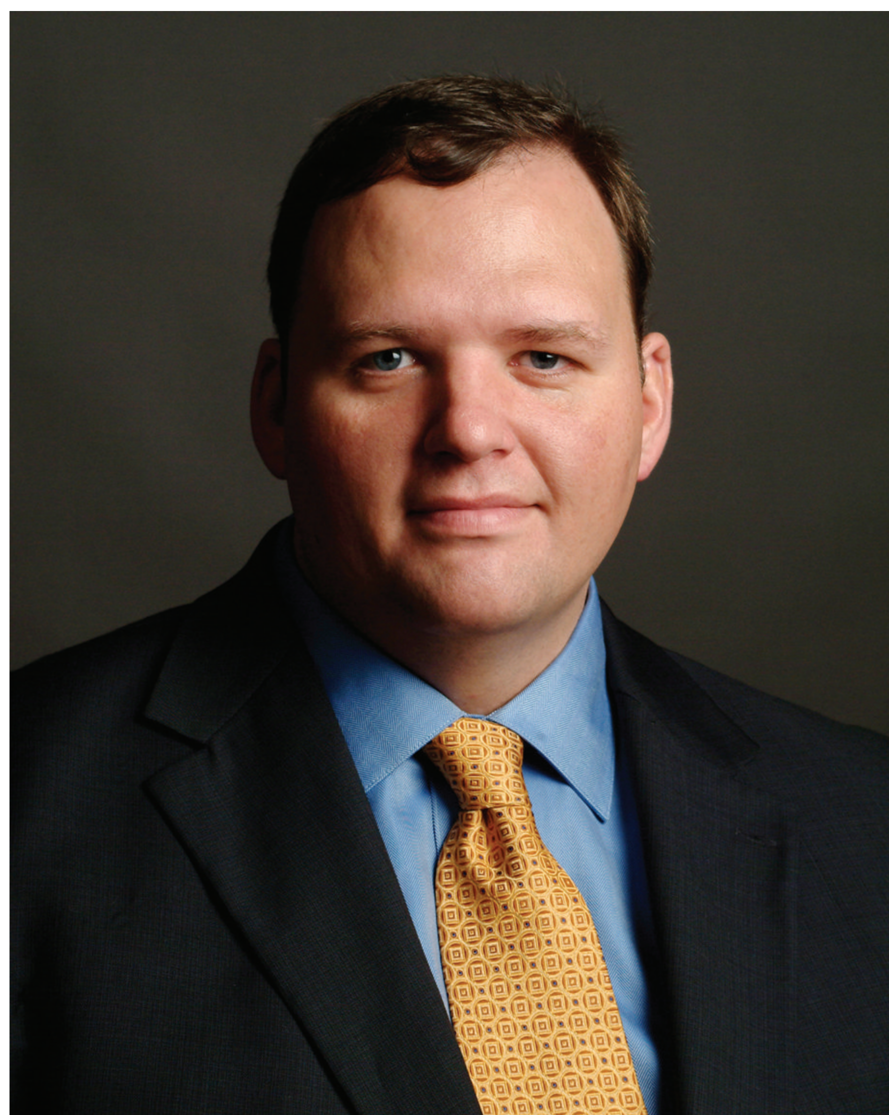
Q&A with Robert Maddox

— by JANET REILLEY HEWITT —

Robert Maddox has been on the front lines during much of the servicing litigation and enforcement actions over the last decade. This senior Bradley Arant Boult Cummings LLP attorney also represented a major servicer during the many months it took to negotiate the National Mortgage Settlement.



Robert Maddox, CMB, is a partner with Bradley Arant Boult and Cummings law firm. He has represented many financial services industry clients in both trial practice and in compliance matters. He was directly involved in the litigation that mushroomed over servicing practices during the foreclosure crisis. ¶ Notably, he represented GMAC (now Ally Bank) during the many months leading up to the massive National Mortgage Settlement (NMS) between the top five servicers and 49 of the nation's attorneys general (AGs). ¶ His trial practice has led Maddox to trial and appellate courts in more than 40 different states from Florida to California.

