan, originators will have an incentive to treat every loan as if it will have a measurable impact on the originator's total compensation. That is the very nature of incentive compensation--to encourage workers to be more productive. Compensation plans based on factors that cannot be measured at the time the rate on one loan is set may even be more effective than individualized, per-loan compensation because the plans permitted under the new rule will allow managers to emphasize peer pressure and esprit de corps as a way to motivate their producers.

The Bureau should not allow creditors and originators to game the rules by merely adding a calculation factor that cannot be determined at the time the interest rate on a transaction is set. The Bureau can resolve this problem in one of two ways. One possibility is by directing creditors to include all originator compensation in the points and fees--regardless of when earned or calculated--and allowing market forces to determine how best to comply with the rule. The most likely result is that some forms of compensation will be eliminated and others will become more favored or new ones developed. An alternative method would be to specify that when compensation cannot be determined at the time of the transaction, a substitute number should be used--for purposes of the points and fees calculation--based on the median amount of compensation for similar loans from the same creditor over the preceding twelve months.

E. The Bureau should acknowledge the reality that manufactured home sales prices often include loan originator compensation.

Proposed Official Interpretation § 1026.32(b)(1)(ii)-5(ii) (on p143) declares: "The sales price of the manufactured home does not include loan originator compensation that can be attributed to the transaction at the time the interest rate is set . . . ." This declaration is problematic because it is not necessarily true. Retailers can easily hide originator compensation in the sale price by inflating the price above what a cash customer would pay.[22] Congress recognized this fact by defining "creditor" as including someone who regularly extends credit "payable . . . in more than four installments . . . ."[23] The need for the "Four Installment Rule" was also recognized by the Federal

[22] *See generally* National Consumer Law Center, Truth in Lending § 3.10 (8th ed. 2012).
[23] 15 U.S.C. § 1602(g).

Reserve Board and the U.S. Supreme Court.[24] Although the difference between cash and credit sale prices should be considered a hidden finance charge, the Bureau's interpretation would prohibit courts and creditors from treating it as originator compensation--regardless of the intent or actual conduct of creditors and loan originators.

The practice of concealing finance charges in the sales price of merchandise is especially problematic for high-cost items, such manufactured homes, because most sales are on credit and there are a multitude of options available so that there are not standard cash prices for particular models as purchased. Therefore it is difficult for anyone to determine what the cash price for equivalent merchandise would be. The Manufacturer's Suggested Retail Price (MSRP) is not a reliable measurement. Many lenders use wholesale dealer costs rather than MSRP to calculate permissible LTV ratios. The MSRP does not include many of the options that are ultimately included with the sale. Also, the close relationship between many lenders, dealers, and manufacturers creates an incentive to inflate MSRPs. This is especially the case when the creditor and the dealership are both owned by a common parent corporation.

The Bureau should replace proposed clause 5(ii) with commentary specifying that any originator compensation concealed in the sales price must be included in the points and fees. It should also be separately disclosed.

III. The Bureau's Revisions on Financing Credit Insurance Should be Adopted with Some Changes.

We support much of the Bureau's analysis and proposed language regarding the financing of credit insurance. We propose a change in the definition of "financing credit insurance" to focus on additional costs to the borrower instead of deferment of premium payments. We address five issues raised in the Bureau's rule proposal:

- Effective Date;
- Definition of "Premium Calculated on a Monthly Basis";
- The Creditor as "Passive Conduit";
- Definition of "Financing Credit Insurance";
- Permissible Levelized Premium Products.

We begin with proposed changes to the text of the regulations.

A. Proposed Changes to Bureau's Proposal

Based upon our analysis and discussion, we propose the following changes, shown in redline, to the Bureau's proposed section regarding financing credit insurance.

[24] *See* Mourning v. Family Publications Serv., Inc., 411 U.S. 356 at 366, 93 S. Ct. 1652, 36 L. Ed. 2d 318 (1973) (discussing history and basis of Four Installment Rule).

