Financial Services Update

February 23, 2015

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Federal Regulatory Developments

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WBK News

Jack Konyk will present an overview of the legislative and regulatory climate in Washington, DC at the Realty Alliance Winter Meeting on February 24 in San Juan, PR. For more information contact Jack at konyk@thewbkfirm.com.

Mitch Kider will lead a panel session titled "What to Expect from Enforcement Actions" at MBA's National Mortgage Servicing Conference on February 24 in Dallas, TX. For more information go to: http://events.mortgagebankers.org/Servicing2015/default.html.

Jack Konyk will participate on two panels, "2015 Regulatory Roundup" and "Compliance Management & Workflow Best Practices," at Ellie Mae's Encompass Experience on February 25 in Orlando, FL. For more information contact Jack at konyk@thewbkfirm.com.

Jason McElroy has been selected to the Banking Law 360 Editorial Advisory Board for the year 2015. For more information contact Jason at mcelroy@thewbkfirm.com.

SUMMARIES

Federal Regulatory Developments

CFPB Enters Into Consent Order with Mortgage Lender Regarding Alleged UDAAP and RESPA Section 8 Violations Related to its Marketing Activities

On February 10, 2015, the CFPB entered into a consent order with a nonbank mortgage lender in connection with alleged deceptive mortgage advertising in violation of the unfair, deceptive, or abusive acts or practices (UDAAP) provisions of the Consumer Financial Protection Act of 2010 (CFPA) and alleged payments for referrals of mortgage origination business in violation of Section 8 of RESPA. The parties involved in the activities at issue included the lender (which engaged primarily in originating refinance mortgage loans guaranteed by the Veterans Benefits Administration), a non-profit veterans' membership organization, and a third party broker company (which essentially managed the relationship between the lender and the veterans' organization and paid the veterans' organization a portion of the fees it received from the lender). Pursuant to the consent order, the lender is required to pay a civil money penalty in the amount of $2,000,000, as well as adhere to numerous other requirements such as reporting obligations and restrictions on future advertising efforts, particularly in connection with potential endorsements from third parties. This order is one of several in recent months in which the CFPB has addressed alleged violations of Section 8 of RESPA.

The consent order provides that the lender had entered into a marketing arrangement with the veterans' organization, facilitated by the third party broker company, in which:

- The lender was named the veterans' organization's "exclusive lender";
- The lender drafted and sent advertisements approved by the veterans' organization to the organization's members;
- The advertisements at issue: (i) included postal and electronic mail; (ii) were identified as the veterans' organization's advertisements; (iii) promoted the relationship between the lender and the organization; (iv) encouraged and recommended use of the lender's mortgage products; (v) were sent to consumers from a pre-screened list based on certain characteristics; and (vi) identified various reasons for which the organization chose the lender as its exclusive lender, which did not include identification of the regular payments made by the lender pursuant to the relationship;
- The third party broker company maintained a website for the veterans' organization's members which recommended the lender as a home financing option and which included hyperlinks to the lender's website;
- The lender paid a "lead generation fee" based on certain member responses to the veterans' organization and to the third party broker company;

- The lender paid a monthly “licensing fee” to the third party broker company; and
- The veterans’ organization’s members were not made aware of the payments.

Based on this activity, the CFPB found that it was a deceptive act or practice to fail to disclose the “material connections” between the lender and the veterans’ organization while at the same time making affirmative statements regarding the substantive underlying reasons for the endorsements. The CFPB indicated that, pursuant to the applicable legal standard, these actions likely would have been: (i) material to consumers evaluating the weight or credibility of the endorsements and whether to obtain a mortgage loan from the lender; and (ii) misleading to reasonable consumers.

Moreover, the CFPB found that, because the parties engaged in this activity (which included the above-described “referrals”) and the lender compensated the other two parties in connection with this activity, such payments in connection with the marketing of home loans constitute payments made in violation of Section 8 of RESPA (payments made pursuant to agreements and understandings to refer real estate settlement service business).

As a result of the consent order, in addition to the $2,000,000 civil penalty (paid to the CFPB’s Civil Penalty Fund), the lender is ordered to:

- Not engage in deceptive marketing with regard to mortgage credit products, specifically misrepresentations regarding the fact that an endorsement from a third party was made free of any material inducement or connection;
- Not assist others in making such misrepresentations;
- Not enter into any business relationships that constitute third-party endorsements that are inconsistent with FTC and CFPB guidance (existing and future) regarding endorsements; and
- Fully comply with RESPA Section 8 and make not payments in exchange for referrals of settlement service business.

