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10 Ways Financial Cos. Can Avoid Payment Relief Pitfalls

By **Vaishali Rao** (May 22, 2020, 2:36 PM EDT)

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As the ramifications of the coronavirus continue to unfold, the 2008 financial crisis provides unfortunate, but important parallels. In many ways, the Great Recession serves as a foundation for the expectations placed on financial institutions' responses to consumers today.

In 2008, the government debated — for many months — principal reductions, and even modifications on mortgages in general, to create the Home Affordable Modification Program. Related programs, like the Home Affordable Refinance Program, took three iterations to expand coverage to a broader set of borrower and loan characteristics.

Now, the Coronavirus Aid, Relief, and Economic Security Act provides a right to forbearance on a federally backed mortgage for up to 180 days. In 2008, we had protesters in the streets of Wall Street demanding reform on Main Street. Now, part of the CARES Act is titled the "Main Street Lending Program," with the idea of ordinary low- and middle-income citizens receiving immediate aid playing a central talking point in its passage.

Prior recessionary responses were almost exclusively focused on mortgage relief. Today, institutions in the credit card, student loan, auto finance, retail installment, personal loan and even debt collection industries may either be mandated to offer payment relief by state or federal law, or choose to offer it as a customer retention policy.

Providing some form of payment relief to customers may sound relatively riskless. Does anyone really complain about a financial institution offering to cut them a break? In fact, consumers routinely (and especially) complain to state and federal regulators during times of financial distress.

Consequently, government entities like the state financial services (or banking) regulators, state attorneys general, the Consumer Financial Protection Bureau, and the Federal Trade Commission remain vigilant about the ways in which payment relief offers are provided to consumers. While each of those governmental bodies employ slightly different mechanisms to investigate a company's practices, the crux of their inquiries all stem from unfair and deceptive trade practice principles.

Signs of regulatory scrutiny on financial institutions are more than looming. The first cries of fraud have already hit vis-a-vis inquiries into banks' lending practices as it relates to the types of borrowers who received benefits from the Paycheck Protection Program.

The second surge was initiated on May 4 by Democratic leaders of various House committees, including the House Financial Services Committee and the Subcommittee on Consumer Protection and Financial Institutions, who sent a letter inquiring about the forbearance practices of at least 11 mortgage servicers. In their letter, they emphasized, "It is critical that you communicate consistent and accurate information regarding the options available to borrowers who are unable to make their mortgage payments due to financial hardship that is directly or indirectly related to the pandemic."

By revisiting 2008, we know that the immediate focus on the mortgage industry marks the beginning of similar inquiries into other financial services sectors. In fact, some financial institutions are still paying the price of offering modifications to payment terms — on secured and unsecured products — nearly 12 years later.

For many companies, simply having a robust existing compliance program may not do the trick. Companies will be tested as to their core abilities to deliver simple, effective and consistent options to consumers, which may not be captured in ordinary audit protocols.

Following are 10 top-of-mind issues for regulators in evaluating a financial institution's effectiveness in administering payment relief options, regardless of the specific financial product to which the payment relief applies.

1. Disclosure and Consistency of Options Offered

Many companies simply advertise, "Call us for help." By doing so, the company places a significant burden on customer services representatives to offer options appropriately. Instead, companies should consider appropriately disclosing the available options on their website and other written materials.

Take, for example, two borrowers, in two different ZIP codes, with similar (though not the same) lending risks, who are both current but about to be 30 days behind on their payments. Are both offered the same type of payment relief? Why or why not?

Companies should have appropriate payment relief policies in place, which address payment relief equity. If possible, potential variances in payment relief options should be identified and appropriately justified pursuant to state and federal law.

2. Ease of Application Procedures

Progressive regulators will want to ensure that payment relief options — particularly those mandated by law — are easily accessible. Consider different populations of people — seniors, veterans, college students — when determining which application methods are appropriate.

3. Underwriting Abilities

Too often, legal departments and counsel find out posthumously that companies' underwriting capabilities are not set up to handle the types of variances that payment modifications impose. Engage with IT personnel or outside vendors thoroughly to understand the systems that are being utilized and any limitations.

4. Statute of Limitations Considerations

Though regulators tend to leave statute of limitations issues to courts, they may seek information regarding a company's policies and procedures regarding assessment of appropriate application of statutes of limitations. Companies should evaluate the current status of any default as it pertains to the statute of limitations, and attempt to fit payment relief options within any applicable state-specific tolling provisions, if appropriate. Such evaluation may significantly help in private litigation as well.

5. Testing

Correlated to the offering of consistent options, testing or auditing is critical in administering payment relief options properly. Inadequate testing of payment relief options both in the offering and outcome stages can increase exposure to fair lending claims.

6. Disclosure of Consequences

Consumers are not implicitly aware of the consequences of payment relief help.

For example, does a forbearance mean that interest will continue to accrue? Is there an option to halt interest? Why or why not? Will there be a balloon payment after a particular period of time? Once the forbearance option has been utilized, is there an option to utilize another one at a different point in time? Why or why not? What are the credit reporting and credit scoring implications of the specific payment relief option being offered?

These are the types of misunderstandings that most commonly result in consumer complaints and, ultimately, unfair or deceptive trade practice claims. Consider communicating the consequences of payment relief, such as through a frequently asked questions webpage or direct mailer. Remember that a particular term like "forbearance" can implicate different consequences for consumers depending on the type of product.

7. Effectiveness of Payment Relief Option

At the end of the day, regulators want to ensure that payment relief options actually benefit consumers. Does the payment relief option make sense for the consumer in light of the circumstances? Does the consumer have any less expensive options, or ones with less detrimental long-term effects? In an ordinary lending context, this balancing test would be called an "ability to repay" analysis. Consider a similar analysis in the payment relief context.

8. Bankruptcy Rules

Be mindful that bankruptcy laws and rules should still be considered and adhered to, even amidst evolving federal and state programs. Companies should have adequate protocols for flagging those in bankruptcy, or those about to face bankruptcy.

9. Cross-Selling

As time passes, companies will inevitably need to shift priorities, continue innovating, and potentially offer new and different financial service offerings to consumers. Cross-selling while offering a payment relief option (or while someone is enrolled in a payment modification option), explicitly or implicitly, can be a risky proposition if not undertaken with adequate care.

10. Record-Keeping

Regulators will, undoubtedly, ask for records on all of the above, and more. It is imperative to adjust record-keeping systems to capture the efforts companies are making to offer payment relief options, as well as to track those taking advantage of the options.

Conclusion

With the patchwork of evolving state regulations across the country, coupled with the intricacies of new federal legislation, it can be difficult to prognosticate exactly what will be the focus of government regulators. Outside counsel who are familiar with the issues above, and the perspectives and judgments of consumer regulators, can help financial institutions structure effective payment modification options and avoid many of the regulatory pitfalls from 2008.

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