

The Rules on Sending Periodic Statements are Changing

March 13, 2017

One of the major provisions of the Consumer Financial Protection Bureau's ("CFPB's") mortgage servicing rules that took effect in 2014 (the "Servicing Rules") was the requirement for residential mortgage servicers to send borrowers a periodic statement. One important exemption to this requirement was included in the Servicing Rules: if the borrower has filed for bankruptcy, then the servicer is not required to send a periodic statement. That blanket exemption is now being eliminated effective as of October 19, 2017.

The Servicing Rules implemented several key requirements of the Dodd-Frank Act by adding new servicing requirements to both Regulation Z (which implements the Truth in Lending Act (TILA)) and Regulation X (which implements the Real Estate Settlement and Procedures Act (RESPA)). One of the many significant requirements added by the Servicing Rules to Regulation Z was the requirement that a servicer sends a borrower a periodic statement showing certain information regarding the mortgage.

At the time the Servicing Rules were proposed, there were many industry comments requesting an exemption to the periodic statement requirement if the borrower was in bankruptcy. Many comments stated that the periodic statement requirement conflicted with certain bankruptcy law provisions, including the automatic stay provision which prohibits a creditor from attempting to collect a debt from a consumer in bankruptcy. Based in part on these comments, the CFPB adopted the bankruptcy exemption to the periodic statement requirement in the Final Servicing Rules.

However, ever since the final Servicing Rules were adopted, the CFPB has continued to explore whether to retain the bankruptcy exemption. After studying the issue for several years, including reviewing a number of bankruptcy cases dealing with the issue of periodic statements, the CFPB has decided to eliminate the broad bankruptcy exemption to the periodic statement requirement and to replace it with a much more limited exemption. The changes are effective on October 19, 2017, as part of a series of amendments to the Servicing Rules issued late last year by the CFPB (the "Amendments").

Under the Amendments, a servicer will be exempt from the periodic statement requirements with regard to a mortgage loan if a two-prong test is satisfied. First, any consumer borrower on the loan must be a debtor in bankruptcy under the Bankruptcy Code or must have discharged personal liability for the mortgage loan through certain provisions of the Bankruptcy Code. Second, one of the following additional conditions must apply with regard to any consumer borrower on the mortgage loan: (1) the consumer requests in writing that the servicer

cease providing a periodic statement or coupon book; (2) the consumer's bankruptcy plan provides that the consumer will surrender the dwelling securing the mortgage loan, provides for the avoidance of the lien securing the mortgage loan, or otherwise does not provide for, as applicable, the payment of pre-bankruptcy arrearage or the maintenance of payments due under the mortgage loan; (3) a court enters an order in the bankruptcy case providing for the avoidance of the lien securing the mortgage loan, lifting the automatic stay pursuant to Section 362 of the Bankruptcy Code with regard to the dwelling securing the mortgage loan, or requiring the servicer to cease providing a periodic statement or coupon book; or (4) the consumer files with the court overseeing the bankruptcy case a statement of intention identifying an intent to surrender the dwelling securing the mortgage loan and a consumer has not made any partial or periodic payment on the mortgage loan after the commencement of the consumer's bankruptcy case.

Once the Amendments are effective in October, the new periodic statement bankruptcy exemption will apply to a mortgage loan irrespective of whether the consumer borrower became a debtor in bankruptcy before or after the effective date. In addition, the exemption will apply at the loan level. Therefore, a servicer is exempt with respect to all consumer borrowers on a mortgage loan if the exemption criteria are met with respect to any one consumer borrower on the loan. A transitional single-billing cycle exemption exists under certain circumstances to enable a servicer to transition to a periodic statement modified for bankruptcy and to an unmodified periodic statement upon the conclusion of the bankruptcy case or the reaffirmation of the debt by order of the court in a bankruptcy case.

A consumer in bankruptcy may opt in or out of receiving a periodic statement by making a written request to the servicer, and the Amendments contain a new provision allowing a servicer to establish an exclusive address for such requests. The servicer must notify the consumer of the address in a manner that is reasonably designed to inform the consumer of the address.

Ever since the broad bankruptcy exemption to the periodic statement requirement was adopted in the Servicing Rules in 2014, there have been a number of bankruptcy courts that have addressed the issue of sending periodic statements to borrowers in bankruptcy. These cases have attempted to reconcile certain bankruptcy law provisions with the exemption in the Servicing Rule. One such a case was recently issued by the United States Bankruptcy Court for the District of Massachusetts.

The borrowers in *In Re Sperry* filed a voluntary petition under chapter 13 of the Bankruptcy Code and proposed a so-called "cure and maintain" chapter 13 plan to repay their debts. The plan required them to pay their pre-bankruptcy arrearage to their lender through the chapter 13 trustee (cure), while at the same time making their current monthly mortgage payments directly to the lender (maintain).

The lender rejected the borrowers' request to receive monthly periodic statements under their "cure and maintain" plan. First, the lender claimed it could not send statements "[d]ue to logistical limitations" and that the statements would be "confusing." The lender also argued that the Servicing Rules exempt it from sending such statements to borrowers during the pendency of their bankruptcy cases, that sending such statements would likely violate the automatic stay, and that the requirement to send monthly statements is an impermissible modification of its claim.

Bankruptcy Code §1322(a) enumerates the provisions that all chapter 13 plans must contain while §1322(b) lists those which are optional. Section 1322(b)(2) permits a debtor to “modify the rights of holders of secured claims, other than a claim... secured only by a security interest in real property that is the debtor’s principal residence. ...” Section 1322(b)(5) creates an exception to § 1322(b)(2)’s anti-modification provision by permitting a debtor to cure pre-petition monetary defaults while maintaining ongoing post-petition payments even for a non-modifiable home mortgage.

The court found that the borrowers’ “cure and maintain” plan was consistent with Section 1322(b) and that the requirements of the Bankruptcy Code relating to chapter 13 plans did not present a valid reason to prohibit the confirmation of the plan. Additionally, the court noted that requiring holders of claims secured by home mortgages to send monthly statements is not a “right” within the meaning of the anti-modification provision, but an obligation, and is “inextricably bound to a debtor’s ability to cure mortgage defaults, one of the primary objectives of chapter 13.” Furthermore, the court stated that even if sending periodic statements is somehow defined as a “right,” its ministerial nature excludes it from being the type of “right” contemplated by the anti-modification provision of the Bankruptcy Code.

Finally, the court held that the plan did not violate Regulation Z, noting that the current regulations merely excuse a servicer from sending monthly statements during a pending bankruptcy and do not prohibit a servicer from doing so.

If you have any questions regarding the Servicing Rules or the Amendments, please feel free to contact Joseph D. Simon at [516-357-3710](tel:516-357-3710) or via email at jsimon@cullenanddykman.com, Kevin Patterson at [516-296-9196](tel:516-296-9196) or via email at kpatterson@cullenanddykman.com, or Diana R. Acosta at [516-357-3739](tel:516-357-3739) or via email at dacosta@cullenanddykman.com.

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