

Testimony of

Debra Miller

May 6, 2008

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OF
Debra Miller

CHAPTER 13 STANDING TRUSTEE
FOR THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF INDIANA, FORT WAYNE AND SOUTH BEND
DIVISIONS

BEFORE

THE SENATE JUDICIARY SUBCOMMITTEE ON ADMINISTRATIVE OVERSIGHT

"Policing Lenders and Protecting Homeowners: Is Misconduct in Bankruptcy Fueling the Foreclosure Crisis?"

May 6, 2008

Mr. Chairman and Members of the Subcommittee:

I am Debra Miller. I serve as the Chapter 13 trustee in the Northern District of Indiana. In my capacity as a Chapter 13 trustee, I have joined with my colleagues as we work with hundreds of families as they struggle to keep their houses in the face of foreclosure. We work with mortgage companies as they seek to recover the funds to which they are legally entitled.

I also serve as the Chair of the National Association of Chapter Thirteen Trustees (NACTT) Mortgage Liaison Committee, a special working group, established by the NACTT, to work with all participants in the mortgage process to develop ways to improve Chapter 13 procedures and perhaps help borrowers keep homes and mortgagors receive payment. Thank you for the opportunity to appear here today to inform you of the activities of the NACTT mortgage liaison committee.

Chapter 13 trustees have a unique role in the world of bankruptcy. Trustees are appointed by the Department of Justice to administer the Chapter 13 bankruptcies in their district. There are approximately 210 trustees throughout the country. In the 2007 fiscal year, the Chapter 13 trustees across the country distributed over \$5.1 billion dollars to creditors. More than half of us paid post-petition mortgage payments through our offices.

Generally, Chapter 13 debtors are behind in their mortgage payments prior to filing. In many cases, a Chapter 13 bankruptcy is filed as a last resort to save the family home from foreclosure. Chapter 13 allows those debtors to reorganize their finances, cure the arrearages owing on their mortgages while they maintain ongoing monthly mortgage payments. The goal is that at the end of the Chapter 13 case, the borrower's mortgage is current and there remain no outstanding fees, costs or other issues that would stop the debtor from receiving their fresh start.

Chapter 13 trustees and their staff review the documents and legal pleadings filed by debtors, creditors and other parties in interest. Chapter 13 trustees often act as mediators and arbiters to ensure that all parties comply with the Bankruptcy Code and Rules. In other words, our job is to make sure that everyone plays fairly and by the rules.

In this role, we observe systemic problems in the mortgage servicing industry. While the bankruptcy is pending, we see mortgage servicers file Motions for Relief from Stay alleging the debtor is delinquent on their payments. Even though records indicate that the payments to the mortgage creditor are current. Trustees try to obtain information from servicers or the servicer's counsel, only to receive confusing, incomprehensible and incorrect records, if records are furnished at all. Debtors call our offices noticeably upset when they receive a notice from their mortgage servicer, years after successfully completing a repayment plan, showing they owe more money on their mortgage than when they filed the bankruptcy. Debtors tell us of demand letters for thousands of dollars and accuse us, their attorneys and the bankruptcy system for denying them the fresh start the Bankruptcy Code promises.

There are many causes for these issues:

?? Trustees have not been advised of mortgage payment changes or advised about changes until years after the payment changed. At the end of the bankruptcy - perhaps months after the debtors receive a discharge - the mortgage account may be reviewed by the servicer and only then a demand made directly to the debtor for an accumulated shortfall.

?? Proofs of claim filed in bankruptcy are often incorrect, failing to show who actually owns a loan and/or may include exorbitant fees, costs and charges, which inflated the amount due to the mortgage servicer. Such fees, costs and attorney fees claimed due and owing are often not itemized, revealing only some amount as a "corporate advance." In one case, while clearly an error, the servicer filed a proof of claim for \$63,665.83 and included \$151,987.75 in "inspection fees", \$38,483.63 in Foreclosure Fees and \$38,020.00 in broker price opinions and over \$13,449.00 in interest. The error was compounded, however, when the debtor's attorney and trustee's office were unable to communicate with the servicer or its attorney. The servicer failed to correct its clearly erroneous proof of claim even after objection was raised. The court, frustrated with the inability to resolve the issue and the repeated failure of the attorney and servicer to appear in court when ordered, directed the U.S. Marshals to bring the attorney from across the country so he could explain his actions to the court.