(i) Prohibition on financing credit insurance.
(1) A creditor may not finance, directly or indirectly, any premiums or fees for credit insurance in connection with a consumer credit transaction secured by a dwelling (including a home equity line of credit secured by the consumer's principal dwelling). This prohibition does not apply to credit insurance for which premiums or fees are calculated and paid in full on a monthly basis.
(2) For purposes of this paragraph (i):
(i) "Credit insurance":
(A) Means credit life, credit disability, credit unemployment, or credit property insurance, or any other accident, loss-of income, life, or health insurance, or any payments directly or indirectly for any debt cancellation or suspension agreement or contract, but
(B) Excludes credit unemployment insurance for which the unemployment insurance premiums are reasonable, the creditor receives no direct or indirect compensation in connection with the unemployment insurance premiums, and the unemployment insurance premiums are paid pursuant to a separate insurance contract and are not paid to an affiliate of the creditor;
(ii) "Filed rate" means, for credit insurance, a rate filed with and not disapproved by the state insurance regulator and, for debt cancellation contracts and debt suspension agreements, the rate disclosed to the borrower prior to the application of that rate. ~~A creditor finances premiums or fees for credit insurances if it provides a consumer the right to defer payment of a credit insurance premium or fee owed by the consumer; and~~
(iii) Credit insurance premiums or fees are calculated on a monthly basis if they are determined mathematically by multiplying a filed rate by the actual monthly outstanding balance; and
(iv) A creditor finances premiums or fees for credit insurance when the borrower is charged more for credit insurance than a premium calculated in (iii).

B. The Bureau Should Set an Effective Date No Later than January 1, 2014.

Insurers have been on notice for years regarding the prohibition against financing credit insurance since the passage of the Dodd-Frank Act. There is and has never been a plausible interpretation of the statute to allow adding credit insurance premium to the borrower's monthly balance in a way that accrues interest charges on the credit insurance premium. The Bureau's implementation delay from June 1, 2013 has already caused borrowers to incur unnecessary and prohibited finance charges. We urge the Bureau to set an implementation date no later than January 1, 2014. If implementation requires credit insurers (and creditors) to modify credit insurance products or rates, there are benefits to implementation at the beginning of the year as opposed to later in January in terms of credit insurers' financial reporting to state insurance regulators.

Even for creditors now offering a levelized product, with equal monthly premiums, and who will shift to a true monthly outstanding balance ("MOB") product because of the statute and regulation, no delay is warranted. Credit insurers currently offering a levelized product to the creditor – as well as other credit insurers – have compliant credit insurance products filed, approved and ready to use. Credit insurers and creditors can implement new rates or a new product within a few months because credit insurance policies provide the creditor and the insurer with the ability to cancel a policy or change a rate with 30 days' notice to the insured borrower.

C. The Bureau Should Adopt Its Proposed Language Regarding "Premiums Calculated on a Monthly Basis" With One Clarifying Change.

We agree with the Bureau's analysis and conclusion that:

> the straightforward interpretation of the statutory language regarding a premium or fee that is "calculated…on a monthly basis" is a premium or fee that declines as the consumer pays down the outstanding principal balance. Credit insurance with this feature is often referred to as a "monthly outstanding balance," or M.O.B. credit insurance product.[25]

The industry proposal – that calculated on a monthly basis simply means a monthly premium is established[26] – is inconsistent with intent of the statute, which is to ensure that borrowers pay for credit insurance and not fees larded onto credit insurance.

We support the Bureau's proposed section 1026.36(i)(2)(iii). We suggest that the term "a rate" be changed to "a filed rate" with "filed rate" defined as,

> for credit insurance, a rate filed with and not disapproved by the state insurance regulator and, for debt cancellation contracts and debt suspension agreements, the rate disclosed to the borrower prior to the application of that rate.

By using the term "a filed rate" with this definition, the regulation will make clear that the calculation of credit insurance premiums must be based on the appropriate rate. This language is included in our proposed changes to the Bureau's proposal as 1026.36(i)(2)(ii). This definition of "calculated on a monthly basis" provides the foundational support for our analysis of levelized premium products and definition of financing credit insurance, below.

D. Creditors Are Never "Passive Conduits" Between Borrowers and Credit Insurers for Credit Insurance Premiums.

The Bureau asks for analysis regarding the extent to which creditors may function as "passive conduits." How one answers this question sheds light on the general definition of financing of credit insurance and on why levelized premiums may be abusive and should therefore in certain circumstances be considered financing of a premium.

Creditors are never "passive conduits" who simply collect premium payments from borrowers and transmit that premium to credit insurers. First, all creditors always receive a portion of the credit insurance premium as compensation when individual borrowers are charged for credit insurance.[27] This compensation can take the form of up-front commission, commission contingent on the performance of creditor's book of credit insurance, profits from an affiliated captive reinsurer and/or free or subsidized services provided by the credit insurer to the creditor which are unrelated to the provision of the credit insurance.

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[25] 78 Fed. Reg. 39901, 39929 (July 2, 2013).

[26] Summarized in the Bureau's rule proposal at 78 Fed. Reg. 39928.

