Disclosure Requirements for Mortgage Transfers: New Amendments to the Real Estate Settlement Procedures Act

Leonard A. Bernstein
Chair, Consumer Financial Services Group, Blank, Rome, Comisky & McCauley, Philadelphia, PA

Follow this and additional works at: http://lawecommons.luc.edu/lclr
Part of the Consumer Protection Law Commons

Recommended Citation
Available at: http://lawecommons.luc.edu/lclr/vol3/iss3/3
DISCLOSURE REQUIREMENTS FOR MORTGAGE TRANSFERS: NEW AMENDMENTS TO THE REAL ESTATE SETTLEMENT PROCEduRES ACT

Leonard A. Bernstein*

I. Introduction

It can happen to anyone. You thought you borrowed money from a lender located in your neighborhood. However, one day you open your mail to discover that suddenly you are required to send loan payments to some post office box in an unfamiliar and distant town. As a result, you do not know who to call if you have a question about your loan. If you had known this would happen, you would have sought financing elsewhere.

This scenario recently befell a United States Congressman and his residential mortgage loan, and guess what happened? Shortly thereafter, legislation was introduced in Congress to establish new regulatory requirements for these so-called mortgage transfers. On November 28, 1990, President Bush signed the Cranston-Gonzalez National Affordable Housing Act (the “Act”), a comprehensive housing bill containing amendments (“the Amendments”) to the Real Estate Settlement Procedures Act (“RESPA”). The Amendments establish new notice requirements for servicing of mortgage loans and mortgage escrow accounts.

This article analyzes these new disclosure requirements for mortgage loan servicing and escrow accounts. First, the article outlines the problems presented to consumers by mortgage transfers and escrow account servicing before enactment of the Amendments. Next, a detailed examination of the new disclosure requirements for mortgage transfers is provided. The article then discusses the new requirements for escrow accounts, and concludes that the new disclosures should be complied with immediately.

II. Mortgage Loan Servicing Before The Act

A. Transfers of Mortgage Loan Servicing

Increasingly, residential mortgage lenders buy and sell portfolios of residential mortgage loans. Instead of selling the loans, residential mortgage lenders often transfer only the servicing of the loan while retaining original ownership. This phenomenon has been accelerated by the secondary market for mortgage loans, the emergence of mortgage-backed securities and the growth of the mortgage brokerage industry.

In many situations, the loan and/or servicing is transferred right after settlement. The borrower then receives the first notice to make payment to an unfamiliar entity. Other times, the transfer takes place years into the loan, without advance notice.

Before the new Amendments, the Real Estate Settlement Procedures Act, federal laws, and most state laws were virtually silent on transfers of mortgage loan servicing. As transfers of servicing accelerated, many consumers experienced difficulty with their mortgages. For example, borrowers reported horror stories about being unable to contact their original lender and to obtain adequate servicing. In response to this problem some states, such as New Jersey, established notice and procedural requirements for mortgage transfers.

B. Problems With Escrow Accounts

Similarly, escrow accounts have been another problem area in residential mortgage lending. Many lenders require payments in addition to principal and interest. These additional payments are placed into an escrow account from which the lender generally pays the borrower’s real estate taxes, property insurance, and similar costs. Recently, several state attorneys general cooperated by initiating a major lawsuit charging that a large residential mortgage lender kept excess funds in an account in violation of RESPA limits.

Many borrowers complain that it is difficult to follow the payments into and out of the escrow account. These consumers claim that in the case of transfers of servicing, the borrower loses the ability to at least annually monitor the payment stream: as a result, violations of escrow account limits occur more frequently. Congress responded to these difficulties with the servicing of mortgage loans and escrow accounts by enacting the new Amendments to RESPA.

