Brown Bag Meeting

MINUTES March 5th, 2015 12:00 P.M.

NORTH BANK BLDG.
432 N. SAGINAW ST. STE 300
FLINT MI

MEETING CALLED BY	Chapter 13 Trustee's Office-Carl L. Bekofske
TYPE OF MEETING	BROWN BAG
FACILITATOR	Carl L. Bekofske, Chapter 13 Trustee
NOTE TAKER	Karen Newman and Katie Quinn
ATTENDEES	Benjamin Allyn, Melissa DiGiamberdine, Dareth Wilson, Lynn Oberhausen, Juanita Massey, Zach Tucker, Alan Walton, John Hicks, John Topping, Jim Frego, Eric Mulka, Peter Mooney, Carl L. Bekofske, Kris Ennis, Melissa Caouette, Leo Foley, Sherry Beasinger, Katie Quinn, Cindy Amey, Diane Smith, Sara Skutt, Tracee DeNicolo, Mark Plude, Tenee Smith and Karen Newman

CARL'S OPENING REMARKS: Welcome

DISCUSSION BY CARL:	3 Handouts: see attachments 1) U.S. Trustee Program Reaches $50 Million Settlement with JPMorgan Chase to Protect Homeowners in Bankruptcy 2) Bankruptcy by the Number-Consumer Debtor Audits – from ABI Journal 3) Servicing Matters by Carolina Reid
#1) U.S. Trustee Program Reaches $50 Million Settlement with JPMorgan Chase to Protect Homeowners in Bankruptcy: Mortgage Services can effect mortgage modifications. Not Sure what will happen with funds on Chase's settlement.	
#2) Bankruptcy by the Number-Consumer Debtor Audits – from ABI Journal: Please read! Our Office has received several audit notices. The trustee's office does nothing with them, just monitor.	
#3) Servicing Matters by Carolina Reid: Please read.	
AGENDA:	Attorney Fee Parameters; Melissa Plan Modifications; Excusal of Plan Delinquency - Melissa Case Law on Direct Payments - Melissa Tax Returns Review Parameters- Mark Motion to Compel - Leo

ATTORNEY FEE PARAMETERS:

DISCUSSION BY MELISSA C.:	The Trustee's Office wants attorney to be well paid and happy about filing Chapter 13s for their work done. Unfortunately, there are cases where the applications are reaching further than they should. The Trustee's Office was recently contacted by 3 different debtors that they had received letters directly from their attorney for direct payment which was not approved by Court. The Trustee's Office is looking for the Judge's clarification as to our role and how to proceed.
Judge Shefferly ruled recently on attorney's being paid for work done at the end of a case. Judge Opperman has stated that he will keep this ruling consistent in the Eastern District. The Trustee's Office still has a case pending before Judge Opperman that is under advisement.	
1. Upon the filing of the Trustee's Notice of Final Cure, debtor's counsel has 21 days to file a fee app for any work that pre-dates the notice. If no fee app is filed, the fees incurred are discharged; 2. If a fee app is filed in that time period, the court will review the fee application and the Trustee has an opportunity to object. 3. If any fees are incurred after the Trustee's notice, a fee application must be filed seeking approval of the fees. As long as the fee app is filed and the fees are ultimately approved by the court, they will survive discharge and can be paid directly by the debtor. 4. The court disapproves of just sending a letter to the debtor after discharge without the filing of a fee app as it impairs the debtor's "fresh start" (he indicated he speaks for all of his colleagues on this issue); 5. In this case, since the fee app was not filed until after discharge, the fees incurred prior to the Trustee's Notice of Final Cure totaling approx. $520 are discharged. The fees in the amount of $760 relating to the creditor's disagree response could not have been provided for in the plan (and therefore subject to the discharge) since the events had not yet happened and the fees had not yet been incurred. Court wants to encourage debtor's counsel to help debtors get to discharge and deal with the unexpected "end of case" issues. 6. He distinguished his prior bench ruling in the Carey case because all of the fees requested in that case were rendered prior to the Notice of completion.	
CONCLUSIONS	In recent poll that was taken by the Trustee's Office per Judge Opperman's request: The majority of the attorneys polled, don't bill for the final work done in a case unless there is money available. Attorneys polled said that a happy client's referral has a greater impact.