[27] As opposed to non-contributory or blanket credit insurance, which covers all loans in a creditor's portfolio for which the creditor pays a premium to the credit insurer without individual charges to borrowers.

Creditors are not "passive conduits" for several other reasons. Creditors are always the named insured on the credit insurance policy and the primary beneficiary of any claims paid by the credit insurer. Creditors are always involved in the sale of the credit insurance with activities ranging from, at a minimum, providing names, contact information and loan information to credit insurers so the credit insurer can market directly to the borrower to actively selling the credit insurance to the borrower as an agent appointed by the credit insurer and licensed by the state insurance department. In addition, according to testimony by credit industry representatives before state insurance legislators, creditors typically maintain information required by credit insurance companies for adjusting claims.

E. The Bureau's Definition of Financing Credit Insurance Should Be Based on Additional Charges to the Borrower Instead of Deferment of Premium Payments.

The Bureau proposes to define "financing credit insurance" in terms of the creditor deferring payment. Proposed section 1026.36(i)(2)(ii) states:

> A creditor finances premiums or fees for credit insurance if it provides a consumer the right to defer payment of a credit insurance premium or fee owed by the consumer.

A borrower is not harmed by a creditor deferring payment of a credit insurance premium if the creditor does not charge the borrower for such deferment. A consumer suffers harm – meaning that the consumer suffers an additional cost – if the creditor charges the borrower for deferring the payment. The Bureau's proposed language could cause creditors to stop offering deferment of premium payments without charge for the deferment. In the situation where a creditor allows the consumer to defer premium payment without any additional cost or charge to the consumer, the consumer is not harmed and likely benefits from the creditor's action. Such a beneficial practice, while likely rare, should not be prohibited. In our view, the key action associated with financing credit insurance is not deferment of payment, but charging amounts in addition to the premium calculated by applying the filed rate to the outstanding balance. Consequently, we suggest changing the definition of financing credit insurance away from deferment and towards charging amounts greater than the premium calculated pursuant to the method established in the proposed rule -- an amount greater than the amount calculated by applying the filed rate to the monthly outstanding balance.

To change the meaning of "financing credit insurance" from deferment of premium payments to charges to the borrower beyond the premium payments calculated in 1026.36(i)(2)(iii), we suggest deleting section 1026.36(i)(2)(ii) and adding a new section which states:

> (iv) A creditor finances premiums or fees for credit insurance when the borrower is charged more for credit insurance than premium calculated in 1026.36(i)(2)(iii).

We suggest that the better approach to clarifying "financing credit insurance" is to do so in terms of additional charges to the borrower. Since the proposed rule provides the baseline for calculating a premium on a monthly basis, it makes sense to utilize that standard for identifying the additional charges that would amount to direct or indirect financing. We develop this analysis in more detail, below, with our discussion of levelized premium products.

In addition to precluding beneficial cost-free deferments to borrowers, defining financing based on deferment raises additional problems. Some debt suspension agreements are contracts between the creditor and the borrower that permit the borrower to defer payment for a fee. With the Bureau's definition, these types of "skip-a-payment" and other debt suspension agreements would be prohibited because the creditor is deferring the borrower's payment for the payment protection product as well as deferring the required monthly payment. In addition, it is confusing to define financing in terms of deferring payment when the purpose of the payment protection product is to allow the consumer to defer her monthly loan payment.

This problem with defining financing credit insurance in terms of deferment is vividly illustrated by the CUNA Mutual proposal that "creditors are not financing monthly premium or fee when the premium or fee is added to the consumer's loan balance each month but the consumer is obligated to pay the fee in full each month. In such a case, the creditor is not providing a right to defer payment of premiums or fees."[28]

We strongly disagree with such an interpretation. As demonstrated in our comments,[29] adding the monthly premium to the remaining principal balance increases the interest charges to the borrower or the term of the loan or both. There can be no more graphic example of a credit insurance financing practice by the creditor that is prohibited by the Dodd Frank Act.

CUNA Mutual's argument for an exception for "paid in full on a monthly basis" for situations where a consumer is "contractually obligated to pay the premium or fee in the same month or period in which it is posted" fails. First, a borrower is contractually obligated to pay any credit insurance premium or debt cancellation fee as part of a policy contract or loan addendum, respectively. There is no monthly-pay credit insurance or debt cancellation / debt suspension product for which the borrower is not contractually obligated to make the required premium or fee payment in full on a monthly basis.