?? Some servicers fail to abide by the requirements of the Real Estate Settlement Procedures Act (RESPA) by failing to analyze a loan to determine whether the required monthly payments could satisfy principal, interest, insurance and taxes. At the conclusion of the bankruptcy, the mortgage account is analyzed and only then a demand made for any shortfall. For example, there is now litigation pending where the debtor made every payment timely to my office, I made every payment timely to the servicer including paying off the amount the borrower was behind on the mortgage at confirmation, only to be advised that the borrower owed an additional \$4,000 which should be paid in order to be current prior to discharge. The servicer, when asked for copies of the escrow analysis conducted during the life of the bankruptcy, advised me, on the Office of the President letterhead, that it did not conduct any analysis on any loan while a borrower was in bankruptcy. This has resulted in every Chapter 13 debtor whose loan was serviced by this nationwide servicer immediately receiving a demand for these sums upon the discharge of their cases.

?? Trustees are unable to locate, therefore communicate with, servicers during the pendency of a bankruptcy. Servicers often do not supply phone numbers on claims or to the trustees. Trustees and/or debtors call the main customer service numbers, only to wait for hours in a surreal telephone queue, then are told that the person answering the call can't or won't help. I can't tell you how many times I have held, been transferred from extension to extension, only to be frustrated when no one can or will tell me the status of a loan or even what the monthly payment should be.

?? Payments are not properly credited to the debtor's mortgage. Trustee checks are often returned without explanation or are cashed, but funds are never applied to the debtor's mortgage. This generally results in the filing of a Motion for Relief from Stay alleging that the debtor is behind on the mortgage when the Debtor is actually current.

?? Late fees, inspection fees or other "contractual costs" are added to the mortgage during the life of the bankruptcy without notice to the debtor, the debtor's attorney or the trustee. While some fees and costs are legitimate, some appear to have no basis in the contract or under applicable law. The end result is that, without providing notice of asserted charges, debtors and trustees are incapable of challenging whether the charges are reasonable or appropriate and are unaware that they are even due.

?? If a servicer does analyze the mortgage loan during the bankruptcy, it often "double dips." For example, a servicer files a proof of claim for a \$600 prepetition charge, asking the court to require the trustee to pay that sum during the bankruptcy. Then, the servicer increases the ongoing monthly mortgage amount by \$50 a month to also recover that cost. The servicer receives the \$600 twice ?? once from the trustee through the bankruptcy plan as a separate claim and once in the increased monthly mortgage payment.

Courts are required to have hearings on Motions for Relief from Stay when mortgage servicers assert that Debtors are delinquent in their payments, even though a Trustee can demonstrate that payments are actually current. Trustees attend the hearings with records showing that all the required payments have been made and can provide cancelled checks as proof. Unfortunately, debtors who pay their own ongoing mortgage payments rarely have cancelled checks and it is difficult to prove that all the required payments have been made.

Trustees have discovered that servicers often claim additional funds are due and owing at the end of a case because of attorney fees, costs or advances made by the servicer during the life of the bankruptcy.

These fees or costs are generally not disclosed to the Debtors when incurred and often place the debtor in a worse position and further behind on mortgage payments than when the case was filed. In an effort to combat this abuse, trustees have been taking actions to bring the status of the mortgage before the court prior to the end of the case.

After debtors obtain a discharge, they often get a bill from their servicer for amounts that have not been paid during the bankruptcy case. Sometimes they choose to walk away from a house, angry that they "wasted their time" by using bankruptcy to save their home. They blame the system, their attorney, the trustee, the court, and their faith in the legal system is destroyed.

Trustees, courts, and debtor's attorneys are understandably frustrated. It appears that some servicers flaunt the bankruptcy law and the court's jurisdiction over them.

Approximately six years ago, Henry E. Hildebrand, III, the Chapter 13 Trustee for Middle District of Tennessee, published an article entitled the "Sad State of Mortgage Servicing." This article outlined the issues and problems with the industry. It brought to a head the festering issue, infuriated some mortgage servicers, and led to some attorneys for servicers and a group of trustees to meet to "discuss" the article.

That discussion was the beginning of the NACTT Mortgage Liaison Committee.