PLAN MODIFICATIONS:

DISCUSSION BY MELISSA	**EXCUSAL OF PLAN DELINQUENCY**:
Common Objection by the Trustee: If requesting to excuse missed plan payments, attorneys need to specifically state the amount and include a good reason as to why.	
Trustee needs a "Complete" copy of the Debtor's Federal most recent Tax Return	
If filing a Modification to the Plan, the Trustee needs amended schedules I and J also be filed. Do not include amended schedules I and J within the Modified Plan as exhibits. They must be filed as separate documents under the proper ECF filing events.	
The Trustee's Office will also need copies of 3 recent pay stubs	
If the Trustee's Office files a plan modification based on a recent tax return review, please do not file a modification yourself, unless you are trying to lower the plan payment. This will reduce the confusion with court and less action will need to be taken with the Court. Just object to the trustee's plan modification. Trustee is willing to work out any issues/circumstances in the Order Confirming Modified Plan.	

DISCUSSION BY MELISSA	**CASE LAW ON DIRECT PAYMENTS**:
Trustee wants secured claims paid inside plan instead of directly by the Debtor.	
If a secured claim is paid directly by Debtor and the Debtor defaults anytime within the plan time, a deficiency claim will then have to be paid by the Debtor and not covered under the discharge.	
If secured claim is paid by the plan and a delinquency in payments, a motion to lift stay is filed, then a deficiency claim CAN be paid inside the plan IN RE: Parmenter 527 F.3d 606 2008 IN RE: Adkins 425 F. 3d 296 2005 NOT PERMITTED TO RECLASSIFY DEBT.	
Carl said that there is a myth that the debtors have the fee on secured claim paid inside the plan; debtor only pays the fee if it is a 100% plan, which is less than 5% of our cases; The only time to pay outside the plan is if the vehicle is not really theirs or they already have it set up as a direct pay out of their pay checks. There ARE many horror stories where client wants to pay direct and then life happens & misfortune. Wants "knee jerk" reaction to be: Paid by Trustee. Paying inside plan also help keep trustee fees LOW.	

DISCUSSION BY MARK PLUDE	**TAX RETURN REVIEW PARAMETERS**:
The Trustee's office started reviewing all tax returns about 1 or 1 1/2 years ago. Used to look at all cases with 15% increase or $15,000 increase. Now we take more things into account: Look at family size and compare median income with national standards; Compares with most recently filed Schedule I & J; Looks at possible missed car payoff	
If Trustee files a mod plan, determine what we're making the adjustment for. It could be a mistake based on how the tax return was prepared. The trustee's office cannot tell if lump sums or if debtor has had medical issues, so please inform the trustee's office of this type of information. Also, we're looking at returns that are 12 months after the fact or more... so we're always behind the curve. If increase, debtor could have had 1 year of the increased income.	
Carl: Congress requires us to examine tax returns. This is how we go about it in Flint.	
Tenee: Sends out requests for returns, and we have received approximately 8% of 2014 returns to date.	

DISCUSSION BY LEO	**MOTION TO COMPEL**:
If we have not received debtor's 2012 Federal tax returns, Trustee is now filing Motion to Compel. If the debtor's 2012 tax return have not been received a Show Cause Hearing will be set.	
Trustee is not sure how the Judge will rule, but is interested to find out. Consequence could be to increase the plan payments, or plan becomes a 100%.	
If taxes are not turned over why? Bad faith (hiding income) Or is it that Debtor's don't have a copy? If so, maybe requesting permission from Debtor to get a tax transcript would be helpful.	

CONCLUSION:	Carl: Our Debtor Education Classes are important to your clients. Encourage your client to attend the additional classes as well. Additional classes; a notice is sent by the Trustee's Office to all Debtors.

