COVID-19: ECHOES DON'T FADE

LESSONS LEARNED FROM THE HOME AFFORDABLE MODIFICATION PROGRAM FOR THE NEXT WAVE OF MORTGAGE CLASS ACTION LITIGATION

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By: Brian M. Forbes, Robert W. Sparkes, III

As the country grapples with the impacts of the COVID-19 pandemic, financial service providers should hold fast to the adage that those who forget the past are destined to repeat it. The last financial crisis centered in large part on the mortgage industry, both in its inception and its slow climb to stabilization. Like the last crisis, a growing percentage of homeowners are not able to make their mortgage payments, requiring loan servicers to employ various loss mitigation tools to reduce individual's financial hardships. While the COVID-19 pandemic is impacting nearly all sectors of the economy, the mortgage industry can look back to past experiences to help mitigate present and future risks. If past is prologue, one risk likely to increase in the coming months is class action litigation.

THE PRESENT: THE CARES ACT AND LOAN FORBEARANCE

As part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act, Congress sought to assist homeowners struggling to make their mortgage payments as a result of COVID-19.1 The CARES Act requires servicers of federally-backed residential mortgage loans to provide homeowners upon request with payment forbearance for up to 180 days and, if necessary, extend the period for another 180 days.[2] In doing so, the servicer may not require any documentation other than a "borrower's attestation to a financial hardship caused by the COVID–19 emergency."[3] According to the Mortgage Bankers' Association, approximately 3.8 million loans were already in forbearance plans as of May 4, 2020.[4]

The forbearance plans themselves are typically straightforward, requiring either a reduced monthly payment or no monthly payment for a set period of time. The CARES Act, however, does not specify what is to happen after the forbearance period ends, leaving many wondering what comes next. The answer is far from simple and will likely vary widely among homeowners based on loan-specific factors. As the lessons of the last decade teach, servicers' activity in the post-forbearance-plan stage is likely to pose the greatest risk of future exposure to class action lawsuits.

THE PAST: THE HOME AFFORDABLE MODIFICATION PROGRAM

The demand for CARES Act forbearance evokes memories of the federal government's response to the last major financial crisis. In 2008, Congress enacted the Emergency Economic Stabilization Act, which created the Troubled Asset Relief Program (TARP).[5] Pursuant to TARP, the Treasury Department implemented the Home

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Affordable Modification Program (HAMP), which provided incentives for loan servicers to modify homeowners' mortgage loans, reduce homeowners' monthly payment amounts, and help homeowners avoid foreclosure.[6]

In some ways, HAMP was a success. Almost 2 million loans were permanently modified under HAMP and countless others received custom non-HAMP modifications. HAMP, however, has a mixed legacy. In particular, servicers' efforts to assist homeowners through HAMP and similar programs generated an enormous amount of litigation against servicers and investors, ranging from individual lawsuits to mass and class actions. Those lawsuits continue to move through the courts even now, a decade after HAMP began.

THE FUTURE: LESSONS FOR THE NEXT WAVE OF CLASS ACTION LITIGATION

Loss Mitigation and Loan Modifications

As with HAMP, the post-forbearance-plan world will likely require servicers to consider loss mitigation options for millions of loans previously in COVID-19 forbearance plans. Fannie Mae, Freddie Mac, the Department of Housing and Urban Development (HUD), and the Veterans Affairs Administration (VA) have provided some initial guidelines for servicers of their loans. Each counsel that forborne payments should not be immediately due and that loans should be evaluated for all available loss mitigation options, which may include:

- Full repayment of the missed payments in a lump sum, if the homeowner is able and willing to do so;
- Repayment plan through which the homeowner gradually repays the missed payments in addition to making full monthly payments;
- Deferral of the missed payments to the end of the loan;
- Loan modification that reduces the monthly payment amount and may include principal forgiveness (these can take many forms depending on a borrower's financial circumstances); or
- A COVID-19 Standalone Partial Claim (for FHA loans), pursuant to which the homeowner takes out a no interest, junior loan secured by her property on which no payments are due until payoff, maturity, sale, or acceleration of the senior loan (effectively deferring the forborne payments).[7]

Areas of Potential Risk

As servicers learned during HAMP, each stage of the loss mitigation and loan modification process is ripe with litigation risk.

CARES Act Forbearance

The CARES Act leaves little discretion for servicers. If a borrower requests forbearance and “attest[s] to a financial hardship caused [directly or indirectly] by the COVID-19 emergency,” the servicer must provide forbearance.[8] The key litigation risk at this stage, therefore, would likely arise from a servicer's denial of a CARES Act forbearance request.

