



OFFICE OF INSPECTOR GENERAL

Evaluation Report

2014-SR-B-015

Opportunities Exist to Enhance the Board's Oversight of Future Complex Enforcement Actions

September 30, 2014

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
CONSUMER FINANCIAL PROTECTION BUREAU

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Abbreviations

Board	Board of Governors of the Federal Reserve System
BS&R	Division of Banking Supervision and Regulation
DCCA	Division of Consumer and Community Affairs
IFR	Independent Foreclosure Review
OCC	Office of the Comptroller of the Currency
OIG	Office of Inspector General
OTS	Office of Thrift Supervision
PACER	Public Access to Court Electronic Records
QSF	Qualified Settlement Fund
Quad/Graphics	Quad/Graphics, Inc.
Rust	Rust Consulting, Inc.
SCRA	Servicemembers Civil Relief Act
SOWs	statements of work
<i>Supervisory Expectations</i>	<i>Complex Servicers Mortgage Foreclosure Supervisory Expectations</i>



Executive Summary:

Opportunities Exist to Enhance the Board's Oversight of Future Complex Enforcement Actions

2014-SR-B-015

September 30, 2014

Purpose

The Board of Governors of the Federal Reserve System (Board) and the Office of the Comptroller of the Currency (OCC) negotiated a payment agreement with mortgage servicers to amend requirements in consent orders that address deficient mortgage loan servicing and foreclosure processing practices. Our objectives for this evaluation were to (1) evaluate the Board's overall approach to oversight of the amended consent orders, (2) determine the effectiveness of the Board's oversight of the slotting process, and (3) determine the effectiveness of the Board's oversight of the servicers' paying agent, Rust Consulting, Inc.

Background

The payment agreement replaced some requirements in consent orders that the Board, the OCC, and other agencies issued in 2011 and 2012, which established the Independent Foreclosure Review—a prior effort to identify and remediate actual harm to borrowers. In January 2013, the Board, the OCC, and 13 mortgage servicers agreed to the payment agreement. In February 2013, the Board and OCC issued amended consent orders that required the servicers to provide about \$3.67 billion in payments to nearly 4.2 million borrowers based on possible harm and to provide other foreclosure prevention assistance.

Findings

The Board's advance preparation and planning efforts for the payment agreement with the 13 servicers that joined the agreement in January 2013 were not commensurate with the complexity associated with this unprecedented interagency effort to remedy possible harm at an individual borrower level for nearly 4.2 million borrowers. This enforcement approach involved multiple mortgage servicers supervised by the Board and the OCC. Further, three Reserve Banks had responsibility for monitoring five servicers' implementation efforts.

In addition, project management resources were not available to the Board's oversight team for this initiative to assist in guiding and supporting this large, complex initiative. We believe that complex initiatives could be better supported with a staffing plan that includes project management resources. Such an approach would allow a project management office to guide an initiative from planning through execution with support and direction from senior Board officials and may limit the need for official staff to engage in daily oversight activities during the execution phase.

The payment agreement required servicers to slot borrowers into categories of possible harm—with payment amounts set for each category—that were defined by Board and OCC staff. While we did not seek to validate the results of the slotting exercise at an individual-borrower level, we found that data integrity issues at two mortgage servicers impacted the reliability and consistency of the slotting results. These issues may have resulted in borrowers who experienced similar harm receiving different payment amounts. We also determined that the Board has not selected its approach to end the payment agreement.

Despite these challenges and limitations, as of August 15, 2014, borrowers of the 13 servicers that joined the payment agreement in January 2013 had cashed or deposited checks representing about \$3.15 billion, or approximately 86 percent, of the total \$3.67 billion.

Recommendations

We made five recommendations to improve the Board's oversight of future complex enforcement strategies. In its response to a draft of our report, the Board generally agreed with our recommendations and noted the corrective actions that it has implemented or intends to implement.

Access the full report: <http://oig.federalreserve.gov/reports/board-future-complex-enforcement-actions-oversight-sep2014.htm>

For more information, contact the OIG at 202-973-5000 or visit <http://oig.federalreserve.gov>.

Summary of Recommendations, OIG Report No. 2014-SR-B-015

Rec. no.	Report page no.	Recommendation	Responsible offices
1	14	<p>Develop a framework to guide planning, vetting, and approving activities for large, complex enforcement strategies that may involve multiple institutions, multiple Board divisions, or multiple Reserve Banks. This framework could include planning and risk assessment activities such as</p> <ol style="list-style-type: none"> identifying key risks and possible risk-mitigating activities. assessing the feasibility of the intended corrective action. vetting possible alternatives. identifying documentation standards for the relevant initiative. defining performance measures as indicators of success and creating key interim milestones to monitor progress. assessing whether service-level agreements could be used to incentivize vendor performance consistent with expectations. identifying key assumptions. assessing whether the Board has the necessary skill sets and the resources available to oversee the intended corrective action. defining roles and responsibilities among the Board team overseeing the corrective action. 	Division of Banking Supervision and Regulation, Division of Consumer and Community Affairs, and Legal Division
2	17	Identify the circumstances in which project management resources should be used and develop a staffing plan to include project management resources with appropriate subject-matter expertise for those situations.	Division of Banking Supervision and Regulation, Division of Consumer and Community Affairs, and Legal Division
3	23	Assess the potential impact of data reliability issues as part of the complex enforcement strategies framework described in recommendation 1. Specifically, consider how data availability or reliability issues may impact the feasibility of the exercise or the consistency of its results. As part of this analysis, consider whether alternative enforcement strategies can be adopted that mitigate or eliminate these challenges. As appropriate, these strategies should be developed, vetted, and approved as part of the planning process.	Division of Banking Supervision and Regulation, Division of Consumer and Community Affairs, and Legal Division
4	25	Finalize an approach to end the payment agreement, including developing, in coordination with the Office of the Comptroller of the Currency, a strategy to appropriately allocate any funds remaining in the Qualified Settlement Funds that have not been cashed or deposited by borrowers, and continuing efforts to locate uncompensated borrowers.	Division of Banking Supervision and Regulation, Division of Consumer and Community Affairs, and Legal Division
5	25	As part of future agreements involving payments to harmed consumers, identify potential options for distributing any residual amounts as part of the planning process.	Division of Banking Supervision and Regulation, Division of Consumer and Community Affairs, and Legal Division



