Lessons for Smaller Creditors

November 13, 2015

As we look back on 2015, it's not surprising that the CFPB's enforcement actions continued to focus on mortgage-related practices. What was surprising was that its actions were not confined to the nation's largest banks and non-bank institutions, but had expanded to smaller originators. Large and smaller originators alike were targeted for vendor practices.

For example, back in February 2015, the CFPB announced enforcement actions against three smaller mortgage lenders – Maryland-based All Financial Services LLC, Utah-based Flagship Financial Group LLC and California-based American Preferred Lending – because of their direct-mail marketing campaigns that had been handled by vendors. All three companies tried to make a selling point of government-guaranteed or government-insured mortgage loans.

Of the three smaller lenders, only All Financial Services attempted to dispute the allegations in the CFPB's complaint before reaching settlement. The complaint and answer in federal district court, therefore, provided a rare glimpse into how the CFPB's investigation and enforcement process plays out.

At issue was All Financial Services' HECM ("home equity conversion mortgage," a reverse mortgage product that is insured by the FHA) solicitations that were sent to consumers between November 2011 and December 2012. All Financial Services used a marketing company to create its solicitations.

The envelopes for the direct-mail solicitations simulated the look of an official government notice by depicting a symbol of an eagle with arrows as well as including various statements on the envelope that sounded official – such as "Home Saver – HECM Program Eligibility Notice," "Government Lending Division" and "Housing and Recovery Act of 2008 Eligibility Notice." The cover envelopes also conveyed a sense of time limitation with statements such as "Important Document Enclosed" and "Open Immediately." Inside, the correspondence described how a reverse-mortgage loan worked, using an easy-to-read, colloquial explanation that amounted to imprecise statements about paying off the loan.

The CFPB asserted that the direct-mail solicitations: 1) misrepresented that the source of the advertisements was, or was affiliated with, a governmental entity; 2) misrepresented that the FHA-insured reverse-mortgage program was time-limited or had a deadline; and 3) falsely stated that no monthly payments are required "whatsoever" under a reverse mortgage "as long as you and your spouse live in the home."

In its response to the complaint, All Financial Services defended itself by arguing that the CFPB's claims were barred or attributable to acts of others over which the company had no control. The company also argued that the claims were time-barred; many of the alleged wrongs were corrected by the company before the investigation began; and many of these allegations were not part of the initial investigation and statement of alleged wrongs to be corrected.

Based on the allegations in the CFPB's complaint and the defenses raised by All Financial Services, however, there were a number of lessons for other creditors:

- First, All Financial Services had stopped the direct-mail solicitations at issue more than two years earlier, and had corrected many of the issues on its own before the CFPB's investigation. Apparently the CFPB did not consider the corrective steps sufficient to avoid an enforcement action. Therefore, the first lesson for smaller organizations is that if statutory violations are suspected by the entity as part of its own self-monitoring, an outside attorney should be retained to assist with the review and documentation. This provides attorney-client protection, and even if the results of the internal investigation are produced to the CFPB, the documentation will be in a useful format.
- Second, one of All Financial Services' affirmative defenses was that the outside marketing company that prepared the materials is directly responsible for the content of the direct-mail solicitations. From the CFPB's point of view, the investigated entity is responsible for a vendor's actions. In fact, the CFPB adopted the same position against U.S. Bank, N.A. in September 2014. Therefore, smaller organizations need to designate an employee to review and monitor services provided by vendors – whether marketing, billing or debt collection.
- Third, the mortgage lender complained that the allegations in the enforcement action were not part of the CFPB's findings submitted to the lender at the conclusion of the investigation. The implication here is that the CFPB's investigation process is more likely to ask for a lot of information, but not to be forthcoming with its findings during the course of the investigation. It is a heads-up that the investigation process is an opaque one.

Based on its actions in 2015, it is believed that the CFPB will continue to investigate and enforce mortgage rules against smaller institutions in the coming year. Therefore, it is important that smaller lenders stay abreast of enforcement actions against companies big and small alike.