AGENDA

Carl L. Bekofske – Opening remarks

Attorney Fee Parameters – Melissa

Plan Modifications

- Carl - Introduction
- Excusal of Plan Delinquency - Melissa
- Case Law on direct payments – Melissa
- Tax Returns review parameters – Mark
- Motion to Compel – Leo

Carl L. Bekofske – Closing remarks

Department of Justice

FOR IMMEDIATE RELEASE
TUESDAY, MARCH 3, 2015
WWW.JUSTICE.GOV/UST

UST
CONTACT: JANE LIMPRECHT
(202) 305-7411

U.S. TRUSTEE PROGRAM REACHES $50 MILLION SETTLEMENT WITH JPMORGAN CHASE TO PROTECT HOMEOWNERS IN BANKRUPTCY

Settlement Addresses Robo-Signing and Other Improper Practices in Bankruptcy Cases

WASHINGTON – The Department of Justice's U.S. Trustee Program (USTP) has entered into a national settlement agreement with JPMorgan Chase Bank N.A. (Chase) requiring Chase to pay more than $50 million, including cash payments, mortgage loan credits and loan forgiveness, to over 25,000 homeowners who are or were in bankruptcy. Chase will also change internal operations and submit to oversight by an independent compliance reviewer. The proposed settlement has been filed in the U.S. Bankruptcy Court for the Eastern District of Michigan, where it is subject to court approval.

In the proposed settlement, Chase acknowledges that it filed in bankruptcy courts around the country more than 50,000 payment change notices that were improperly signed, under penalty of perjury, by persons who had not reviewed the accuracy of the notices. More than 25,000 notices were signed in the names of former employees or of employees who had nothing to do with reviewing the accuracy of the filings. The rest of the notices were signed by individuals employed by a third party vendor on matters unrelated to checking the accuracy of the filings.

Chase also acknowledges that it failed to file timely, accurate notices of mortgage payment changes and failed to provide timely, accurate escrow statements.

"It is shocking that the conduct admitted to by Chase in this settlement, including the filing of tens of thousands of documents in court that never had been reviewed by the people who attested to their accuracy, continued as long as it did," said Acting Associate Attorney General Stuart F. Delery. "Such unlawful and abusive banking practices can deprive American homeowners of a fair chance in the bankruptcy system, and we will not tolerate them."

"This settlement should signal once again to banks and mortgage servicers that they cannot continue to flout legal requirements, compromise the integrity of the bankruptcy system and abuse their customers in financial distress," said Director Cliff White of the U.S. Trustee Program. "It should be acknowledged that Chase responded to the U.S. Trustee's court actions by conducting an internal investigation and taking steps to mitigate harm to homeowners. But years after uncovering improper mortgage servicing practices and entering into court-ordered settlements to fix flawed systems, it is deeply disturbing that a major bank would still make

improper court filings and fail to provide adequate and timely notices to homeowners about payments due. Other servicers should take note that the U.S. Trustee Program will continue to police their practices and will work to ensure that those who do not comply with bankruptcy law protections for homeowners will pay a price, just as Chase has done in this matter."

Payments, Credits and Contributions of More Than $50 Million.

In the proposed settlement, Chase agrees to provide payments, credits and contributions totaling more than $50 million:

- Chase will provide $22.4 million in credits and second lien forgiveness to about 400 homeowners who received inaccurate payment increase notices during their bankruptcy cases.
- Chase will pay $10.8 million to more than 12,000 homeowners in bankruptcy through credits or refunds for payment increases or decreases that were not timely filed in bankruptcy court and noticed to the homeowners.
- Chase will pay $4.8 million to more than 18,000 homeowners who did not receive accurate and timely escrow statements. This includes credits for taxes and insurance owed by the homeowners and paid by Chase during periods covered by escrow statements that were not timely filed and transmitted to homeowners.
- Chase will pay $4.9 million, through payment of approximately $600 per loan, to more than 8,000 homeowners whose escrow payments Chase may have applied in a manner inconsistent with escrow statements it provided to the homeowners.
- Chase will contribute $7.5 million to the American Bankruptcy Institute's endowment for financial education and support for the Credit Abuse Resistance Education Program.

Changes to Internal Operations: In the proposed settlement Chase also agrees to make necessary changes to its technology, policies, procedures, internal controls and other oversight systems to ensure that the problems identified in the settlement do not recur.

Oversight by Independent Reviewer: Amy Walsh, a partner with the law firm Morvillo LLP, has been selected to serve as independent reviewer to verify that Chase complies with the settlement order. The independent reviewer will file public reports with the bankruptcy court.

No Effect on Additional Relief by Homeowners: This settlement does not affect the rights of any homeowners to seek any relief against Chase that they may deem appropriate.

Chase Contact Information: Homeowners with questions about the settlement may contact Chase at 866-451-2327.