Our committee began as a cooperative effort between trustees and attorneys for servicers to discuss procedural and administrative issues that arise for both parties when borrowers become debtors in Chapter 13 bankruptcy. Lines of communication began to open, employees of servicers were added to the committee and all parties learned that both were willing to work toward solutions.

Telephone conference calls and face-to-face meetings were held. Frank discussions explained what the servicers and trustee accounting systems could and could not do. Trustees relayed their frustration of the lack of communication. Servicers relayed their frustration with a federal bankruptcy system that was administered differently in each court.

As time has passed, more trustees and servicers participated, and the group grew large enough that it was split into subcommittees. The committee's mission was to foster communication between the parties, resolve differences and to recommend best practices of conduct for all stakeholders. Our collective goal is to improve the bankruptcy system.

In May 2007, we met for a face-to-face meeting in Columbus, Ohio. Over a two-day period, the committee members discussed what should be a "best practice" in various situations. We attempted to come up with practical solutions for issues facing the servicer of mortgage loans while the borrower is in a Chapter 13 bankruptcy. Our collective efforts were put in writing.

What are Best Practices? Best Practices are management ideas which assert that there are techniques, methods and processes that are more effective at delivering a particular outcome. The idea is that with proper processes, a desired outcome can be delivered with fewer problems and unforeseen complications. Best Practices are not the only way to achieve a desired goal ?? there may be other procedures that deliver the same outcome - however they are an acceptable and efficient way of accomplishing a task, based on repeatable procedures that have proven themselves over time.

Some of the Best Practices suggest a procedure that was not used in many jurisdictions - such as the servicer filing a notice with court when a mortgage payment changed or a fee or cost was assessed. Some Best Practices simply restated what the committee believed the law required ?? such as analyzing the loan each year for negative escrow issues.

After the Best Practices were initially drafted, the committee approached the judiciary and the attorneys for the debtors. We wanted to have a set of Best Practices in place that would be accepted by all parties. A few judges participated in the committee's phone conferences. The Best Practices were distributed and comments made. Some Best Practices were found to be not acceptable or so contrary to current case law as to not be feasible. Additional issues were raised and were placed on the agenda for the next set of best practice discussions. The Best Practices were distributed to debtor's attorneys' groups for comments. Again, some Best Practices were found not to be acceptable and were dropped or revised.

In the fall of 2007, committee members met in another face-to-face discussion with various members of the judiciary and debtor's counsel to attempt to finalize the Best Practices.

The Best Practices have now been presented at meetings of the National Conference of Bankruptcy Judges (NCBJ), the Mortgage Bankers Association (MBA), American Financial Network (AFN) and United States Financial Network (USFN).

So what are the current approved Best Practices?

Proofs of Claim

? When servicers/mortgagees include a flat fee cost in the proof of claim for review of the Chapter 13 plan prior to confirmation and for the preparation of the proof of claim, the fee should be reasonable and fairly reflect the attorney (outside counsel) fees incurred.

? Servicers/mortgagees should not include any prepetition costs or fees or prepetition negative escrow in any post petition escrow analysis. Such amounts should be included in the prepetition claim unless the payment of such fee or cost was actually made by the servicer after the date of the filing of the bankruptcy.

? Servicers/mortgagees should state mortgage arrearage up to the date of the filing of the bankruptcy petition, unless the plan or trustee indicates otherwise, or local rule provides otherwise. The Chapter 13 Trustee will use the mortgage arrearage claim to set up the arrearage balance on the claim, which in turn will show up as the "balance" on the voucher check, absent objection to the claim.

? Servicers/mortgagees should clearly identify if the loan is an escrowed or escrowed loan and break out the monthly payment consisting of Principal, Interest, Escrow and PMI components.

? Servicers/mortgagees should identify nontraditional mortgage loans in their proof of claims. Loans with options should identify on the proof of claim the type of loan as well as the various contractual payment options available during the bankruptcy to the borrower/Debtor.

Payment Application

? Pre petition payments should be tracked as applied to pre petition arrears, post-petition payments should be tracked as applied to post petition ongoing mortgage payments

? Prior to the filing of a Motion for Relief from Stay in a Trustee pay jurisdiction, the trustee website or the National Data Center website should be reviewed.

Post Petition Costs and Claims

? Servicers/mortgagees should file a notice and reason of any payment change with the court and provide same to the Debtor.

