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How mortgage servicers are strong-arming the victims of the Moore, Oklahoma tornado among others)

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Unnatural Disaster: How mortgage servicers are strong-arming the victims of the Moore, Oklahoma tornado among others)
On May 20, a massive EF5 tornado whipped through heavily populated Moore, Oklahoma, killing 24 and injuring nearly 400. That tragedy has now shifted into the drudgery of recovery. According to the state's Insurance Department, claims from the tornado in Moore and a subsequent twister in the city of El Reno have topped 60,000. The damage is expected to reach $2 billion.

But residents of Moore may be shocked when they receive their insurance checks in the coming weeks. Like survivors of previous natural disasters, they will encounter a major obstacle to rebuilding their homes and putting the catastrophe behind them: their mortgage servicer. Turns out the same companies that ripped off homeowners during the foreclosure crisis are, after disasters like the Moore tornado, withholding repair money, often to force homeowners to use the proceeds to pay their mortgage.
The key issue concerns the standard practice for large homeowner's insurance claims. As laid out in the fine print of mortgage and insurance contracts, the insurance company will make out the check jointly to the homeowner and the homeowner's mortgage servicer. If the homeowner has a second mortgage on the home with a different servicer, the insurer writes a three-party check. This is intended to protect the lender if the house simply cannot be rebuilt, at which point the proceeds from the insurance claim can get used to pay off the loan. But in all other cases, it means that the homeowner must secure the endorsement of the check from the servicers) before they can get the money to pay for repairs.

Only the most fastidious of homeowners know this. The rest learn the hard way—like the residents of

Bastrop, Texas. The most destructive wildfires in Texas history tore through the town in September 2011 and destroyed 1,691 homes. Most of these were total losses, and the insurance claims should have gone toward rebuilding. But a survey by the nonprofit consumer advocacy group United Policyholders found that over one-third of respondents were told by mortgage servicers that they would only release funds if the homeowner used them to pay off or pay down their mortgage, rather than make repairs. Though United Policyholders executive director Amy Bach hadn't seen such a scenario in her 21 years of advocacy, "It made me think that the problem is more common than I realized," she said. "It's not like Bastrop is the only time lenders ever overreached."

Standard mortgages typically say that insurance claims should be used to rebuild, as they are intended to return the home to an undamaged state. Federal regulators routinely put out guidelines asserting that servicers may not withhold policy claims to cover mortgage balances "without the written consent" of the homeowner. But that language offers ample wiggle room for servicers to try to obtain written consent, simply by refusing to release repair funds any other way. And homeowners often don't know any better. "When a guy in a nice suit and tie tells you that you need to pay down your mortgage, you do it," said Michael Figgins, executive director of Legal Aid Services of Oklahoma.

If the homeowner happens to be in foreclosure at the time of the disaster, the rules get even more abstract. In that case, many insurers write claim checksdirectly to the servicers. Michael Northagen of Wells Fargo Mortgageacknowledged last year that delinquent borrowers are "handled on a case-by-case basis," and in some cases, the servicer will ask for insurance payments to be applied to the loan balance. A statement from Housing and Urban Development HUD) Secretary Shaun Donovan in February didn't give much comfort. "It's critical that banks become partners in recovery and make sure that insurance payments are available to rebuild damaged properties and are not misapplied to pay off outstanding loan balances," said Donovan, which sounded more like pleading than a confident assertion of law.

Now consider the recent history of mortgage servicers. Since 2012, state and federal regulators have reached settlements in two major investigations alleging that servicers used fraudulent foreclosure practices and, in some instances, illegally repossessed homes of people not in foreclosure. A report by the HUD Inspector General looked at 36 foreclosure affidavits from JPMorgan Chase, and could not find documentation for what the borrower actually owed in 35 cases. Servicers routinely lose homeowner documents, pile illegal fees on delinquent borrowers, fail to provide loan modifications to those eligible, and have basically set a new bar for ongoing criminal conduct masquerading as customer service. They simply cannot be trusted to correctly identify homeowners in foreclosure, or how much they legitimately owe. Yet in the case of a major insurance payout, they can force desperate homeowners into signing away their claims, robbing them of due process rights to fight the foreclosure, while making profits for themselves. This is magnified when the individual in question has nowhere to live, no worldly possessions, little understanding of their own rights, and a desire only to start over.

Even if the homeowner isn't in foreclosure, obtaining insurance funds from the servicer can be a backbreaking process. When the total payout exceeds a nominal amount around $10,000), servicers usually place the money in an interest-bearing escrow account, to be distributed in installments. And homeowners run into all of the problems with servicers seen over the past few years. Homeowners talk to a different representative at the servicer every time they call, and must explain their situation all over again. Nobody at the servicer can figure out who actually owns the loan, and has authority to release the money. Paperwork gets misplaced or takes forever to get processed. Servicers usually send inspectors to obtain proof of repair work before releasing each installment, which can take more time.

The disaster survivor, saddled with limited resources and a host of other crises to manage, must navigate all this. "The homeowners we work with cannot front money to a contractor to begin repairs while they wait for the servicer," said Meghan Faux, Acting Project Director of Legal Services NYC in Brooklyn, who dealt with several case files in the aftermath of Superstorm Sandy. "Meanwhile the house is sitting with mold growing, and it leaves people with few options." Faux described the plight of one family where the servicer withheld $40,000 for five months. "The family had to borrow money from their son, who had saved it to go to college."

The situation after Sandy would have likely been worse, were it not for the aggressive response from state officials, particularly the New York Department of Financial Services. In December, DFS struck agreements with major servicers, including Bank of America and JPMorgan Chase, to expedite initial installment payments. They set up workshops for homeowners to meet face-to-face with servicers who were authorized to endorse the checks and release funds. They hounded servicers over $200 million in unreleased payments, issued new rules to stop endless disbursement delays, andshamed servicers by publicizing them in the media. "They have been very aggressive," said consumer attorney Meghan Faux.

Despite this, New York continues to see complaints from Sandy victims over mortgage servicer practices, which often stretch beyond release of insurance funds. Though servicers agreed to a moratorium on mortgage payments for displaced homeowners in the months after Sandy, some didn't follow their own guidelines and sought payment. Homeowners have reported getting pre-foreclosure notices in the mail. Some servicers demanded lump-sum payments of all deferred mortgage payments after the moratorium was lifted. Others sent notices of delinquency to consumer credit bureaus, harming credit ratings. And this is in a state with deep knowledge of financial industry practices and an uncompromising regulator. What will happen in Oklahoma, a state without the same history of regulatory persistence?

“We definitely see lenders behave differently in states, depending on the cop on the beat,” said Amy Bach of United Policyholders. “In Texas, with its move toward deregulation under Governor Rick) Perry, it made sense to see shenanigans there.”

Oklahoma regulators claim they’re ready. Julie Meaders, an attorney with the Oklahoma Insurance Department, says that they consulted with other states that experienced natural disasters, and in their early work they’ve found that “most insurance companies are willing to work with the homeowner.” But the issue of jurisdiction may present problems. The Oklahoma Insurance Department only oversees insurance companies, not mortgage servicers. That falls to the attorney general, and groups like Michael Figgins’ Legal Aid Services of Oklahoma, who only have so much reach. “If servicers try this with 10 people and we catch five of them,” said Figgins, “they’re still getting a payday.”

Meaders, from the state Insurance Department, is well aware of the potential pitfalls. “We had a volunteer group in from Texas, I think from the wildfires down there a couple years ago,” she said. “And they were telling homeowners, ‘Don’t let the mortgage company tell you to pay your mortgage off with the insurance money.’”