The settlement is the culmination of actions taken by the U.S. Trustee Program in districts around the country concerning Chase's improper practices in bankruptcy cases, including robo-signing. Director White commended the U.S. Trustee Program team in the field and headquarters who expertly identified, investigated, litigated and settled this matter, including Deputy Director and General Counsel Ramona Elliott, National Creditor Enforcement Coordinator Gail Geiger and Trial Attorneys Diarmuid Gorham and Kelley Callard.

The U.S. Trustee Program is the component of the Justice Department that protects the integrity of the bankruptcy system by overseeing case administration and litigating to enforce the bankruptcy laws. The U.S. Trustee Program has 21 regions and 93 field office locations.

Contact: Jane Limprecht, Public Information Officer
Executive Office for U.S. Trustees
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15-256

Bankruptcy by the Numbers

By Ed Flynn

Consumer Debtor Audits

One of the less-prominent consumer debtor provisions of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) is the requirement that audits be conducted of some debtors. This article will examine the available data on the number of audits conducted since 2006 and their outcomes. The following is a brief refresher on the major components of the debtor audit provisions contained in § 603 of BAPCPA.[1] Two *ABI Journal* articles have discussed the background and mechanics of debtor audits in much greater detail:[2]

- The attorney general should establish procedures to select qualified auditors and cases to be audited;
- Prior to filing their audit reports, audit firms must notify debtors of potential material misstatement findings and allow them an opportunity to respond;
- Audit reports are to be filed with the court and must identify any material misstatement of income, expenses or assets made by the debtor;
- Notice of material misstatements will be given to all creditors;
- The attorney general must take appropriate action if a material misstatement is identified; and
- The attorney general must publicly report on the results of audits.

The Department of Justice set forth nine standards for debtor audits in the Oct. 2, 2006, edition of the *Federal Register*.[3] These standards basically hold that the audits should be conducted by independent professionals who are adequately trained and supervised and are familiar with the bankruptcy process, and that there must be sufficient evidence to support the conclusions in the audit reports. In addition, several of the standards address the content and use of the audit reports.

Ed Flynn
ABI
Alexandria, Va.

Ed Flynn is a consultant with ABI and serves as a coordinating editor for the ABI Journal. *He previously worked for more than 30 years at the Executive Office for U.S. Trustees and the Administrative Office of the U.S. Courts.*

Types of Audits

BAPCPA contemplated two types of audits. The first involves cases that are selected at random, one per every 250 cases filed in a judicial district. The second involves what have been termed by the U.S. Trustee Program (USTP) as "exception audits."

The actual language in § 603(a)(2)(c) of BAPCPA was to "require audits of schedules of income and expenses that reflect greater-than-average variances from the statistical norm of the district in which the schedules were filed if those variances occur by reason of higher income or higher expenses than the statistical norm of the district in which the schedules were filed." Similar language had appeared in earlier bankruptcy reform proposals going back to 1997.[4]

Terms such as "average" and "variance" have a precise meaning in a mathematical context. The term "statistical norm" could refer to a number of specific measures (*e.g.*, average, median, mode, within one standard deviation, etc.). A plain reading of this provision might lead one to conclude that it is indecipherable gibberish. However, it appears that the intent was to make debtors with unusually high incomes or expenses more likely to be selected for an audit.

Material Misstatements

The audits are designed to uncover "material misstatements" by debtors. This term is not among the 86 words and terms defined in § 101 of the Bankruptcy Code. Nevertheless, guidance from the director of the Executive Office for U.S. Trustees (EOUST) takes it beyond the "I-know-it-when-I-see-it" standard:[5] "In general, a material misstatement is an inaccuracy or omission that compromises the integrity and reliability of the bankruptcy documents filed, including an inaccuracy or omission that may impede a determination of whether there are estate assets to administer or whether an enforcement action should be taken."[6] However, the USTP does not make public the pre-

1 Parts of the audit provisions in BAPCPA are uncodified, while others involve revisions to § 586 of title 28, and §§ 521 and 727 of title 11. *See* www.gpo.gov/fdsys/pkg/BILLS-109s256enr/pdf/BILLS-109s256enr.pdf (last visited Dec. 22, 2014).