? Servicers are required to file a notice of any protective advances made in reference to a mortgage claim, such as non escrow insurance premiums or taxes. Such notice should be provided to the debtors and filed with the court.

? If Servicers/mortgagees include attorney fees for pursuing relief from stay, such fees should be clearly identified as well as how such fees are to be paid in any agreed order resolving a Motion for Relief from Stay or any other matter before the court.

? Servicers/mortgagees should analyze loans for escrow changes upon the filing of a bankruptcy case and each year thereafter. A copy of the escrow analysis should be provided to the debtor and filed with the Bankruptcy Court by the servicers/mortgagee or their representative each year.

? Servicers/mortgagees should attach a statement to a formal notice of payment change outlining all post petition contractual costs and fees not previously approved by the court and due and assessed since the prior escrow analysis or date of filing whichever is later. This statement need not contain fees, costs, charges and expenses that are awarded or approved by the Bankruptcy Court order. In absence of any objection or challenge to such fees, the trustee should take appropriate steps to cause such fees to be paid as part of Debtor's Chapter 13 plan.

? Mortgage servicers should monitor post petition payments. If the mortgage is paid post petition current then the servicers/mortgagees should not seek to recover late fees. No late fees should be recovered or demanded for systemic delay but should be limited to actual debtor default.

Communication

? Servicers/mortgagees should supply and maintain a contact for debtor's counsel and trustee's for the purpose of restructuring, modifying a mortgage, or other loss mitigation assistance including a short sale or deed in lieu of foreclosure. The contact should be an individual or group with the ability to implement or assess with objective criteria a loss mitigation modification after filing of a chapter 13 petition with the goal of keeping the Debtor in the house and the success of the bankruptcy.

? Mortgage servicers should provide a dedicated phone line and contact for Chapter 13 Trustee inquiry use only.

? Trustees should initiate a communication with mortgage servicers when questions arise in a review of a post petition escrow analysis.

Education

? United States Trustees and the Trustee Education Network should modify the requirements of the financial management class regarding adjustable rate mortgages, the calculation of mortgage escrows and, in particular, the potential of increased mortgage payments resulting from increased taxes, interest rate hikes and/or mortgage premiums.

The next step - Implementation.

Courts, local counsel and trustees throughout the country as they struggle with mortgage issues are using the Best Practices as a starting point for drafting local rules and plan provisions. Servicers on the committee are reviewing their procedures, asking for the funds in their budgets to implement the Best Practices.

Servicers are reaching out to other servicers not on the committee to inform and discuss the Best Practices.

Trustees are conducting seminars for creditor and debtor attorneys, small local banks and mortgage servicers to discuss the Best Practices.

Trustees, servicers and their counsel are conducting informational webinars to inform general counsel and management of mortgage servicers of the Best Practices.

Courts are using the Best Practices as a tool to reform servicers' conduct in litigation arising from issues and possible misconduct.

Legislative and Administrative Assistance

We are also running into some unexpected roadblocks in implementing the proposed Best Practices, and we hope for your assistance.

We believe that notices of payment changes, assessment of fees and costs should be made with the bankruptcy court. This proposal is encountering resistance by some courts who refuse to accept these filings. We are trying to address this issue through the Bankruptcy Clerks' Committee and the Administrative Office of the United States Courts but it appears that a change to the Bankruptcy Rules may be required to allow this to be implemented nationwide.

Our Best Practices would encourage the analysis of each mortgage loan, but this may appear inconsistent with the murky language in the RESPA guidelines governing escrow analysis. We encourage clarification.

Our Best Practices related to the annual escrow statements should be a requirement under RESPA as some courts have found that simply providing these important notices to debtors in bankruptcy violates the automatic stay.

The GSE's Fannie and Freddie should be required to ensure that their servicers follow the Best Practices or have a procedure in place that accomplishes the same result.

We are pleased to work with this committee to further the implementation of our recommended Best Practices and to work with you to draft language to help in the implementation of these nationwide.

In closing, I wish to thank the Subcommittee again for the opportunity to provide information regarding the NACTT mortgage liaison's committee's Best Practices and our committee's attempt to begin to resolve the ongoing issues of problems with mortgage servicing in a Chapter 13.

Mr. Chairman, I would be pleased to answer any questions that you or members of the Subcommittee may have.