Q: *Describe your very first involvement with mortgage servicing litigation.*

A: My first case involving mortgage servicing was one of the first cases I ever had. It was quite interesting. It involved a closing attorney who, instead of paying off the mortgage, was essentially making the monthly payments on the house [that was supposedly being sold]. He was never actually doing a real estate closing. Instead of paying off the prior mortgage company when it wired the new money into his account, he was just paying off the monthly payment the earlier borrower had.

It was a pretty successful closing business, so he was able to do that for about two or three months. This was during the refinance boom—when people went back to refinance, [they found] there were two liens on their property instead of one, which was complicating their servicing.

It was a cross between mortgage origination fraud and servicing litigation, and that was in 2000. It was the first year I started practicing law.

Q: *Then how did you get more deeply involved in mortgage servicing litigation?*

A: I was supposed to be a medical malpractice attorney, but that didn't work for me. All those biology, genetics and organic chemistry classes aren't doing too much for me these days.

We did the origination fraud work, and gradually more and more mortgage companies began to hire us in 2000, 2002, 2003, 2004, 2005 and 2006. We worked through the origination issues popping up during that time, and then comes the financial crisis.

The first sign we had that things were changing was [when] clients abruptly started suing on their warehouse lines. That had never happened before because warehouse lines were [non-bank mortgage] lenders' lifelines.

If they didn't have money, they couldn't close loans, and if you stopped that process—industrywide—you shut down everything. In late 2007, that was the first inkling we had that something was definitely going wrong.

In 2008 and 2009, the foreclosure crisis hit; our litigation matters were taking place across the entire country. Lawsuits were ramping up, and then in 2009 you began to see some relief in the form of loan modifications.

Then into 2010, we represented Ally Bank and GMAC in what would eventually become the National Mortgage Settlement.

Those negotiations took a great deal of time, ultimately culminating in 2012. That agreement [with the state attorneys general and the Department of Justice] had a monitoring compliance factor included in it as part of the settlement. The settlement established both servicing standards and metrics built into the consent judgment to measure servicer compliance with the settlement terms and metrics. Compliance with the terms was to be tracked for three and a half years, so that monitoring of compliance still is ongoing.

Q: *What more recent cases have you worked on that followed in the wake of the National Mortgage Settlement?*

A: Ocwen Financial Corporation had a consent judgment that was filed in December 2013 and entered in February 2014. We served as counsel for Ocwen and there were some similar parties involved, including the Consumer Financial Protection Bureau [CFPB], state attorneys general and state banking regulators. Then SunTrust Mortgage filed a consent judgment in June 2014 that was entered Sept. 30 by Judge Rosemary Collyer, who is the same judge for all the NMS matters.

In 2013, we worked on the Southern District of New York/HSBC [Bank] matter that was public, and Ocwen settled a matter with the Massachusetts attorney general.

In addition to the National Mortgage Settlement cases, throughout this same period you had a great deal of enforcement actions on [individual servicers with] regard to subpoenas and civil investigative demands. We worked fairly closely with government entities at multiple levels, whether on the regulatory side or on the enforcement side.

Additionally, we worked with quite a few mortgage servicers in settling some of their [legal and enforcement] matters. But the ones I mentioned are the public ones.

Q: *Has your practice grown, in terms of number of attorneys and in other ways, during this period of stepped-up servicing litigation and enforcement?*

A: Yes, there's no question. I think our practice is a reflection of the financial services industry as a whole. We were a corporate counsel to regional banks and some nationals, and as we stepped in more and did more and more enforcement work, our practice has grown substantially since 2008.

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Q: *What are some of the most common practices by servicers that resulted in costly litigation?*

A: Looking back, I think there were two of them. The first was dual tracking, with that being defined [as] foreclosing on a borrower while at the same time trying to work with them [using] loss-mitigation techniques.

When the negotiations for the National Mortgage Settlement were taking place, servicers were in a very difficult position. [They faced] predominantly GSE [government-sponsored enterprise] timelines [that consisted of] foreclosure timelines in states, to ensure the foreclosure took place in a timely manner. Yet at the same time, you were working with a borrower to gather information or documentation that could assist them in [finding] a loss-mitigation option hopefully to save their home.

