

Payment Application Issues

Mortgage servicers are typically responsible for collecting and processing mortgage payments from borrowers. Servicers' delays in processing payments can result in unwarranted late fees and unjustified claims of borrower default. Complaints about slow payment processing led the Federal Reserve Board in 2008 to promulgate a rule requiring mortgage servicers to credit payments to consumers' accounts as of the date of receipt.¹ Section 1464 of the Dodd-Frank Act, enacted in 2010, essentially codified the FRB rule.² The CFPB finalized regulations implementing the prompt crediting provision of the Dodd-Frank Act.³ The CFPB regulations became effective January 10, 2014.⁴ Prior to January 10, 2014, the FRB rule was in effect.

Prompt Crediting Under FRB Rule

Under the former FRB rule, effective prior to January 10, 2014, a servicer was required to credit payments to the consumer's loan account as of the date of receipt. The rule applied to loans secured by a consumer's principal dwelling.⁵ There were two exceptions to the "same-day" requirement: (1) when a delay in posting did not result in any charge to the consumer or in the reporting of negative information to a consumer reporting agency;⁶ and (2) when a servicer specified in writing requirements for the consumer to follow in making payments, but accepted a payment that did not conform to these requirements.⁷ In this latter case, the servicer would have to credit the nonconforming payment within five days after receipt. The date of receipt was the date when the payment (in whatever form) reaches the servicer.⁸ For example, payment by check was received when the check reaches the servicer, not when the funds are collected. Electronic fund transfers, preauthorized payment arrangements, and the like were received when the servicer received the transfer.

¹ Reg. Z, 12 C.F.R. § 1026.36(c)(1)(i); 73 Fed. Reg. 44,522, 44,604 (July 30, 2008). *See* National Consumer Law Center, Truth In Lending § 9.4.3.2 (8th ed. 2012 and Supp.).

² 15 U.S.C. § 1639f, *as amended by* Pub. L. N. 111-203, § 1464, 124 Stat. 1376 (July 21, 2010).

³ *See* 78 Fed. Reg. 10,902 (Feb. 14, 2013) (effective Jan. 10, 2014).

⁴ *See id.* at 10,902.

⁵ Former Reg. Z, 12 C.F.R. § 1026.36(c)(1); 73 Fed. Reg. 44,522, 44,604 (July 30, 2008). *See also* *Schneider v. Bank of Am.*, 2014 WL 2118327, at *5 (E.D. Cal. May 21, 2014) (applying this provision when servicer failed to post payment for eight days after it was received and then charged a late fee as a result of its own delay); *Fenske-Buchanan v. Bank of Am.*, 2012 WL 1204930 (W.D. Wash. Apr. 11, 2012) (applying this provision when a consumer made several prepayments of principal that were not applied as of the date of receipt; noting that statute of limitations on claim does not start to run until the first loan history statement has been provided because that is when such an error can first be detected).

⁶ Former Reg. Z, 12 C.F.R. § 1026.36(c)(1)(i); 73 Fed. Reg. 44,522, 44,604 (July 30, 2008); Official Interpretations to Reg. Z, ¶ 36(c)(1)(i)-1; 73 Fed. Reg. 44,522, 44,614 (July 30, 2008).

⁷ Former Reg. Z, 12 C.F.R. § 1026.36(c)(2); 73 Fed. Reg. 44,522, 44,604 (July 30, 2008).

⁸ Former Official Interpretations to Reg. Z, ¶ 36(c)(1)(i)-3; 73 Fed. Reg. 44,522, 44,614 (July 30, 2008).

