

The WSJ quoted me as claiming what amounts to a “quality tax” as a result of the mortgage debacle both from the origination side and the default sides of the house. [citation issue, placement, author] of The “tax” that I estimate to be approximately \$300 will come in the form of higher processing fees or higher interest rates borne by borrowers. The logic behind such an increase is that tools, technology, and proxies that the industry relied on for the past ten years have proven to be unreliable and often flat out wrong – FICOs, AVMs, AUS, data validation and verification tools, etc. In response, the industry has got back to the process of human inspection and validation of key underwriting, processing, and servicing tasks and that drives efficiencies out of the process and ultimately increases costs. It will likely be a long time before we as an industry have enough confidence in these tools and proxies to require human analysis of their findings.

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Mortgage Lenders Set Back in Courts

By Ruth Simon, Robin Sidel, and Nick Timiraos
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The push by mortgage companies to accelerate the snarled foreclosure process is running into resistance from judges who are cracking down on sloppy paperwork. In Florida, a state-court judge has begun forcing lawyers to defend fees charged to borrowers by law firms. Maryland's state appeals court told judges that they can hire experts to scrutinize paperwork filed in foreclosure proceedings—and make lawyers swear that the documents are accurate.

Since last month, New York has threatened to use "penalties of perjury" against lawyers caught filing bad documents, even if they didn't know about the problems when the foreclosure process began.

The moves by dozens of state courts across the U.S. could add to the delays brought about by foreclosure-document crisis. Sales of foreclosed homes have slowed, and mortgage servicers face new expenses as they scramble to shore up their operations. Over the long run, borrowers are likely to pay hundreds of dollars in additional fees or slightly higher interest rates, as toughened quality control ripples through the market for new and refinanced mortgages, many experts predict.

"The cost of servicing has gone through the roof, and the legal risks are almost unknowable," said Dan Cutaia, president of capital markets at Fairway Independent Mortgage Corp. in Sun Prairie, Wis. As a consequence of rising servicing costs for lenders, "there will be higher pricing for the consumer."

The new roadblocks being imposed by judges come just as many mortgage companies claim they are starting to see the end of the foreclosure mess, which erupted six weeks

ago. J.P. Morgan Chase & Co. said in a securities filing Tuesday that it hopes to start foreclosures again "expeditiously."

J.P. Morgan said in its filing that it found "certain instances" where "underlying loan file review and verification" of documents submitted in foreclosures was handled by someone other than the employee who signed an affidavit, or that the affidavit might be improperly notarized. The basic information was "materially accurate," the company said.

Delays are costing the nation's second-largest bank in assets as much as "a couple hundred million dollars a month," said Charles Scharf, head of the New York bank's retail financial services-unit.

J.P. Morgan and Ally Financial Inc. both said they brought in outside law firms and auditors to review their foreclosure procedures. Still, just one-third of the 34 mortgage-servicing companies tracked by Fitch Inc. have finished vetting themselves, according to the credit-ratings firm.

The reviews are still in their "infancy," said Ed Delgado, a former Wells Fargo & Co. executive who leads the Five Star Institute, a provider of educational and training programs for the mortgage industry.

Pressure from state attorneys general, federal regulators, title insurers and judges is prodding the mortgage-servicing industry to do a "broad-based examination of the servicing process," not just fix the problem of robo-signing, he added, referring the practice of signing lots of documents without reviewing their contents.

Bank of America Corp. recently created a new affidavit that can be used in the 23 states where courts handle homeowners in default.

The largest U.S. bank says it is trying to streamline the foreclosure process and reduce the chances of error. It now requires that a notary and affidavit signer both be present when an affidavit is signed.

Ally, which is majority-owned by the U.S. government, now reviews pending foreclosure sales the week before a scheduled foreclosure sale and is inspecting a sample of newly filed affidavits "to ensure that no wrongful foreclosures take place," a company spokeswoman said. Last week, Ally Chief Executive Michael Carpenter said the company "screwed up on robo-signer affidavits." The company says no one was foreclosed on in error.

Tim Rood, a partner with real-estate-finance advisory firm Collingwood Group in Washington, predicts that the six-week-old foreclosure mess will result in a "quality tax" that could amount to about \$300 per loan. Borrowers typically pay about 2% of the loan amount in closing costs, according to HSH Associates in Pompton Plains, N.J.

Sales listings of bank-owned homes have shrunk as loan servicers and mortgage giants Fannie Mae and Freddie Mac pull properties off the market. In south Florida, listings of foreclosed homes are down 24% since September 27, according to data tracked by real-estate brokerage Condo Vultures LLC.

Over the long run, the foreclosure process could take a few weeks longer as a result of changes made by mortgage companies, said Clifford Rossi, a former Citigroup Inc. consumer-lending executive now teaching at the University of Maryland. The typical foreclosure already takes nearly 16 months, according to LPS Applied Analytics, a unit of Lender Processing Services Inc.

Judges are a major cog in the foreclosure machine, especially in the 23 states where foreclosure cases are required to go through the court system.

"What is at stake is the integrity of the judicial process," says Alan Wilner, a retired judge for the Maryland Court of Appeals who now is chairman of the state rules committee reviewing court procedures.

The Maryland appeals court's new policy permits judges to require lawyers to testify to the validity of the underlying affidavit in a foreclosure case. Judges also can order notaries public to appear in court or appoint special masters to review foreclosure documentation.

Ohio's Cuyahoga County Court of Common Pleas said last week it would give servicers and lenders 30 days to ensure that they have filed proper paperwork—or else their cases will be dismissed. The court, which covers Cleveland, also said judges will require lawyers in residential foreclosure cases to file affidavits swearing that they have taken "reasonable steps" to verify the accuracy of documents filed to the court.

In New York, lawyers representing lenders filing a foreclosure complaint are now required to sign a document verifying the paperwork in the case is accurate. The state has about 78,000 pending foreclosure cases, up nearly 60% from a year earlier.

"Given the serious consequences of these kinds of proceedings, it behooves the lawyer to make sure these proceedings are not frivolous or fraudulent or lacking in credibility," said Jonathan Lippman, chief judge of New York's statewide court system, in an interview.

In Florida last week, Judge Susan Gardner of the Sixth Judicial Court, a two-county region that includes St. Petersburg, ordered three lawyers to appear in her courtroom next month to defend fees contained in foreclosure affidavits. She threatened to lock them up if they don't show.

In one case, a lawyer for Florida Default Law Group in Tampa signed an affidavit that included \$1,630 in fees for a process server, according to legal documents. A review of

the file found that the fees incurred were \$175, according to an order signed by Judge Gardner.

Robert Schneider, the lawyer ordered to appear in court in that case, referred requests for comment to Ronald Wolfe, a managing partner at the firm. Mr. Wolfe couldn't be reached for comment.