2 *See* Clifford J. White III and Thomas C. Kearns, "BAPCPA Update: Debtor Audit Procedures and the Reporting of Material Misstatements," *ABI Journal*, Vol. XXVI, No. 10, p. 14, December/January 2008; Lisa A. Tracy and Thomas C. Kearns, "The Top Five Myths about Debtor Audits," XXVII *ABI Journal* 10, 14, 52, December/January 2009.

3 *See Federal Register*, Vol. 71, No. 190 (Monday, Oct. 2, 2006), *available at* www.gpo.gov/fdsys/pkg/FR-2006-10-02/html/E6-16129.htm (last visited Dec. 22, 2014).

4 *See, e.g.*, Section 307 of S.1301, Consumer Bankruptcy Reform Act of 1997, *available at* www.gpo.gov/fdsys/pkg/PLAW-109publ8/html/PLAW-109publ8.htm (last visited Dec. 22, 2014).

5 From the famous statement of Justice Potter Stewart regarding his threshold test for obscenity: *See Jacobellis v. Ohio*, 378 U.S. 184 (1964).

6 *See* White and Kearns, fn.3 at p. 46.

Table 1: Random Audit Selection Rate

Time Period		
Beginning	**End**	**Selection Rate**
Oct. 1, 2006	Sept. 30, 2007	1 per 250
Oct. 1, 2007	Sept. 30, 2010	1 per 1,000
Oct. 1, 2010	June 9, 2011	1 per 1,700
June 10, 2011	Dec. 31, 2011	No audits
Jan. 1, 2012	Sept. 30, 2012	1 per 1,450
Oct. 1, 2012	March 18, 2013	1 per 2,050
March 19, 2013	Sept. 30, 2013	No audits

cise thresholds for determining what constitutes a material misstatement because to "publish them would jeopardize the deterrent value of debtor audits and present enhanced opportunities for gaming the system."[7]

Cost

There is no additional cost to the debtor who wins the audit-selection lottery; the audits are paid for with government funds. Specific cost information is not publicly available, but USTP budget requests indicate that the average cost is about $1,000 per audit.[8]

Random Audit Selection Rate

Due to budgetary constraints, Fiscal Year 2007 was the only year that the USTP actually selected one out of every 250 cases for a random audit. Since then, the selection rate has not exceeded one in 1,000 cases, as shown in Table 1.

Audits in Bankruptcy Administrator Districts

Bankruptcy Administrators are responsible for administering cases filed in North Carolina and Alabama. The Judicial Conference adopted audit standards modeled after those adopted by the USTP.[9] The Administrative Office of the U.S. Courts reports that 1,570 total debtor audits were conducted between Fiscal Year 2007 and Fiscal Year 2013.[10] This works out to one audit per 228 cases filed in North Carolina and Alabama.[11]

No further information is given on the breakdown of random-vs.-exception audits or on the outcomes of these audits. Therefore, all remaining statistics in this article do not include audits of debtors who filed in North Carolina and Alabama.

Total Audits

The audit provisions took effect on Oct. 20, 2006, 18 months after BAPCPA's enactment. EOUST has issued seven annual reports on the results of debtor audits conducted during Fiscal Years 2007-13.[12] During this time, U.S. Trustees designated 13,903 cases for audit. Of these, 8,446 were selected at random and 5,457 were exception audits.

Audit Outcomes

There are four possible outcomes for cases selected for audit.

1. *Audit not completed.* Some audits have not been completed by the time the USTP prepares its annual report on audits, or have been dismissed upon request of the debtor before the case was assigned to an audit firm.
2. *Report of no audit filed.* This outcome includes selected cases in which the debtor did not provide sufficient information to complete an audit or the case was dismissed while the audit was being conducted.
3. *Audit report filed with one or more material misstatements.*
4. *Audit report filed with no material misstatement.*

Excluding cases in which the audit was not completed or the report was not completed at the time that the EOUST report was prepared, there were 12,430 cases with completed audits during the seven-year period. About one-quarter of these audits resulted in a finding of one or more material misstatements (*see* the chart on p. 57).

Material misstatements are much more commonly found in the exception audits compared to the random audits. Material misstatements from both types of audits were substantially higher in Fiscal Year 2007, the first year of debtor audits, than in any subsequent year. EOUST has reported that in Fiscal Year 2008, the USTP "adjusted the criteria used by audit firms for identifying material misstatements."[13] Since Fiscal Year 2008, the percentage of random audits with material misstatements has been fairly flat, while the percentage of exception audits with material misstatements has risen slightly.