Post-Forbearance Loan Modifications

The most serious litigation risk is posed by borrowers denied a loan modification or other loss mitigation option. The decision of whether a borrower qualified for a modification, however, is not the end of the analysis. How servicers arrive at a final decision is just as important. Indeed, HAMP teaches that litigation may arise from activities undertaken and decisions made (or not made) throughout the loss mitigation application process. The

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following are a few examples of loan-modification-related litigation that arose from HAMP (albeit only scratching the surface):

- Application: Borrowers challenged (i) the terms of applications, alleging, for instance, promises to modify a loan; (ii) the documentation required, alleging, for example, that submission of sufficient documents despite the servicer's requests; and (iii) the servicer's consideration of the application;
- Communications: Borrowers based claims on communications with servicers, including written notices, requests for documents, and telephone calls regarding their applications;
- Eligibility: Borrowers argued that they were eligible for temporary or permanent loan modifications and that servicers either improperly denied them or did not adequately consider their eligibility (often after a denial for failing to submit required documentation);
- Payment Terms: Borrowers premised claims on temporary payment plans (TPPs), alleging the TPPs mandated that the servicer provide a permanent modification after three months of TPP payments; other borrowers who obtained permanent modifications and were unable to make the modified monthly payments, brought claims alleging entitlement to better or different loan terms;
- Withholding Payments: Borrowers alleged that servicers instructed them to withhold monthly payments while applications were pending and were penalized by default fees and late charges; and
- Dual Tracking: Borrowers frequently centered their claims on alleged “dual tracking,” which refers to a scenario where foreclosure is initiated or continues while the borrower is being considered for a loan modification or loss mitigation option. The Real Estate Settlement Procedures Act, state laws, and other authorities address this issue, but the lines between permitted and prohibited activities in this area are fact specific and may depend on how state law defines the foreclosure process.

Defenses to Class Actions

The lessons learned from HAMP class actions offer a silver lining. Most notably, courts faced with loan modification claims frequently denied plaintiffs' motions for class certification.[9] Often the types of claims discussed above are borrower and loan-specific, such that the resolution of each putative class member's claim requires evaluation of individual evidence unique to that borrower and her loan. For example, did the plaintiff provide sufficient documentation; did the plaintiff have sufficient income to qualify for a modification; or did the plaintiff receive some representation that she need not need to make payments, would qualify for a modification, or would not be subject to foreclosure? Additionally, claims requiring proof of reliance or causation and those that turn on alleged promises regarding eligibility, qualifications, or dual tracking present highly individualized issues. For these reasons, among others, modification-related claims frequently ran aground on the predominance and superiority requirements of Fed. R. Civ. P. 23(b)(3).[10] History also teaches that named plaintiffs in these cases may face unique circumstances and defenses that call into question the typicality of their claims and their adequacy and standing to represent a class.[11]

CONCLUSION

Although the future defies prediction, one thing is certain: Over the coming months, mortgage loan servicers will receive an unprecedented number of requests for loan modifications and other relief as CARES Act forbearance

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periods expire. As servicers continue their efforts to provide homeowners relief from COVID-19 hardships, we are reminded of William Faulkner's oft-quoted phrase: “The past is never dead. It's not even past.”[12] As echoes of HAMP and the Great Recession continue to sound in courts throughout the country, servicers cannot forget the lessons learned over the last decade. Attention to the past may be essential to mitigating potential exposure to future class action litigation.

FOOTNOTES

[1] Coronavirus Aid, Relief, and Economic Security Act, Pub. L. No. 116-136, 134 Stat. 281, §§ 4022-43 (2020).

[2] *See* 15 U.S.C. § 9056.

[3] *Id.* § 9056(c).

[4] Mortgage Bankers Ass'n, *MBA: Share of Mortgage Loans in Forbearance Increases to 7.54%*, MBA NEWSLINK (May 4, 2020).

[5] *See* 12 U.S.C. § 5219.

[6] *See id.*; 12 U.S.C. § 5219a.

[7] *See* Fannie Mae, *Fannie Mae Announces COVID-19 Payment Deferral*; Freddie Mac, *Freddie Mac Announces COVID-19 Payment Deferral*; HUD, *If You Need Assistance in Making your Mortgage Payments, Help is Available*; VA, *Guidance for VA Home Loan Borrowers During COVID-19*.

[8] 15 U.S.C. § 9056(b), (c).

[9] *See Bernard v. CitiMortgage Inc.*, 637 F. App'x 471, 472-73 (9th Cir. Mar. 2, 2016); *Jackson v. Bank of Am., N.A.*, No. 16-CV-787, 2019 WL 7288508, at *7-9 (W.D.N.Y. Dec. 30, 2019); *Cave v. Saxon Mortg. Servs., Inc.*, Nos. 114586, 12-5366, 2016 WL 5930846, at *19-23 (E.D. Pa. Oct. 11, 2016).

[10] *See* Note 10, *supra*.

[11] *See Burton v. Nationstar Mortg.*, LLC, No. 1:13–cv–00307–LJO–JLT, 2014 WL 5035163, at *11 (E.D. Cal. Oct. 8, 2014).

[12] William Faulkner, REQUIEM FOR A NUN, 73 (Random House, 1951).

KEY CONTACTS

BRIAN M. FORBES
PARTNER
BOSTON
+1.617.261.3152
BRIAN.FORBES@KLGATES.COM

ROBERT W. SPARKES, III
PARTNER
BOSTON
+1.617.951.9134
ROBERT.SPARKES@KLGATES.COM

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