But [between the GSE foreclosure timelines and the loss-mitigation requirements], the servicer was jammed on two sides with regard to this issue.

[So you had the consumer thinking:] "I'm receiving this outreach from the mortgage servicer that says they want to work with me while I'm in the home, but at the same time I may be receiving a foreclosure notice or the servicer's attorney might be contacting my attorney."

So there was confusion for the consumer about competing messaging. I think that the government as a whole looked at it as a consumer messaging issue. They utilized different terms as far as "deception" and "dual tracking," but in my personal opinion, I believe they understood, at the end, that the servicer was acting within its contractual obligations to move the foreclosure forward while at the same time truly trying to work with the borrower.

The end result is that now, based on CFPB's mortgage servicing rules, if the borrower has already submitted a complete application for mortgage assistance—a loss-mitigation application—the servicer cannot begin the foreclosure process while the borrower is being evaluated for a loss-mitigation plan.

The other [area of costly litigation]—and again, I think it has to do with communication and misunderstanding—is lender-placed insurance. A borrower could be in default just with regard to their escrow or specifically with regard to their insurance, but they could be making their monthly payments. [But the problem there is] if you don't have insurance, the investor is not insured.

For example, an insurance company would receive notice from the mortgage servicer, usually after multiple notices to the borrower, and the insurance company would automatically place insurance on the dwelling, sight unseen, based usually upon ZIP code. So no traditional underwriting would take place. You just have insurance put on right there, on the date designated by the servicer, which would normally be when the borrower's insurance coverage would have lapsed. That type of risk obviously is not going to be borne by the insurance company. It's going to be borne by the consumer for failure to maintain insurance coverage on the dwelling. One of the misconceptions was, why if [as a consumer] I can go to Allstate or Nationwide and get this type of insurance, is the lender-placed insurance so much more expensive?

One reason for the added expense is that there was no underwriting. It was a completely blind [placement of coverage]. Plus, as with most things throughout the late 1990s and the first [several] years of this century, there were affiliate relationships that were developed. I don't think the regulators, enforcement agencies and private litigants like the affiliate relationships when mortgage companies either were affiliated and/or horizontally or vertically integrated with an insurance company.

They perceived the servicers had the ability to take advantage of a borrower because the servicers had the ability to make the call and force-place insurance on the dwelling. They thought the decision to place insurance on the dwelling was not completely transparent; however, with the proper documentation, you can determine if the borrower's insurance lapsed by the policy period and whether the servicer was within their contractual rights to place insurance on the dwelling.

Those were costly litigation [areas that servicers] had to deal with and will have to continue to address on an individual borrower level. Both, I believe, predominantly dealt with a PR or communication position that was taken with regard to the industry. There was some misinformation as to when and why and where these default matters took place. And they developed a life of their own. Plus, the messaging that was coming out of regulators and out of enforcement [circles] was that this was not good news for servicers.

In civil litigation, these [issues could be more] controlled.

You had a neutral third party sit down and look at them, whether it was arbitration and/or litigation. In most of those [decisions], mortgage servicers prevailed because civil litigation happens in front of a judge, who was objectively viewing it as a breach-of-contract case where the borrower was in default. [Whereas] in negotiation with a regulator, it's a different table and a different group of people that you have to work with.

Q: *Can you review the whole robo-signing legal issue—what it was, where it got started and whether there were instances when the servicer prevailed in cases involving that issue?*

A: The allegation around robo-signing was that there were people who were signing documents, whether it was an affidavit of indebtedness or some type of attestation with regard to account figures, to prove that borrowers were in default.

Whether it came into bankruptcy, a judicial foreclosure or in some other [proceeding], these people were signing these documents at a very high volume.

When you or I think about signing an affidavit, it usually only occurs in very limited circumstances during our lifetimes. For example, at a real estate closing or in connection with doing our will. We carefully review all the terms, have the ability to ask the lawyer or other professional questions. Whereas in the allegations of robo-signing, this was the document that these people saw day in, day out—it was essentially the same document.

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What they had to do was compare the information listed on the affidavit to what they saw in the system of record, sign it, and then it would be notarized. So the question [for them] was could they actually get it all done in time? And if that's the one thing that you do all day—look at numbers and validate them—it is possible to get it done.

