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CFPB Resists Mortgage Rule Delays, Putting Heat On Lenders

By **Evan Weinberger**

Law360, New York (August 29, 2013, 8:22 PM ET) -- The Consumer Financial Protection Bureau is holding fast to its plan to fully implement a raft of new mortgage rules in January despite industry pleas for more time, a tough stance banks fear will force them to cut back on lending or face a wave of enforcement and private litigation.

The nearly 4,000 pages of new mortgage rules, which the CFPB released over the course of this past January and is still revising, will change every aspect of a mortgage lender's business, including how they determine whether a borrower can afford the loan sought, how payments are collected and how lenders engage with borrowers who run into trouble. All of those new rules require a revamp of lenders' compliance systems, and bankers are beginning to worry that they will not be ready when the rules go live over a 10-day span next year.

With the CFPB already proving to be an aggressive enforcement agency, lenders believe that without at least a grace period they could be subject to enforcement actions even if compliance problems are caused by a lack of time to make sure their new systems work.

"There's so little time to be able to push out the new compliance requirements, the concern is that there's not going to be enough time to test them properly," said Joseph Lynyak, a partner with Pillsbury Winthrop Shaw Pittman LLP. "The penalties are so great that people are afraid they're not going to be ready."

So far, it appears that smaller banks and community banks as well as nonbank mortgage lenders are having the most trouble getting up to speed on the new rules.

According to a survey released Tuesday by the American Bankers Association, around 79 percent of responding banks are relying on outside vendors to provide the software needed to comply with the new mortgage rules.

Of those banks, 60 percent said that their vendors had not informed them of when the software would be ready as of the end of June, the survey found. And even among the banks that know when the software will arrive, only 8 percent expect to receive the software by the end of October.

That could present a major problem on several levels.

For one, the ABA said that many banks have an information technology "freeze" in place at the end of the year that allows them to focus on year-end tax and reporting requirements.

For larger, publicly traded banks, that freeze is mandated by the Sarbanes-Oxley Act, according to Robert Davis, the ABA's executive vice president for mortgage policy. Smaller banks tend to find that the freeze is good practice, he added.

And since nearly half of the banks that responded to the ABA survey said it would take between two and three months to fully test the new software, they are unlikely to know whether their new tools will work before they have to be up and running, Davis said.

"Community banks in particular have indicated that updated software, programming and training are big concerns, and training can't occur until systems are operational," he said, noting that over 70 percent of the 187 banks that participated in the survey had total consolidated assets of under $1 billion.

Along with the problems of creating and testing the technology necessary for complying with the new rules, nonbank mortgage lenders are still getting used to having a single federal watchdog, said Dylan Howard, a shareholder with Baker Donelson Bearman Caldwell & Berkowitz PC.

The CFPB has proven itself to be an aggressive regulator that seeks big penalties, and the fear is that a small problem on the tech side could result in a major financial hit, Howard said.

"Everybody's going to have issues, and we're going to see a lot of enforcement actions right out of the gate," he said.

That's why the ABA and other lenders have asked the CFPB to at least provide a grace or transition period before enforcing the rules if it won't delay their implementation date, which was mandated by the Dodd-Frank Act. But that seems unlikely.

"Congress established an outside deadline for the effective date of the mortgage rules it directed us to write, and we set the effective date to reflect that deadline. We fully expect all institutions to be in compliance by Jan. 10, 2014," a CFPB spokeswoman said in an email to Law360 on Thursday.

Even if the CFPB were to provide some sort of a break for banks and other lenders that have tried in good faith to comply with the rules, there are still risks that other players won't be as understanding, Davis said.

Other federal regulators will be examining banks for compliance with the ability-to-repay, mortgage servicing and other rules and coordination will be difficult, he said.

And those aren't the only risks lenders face.

"The reason we are skeptical that there can be a regulatory-mandated get-out-of-jail-free card is that in the interim state [attorneys general] can enforce the law and private litigants can do all sorts of things in court," Davis said.

The best way for lenders to protect themselves without some sort of a transition period is to raise their credit standards even higher as they test their systems, and curtail lending in the near term, he said.

While that may be a common refrain from banks whenever new rules are introduced, in this case the lending cut may actually come to pass until lenders can be sure their systems work.

--Editing by John Quinn and Katherine Rautenberg.