With regard to this last bullet point, the CFPB stated that the lender “may not violate Section 8 of RESPA, including by providing a thing of value to a third party pursuant to an agreement or understanding to refer real estate settlement service business, including, but not limited to, providing a thing of value in exchange for an endorsement of [the mortgage lender] that is directed to a person.” Accordingly, the CFPB appears to be stating that compensation for endorsements constitutes a violation of Section 8 of RESPA, which may have a substantial impact on the manner in which affected parties engage in these types of activities in the future.

The CFPB’s summary of its action taken, as well as a copy of the consent order, can be found here: http://www.consumerfinance.gov/newsroom/cfpb-takes-action-against-newday-financial-for-deceptive-mortgage-advertising-and-kickbacks/

CFPB Takes Action Against Three Mortgage Companies for Deceptive Marketing

As part of a joint sweep with the FTC, the CFPB sued a mortgage lender and entered into consent orders with two other mortgage lenders for allegedly misrepresenting U.S. Government affiliation or approval of their products in violation of the Mortgage Acts and Practices Rule (the MAPs Rule or Regulation N) and the provisions of the Consumer Financial Protection Act (CFPA) prohibiting lenders from engaging in deceptive acts and practices. The CFPB filed a complaint against the Maryland-based mortgage lender in the U.S. District Court for the District of Maryland seeking a civil fine and a permanent injunction to prevent future violations. The consent orders with the other two lenders demand civil money penalties of $225,000 and $85,000, respectively. The $85,000 civil penalty amount reflects, in part, that company's financial condition, and will be paid with funds contributed to the company by its owners.

Specifically, the complaint and the consent orders identify the following problematic advertisement features:

- Misrepresenting that the source of the advertisements was, or was affiliated with, a governmental entity.
    - Displaying an eagle resembling the Great Seal of the United States.
    - Including a header that read "GOVERNMENT LENDING DIVISION" and "Housing and Recovery Act of 2008 Eligibility Notice."
    - Statements that the company "has been directed to" provide loans with certain features, in combination with references to federal legislation and references to the "Benefits Department."
- Misrepresented that the advertised mortgage credit products were endorsed, sponsored by, or affiliated with a government program.
- Direct mail pieces appeared as if they were United States government notices.
    - The overall format of the advertisements, including the use of plain text in labeled boxes and the title "Payment Reduction Notice," evoked a government form and obscured that the advertisements were from the company.
    - Envelopes included a reference to federal law but did not include a return address, and on the primary page of the advertisement the company's name appeared only in the small print disclosures.
    - Advertisements did not emphasize the company name, and the FHA Approved Lending Institution logo was displayed in a manner that created the false impression that the advertisements were an official government form, notice, or document, or otherwise conveyed the false impression that the advertisements were authored, approved, or endorsed by the government.
    - Displaying the web address "www.FHAdept.us."
    - Including the heading "PURSUANT TO THE FEDERAL HOUSING ADMINISTRATION (FHA) HUD No. 12-045."
    - Instructing consumers to call their "assigned FHA loan specialist."
    - Obscuring the company's name as the source of the advertisements in the disclaimer on the back of the advertisement that stated the company was

not an agency of the federal government and was not affiliated with the borrower's current lender.

- Advertisements included deceptive claims regarding reverse mortgages:
  - Misrepresented that the FHA-insured reverse mortgage program was time-limited or had a deadline.
  - Falsely stated that no monthly payments are required "whatsoever" under a reverse mortgage "as long as you and your spouse live in the home."
- One company claimed to be "HUD-Approved" when in fact it had surrendered its approval before such advertisements were distributed.

Regulation N prohibits any person from making "any material misrepresentations, expressly or by implication, in any commercial communication, regarding any term of any mortgage credit product, including but not limited to misrepresentations" that the "provider is, or is affiliated with, any governmental entity," or that the "product is or relates to a government benefit, or is endorsed, sponsored by, or affiliated with any government or other program, including but not limited to through the use of formats, symbols, or logos that resemble those of such entity, organization, or program." 12 C.F.R. § 1014.3(n). Section 1036(a)(1)(B) of the CFPA prohibits "unfair, deceptive, or abusive" acts or practices. 12 U.S.C. § 5536(a)(1)(B).