The other issue was when did the notarization take place? You can imagine that if what the affidavit signers did all day was check information from the system of record and make sure it's on a document, or if it's wrong, put it over in a different pile, that notary is not [going to be] sitting there like in a real estate closing waiting to notarize a single or small group of documents. The notarizations might take place at intervals throughout the day. In the robo-signing attacks, the allegations were focused on these intervals. [Critics argued] that the affidavit or the document utilized to prove the borrower's account information had been turned into a commodity piece of work. [But that kind of approach] was not uncommon because it was usually—not always, but usually—the same document, just with different borrower information.

Whereas when someone else outside of the default servicing world would sign an affidavit, he understands that I'm attesting to everything that's inside of this document. I'm going to double-check it. I'm going to make sure it's accurate and correct.

So those [different perceptions] helped to breathe life into the robo-signing allegations.

In most of the individual borrower cases, even if there was an allegation that the person who signed the document didn't sign directly in the presence of a notary, [the real question centered on] were the underlying numbers correct and could they validate that through the system of record? This is kind of making a broad statement, but based on many of the prior cases involving allegations of robo-signing, most judges in judicial foreclosure states said, "Wait, does it really matter how they signed it?" Because filing supplemental documentation, including affidavits, in civil litigation matters is not an uncommon practice.

The other underlying issue is: Are you, John Q. Borrower, in default? Did you make your payments? If you're debating whether you made your payments or not, well, that's one thing.

If you didn't make your payments but this person didn't sign it accurately, that's a different thing. I think a lot of times we saw the underlying document signature issue not be the driving force in these cases. At issue really was whether the borrower was in default.

The same thing [applied in cases where the court was asked to rule on] whether the foreclosing entity had proper standing. [Is the loan being serviced] involved in a trust, a securitization? Is it a MERS® loan and what does that involve? All of those issues were raised by the foreclosure defense bar, and sometimes they were able to gain traction in some courtrooms with those arguments.

I would say the overall issue was did the individual borrower make the payment? No. OK, so let's address those issues. I would say that was the early experience.

If you think back to 2008, 2009, 2010, even into 2011, we continued to see foreclosure numbers move in an upwardly direction and I think, candidly, robo-signing was an easy way to vilify the financial industry when actually what you were dealing with was a global recession.

But there again, I'm obviously biased. I know you're not going to find too many people who were sitting in the same spots we were over the last five years and perhaps looking at this from our vantage point.

Q: *How many attorneys and firms specialize in this area of the law?*

A: On major enforcement matters, probably not that many. You've got a handful of firms that do what we do, specialize in this area—maybe a dozen. There are different components that are brought into this work.

So if I have to go deal with the board of directors for one company, they've got their own counsel who deal with that issue.

Servicers may have litigation counsel for a whole host of different litigation matters. Over the past couple of years, in doing these large-scale matters we've had to work with multiple good lawyers inside and outside to handle and resolve these matters. There's a whole host of firms that touch the financial services world, but with regard to people handling these enforcement matters on a regular basis, who are doing the CFPB examinations, investigations or enforcements or dealing with attorneys general on a fairly consistent basis, there's really a dozen or so that we routinely see again and again.

Q: *What was the costliest practice in terms of servicing that resulted in the biggest fines or settlements?*

A: Certainly in terms of the biggest settlement, robo-signing was the genesis of the National Mortgage Settlement.

That first NMS settlement with Bank of America, GMAC, Citi, Chase and Wells contained allegations of robo-signing, and clearly some of the servicing standards are focused directly on those issues. But the subsequent servicer [enforcement cases], the Ocwen NMS settlement and SunTrust NMS settlement that came two years later, I wouldn't paint those with the same broad brush as a robo-signing issue.

Clearly, there are servicing standards dealing with robo-signing that are consistent across all of those settlements, but you didn't hear when those [later] consent judgments came down that it was robo-signing.