Payments were required to be credited based on the legal obligations between the parties to the transaction, which were determined by applicable state or other law.⁹ In addition, the servicer could specify reasonable requirements for making payments in writing. The former Official Interpretations listed some examples: setting a cut-off hour for payment to be received; requiring that the payment be accompanied by the account number or payment coupon; specifying that only checks or money orders be sent by mail; requiring that payments be in U.S. dollars; specifying that the consumer use a particular address.¹⁰ However, such requirements were not to be difficult for most consumers to follow. The former Official Interpretations mention that a cut-off time of 5:00 p.m. for receipt of a mailed check was reasonable.¹¹ In the absence of servicer guidelines for making payments, payments were to be made at any location where the servicer conducts business, at any time during normal business hours, and by cash, money order, draft, or other similar instrument in a properly negotiable form, or by electronic fund transfer if so agreed by the consumer and the servicer.¹²

Prompt Crediting Under Dodd-Frank TILA Amendments and CFPB Regulations

The Dodd-Frank Act amendments to the Truth in Lending Act also mandate that servicers credit periodic payments on consumer credit transactions secured by a consumer's principal dwelling as of the date of receipt.¹³ Like the FRB rule, there is an exception when a delay in crediting the payment does not result in any charge to the consumer or in the reporting of negative credit information to a consumer reporting agency.¹⁴ There is also an exception, as in the FRB rule, that if a servicer specifies in writing requirements for the consumer to follow in making payments, but accepts a payment that does not conform to the requirements, the servicer shall credit the payment as of five days after receipt.¹⁵ These statutory requirements were implemented through regulations that became effective on January 10, 2014.¹⁶

The Official Interpretations to Regulation Z provide guidance on the exception permitting a delay in posting if there are no negative consequences to the consumer:

Under § 1026.36(c)(1)(i), a mortgage servicer must credit a payment to a consumer's loan account as of the date of receipt. This does not require that a mortgage servicer post the payment to the consumer's loan account on a particular date; the servicer is only required to credit the payment *as of* the date of receipt. Accordingly, a servicer that receives a payment on or before its due date (or within any grace period), and does not enter the payment on its books or in its system until after the payment's due date (or expiration of any grace period), does not violate this rule as long as the entry does not result in the imposition of a late charge, additional interest, or similar

9 Former Official Interpretations to Reg. Z, ¶ 36(c)(1)(i)-2; 73 Fed. Reg. 44,522, 44,614 (July 30, 2008).

10 Former Official Interpretations to Reg. Z, ¶ 36(c)(2)-1; 73 Fed. Reg. 44,522, 44,614 (July 30, 2008).

11 Former Official Interpretations to Reg. Z, ¶ 36(c)(2)-2; 73 Fed. Reg. 44,522, 44,614 (July 30, 2008).

12 Former Official Interpretations to Reg. Z, ¶ 36(c)(2)-3; 73 Fed. Reg. 44,522, 44,614 (July 30, 2008).

13 15 U.S.C. § 1639f(a).

14 *Id.*

15 15 U.S.C. § 1639f(b).

16 Reg. Z, 12 C.F.R. §§ 1026.36(c)(1)(i), 1026.36(c)(1)(iii).

penalty to the consumer, or in the reporting of negative information to a consumer reporting agency.¹⁷

The CFPB Interpretations refer to the “date of receipt” as the date that the “payment instrument or other means of payment reaches the mortgage servicer.”¹⁸ An example is provided of a payment made by check, noting that payment is received when the servicer receives the check, not when the funds are collected.¹⁹ Similarly, if the consumer arranges to have the payment made through a preauthorized payment or telephone bill-payment arrangement, using a third-party payor such as a financial institution, the payment is received when the servicer receives an electronic fund transfer, check, other transfer medium from the third-party payor, not when the funds are actually received.²⁰ The Seventh Circuit has held that the phrase “payment instrument or other means of payment” in the Official Interpretations should be construed broadly to include electronic payments, and that the date of receipt for an electronic payment is the date the consumer electronically authorizes the servicer to debit her bank account, by clicking a “submit payment” button for example, not the date that the funds are received by the servicer from the consumer’s account through the Electronic Payments Network (EPN).²¹