III. Amendments To RESPA

A. Scope of New Notice Requirements

All lenders making RESPA loans must now provide new disclosures. RESPA governs loans which: (1) finance the purchase of and are secured by a first lien on residential real property (including condominiums) designed principally for the occupancy of one to four families; and (2) are federally insured or made by a federally insured financial institution, are intended to be sold by the originat-
ing lender to a federally affiliated entity, or are made by any creditor who makes or invests in residential real estate loans aggregating more than $1,000,000 per year. Therefore, just about any residential mortgage lender will be affected by the new RESPA notice requirements. Additionally, “servicers,” or entities that merely receive scheduled periodic payments from a borrower, are also covered by the RESPA amendments. Even consumer lenders offering loans which “refinance” a loan subject to RESPA may be covered.

B. Application Disclosure - Servicing Intentions

The Amendments require that the lender (or possibly a broker on the lender’s behalf), at the time of the application for the loan, provide the following disclosures to “each person who applies for the loan.” First, the lender must address possible transfers by indicating whether the servicing of the loan may be assigned, sold or transferred during the term of the loan. Second, the lender must disclose the historical percentages of previous transfers—the percentage (rounded to the nearest quartile e.g. 0%, 25%, 50%, etc.) of a lender’s loans for which servicing has been transferred for each of the three most recent calendar years completed at the time of application. This three year historical disclosure of loan servicing will be phased in. Presently, only figures for the one most recent calendar year must be provided. Also, for this disclosure, servicing transfers do not include transfers made to an affiliate or subsidiary.

Third, the lender must declare any present intention to transfer. If the lender does no servicing of any federally related mortgage loans, the disclosure must state that there is a “present intention” to assign, sell, or transfer the servicing to another.

Fourth, the lender must outline servicing procedures, transfer practices and requirements, and complaint resolution, as described in HUD’s model application disclosure form.

Fifth, the notice must describe the lender’s capacity to service and future percentage estimate of loan servicing to be assigned. HUD’s model application disclosure requires the originator to disclose its capacity to service loans and the “best estimate” of the percentage of all loans for which servicing will be assigned in the future twelve month period. This future percentage estimate must be expressed as a range of between zero and 25%, 26% and 50%, 51% and 75%, or 76% and 100%. As is the case with the historical percentage disclosure above, servicing transfers do not include transfers made to an affiliate or subsidiary of the originator.

Finally, the disclosure must include a signed acknowledgment. HUD’s model application disclosure requires applicants to acknowledge in writing that they have read and understood the disclosure. According to the Act, the entire application disclosure is not effective without the signature of, arguably, all of the applicants on the acknowledgement form prescribed by HUD.

Since enactment of the Amendments, many concerns have arisen about the required disclosures. For example, it is evident that a lender who has never transferred, nor ever intends to transfer servicing, must nevertheless provide the application disclosures. In contrast, it is unclear from the statute what the lenders that take applications by telephone or through the mail must do to comply with the disclosure requirements. When application forms are made available in the lender’s lobby, it seems prudent to attach a disclosure so that no borrower can claim that the disclosure was not provided at the time of application.

C. Transfer of Loan Servicing - Transferor Notice

In addition to the application disclosure, the RESPA amendments also require advance notice of the transfer of servicing. Each

(continued on page 88)
Mortgage Transfers
(continued from page 87)

The servicer must provide written notice to the borrower of such a transfer at least fifteen days before the "effective date of transfer."28 The "effective date of transfer" is defined as the date on which the borrower's mortgage payment is first due to the transferee servicer.29

One of several exceptions to the fifteen day advance notice requirement applies if the lender itself gives the notice of transfer of servicing at settlement.30 Lenders that do not service their loans must consult with their various assignee servicers in order to design appropriate forms of settlement disclosures.

Although some of the specified disclosures are duplicative, lenders may still want to include more items or detail than required. The servicer's notice of transfer must, at a minimum, contain the following information.

First, the disclosure must include the "effective date of transfer"31 and vital information about the transferee such as the name, address and toll free or collect telephone number of the transferee servicer.32

Second, the lender must provide a toll free or collect call telephone number for an individual or department of the servicer that can answer mortgage inquiries.33 Likewise, the lender must include information for transferee inquiries, such as the name and toll free or collect call telephone number for an individual or department of the transferee servicer that responds to mortgage inquiries.34

Third, the disclosure must specify the date on which the transferee servicer will cease to accept payments and the date on which the transferee servicer will begin to accept payments.35 Fourth, the lender must describe any effects of the transfer on existing credit life and other optional insurance policies.36 Finally, the disclosure must include a statement that the transfer does not affect the underlying terms of the loan.37

The fifteen day notice requirement may restrict certain transfers if the parties are not careful. Often, the servicer cannot give the notice at settlement because it has not established the identity of the transferee at that time, or it has not received funds from the transferee. If such a transfer does not provide the notice within fifteen days of the effective date of transfer, that servicer must collect the first payment even if the transfer is consummated during that period.