Q: *Describe what it was like to sit in on those state AG settlement negotiations. The settlement talks seemed to last forever to outside observers.*

A: Without getting into specifics or attorney/client privileges, it was interesting to have such a large dynamic not only across so many different jurisdictions, but also with regard to multiple points of views as to the way certain attorneys approached the issue.

Obviously you've got different viewpoints. You had some people who were very focused on—at all costs—keeping the borrower in the home. [Discussions about] the proper path for doing that were very interesting, because you had some people that asked questions like, "Can you amortize it out farther, can you forebear more?" [and so on]. There were really, really intelligent people, from both the industry's perspective and the government's perspective, [focused] on trying to stem the foreclosure crisis. [They were suggesting] multiple different ways to [do that]. The group included representatives from all across the federal and state governments.

[One complicating factor was that in many instances, we were trying to find solutions for] people who had lost their jobs. The negotiators were looking for the best way to try and work through the process with them to give the borrower in default, if you will, a graceful exit from a home. For me, it was a recognition that we're all Americans realizing that we were dealing with another American losing their home, because of a lost job or decreased income, and that's a travesty. [So part of the discussion was focused on] the best way to go about handling that issue.

That was unique—trying to work through those pressure points. But at the same time, you had to be able to move on what essentially is a breach-of-contract case. Breach-of-contract cases have been around for centuries, and it wasn't overly complex as to what was supposed to actually be going on. It was the manner and approach in which to do it.

Candidly, and this is just my opinion, from the government's perspective—and this is not specific to any negotiations—but I think there was a view, which has never been expressly articulated, but you can point to multiple events, legislation, new laws, that if the foreclosure process was lengthened, hopefully the economy would have more time to heal, meaning some of these people who were in default now could [recover financially either with employment or regain some of the equity in their homes]. I think that you've seen that play out in various jurisdictions where timelines to actually be able to foreclose [were extended]. The theory being the economy in those areas would begin to heal itself and that ultimately would help people avoid default.

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One other feeling that I took away from the experience was, and] I can't speak for anybody else, but at least I had a perception that the servicing standards we were negotiating were going to become maybe a blueprint for what the CFPB was going to be doing down the line.

I don't think I was alone in this perception, but I don't recall anyone said specifically: Yes, this is what will happen.

The California and Nevada and a few other homeowner bill of rights came out around the [time of the] NMS settlement. [Then you see] the CFPB create its mortgage servicing rules.

Clearly there's not [an exact] blueprint between the NMS servicing standards and the CFPB mortgage servicing rules, but there are areas of significant overlap.

Q: *In terms of the role played by the individual state attorneys general versus the federal government negotiators, how did they divide up their roles?*

A: I think they were fairly uniform in their views, and they obviously met and worked together. I don't think that anyone was tougher or easier, or anything of that nature.

There were public news reports with regard to some attorneys general joining or leaving or rejoining [the settlement talks], and obviously there were some press reports as to certain people's issues in the negotiations. But I think when one attorney general's office spoke they weren't just speaking for themselves.

[Some of the individual attorneys general] might have had greater issues with regard to their states. But when they spoke, I took it as though it was an issue that had to be addressed and was therefore a concern for all of them.

Q: *In terms of the one holdout from the final agreement, was it clear from the start you were never going to get—was it Oklahoma?*

A: It was Oklahoma.

Q: *Was it clear from the start you were never going to get Oklahoma?*

A: You know, thinking back on it now, I don't think it was clear. I never knew who I was going to [get to] join and who wasn't going to join. I've done it three times now, and every time it's still kind of a nail-biter.

I don't think I had a view that we definitely had somebody or we didn't, because each one of them is a sovereign entity that had to look at it in an individual way. They obviously have unique pressures in each jurisdiction. So I didn't have a view that this is definitely a solid "in" and this one is definitely a solid "out." Even the ones who were lead negotiators with us, I didn't feel like we knew one way or the other. Because they all had to internalize it and because, as you said earlier, you thought the negotiations went on forever.

Over time, I learned that nothing should surprise me with regard to those negotiations, so I kept kind of a straightforward view.

Obviously at the end, when we negotiated a separate individual state settlement with Oklahoma, we knew they weren't going to join. But up until that point in time, were there indications? Yes, but there were indications everywhere, and there were public comments everywhere. This person says this, that person says that.

