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One Person's Junk Fee Is Another's Treasure

On January 26, 2022, Rohit Chopra, the director of the Consumer Financial Protection Bureau (CFPB), issued a Request for Information (RFI) seeking public comments on fees that "are not subject to competitive processes that ensure fair pricing." The director indicated that when consumers do not select their provider, like in loan servicing, "it can lead to stagnation, junk fees, and poor treatment." Chopra also stated that the CFPB would be launching other initiatives to identify ways to lower barriers to entry and increase the pool of firms competing for customers based on quality, price, and service.

As of the close of the comment period on April 11, the CFPB had received thousands of responses. While the broad RFI extends to providers of consumer financial products and services, mortgage servicing is singled out and should put mortgage servicers on alert that their fees will be closely scrutinized. In fact, Chopra indicated in a blog post that the CFPB will use this information to review existing, and to craft new, rules "to spur competition and transparency" and to identify "illegal practices through … supervision and enforcement."

The CFPB sought comments on what the CFPB pejoratively refers to as "junk fees" and "exploitative, back-end, excessive fees." Exemplars of such mortgage servicing fees cited by the CFPB include late fees, nonsufficient fund (NSF) fees, convenience fees for processing payments, and delinquency-related fees such as monthly property inspection fees, new title fees, legal fees, appraisal and valuation fees, broker price opinion fees, force-place insurance, foreclosure fees, and corporate advances. Comments received by the CFPB include those from attorneys general (AGs) in Republican- and Democratic-leaning jurisdictions.

The Republican AGs: How About Some Federal–State Cooperation?

To date, the AGs in Alabama, Arizona, Arkansas, Georgia, Idaho, Indiana, Kentucky, Louisiana, Mississippi, Montana, Ohio, Oklahoma, South Carolina, South Dakota, Utah, Texas, and West Virginia have all requested that the CFPB abandon its plan to regulate fees and, instead, coordinate and cooperate with the states to determine where federal action is "duplicative or unwarranted." The Republican AGs argue that the CFPB is trying to establish itself as the primary regulator in the consumer financial products fee-servicing space and consequently infringing on the rights of the states to regulate business practices within their borders. These AGs argue that the CFPB's RFI about "junk fees—exploitative, back-end, hidden, or excessive" suggests that the CFPB is "predisposed to create a subjective standard for the identification of problematic fees."

And these Republican AGs argue that the CFPB fails to recognize that state statutes already regulate many such fees in consumer financial products and that federal regulation would be duplicative. According to the Republican AGs, the states are better suited to assess the needs of their citizens as well as the impact of fees on state markets. They highlight the fact that the states specifically authorize many types of fees, such as late fees, NSF fees, application fees, administrative fees, modification and deferral fees, and title fees. They also note that states are ready to enforce their laws if a consumer financial provider fails to comply or take action under the state's unfair or deceptive acts or practices (UDAP) provisions when a consumer is misled. The Republican AGs also expressed concern that the CFPB would seek to use its UDAAP authority to regulate fees and questioned the use of that authority for fees that are "disclosed in accordance with state or federal law, in some cases authorized by state law, and agreed to by a consumer in writing."

The concern is one of dominance—the Republican AGs fear that the CFPB views itself as the primary regulator and intends to limit the authority of the states to regulate fees. Of course, the CFPB's rejoinder may be simply that it is setting the floor and the states are free to go further. The real question is where the CFPB draws the line—and if that line goes further than some states have gone, will it prompt preemption concerns.

The Democratic AGs: Go Get 'Em Director Chopra!

The Democratic AGs praise the CFPB's RFI and call for comments and limit their feedback to one issue—convenience fees charged by mortgage servicers. The AGs of California, Colorado, Connecticut, Delaware, the District of Columbia, Hawaii, Illinois, Iowa, Maine, Maryland, Massachusetts, Michigan, Minnesota, Nevada, New Jersey, New Mexico, New York, North Carolina, Oregon, Pennsylvania, Rhode Island, and Washington, and the Hawaii Office of Consumer Protection, consider convenience (along with overdraft and NSF) fees "harmful junk fees" and urge the CFPB to prohibit mortgage servicers from imposing convenience fees or, in the alternative, restrict mortgage servicers from charging convenience fees that exceed the documented actual cost of the service.

It's ironic: Not too long ago, many of these same blue states permitted convenience fees with restrictions in a multistate settlement agreement with a large loan servicer.

Now, the Democratic AGs argue that because lenders are supposed to earn their profit for mortgage servicing through the interest rate and other charges at origination, servicers have already been compensated for the costs of accepting payments (a core function of servicers) and, therefore, are compensated twice for accepting payments. The CFPB should recognize that this argument reflects a fundamental misapplication of the basic practices of the servicing business.

In fact, the CFPB acknowledged the compensation structures for the servicing business in its 2013 Mortgage Servicing Rules. While the structures can vary between portfolio loans and securitized loans, as well as other factors, generally the owners of loans negotiate pricing with the servicer—typically a monthly servicing fee. Servicers also receive ancillary fees, late fees, and as acknowledged by the CFPB in 2013, "fees for processing telephone payments." It is worth noting that the CFPB did not prohibit convenience fees in its 2013 Mortgage Servicing Rules. The CFPB also declined to address convenience fees in its recently promulgated Regulation F, although that issue was raised during the CFPB's Small Business Regulatory Enforcement Fairness Act review process.