Neither the former FRB rule nor the Dodd-Frank Act defines the term “payment” for purposes of the prompt crediting rule. The CFPB rule uses the term “periodic payment” and defines it as the amount necessary to cover principal, interest, and escrow (if applicable) for a given billing cycle.²² Though servicers may charge and collect fees for late payments, the prompt crediting rule applies even if the payment does not include a late fee. The rule also applies if the consumer’s payment does not include other fees or non-escrow payments that the servicer has advanced on the consumer’s behalf.²³

The CFPB rule offers new and specific guidance to servicers on how to deal with partial payments (i.e., payments less than periodic payments).²⁴ Nothing in the rule compels a servicer to accept a partial payment, and it therefore may be returned to the borrower if permitted under the terms of the uniform mortgage or deed of trust and state law.²⁵ The final rule allows, but does not

17 Official Interpretations to Reg. Z, ¶ 36(c)(1)(i)-1 (emphasis in original).

18 Official Interpretations to Reg. Z, ¶ 36(c)(1)(i)-3.

19 *Id.*

20 *Id.*

21 *Fridman v. NYCB Mortg. Co.*, 780 F.3d 773 (7th Cir. 2015).

22 Reg. Z, 12 C.F.R. § 1026.36(c)(1)(i). Obligations for force-placed insurance or delinquent taxes that have been paid through an escrow account are considered part of the periodic payment. *See* 78 Fed. Reg. 10,902, 10,954 (Feb. 14, 2013). If the mortgage loan has been accelerated, the periodic payment constitutes at least the total amount owed for all principal and interest. *See id.* For accelerated loans the CFPB’s analysis of the rule is unclear as to whether amounts for escrow advances and fees are part of the periodic payment.

23 Reg. Z, 12 C.F.R. § 1026.36(c)(1)(i).

24 Reg. Z, 12 C.F.R. § 1026.36(c)(1)(ii).

²⁵ *See also Ballenger v. Nat'l City Mortgage, Inc.*, 2015 WL 5062770 (N.D.W. Va. Aug. 26, 2015) (where express terms of the deed of trust permitted servicer to refuse to accept partial payments, servicer’s practice did not breach implied covenant of good faith and fair dealing;

require, servicers to place partial payments received into a suspense account, also known as an unapplied fund account. Suspense accounts, however, may be used only if authorized by the contract and permitted by state law.²⁶ Funds must be applied from the suspense account when the amount in suspense is equal to or greater than a periodic payment.²⁷ If the servicer elects to hold funds in suspense rather than crediting the partial payment or returning it to the consumer, the servicer must disclose the amount of funds held in suspense on the periodic statement, if such a statement is required.²⁸ The method by which periodic payments are credited to the account is based on the legal obligation between the creditor and consumer, subject to applicable law.²⁹

A separate subsection of the Dodd-Frank Act and the CFPB rule address non-conforming payments.³⁰ Non-conforming payments are payments that have been accepted by the servicer and are distinguished from partial payments that are placed in suspense, which are considered not to have been accepted.³¹ Any non-conforming payment must be credited within five days of receipt. As with the FRB rule, the servicer may specify reasonable requirements for making payments in writing.³² Failure to comply with these written payment instructions may result in a non-conforming payment. What constitutes reasonable requirements remains unchanged from the FRB rule to the CFPB rule.³³

There is no exception to the prompt crediting rules when the borrower is in bankruptcy or in a trial loan modification.³⁴ There is also no specific exception to the rule for small servicers.³⁵

practice could, however, violate West Virginia Consumer Credit and Protection Act, which prohibits the refusal of partial payments).

26 Official Interpretations to Reg. Z, ¶ 36(c)(1)(ii)-1; 78 Fed. Reg. 10,902, 11,019 (Feb. 14, 2013). The CFPB omitted language from the proposed rule that would have required periodic payments to be credited to the oldest outstanding delinquency. The Bureau removed this language after concluding that it may conflict with state law and that the problem is mitigated through other means. 78 Fed. Reg. 10,902, 10,956 (Feb. 14, 2013).

