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Experts: Improper fees play part in crisis

Servicers may benefit from loans in default

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Charging improper or unexplained fees is a common practice for some mortgage servicing companies and is a larger part of the national foreclosure crisis than most people realize, experts say.

Questionable property inspections, late fees when payments aren't late, forcing homeowners to buy insurance even when they already have it — all occur nationwide and often go unchallenged by consumers, they say.

"It's really a major problem, and it's been around for a long time," said O. Max Gardner III, a North Carolina attorney who teaches bankruptcy boot camps for other lawyers.

A mortgage servicer is responsible for collecting monthly loan payments and crediting the homeowner's account. The servicer also handles escrow accounts for taxes and insurance.

The servicing companies don't actually own the loan, so they may not have a strong interest in providing good customer service. In fact, they may have an incentive to force a homeowner into foreclosure.

"The more defaults they have, the more fees they collect, the more money they make," said David P. Leibowitz, a Chicago-based foreclosure defense attorney.

Mortgage servicing fees aren't to blame for every home foreclosure. But some experts say mounting fees and charges are likely a factor in many if not most failed homeowners' downward spirals. Desperate families facing foreclosure are often confused by the fees and don't question or challenge them, they say.

"I think we're starting to see an understanding of the role of mortgage servicers in facilitating foreclosure or preventing foreclosure," said Katherine Porter, a law professor at the University of Iowa who has studied the role of mortgage servicing fees in bankruptcy.

April and Dan Lange, a Rice couple who lost their former home in Sauk Rapids to foreclosure last year, believe they were the victims of questionable mortgage servicing practices and that the problem likely has touched many others like them.

"I imagine that there's a lot of people that saw these fees and saw these same things, and never were able to discover that it had a name," April Lange said.

No options

Decades ago, people simply went to their local bank to borrow money to buy a house. The bank kept the mortgage for the life of the loan and collected the payments, said Lucy Morris, a senior attorney with the Federal Trade Commission.

"They were interested in ensuring a happy customer," Morris said.

But that's changed. Before the housing market collapse, mortgages and their servicing rights were being sliced and sold again and again. A consumer can't simply stop by their local bank and ask a question about a fee.

Some mortgage companies have their own servicing arm. Others sell the servicing rights on their loans to large companies that specialize in handling thousands of accounts.

The servicers make very little profit from the collection of payments, Gardner said. However, whatever the servicer can collect in fees — for late payments, property inspections or anything else — it gets to keep. That provides the servicer an incentive to put the loan into default, he said.

"They really don't care about customer satisfaction, because the consumer does not pick the servicer," he said.

Consumers should be aware that mortgage servicing companies don't work for them, Porter said.

"You rely on them at your peril," she said.

And it's nearly impossible to get rid of a servicer. Some of Gardner's clients have refinanced their loans just to get away from a servicing company, only to wind up back with the same company under the new loan.

"There's really just no option for the consumer," he said.

April Lange tried numerous times to contact her servicing company, with little success. When she did speak to a representative, she was told the fees were just "standard servicing of the loan."

"I think there was never a real intention on the part of the servicers that we were dealing with to let us succeed," Lange said. "I think that the odds were against us."

Questionable tactics

Improper servicing can show up in many ways. The Langes noticed late charges when their payments weren't late, fees for unexplained property inspections and a charge for homeowners' insurance although their property was already insured.

Those are similar to examples of improper servicing Leibowitz has seen. A homeowner's payments are supposed to go toward the principal or the interest on the loan. But if a payment is late — or held so that it's late — the servicer often puts the money into a suspense account, which means it's not being applied to the loan.

That puts the loan into default, setting off a cascade of other fees such as late charges, attorney's fees and drive-by property inspections, Leibowitz said.

Some of the charges might be legitimate. One drive-by inspection to make sure a home is still occupied is understandable, Leibowitz said.

"It's fine once to see the property," he said. "Is it legitimate to have six drive-by inspections?"

There's also some question about whether the inspections actually are taking place, or if homeowners are being billed for a service that never occurred, Leibowitz said.

For a low- to medium-income homeowner, the additional charges might be just enough to push them over the edge, Gardner said.