Mortgage servicers will argue that borrowers enter into a contract, in the form of a promissory note, and agree to pay back the money borrowed in monthly periodic payments. The borrower also agrees to pay late fees if their payments are not received by the end of the grace period, commonly 15 days after the contractual due date. Typical mortgage agreements do not require servicers to offer expedited payment options, such as online and phone payments, for borrowers who wait until the last day to make their payment.

Nonetheless, many mortgage servicers choose to make these payment options available for the benefit of borrowers, even though these expedited options come with costs to the servicer. For example, expedited options often require the use of third-party payment processing vendors such as Western Union, and among other costs, the mortgage servicer typically needs to hire and train customer service agents to receive payments over the phone and hire computer programmers to build and maintain systems needed to accept payments online or through interactive-voice-response telephone technology. It's also worth noting that servicers do not assess convenience fees without borrowers' knowledge and consent. Rather, the fact and amount of the convenience fee are disclosed to borrowers at that time—before borrowers elect to continue with that payment method.

The Democratic AGs argue that "like refinancing, this purported choice is actually illusory for many borrowers," noting that "the convenience fee actually operates as an alternative late fee—perhaps cheaper, but with a shorter grace period, and in contravention to the contractual terms in most mortgages that outline the specific amount and timing of late fees. So, rationally, the consumer chooses the option that costs less and accepts the convenience fee charge. But simply choosing the less bad option doesn't mean that the consumer really has a choice." Doesn't the borrower have the choice to make their payment on time, or at least within the contractually agreed grace period? Borrowers who elect a fully disclosed modest convenience fee leave themselves far better off financially than incurring the considerably more expensive late fee (not to mention avoiding negative credit reporting, which can adversely impact the consumer in even broader ways).

Penalizing mortgage servicers by eliminating their ability to charge clearly disclosed and agreed-to fees for services—ones they are not required to provide—will, at a minimum, reduce their incentive to offer such options, limit consumer choice, and deter future servicing innovations benefiting borrowers.

Takeaways

In 2013, the CFPB recognized that servicers aren't really subject to market discipline from consumers because consumers have little opportunity to switch servicers. The CFPB recognized, however, that "servicers compete to obtain business from the owners of loans—investors, assignees, and creditors—and thus competitive pressures tend to drive servicers to lower the price of servicing and scale their investment in providing service to consumers accordingly." Chopra appears to be challenging that premise. While servicer portability is something to consider in the future, now is the time for servicers to closely examine fees charged to consumers to ensure such fees are legally permissible and properly disclosed.

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Nanci Weissgold
202.239.3189
nanci.weissgold@alston.com

Anoush Garakani
213.576.1181
anoush.garakani@alston.com

Brian Johnson
202.239.3271
brian.johnson@alston.com

ALSTON & BIRD

WWW.ALSTON.COM

ATLANTA: One Atlantic Center ▪ 1201 West Peachtree Street ▪ Atlanta, Georgia, USA, 30309-3424 ▪ 404.881.7000 ▪ Fax: 404.881.7777
BEIJING: Hanwei Plaza West Wing ▪ Suite 21B2 ▪ No. 7 Guanghua Road ▪ Chaoyang District ▪ Beijing, 100004 CN ▪ +86.10.85927500
BRUSSELS: Rue Guimard 9 et Rue du Commerce 87 ▪ 3rd Floor ▪ 1000 Brussels ▪ Brussels, 1000, BE ▪ +32.2.550.3700 ▪ Fax: +32.2.550.3719
CHARLOTTE: One South at The Plaza ▪ 101 South Tryon Street ▪ Suite 4000 ▪ Charlotte, North Carolina, USA, 28280-4000 ▪ 704.444.1000 ▪ Fax: 704.444.1111
DALLAS: Chase Tower ▪ 2200 Ross Avenue ▪ Suite 2300 ▪ Dallas, Texas, USA, 75201 ▪ 214.922.3400 ▪ Fax: 214.922.3899
FORT WORTH: Bank of America Tower ▪ 301 Commerce ▪ Suite 3635 ▪ Fort Worth, Texas, USA, 76102 ▪ 214.922.3400 ▪ Fax: 214.922.3899
LONDON: 4th Floor ▪ Octagon Point, St. Paul's ▪ 5 Cheapside ▪ London, EC2V 6AA, UK ▪ +44.0.20.3823.2225
LOS ANGELES: 333 South Hope Street ▪ 16th Floor ▪ Los Angeles, California, USA, 90071-3004 ▪ 213.576.1000 ▪ Fax: 213.576.1100
NEW YORK: 90 Park Avenue ▪ 15th Floor ▪ New York, New York, USA, 10016-1387 ▪ 212.210.9400 ▪ Fax: 212.210.9444
RALEIGH: 555 Fayetteville Street ▪ Suite 600 ▪ Raleigh, North Carolina, USA, 27601-3034 ▪ 919.862.2200 ▪ Fax: 919.862.2260
SAN FRANCISCO: 560 Mission Street ▪ Suite 2100 ▪ San Francisco, California, USA, 94105-0912 ▪ 415.243.1000 ▪ Fax: 415.243.1001
SILICON VALLEY: 1950 University Avenue ▪ Suite 430 ▪ East Palo Alto, California, USA 94303 ▪ 650.838.2000 ▪ Fax: 650.838.2001
WASHINGTON, DC: The Atlantic Building ▪ 950 F Street, NW ▪ Washington, DC, USA, 20004-1404 ▪ 202.239.3300 ▪ Fax: 202.239.3333