In addition, HUD Mortgagee Letter 2011-17 (April 15, 2011) places restrictions on the manner in which FHA lenders may advertise their products, including requirements that advertisements emphasize the HUD-registered business name, alias or d/b/a of the mortgagee and not the federal government; be written, formatted and structured in a manner which clearly identifies the mortgagee as the sole author and originator of the advertisement; and use of the FHA Approved Lending Institution logo(s) must include a conspicuous disclaimer that clearly informs the public that the mortgagee authoring the advertisement is not acting on behalf of or at the direction of HUD/FHA or the federal government. The disclaimer must be prominently displayed in a location proximate to where the FHA Approved Lending Institution logo(s) is displayed.

The CFPB and FTC looked at approximately 800 randomly selected, mortgage-related advertisements in newspapers, on the Internet, and on mail solicitations. In addition, the agencies became aware of some of the advertisements through consumer complaints.

A copy of the complaint and the two consent orders are available on the CFPB's website: http://www.consumerfinance.gov/newsroom/cfpb-takes-action-against-mortgage-companies-for-misrepresenting-u-s-government-affiliation/.

FTC Sends Letter to CFPB Summarizing Recent Efforts in Debt Collection

On February 5, 2015, the FTC sent a letter to the CFPB that describes the FTC's efforts in debt collection over the last year. Dodd Frank requires the CFPB to report to Congress on the federal government's implementation and administration of the Fair

Debt Collection Practices Act (FDCPA), and the FTC's letter is intended to assist the CFPB in preparing its report.

According to the letter, the FTC's work in debt collection over the last year focused on the following three areas: 1) egregious collection practices, such as "phantom debt collection" (when a debt collector attempts to collect debts that either do not exist or are not owed to the phantom debt collector); 2) the security of consumer data when debt is bought and sold; and 3) protecting limited-English-proficiency consumers from unlawful collection practices.
The FTC's letter also summarizes the three-pronged approach it takes with respect to debt collection: 1) vigorous law enforcement; 2) education and public outreach; and 3) research and policy initiatives. With respect to its law enforcement efforts, according to the letter, the FTC has focused in recent years on bringing a greater number of cases and obtaining stronger monetary and injunctive remedies against debt collectors that violate the law. The letter states that in 2014, the FTC filed 10 new cases against 56 defendants, resolved 9 cases and obtained $140 million in judgments, and banned 47 companies and individuals that engaged in serious and repeated violations of law from working in debt collection again. It also filed two amicus briefs with the CFPB, who it calls a "valuable partner," on key debt collection issues.

The FTC indicates that its staff regularly works with the CFPB in discussing ongoing and upcoming law enforcement, rulemaking and other activities. In addition to sharing debt collection complaints and cooperating on consumer education efforts, the FTC has been advising the CFPB on its rulemaking and guidance initiatives.

The FTC's letter can be found at the following link:
http://www.ftc.gov/system/files/documents/reports/federal-trade-commission-enforcement-fair-debt-collection-practices-act-report-consumer-financial/150209cfpbreport.pdf.

Litigation Developments

Class Recoveries Under Fair Debt Collection Practices Act Limited to Action, Not Per Defendant

According to a class action pending in Pennsylvania, two defendants violated the Fair Debt Collection Practices Act ("FDCPA") by sending a collection letter suggesting a debtor could avoid interest by paying a reduced amount to satisfy the debt. According to the allegations, Defendants were not actually applying interest to the debt, which made the collection letter false. Focusing on the issue of damages, the U.S. District Court for the Eastern District of Pennsylvania recently granted Defendants' *motion in limine* on the statutory limits to damages in the case. The court held that the relevant provision in §1692k of the FDCPA limits damages to the entire action, and not to each Defendant in the case.

In *Violet P. Blandina v Midland Funding and Midland Credit Management*, the trial court certified a class of plaintiffs in December 2014. The plaintiff, on behalf of the class, argued the maximum statutory damages recovery in the case should be $500,000 for each of two Defendants, or $1,000,000 overall. The two relevant damages provisions of the FDCPA, allow, in the first instance, damages in cases of an action by an individual up to $1,000, and in the second instance, damages in class actions up to $500,000, or 1 percent of the net worth of the defendant debt collector.

The Third Circuit Court of Appeals and other courts have found the $1,000 statutory limit for individual plaintiffs applies *per action*. The District Court noted the Third Circuit Court of Appeals has not yet directly addressed the damages limitation question for class actions. Relying of the logic of Third Circuit precedent, the District Court explained the word "action" in Section1692k(a)(2)(A), for both individual and class cases, meant that Congress chose to limit all statutory damages by action. The number of defendants did not matter.

Weiner Brodsky Kider regularly represents mortgage lenders and servicers throughout the United States, in connection with claims about mortgage loan servicing.