D. Transfer of Loan Servicing - Transferee Notice

The Amendments require transferee servicers to provide a notice identical to that described above for servicers.38 However, transferees have until fifteen days after the "effective date of transfer" to provide their notice.39 As with the transferrer notice, the transferee notice is not required if the lender provides the transferee notice at settlement.40

E. Late Charges Prohibition

The Amendments prohibit imposition of late charges by the transferee during the sixty day period after the "effective date of transfer" if the payment is inadvertently sent by the borrower to the servicer.41 If such payment is received by the transferrer before the expiration of any applicable grace period, imposition of late charges by the transferee is prohibited.42

In negotiating transfers of servicing, parties will need to consider whether and how to document the transferrer's apparent burden of advising the transferee of the exact date of receipt of misdirected payments.

F. Borrower Inquiries - Duty To Respond

The drafters of the Amendments not only created new notices, but also established the borrower inquiry response procedures required of servicers. The servicer's responsibilities to respond are triggered upon receipt of a "qualified written request."43 Such a request is defined as one that is in writing, is not on a payment coupon or other payment medium, includes or enables the servicer to determine the writer's name and account number, and includes a statement of reasons why the writer believes there is an error or a description of requested information.44

Although the borrower has no apparent way of knowing what must be included in the "qualified written request," most written inquiries will probably contain the required information, and servicers should consider treating all written inquiries as if they are "qualified written requests."

A loan servicer who receives a "qualified written request" from the borrower must provide a written acknowledgement of receipt within twenty days (excluding legal public holidays, Saturdays and Sundays).45 No acknowledgment is required if the requested action is taken during that period.46

Not later than sixty days after receipt of the "qualified written request", and, if applicable, before taking action on the inquiry, the servicer must make appropriate corrections in the borrower's account and transmit a written notification of such corrections, including the name and telephone number of the servicer's representative, to the writer.47 Alternatively, after conducting an investigation, the servicer must provide the borrower with a written explanation or clarification that includes a statement of the reasons why the borrower's account is correct, and the name and telephone number of an individual or department that can provide assistance.48

For mere information inquiries, the servicer must provide a written explanation that includes the information requested by the borrower or a statement why it is not available, and the name and telephone number of the officer or department which can provide assistance.49 Finally, during the sixty day period after receipt of a "qualified written request" concerning a payment dispute, the servicer may not report a contested overdue payment to a consumer reporting agency.50

G. Civil Liability and Damages

The Amendments contain civil damage provisions for violations of any of the requirements discussed above.51 The penalty structure is similar to that of the Truth-in-Lending Act.52 Liability to indi-
vidual borrowers will be equal to the sum of actual damages (if any) plus additional damages resulting from a "pattern or practice of noncompliance" in an amount not to exceed $1,000.53 Class action damages can equal the actual damages of the borrowers (if any) plus additional damages as a court may allow upon a "pattern or practice of noncompliance."54 These additional damages cannot exceed $1,000 for each member of the class, except that the total may not exceed the lesser of $500,000 or 1% of the servicer's net worth.55

Successful plaintiffs in these actions may obtain costs together with attorneys' fees.56 However, the statute does include a sixty day correction period which affords a servicer an opportunity to eliminate its liability if it notifies the borrower about the error and makes appropriate adjustments.57 Finally, in addition to civil liability for disclosure or error resolution provisions described above, the statute creates civil liability for a servicer's failure to make payments from escrow accounts for taxes and insurance "in a timely manner as such payments become due."58

H. Limited Preemption of Conflicting State Laws

Several states, such as New Jersey, have previously enacted similar legislation covering loan servicing and escrow account administration.59 The Amendments contain a limited preemption of state law provisions which require delivery to borrowers of an application disclosure and a notice of transfer of servicing.60 In New Jersey, for example, servicers or lenders that comply with the timing, content and procedures of the RESPA notice of transfer provisions can consider the corresponding New Jersey notice of transfer requirements preempted.