27 Reg. Z, 12 C.F.R. § 1026.36(c)(1)(ii)(B); Official Interpretations to Reg. Z, ¶ 36(c)(1)(ii)-1(iii); 78 Fed. Reg. 10,902, 11,019 (Feb. 14, 2013). See *Pineda v. Nationstar Mortgage, LLC*, 2015 WL 6438154 (N.D. Tex. Sept. 29, 2015), *report and recommendation adopted*, 2015 WL 6460017 (N.D. Tex. Oct. 21, 2015).

28 Reg. Z, 12 C.F.R. §§ 1026.36(c)(1)(ii)(A), 1026.41(d)(3)(i), 1026.41(d)(3)(ii); Official Interpretations to Reg. Z, ¶¶ 36(c)(1)(ii)-1(iii), 41(d)(3)-1; 78 Fed. Reg. 10,902, 11,019–20 (Feb. 14, 2013). See § 3.6.4, *infra* (discussion of periodic mortgage statements). Servicers not required to send periodic statements are exempt from this provision requiring disclosure of the amount of funds held in the suspense account on the periodic statement. See 78 Fed. Reg. 10,902, 10,955 (Feb. 14, 2013).

29 Official Interpretations to Reg. Z, ¶ 36(c)(1)(i)-2.

30 15 U.S.C. § 1639f(b); Reg. Z, 12 C.F.R. § 1026.36(c)(1)(iii).

31 See 78 Fed. Reg. 10,902, 10,956 (Feb. 14, 2013).

32 Official Interpretations to Reg. Z, ¶ 36(c)(1)(iii); 78 Fed. Reg. 10,902, 11,019 (Feb. 14, 2013).

33 See § 3.6.3.2, *supra* (setting forth examples of reasonable requirements).

34 See 78 Fed. Reg. 10,902, 10,956 (Feb. 14, 2013) (“[w]hile the Bureau understands the requirement that the prepetition and postpetition accounts must be kept separate during a bankruptcy, the Bureau believes that if sufficient funds accrue in either account to make a periodic payment due, those funds should be applied.”).

Pyramiding of Late Fees

Under the former FRB rule, a servicer could not impose any late or delinquency fee when the only delinquency was attributable to the late or delinquency fee itself, and the payment was otherwise a full payment for the applicable period and was paid on its due date or during an applicable grace period.³⁶ Effective January 10, 2014, the CFPB renumbered and adopted the FRB's rule, making only non-substantive phrasing changes.³⁷ The FRB intended that its rule be construed consistently with the Federal Trade Commission's "Credit Practices Rule" adopted by the FRB in Regulation AA for depository institutions.³⁸ The CFPB reaffirmed this position.³⁹

35 Small servicers are exempt from some of the CFPB's mortgage servicing rules. Small servicers are defined as servicers that service 5000 mortgage loans or less and only service mortgage loans the servicer or an affiliate owns or originated.

Note that small servicers are not required to provide periodic mortgage statements and as a result they are exempt from the requirement to disclose funds held in suspense pursuant to § 1026.36(c)(1)(ii)(A).

36 Former Reg. Z § 1026.36(c)(1)(ii) (effective prior to Jan. 10, 2014); 73 Fed. Reg. 44,522, 44,604 (July 30, 2008).

37 Reg. Z § 1026.36(c)(2) (effective Jan. 10, 2014).

38 Official Interpretations to Reg. Z, ¶ 36(c)(1)(ii)-1 (effective prior to Jan. 10, 2014); 73 Fed. Reg. 44,522, 44,614 (July 30, 2008). *See generally* National Consumer Law Center, Federal Deception Law § 2.3 (2012), *updated at* www.nclc.org/library (discussing FTC rule).

39 Official Interpretations to Reg. Z, ¶ 36(c)(2)-1.