Audit Results by District

There are 66 judicial districts in which at least 50 audit reports have been completed. About one-quarter of these audits resulted in a finding of one or more material misstatements. In most districts, the rate was fairly close to the national average. The districts with the lowest material misstatement rates were the District of Puerto Rico (11.2 percent), District of South Carolina (13.5 percent), Western

7 *Id.*

8 For example, in the "USTP FY 2014 Budget Request" (dated March 6, 2013), the USTP indicated that $2.9 million was obligated in Fiscal Year 2010 to fund 2,729 audits and approximately $1 million was obligated in Fiscal Year 2011 to fund 1,077 audits. *See* p. 21, www.justice.gov/sites/default/files/jmd/legacy/2014/05/09/ustp-justification.pdf (last visited Dec. 22, 2014).

9 *See* Report of the Proceedings of the Judicial Conference of the United States, Sept. 19, 2006, p. 9, *available at* www.uscourts.gov/FederalCourts/JudicialConference/Proceedings/Proceedings.aspx?doc=/uscourts/FederalCourts/judconf/proceedings/2006-09.pdf (last visited Dec. 22, 2014).

10 This figure was computed from the individual annual totals reported in the "Annual Reports of the Director of the Administrative Office of the United States Courts, 2007-13, www.uscourts.gov/FederalCourts/UnderstandingtheFederalCourts/AdministrativeOffice/DirectorAnnualReport/annual-report-2013.aspx (last visited Dec. 22, 2014).

11 During the same period, about one in 583 cases filed in USTP districts received an audit. Thus, a debtor in North Carolina or Alabama has been more than twice as likely to be audited as debtors outside of these two states.

12 The reports can be found at www.justice.gov/ust/eo/public_affairs/reports_studies/index.htm#studies.

13 *See* "United States Trustee Program Annual Report, Fiscal Year 2008," p. 16, *available at* www.justice.gov/ust/eo/public_affairs/annualreport/docs/ar2008.pdf (last visited Dec. 22, 2014).

continued on page 57

Table 2: Debtor Audits, Fiscal Years 2007-13

	All Audits		Random		Exception	
	Cases	Percent	Cases	Percent	Cases	Percent
Total Cases Selected	13,903		8,446		5,457	
Audit Not Completed	637	4.6%	449	5.3%	188	3.4%
Report of No Audit Filed	836	6.0%	555	6.6%	281	5.1%
Audit Complete						
No Material Misstatement	9,335	67.1%	5,893	69.8%	3,442	63.1%
At Least One Material Misstatement	3,095	22.3%	1,549	18.3%	1,546	28.3%

Bankruptcy by the Numbers: Debtor Audits

from page 47

District of New York (14.5 percent) and Western District of Missouri (14.7 percent). The districts with the highest rates of material misstatements included the District of New Jersey (32.1 percent), Northern District of Illinois (33 percent), Western District of Tennessee (35.2 percent) and District of Maryland (36.9 percent). The latter two districts also had the highest percentage of cases in which audits were not completed because of dismissal or lack of documents.[14]

The U.S. Trustee has a wide variety of responses available to a reported material misstatement, including no response, various civil enforcement remedies and a criminal referral. The USTP has not published any data on enforcement actions taken as a result of debtor audits, but their annual reports of significant accomplishments have included a number of examples of specific actions taken as a result of information uncovered by audits.[15]