However, New Jersey law, for example, also requires that certain notices of transfer be sent to tax collectors.61 Such tax collector notice requirements are not preempted. As this scenario demonstrates, counsel should not make the error of overestimating the scope of the RESPA preemption and consequently ignoring state laws.

IV. The New Escrow Account Disclosures

In addition to the transfer of servicing disclosures, the Act also amended the existing escrow account provisions of section 10 of RESPA by requiring mortgage servicers to provide a series of new escrow disclosures to borrowers. This section of the Act on escrow disclosures has its own set of penalties, independent of the penalties discussed above.62 The Act also makes clear that lenders or servicers may not impose a charge on a borrower for preparation of any of the required escrow disclosures.63

With increasing delinquencies reported on residential mortgage loans, and with increased scrutiny by regulators and examiners of lenders' operations, it is unlikely that RESPA compliance deficiencies will long remain unnoticed.

A. Annual Shortfall Notice

First, servicers must notify borrowers at least annually of any shortfall in their mortgage escrow accounts.64 This new disclosure does not otherwise modify the existing right of mortgagees under RESPA to require the replenishment of deficient escrow accounts.

B. Settlement Disclosure

The second new escrow disclosure must be given at settlement or not later than forty-five days after the establishment of an escrow account.65 This disclosure must estimate the amounts and expected dates of payment during the first year, of taxes, insurance premiums, and other charges "reasonably anticipated" to be incurred.66 Congress has instructed HUD to create a modified HUD-1 settlement statement which can be used as the vehicle for providing this disclosure, or servicers could provide the disclosure later.67 Servicers are nevertheless free to use their own forms.

C. Annual Escrow Account Statement

Servicers must provide an annual disclosure statement to mortgagees which summarizes the year's escrow account activity.68 This disclosure must clearly itemize the borrower's current monthly payment, the portion of the monthly payment which goes into escrow, totals paid during the past year into and out of escrow identified by payment item (i.e. taxes), and the balance of funds in the escrow account at year end.69

This annual statement must be provided within thirty days of the close of each year by computation period, effective with calendar year 1991.70 Therefore, the first RESPA annual escrow statement must be provided in 1992.71

D. No State Law Preemption

None of the three federal escrow account disclosures described above preempt state law escrow account disclosures or procedures. Again, an examination of New Jersey law will provide a helpful illustration of the interplay between the new RESPA disclosure requirements and existing state law. Escrow account servicers active in New Jersey should be mindful of New Jersey's requirement that annual statements be provided within forty-five days of the end of each calendar year (unlike RESPA's thirty days). The New Jersey annual disclosure requirement first became applicable in 1991.72 Such lenders should not have waited until 1992 to provide annual statements.

...the notices should decrease instances where angry borrowers can claim that they did not know about a servicing transfer. Likewise, the estimated escrow expenditures shown in the settlement statement should reduce later inquiries.

Also, New Jersey's annual escrow account disclosure differs from the RESPA version by requir-

(continued on page 90)
Mortgage Transfers
(continued from page 89)

ing the additional disclosure of the beginning calendar year balance of the escrow account, as well as an itemized statement of all expenditures. This itemization appears to be more detailed than the RESPA requirement of totals disbursed for each item. Finally, the New Jersey Mortgage Escrow Act requires a ten day advance notice of change in the mortgagor's account payment.73

Such entities should comply now, with or without HUD forms, to the best of their ability, principally because of the risk of private actions, including class actions.