Second, the fact that a borrower is obligated to pay a fee for the credit insurance or debt cancellation in the month the premium or fee is due is totally irrelevant to whether that fee is financed by adding it to the principal balance each month. If the premium or fee is added to the principal balance and the borrower pays only the required monthly mortgage amount, the credit insurance premium becomes financed by adding it to the remaining principal balance unless that amount of premium or fee is removed by the creditor in the same month it was added. Such a removal is not only unlikely as a matter of corporate policy but also difficult to implement even if such a policy is implemented (leading to the inevitable result that the premium is financed).

Third, CUNA Mutual makes contradictory arguments that, on one hand, financing credit insurance should be defined in terms of deferring payment of the monthly premium, and on the other hand, that adding the premium to the outstanding loan balance and charging interest on that additional loan balance -- deferring the payment of the premium and charging interest for the deferment – is neither deferment nor financing. The CUNA Mutual proposals are inherently

[28] CUNA Mutual comments Docket No. CFPB-2013-0018, July 19, 2013

[29] http://www.nclc.org/images/pdf/foreclosure_mortgage/dodd-frank/comments-cej-nclc-credit-insurance-delay05242013.pdf.

contradictory, would create massive confusion among creditors and borrowers, would create regulatory uncertainty and would conflict with the clear intent of the Dodd Frank Act.

F. The Fact That Creditors are Never "Passive Conduits" for Credit Insurance Premiums Requires the Bureau to Prevent Abusive Levelized Premium Products That Replicate the Harms of Financed Single Premium Credit Insurance.

Some levelized premium products should be considered financed. As described above, creditors are never "passive conduits." They receive compensation from credit insurers from the sale of credit insurance and this compensation can be provided in many forms. As a result, a creditor and a credit insurer could precisely replicate with a levelized monthly credit insurance product the monthly charges to borrowers and total compensation to a creditor as those produced by a financed single premium credit insurance product. Under the financed single premium scenario, the creditor's compensation would be commission from the credit insurer plus interest charged from financing the credit insurance. Under the levelized monthly premium scenario, the creditor's compensation could be all commission, but at a higher level equal to the amount of commission and finance charges from the financed single premium scenario. By any reasonable interpretation, such a levelized monthly premium product would be indirect financing of the credit insurance premium by the creditor.

The potential for a levelized product to replicate the harms to the borrower produced by a financed single premium product – a product that credit unions and the Departments of Treasury and Housing and Urban Development have identified as unfair and abusive to borrowers, and that Congress has prohibited – requires the Bureau to ensure that levelized products are not a loophole to evade the intent of Congress.

We interpret the Bureau's intent to be to provide a safe harbor for true MOB products, but to exclude levelized premium products from that safe harbor, while not specifically prohibiting levelized premiums products. Given the potential for abusive levelized premium products, we suggest the Bureau include commentary in the rule that a levelized premium product will not be considered to be financed directly or indirectly by the creditor if the monthly premium for the levelized premium product is determined as follows:

1. Calculate the premium for each month of the term of coverage pursuant to the method set out in proposed iii (*i.e.,* true MOB calculation);
2. Sum these monthly premium amounts;
3. Divide by the number of months of coverage;
4. Perform this calculation each month the credit insurance is in force.

This approach would provide a levelized monthly premium which was calculated each month based on the true MOB method set out by the Bureau and which would, presumably, be paid each month. If a borrower paid extra principal in one or more months, the monthly calculation would reflect the changed amortization schedule. On the other hand, if a borrower simply made the required monthly mortgage payments throughout the term of credit insurance coverage, there would effectively be only one premium calculation valid for every month of coverage.

Our proposed definition of "financing credit insurance," discussed above, is consistent with this levelized premium methodology because it does not increase the consumer's costs. Some current credit insurer practices, however, would not be consistent with this approach and would amount to indirect financing by the creditor. For example, some levelized premium products calculate a monthly premium based on discounts of future premium payments for the time value of month and for estimates of the percentage of consumers who will cancel or lapse their credit insurance each month over the term of a loan. Both practices raise the monthly premium amount above the amount produced by the methodology we set out above ("the base case"). By discounting future payments for the time value of month, the levelized monthly premium will increase over the base case and, consequently, increase the commissions paid to creditors over the base case. By assuming that some percentage of borrowers will cancel or lapse their credit insurance each month, the levelized monthly premium will also increase over the base case and, again, result in greater commission to the creditor. By introducing a product which provides more commission to the creditor than a true MOB product with the exact same coverage and benefits, the creditor is indirectly financing the credit insurance.

In summary, our proposed language and additional commentary would provide creditors and credit insurers with clear guidance about levelized products, clearly permit some levelized premium products and clearly prohibit levelized products that could replicate the consumer harms of financed single premium credit insurance.