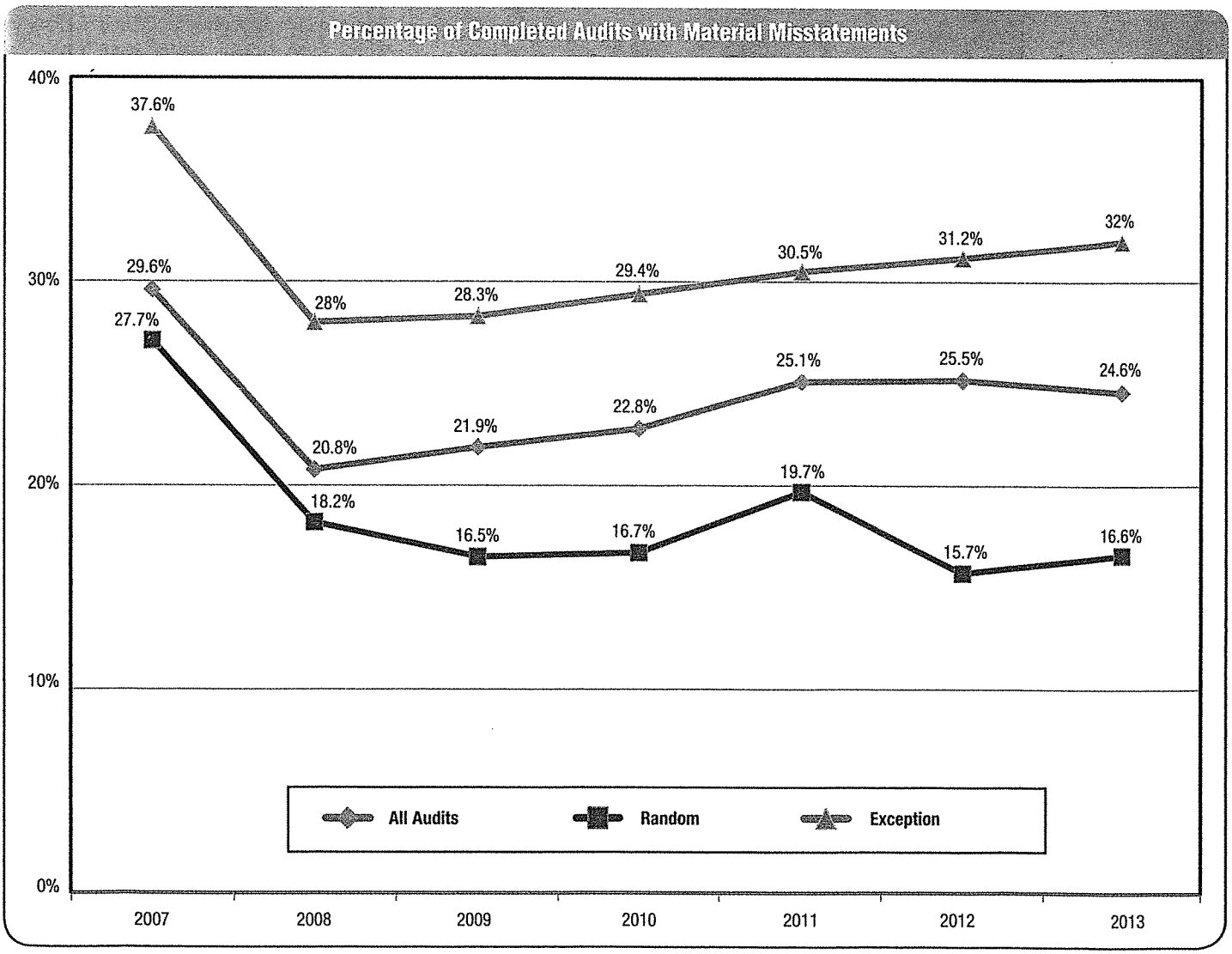
14 These figures are derived from the individual audit annual reports prepared by the EOUST. *See* www.justice.gov/ust/eo/public_affairs/reports_studies/index.htm#studies.

15 *See, e.g.*, Annual Reports of Significant Accomplishments for the following: FY 2013 Report at p. 21, FY 2012 report at p. 24, FY 2011 report at p. 21, FY 2010 report at p. 19, FY 2009 report at p. 20, and FY 2007 report at p. 20, *available at* www.justice.gov/ust/eo/public_affairs/annualreport/index.htm (last visited Dec. 22, 2014).

Conclusion

Debtor audits have been conducted for more than eight years but are still a largely overlooked consequence of BAPCPA. This much we do know about debtor audits:

- Audits are a fairly rare event. Less than one in 500 consumer cases is selected for an audit, and few practitioners will have more than one client selected for an audit each year.
- In cases selected for audit, about 6 percent do not result in an audit because of dismissal or lack of documents.
- Of the cases with completed audits, about one-quarter result in material misstatements.
- Material misstatements are much more commonly found with exception audits than with random audits.
- The percentage of exception audits with material misstatements has risen slightly over the last five years.
- The consequences of a material misstatement can range from no action to a criminal referral.
- To protect the integrity of the process, the USTP is not likely to ever disclose the specific criteria used for selecting cases for exception audits, or the exact standards used to determine what constitutes a material misstatement. abi



Servicing Matters

Posted: 04 Mar 2015 08:41 AM PST

I am so pleased to offer the following post by **Carolina Reid**, a premier housing researcher at UC Berkeley, about her excellent study of how mortgage servicers matter in creating home-saving opportunities. Welcome Carolina to *Credit Slips*.