E. Escrow Notice Penalties

Unlike the servicing transfer notice penalties discussed above, the escrow account notice penalties are assessed by HUD and are retained by HUD. There is no private right of action. Unintentional violations of the new escrow account disclosure requirements may result in penalties to HUD of $50 per failure, not to exceed $100,000 per year per lender. For intentional violations, the penalty is raised to $100 per failure and there is no annual cap.74

V. Conclusion

With increasing delinquencies reported on residential mortgage loans, and with increased scrutiny by regulators and examiners of lenders’ operations, it is unlikely that RESPA compliance deficiencies will long remain unnoticed. Mortgage lenders and servicers are now facing class action law suits and regulatory examinations concerning their administration of adjustable rate mortgage loans, and the spotlight on these activities could soon shine on RESPA compliance.

Lenders may question the efficacy of the new requirements. Indeed, for lenders that never transfer servicing, providing the application disclosure seems meaningless. In addition, there is always the question of whether borrowers ever read consumer disclosures.

However, the new notices are not particularly burdensome. The application disclosure, notice of transfer, and the escrow notices should not cause significant disruption to the operations of lenders and servicers. Some lenders report that computer programs may need adjustment to accommodate the new annual escrow disclosures. Nevertheless, the notices should decrease instances where angry borrowers can claim that they did not know about a servicing transfer. Likewise, the estimated escrow expenditures shown in the settlement statement should reduce later inquiries. The borrower inquiry procedures were probably implemented to some extent by most prudent servicers before the Act was signed.

Finally, there has been significant controversy about the effective date of the RESPA amendments. Technically, they were effective upon the President’s signature. HUD then convinced Congress to state that the RESPA amendments were not effective until HUD regulations were promulgated.75 For most prudent lenders and servicers, this technical legal controversy should become irrelevant. Such entities should comply now, with or without HUD forms, to the best of their ability, principally because of the risk of private actions, including class actions.

ENDNOTES

1 Pub. L. 101-625.
13 12 U.S.C. § 2605(b)(3). If the percentages of transfers are less than 12.5%, HUD allows the actual percentage to be used. 56 Fed. Reg. 19508.
17 On March 20, 1990, HUD published a Notice in the Federal Register, effective immediately, which contains its Model Disclosure Statement and Applicant’s Acknowledgment of Servicing Transfer (the “HUD Notice”). 56 Federal Register 11866. This notice has been replaced by the Model Disclosure Statement published in the April 26, 1991 interim rule. 56 Fed. Reg. 19510. Use of the HUD language is mandatory, except for the form of the acknowledgment.
18 Id.
19 Id.
21 Id. at 19511.
22 Id.
23 Id.
24 Id.
25 The HUD Interim Rule requires the acknowledgement to be signed by the applicant and coapplicant, if any. 56 Federal Register 19511.
26 The HUD Interim Rule, however, states that if no face to face interview is held at the time of application, the Disclosure Statement is to be delivered to the applicant within three business days of receipt of the application. 56 Fed. Reg. 19509. The lender must thereafter obtain the signed acknowledgement. Id.
42 Id.
CONSUMER UPDATE

The Consumer Subcommittee of the Senate Committee on Commerce, Science and Transportation recently held a hearing on the Highway Fatality and Injury Reduction Act, S. 591. Senator Richard H. Bryan (D-NV), Chairman of the Consumer Subcommittee presided at the hearing to gather information on S. 591 and airbags as a highway safety measure.

S. 591 would require airbags in cars and light trucks manufactured after 1997. Senator Bryan, author of the legislation has stated that "this legislation is the single best measure the Senate can pass to protect the motoring public." The bill has received bi-partisan co-sponsorship. According to Senator Jack Danforth (R-MO), a co-sponsor, "[a]irbags provide protection for passengers that is superior to any other technology. Every American deserves this protection. It is my hope that this legislation will receive consideration by the full Senate very soon."

Witnesses at the hearing included Mr. Jerry Curry, Administrator, National Highway Safety Administration; Ms. Joan Claybrook, President of Public Citizen; Mr. Clarence Ditlow, Director of the Center for Auto Safety; and Mr. Thomas V. Hanna, President of the Motor Vehicle Manufacturers Association.

Read the Recent Legislative Activity section of the Loyola Consumer Law Reporter for details of this bill and other current developments in the federal and state legislatures.