

# LEGAL LEAGUE QUARTERLY

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*National*

## EXPLORING NEW TERRITORY *Mortgage Servicing professionals and their attorney network adopt new policies, practices, and processes in the wake of the recent OCC consent orders.*

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IN 1492, Christopher Columbus first introduced the New World to the Old World and forever changed how the Old World operated. More than five centuries later, a similarly transformative event took place in the mortgage servicing industry. In April 2011, 14 major mortgage servicers signed consent orders with the Office of the Comptroller of the Currency (OCC), the Office of Thrift Supervision, and the Federal Reserve changing not only how servicers will operate, but also how their mortgage default law firms operate. The OCC consent orders have law firms scrambling to keep up with varying interpretations of the broadly stated guidelines, significant additional requirements, and voluminous document requests for file-specific audits.

### AN ATTEMPT AT REFORM

The consent orders and the report entitled “Interagency Review of Foreclosure Policies and Practices” provide guidelines for the mortgage servicing industry following the robo-signing scandals of late 2010. In June, the OCC broadened the scope of the consent orders to include all servicers under OCC supervision. The underlying intent is to ensure compliance with foreclosure laws, conduct foreclosures in a safe and sound manner, and establish responsible business practices that provide accountability and appropriate treatment of borrowers. The guidelines attempt to address perceived issues found in the following

areas of servicer operations: foreclosure process governance, organizational structure and availability of staffing, affidavit and notarization practices, documentation practices, third-party vendor management, and quality control and audit.

### BEFORE AND AFTER

In the old servicing world, pre-consent order, servicers had frequent contact with the law firm personnel on file-specific issues or state-specific legal requirements. Questions regarding breach letters, collectable fees, costs, and timelines were commonplace. Surveys from servicers asked attorneys to respond with information regarding licensing, third-party dependence, experience, and insurance amounts. As noted in the interagency report, rather than conducting their own due diligence, servicers in some cases depended on the fact that certain firms had been designated as approved by investors or had contractual relationships with default management service providers.

In the new servicing world, since April 2011, servicers are taking a more structured role in attorney selection and requirements to comply with consent order directives to manage the relationships. Attorney review is performed by the vendor management function, which utilizes a defined, systematic process to evaluate the entire scope of the relationship—not just the file or state spec-

ics. The attorney network is now held to the same standards as all other bank vendors who process critical data, whether that is a large multinational credit card processor, a server farm hosting corporate websites, or a business continuity provider.

In the new world, servicers are auditing the attorney network and more actively managing the relationship in order to comply with the consent orders. Law firms, in turn, are quickly implementing procedures, formalizing policies, and acquiring infrastructure to maintain their position as approved vendors.

### SECURITY, OVERSIGHT AND NEW PROCEDURES

Today, attorneys must have a comprehensive, documented Information Security (InfoSec) policy that incorporates physical security policies as well. A comprehensive InfoSec policy includes written policies for privacy, record retention, and anti-fraud. The OCC noted potential weaknesses in the safeguarding of original loan documentation and critical foreclosure documents and, therefore, determined that clear records management policies and procedures must be administered. The new focus on information security includes regulations regarding how case management software is configured and what are the controls surrounding change management and password protection. Encryption and two-factor authentication are other mandatory attributes of an effective InfoSec policy.

Mortgage servicers are requiring significant physical security policies as well. Not only are access badges required, but new policies are being implemented to ensure they are accounted for at all times. A data center with very limited access, a log tracking who entered, and special monitoring (both local and remote) for smoke, fire, temperature, humidity, and water discharge is essential. In addition, non-Information Technology (IT) incidents must also have documented handling procedures. Examples of non-IT

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incidents include medical emergencies, power outages, fire damage, violent debtor incidents, and other non-routine events.

Not surprisingly, the interagency report noted potential weaknesses in affidavit and notarization practices, the specific issues that contributed to the robo-signing scandals. Individuals who signed foreclosure affidavits often did not personally check the documents for accuracy or possess the level of knowledge of the information that they attested to in those affidavits. Examiners also found that many servicers had improper notary practices that failed to conform to state legal requirements. As part of the attorney review, servicers are now confirming the affidavit and notary process, verifying the existence of notary logs, questioning the depth of personal knowledge in the process, and confirming compliance with state- and client-specific requirements.

A thorough attorney review requests attorney and processor per-file ratios and information on the experience level of individual attorneys in order to assess capacity planning as part of the risk assessment portion of the consent orders. A structured training program on legal issues—like FDCPA, for example—and client-specific requirements mitigates the risk of invalid foreclosures. In the new world, law firms must demonstrate that they have the capacity

and capability to perform foreclosure practices in accordance with servicer expectations. Servicers have always looked for attorneys who stand behind their work. Past practices and informal “handshake” arrangements, however, are no longer satisfactory. Now servicers may insist upon financial statements and insurance coverage for malpractice, crime, and cyber theft in order for an attorney to be approved to receive default-related referrals.

The law firms have many new requirements to create and implement in a short period of time. As an added level of difficulty, servicers are also looking for validation that the law firm is holding its vendors to the same standards and has a third party vendor management program of its own. This pushes the compliance requirements down to title agencies, pub and post providers, and process servers, among others.

The last piece of the interagency report with a significant impact on the attorney network is the foreclosure review. The consent order requires the servicer to retain an independent firm to conduct a review of residential foreclosure actions that were pending at any time from January 1, 2009, through December 31, 2010, to identify any potential financial injury to borrowers. The result is an onslaught of file-specific requests from

servicers to the attorney network. The reviews, covering thousands of files, request specific information, including documents, foreclosure milestones, results, and related notes. All servicers are under similar time frames to respond to the OCC, making time-sensitive file reviews a significant undertaking for law firms. At the same time, newly instituted audit requirements and quality control programs have made these requests an ongoing part of the process.

With the new consent orders providing a range of specific initiatives and a number of additional broad-based guidelines for the future, it is clear that for default servicing professionals, and especially for attorneys providing mortgage default processing, the world is no longer flat. Quite the contrary, the mortgage servicing map has become newly multidimensional and very complex. This is uncharted territory for all of us, and it is going to be fascinating to watch this new world take shape.

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