By now we're all familiar with a plethora of Wall Street financial acronyms, from ABSs to CDOs and CDSs. But what about MSRs (mortgage servicing rights)? Until a year ago, I had never heard of MSRs, so I was surprised to find out that the rights to collect my mortgage payment are traded on Wall Street, much in the same way mortgage backed securities are traded. And, as a borrower, I have very little control over who purchases the servicing rights to my mortgage, despite the fact that it is usually the servicer who decides whether to offer a loan modification or start the foreclosure process if I become delinquent. Borrowers can't "shop around" for the best servicer – you get who you get (but maybe you should get upset).

Does it really matter who services your loan? To date, research has very little to say about this, though ask any housing counselor who has tried to shepherd a distressed loan through the modification process and the answer will be "most definitely." Unfortunately, most data on loan performance don't allow researchers to identify the institution that services the loan, which makes analysis of servicer performance challenging. So other than headlines about robo-signing or dual tracking, we have few studies that systematically study servicers and the ways in which they assist distressed borrowers.

My colleagues, Carly Urban and J. Michael Collins, and I recently released a **Fisher Center Working Paper** that explores differences in servicer behavior, to shed some light on the servicing industry. Using a unique dataset on subprime loans that were at least 60 days delinquent, we examined the modification practices of 20 large, national servicing institutions. We wanted to know whether servicers differed in the likelihood of offering modifications with interest rate or principal reductions, even for similar borrowers living in the same neighborhood. And we wanted to know whether some servicers did a better job of helping borrowers retain their homes, all other things being equal.

What we found is that servicers differ dramatically in their loan modification practices and their loan cure rates. Servicers with higher cure rates performed permanent modifications on almost 48 percent of their delinquent loans, while servicers with the lowest cure rates only granted modifications to 2 percent of delinquent borrowers. Some servicers favored interest rate reductions; others were more willing to offer borrowers principal write-downs, or even offer a second modification. These differences in servicer practices led to very different cure and re-default rates for distressed borrowers, even after controlling for a wide range of borrower, loan, and housing market characteristics. Who your servicer is really does matter. We also examined whether there were differences across servicers for Black, Hispanic, Asian and white borrowers. In general, we did not find any substantive race or ethnicity effects within any one

servicer, rather, the differences across servicers remained constant. In other words, if you end up with a servicer unwilling to do modifications, you're not getting a modification regardless of your race.

A more vexing question is why these differences across servicers exist, particularly with the existence of programs like the Home Affordable Modification Program (HAMP) that were designed to streamline and standardize the modification process. Unfortunately, we can't really answer this question with existing data. We do examine differences between bank and non-bank servicers, to examine whether a servicer's capital structure influences their practices. Adam Levitin's work (a regular contributor to this blog and the co-author of a terrific paper on **mortgage servicing**) gave us that idea. We find that non-bank servicers are more likely to offer modifications, especially principal reductions. But the bank/non-bank divide is unlikely to be the whole story, and we find that differences across bank and non-bank servicers have diminished over time.

What this suggests to us is that the Bureau of Consumer Financial Protection (CFPB) and other financial regulators at the federal and state levels need to be supported in **their ongoing efforts** to ensure greater transparency and accountability in mortgage servicing. For example, the CFPB recently implemented **servicer rules** which include improvements in borrower communication and disclosure, specific obligations to respond to borrower requests for information within specified timeframes, rules related to early intervention with delinquent borrowers and a single point of contact, and a prohibition on dual tracking. Future research should seek to assess whether these new rules reduce servicer heterogeneity and improve outcomes for delinquent borrowers. Without better data on servicing practices and borrower outcomes (especially over the long-term), policy-makers are in the dark when it comes to designing effective foreclosure prevention strategies and ensuring that every borrower gets fair and equal treatment.