"They're having enough of a problem trying to make their regular contract payments," he said. "If you add another \$200 to \$300 to what they have to pay, they're just not able to make that payment. You're going to create a default."

And even when a home is in foreclosure or a homeowner files bankruptcy, the charges don't necessarily cease.

In 2007, Porter studied 1,733 bankruptcy cases filed in 24 states in 2006 and concluded that mortgage companies frequently do not comply with the law. A majority of mortgage creditors' proofs of claim were missing information and frequently did not identify fees.

In nearly all cases, the homeowners and the mortgage companies disagreed on how much money was owed, Porter found. The creditors asserted that bankrupt families owed them at least \$1 billion more than the families believed they owed, she found.

Although Porter studied only bankruptcy cases, she believes the misbehavior and mistakes made by some mortgage servicers are just as problematic for nonbankrupt homeowners.

The findings "suggest that flawed mortgage servicing practices are a key contributor to the current crisis in the home mortgage market," Porter wrote.

Legal trouble

The Federal Trade Commission has charged two companies with fraudulent loan servicing and settled with both companies for substantial sums, although neither admitted any guilt.

In 2003, the FTC agreed to accept a \$40 million payment from Fairbanks Capital Corp. to settle its case against the Utah-based company, which the FTC accused of unfair and illegal practices. The company has since been renamed Select Portfolio Servicing Inc.

The FTC charged that Fairbanks frequently failed to post consumers' mortgage payments in a timely manner, then charged them late fees or additional interest. The FTC also said Fairbanks charged consumers for placing insurance on their loans when they already had insurance and collected other unwarranted fees.

In 2008, Bear Stearns Cos. and its subsidiary, EMC Mortgage Corp., agreed to pay \$28 million to settle the FTC's charges that it engaged in similar misbehavior, including misrepresenting the amounts that borrowers owed.

Morris, who was the lead attorney on both cases, said the FTC's view is that the mortgage contract "isn't a blank check just to charge any and all fees they want to charge."

In the Bear Stearns case, the FTC alleged that the company was buying and selling loans at such a fast pace that they weren't paying adequate attention to making sure they had accurate information on all their consumers, Morris said.

A third company, the mortgage giant Countrywide Financial Corp., recently disclosed that the FTC is looking into its loan servicing practices. Morris confirmed the investigation.

Changes needed

So why don't more homeowners question unexplained fees that show up on their mortgage statements?

Like other families facing foreclosure, the Langes were struggling to keep up with their payments. They didn't understand all the fees and charges, but kept sending payments to avoid losing their home.

"You're doing everything you can to come up with money and to pay them," April Lange said. "It was like this constant confusion and trying to satisfy them."

It was difficult for the Langes to accept that the people they were trusting with their money may not have had their best interests in mind.

"Part of the mistake that my husband and I made is that we trusted the mortgage companies to be keeping track of what we actually did owe," April Lange said.

Under the Real Estate Settlement Procedures Act, loan servicers are required to make timely insurance and property tax payments on behalf of borrowers and properly administer their escrow accounts. RESPA is enforced by the U.S. Department of Housing and Urban Development.

But many homeowners aren't aware of the law, and not all bankruptcy attorneys are aware of servicing fraud, Leibowitz said. Bankruptcy and foreclosure cases typically move through the courts in an assembly-line fashion, with little time spent on each case, he said.

"Most people don't know that they can stand up and say, 'I don't owe this much money,'" Leibowitz said. "Just because the mortgage company says you owe it doesn't mean you owe it."

Some experts believe tighter federal regulations are needed to stop servicing fraud.

The Obama administration is starting to address the issue by proposing giving mortgage servicers a bonus if they work with struggling homeowners to modify their loans, Porter said. "It's clear to me that we need to realign the incentives of the mortgage servicers so they are actively working to prevent foreclosure," she said.

But for many families, the changes will come too late.

"It's been so traumatic, because you have faith in institutions and businesspeople that you think are looking out for your interests," April Lange said. "And it feels to us, over the last couple of years now, we just can't have faith in anyone. We have to have faith in ourselves."