Until the very end, you had no idea who would actually join.

Q: *With Attorney General Eric Holder leaving the Department of Justice, do you expect any shift in the posture of the Justice Department toward the servicing business?*

A: Obviously there are changes with regard to personnel on a regular basis at the Department of Justice. We've dealt with different people throughout the last few years.

I don't have any indication with regard to the Department of Justice or, candidly, any regulating entity that there is a substantial change in direction on investigation or enforcement matters.

Q: *So the enforcement posture may never retreat back to where it was?*

A: I have no indication, regardless of whether Eric Holder left, stayed or moved on. I just think that we're at a different posture not only with regard to federal and state law, and obviously with the CFPB, but also from a regulatory oversight position.

I think we have changed the dynamic of what was a contract issue: Purchaser borrows money from lender for purchase of a home. If the borrower doesn't pay the money back per the terms of the note and mortgage, the lender has the contractual right to recover its losses through foreclosure.

That basic simple contract issue now has been so changed and altered, not only in law but also with regard to the relationship between financial institutions and their regulators. I don't know if we'll ever go back.

Before, if someone couldn't pay his or her bill, you foreclosed. Now it's much more difficult to recapture the collateral that was utilized to loan money in the first place. And it's not just in mortgages. This change is happening across many consumer financial matters. It's almost a regulatory minefield when you loan money to a consumer. The financial institution almost has to be regulatorily perfect in order to recover.

To be clear, I'm not saying there shouldn't be safeguards throughout for consumers, but the pendulum has swung so far now, the question of whether the person borrowed the money and failed to pay it back almost appears to be a secondary issue. The primary issue has become the technical proficiency and performance of the financial institution.

Q: *You talked a little about the legacy of this servicing industry chapter. What will be the lasting legacy, either in the law or regulation or in industry practices?*

A: I believe when business historians focus on this time period, the dynamic that we'll see is this very consumer-oriented viewpoint. "I wasn't treated appropriately [or] fairly and provided multiple opportunities," versus the question of were you loaned the money and did you pay it back?

We've had UDAAP [unfair, deceptive or abusive acts or practices] statutes on the books for decades to make sure that if someone borrows money, that the lender or servicer was not deceptive or abusive with the borrower. We've also had protection around [the Fair Debt Collection Practices Act] for decades, to make sure that someone is not abusive in trying to collect debt. So those remedies for borrowers have always been available, but more or less from a civil standpoint.

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The other thing that I think has changed significantly is third-party vendor management. When you go back to robo-signing and the foreclosure crisis, the banks, the servicers, the GSEs, etc., were all held accountable, to a certain extent, for what the default firms did.

I'm responsible for the services of people that I contract with, and I think that may also be a lasting legacy issue.

You go back to "too big to fail"—some institutions are considered too big to fail. But from a regulatory standpoint, especially in third-party vendor management, if you're going to make me responsible for my law firms, my print vendor, my IT [information technology] vendor, my REO [real estate–owned] vendor—we're creating an environment where we have such [extensive] external risks that financial institutions are going to want to internalize it.

An institution will desire to [bring those functions inside its corporate structure]. That way it can control them and reduce risk. So we may have the pendulum eventually swinging back again. If institutions and servicers are going to be criticized by their regulators, investigated by the enforcement arms of the state and sued in civil litigation for the actions of their third-party vendors, then we are going to see a struggle between those institutions/servicers desiring to internalize the work of their vendors to eliminate risk, [which is at odds with] the regulator's [desire to not let lenders expand] affiliate businesses. The irony is, it is partially the regulatory and enforcement entities that are helping create the environment and results they don't want.

So now servicers and financial institutions appear to be held responsible, at some level, for everybody they contract to do work with. Whether fair or unfair, it appears that it all comes back to the mortgage servicer.

Financial institutions utilize many vendors on a daily basis. If a financial institution is responsible for their vendors' actions, then it's almost like they are self-insured.

Q: *So what you're saying is they've built in all the incentives for banks to become too big to fail?*

A: Exactly. **MB**

Janet Reilley Hewitt is editor in chief of *Mortgage Banking.*