OFFICE OF INSPECTOR GENERAL
BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
CONSUMER FINANCIAL PROTECTION BUREAU

September 30, 2014

MEMORANDUM

TO: Distribution List

FROM: Melissa Heist *Melissa Heist*
Associate Inspector General for Audits and Evaluations

SUBJECT: OIG Report No. 2014-SR-B-015: *Opportunities Exist to Enhance the Board's Oversight of Future Complex Enforcement Actions*

The Office of Inspector General (OIG) has completed its final report on the subject evaluation. We conducted this evaluation to (1) evaluate the Board of Governors of the Federal Reserve System's (Board) overall approach to oversight of the amended consent orders, (2) determine the effectiveness of the Board's oversight of the slotting process, and (3) determine the effectiveness of the Board's oversight of the paying agent, Rust Consulting, Inc.

Our report contains five recommendations to enhance the Board's oversight of future complex enforcement actions. In your response, you stated that you generally agreed with our recommendations and that you will leverage information learned throughout the IFR process and the implementation of the payment agreement for similar complex enforcement actions in the future. We have included your response as appendix C in our report.

We appreciate the cooperation that we received from the Board's Division of Banking Supervision and Regulation, the Division of Consumer and Community Affairs, and the Legal Division. Please contact me if you would like to discuss this report or any related issues.

cc: Tonda Price
Jack Jennings
Suzanne Killian
Richard Ashton
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Introduction

Objectives

The Office of Inspector General (OIG) conducted an evaluation of the Board of Governors of the Federal Reserve System's (Board) oversight of the Independent Foreclosure Review (IFR) payment agreement.¹ In January 2013, the Board and the Office of the Comptroller of the Currency (OCC)² agreed to the payment agreement with certain mortgage servicers to provide approximately \$3.67 billion in payments to approximately 4.2 million borrowers based on possible harm.³ The payment agreement replaced requirements in consent orders that the Board, the OCC, and the Office of Thrift Supervision (OTS) issued in 2011 and 2012 to address deficient mortgage loan servicing and foreclosure processing practices.⁴ Those consent orders had established the Independent Foreclosure Review (IFR)—a prior effort to identify and remediate actual harm to borrowers.

In February 2013, the Board and the OCC issued amended consent orders. Under the amended orders, servicers slotted borrowers into various categories of possible harm established by Board and OCC staff. After the servicers subject to the amended orders placed borrowers in the various categories, the Board and the OCC published payment amounts for each category ranging from \$300 to \$125,000. The servicers selected Rust Consulting, Inc. (Rust) as the paying agent to administer the payment agreement and distribute checks to borrowers, and the Board and the OCC did not object to this selection. Our objectives for this evaluation were to (1) evaluate the Board's overall approach to oversight of the amended consent orders issued in February 2013, (2) determine the effectiveness of the Board's oversight of the slotting process, and (3) determine the effectiveness of the Board's oversight of the servicers' paying agent, Rust. For additional information regarding our scope and methodology, see appendix A.

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1. The Board is responsible for supervising and regulating a variety of financial institutions, such as bank holding companies, including financial holding companies formed under the Gramm-Leach-Bliley Act; foreign banks with U.S. operations; and state-chartered banks that are members of the Federal Reserve System. The Federal Reserve System consists of the Board of Governors of the Federal Reserve System and 12 regional Federal Reserve Banks. Subject to the Board's oversight and direction, the responsible Federal Reserve Banks conduct ongoing supervision of these financial institutions.
 2. The OCC's primary mission is to charter, regulate, and supervise all national banks and federal savings associations.
 3. The Board's amended consent orders associated with the payment agreement are available at <http://www.federalreserve.gov/newsevents/press/enforcement/20130228a.htm>.
 4. In April 2011, the Board, the OCC, and OTS issued 24 consent orders against 16 financial institutions engaged in residential mortgage servicing activities. The Federal Deposit Insurance Corporation was also an issuing agency for one of the April 2011 consent orders. Additionally, in September 2011 and April 2012, the Board issued 2 more consent orders. Together, these 26 orders established the IFR. Board enforcement actions issued in 2011 are available at <http://www.federalreserve.gov/newsevents/press/enforcement/2011enforcement.htm>.

Background

In 2010, reports of widespread irregularities and potential violations of law in the documentation and processing of foreclosures prompted some mortgage servicers to temporarily suspend certain foreclosures in process. Congress held hearings to examine these issues. During the fourth quarter of 2010, the Federal Reserve System, the OCC, OTS, and the Federal Deposit Insurance Corporation initiated a horizontal review to assess the potential impact of the foreclosure processing issues of certain mortgage servicers.

Horizontal Review of Mortgage Servicer Foreclosure Practices Resulted in Enforcement Actions

The interagency horizontal review sought to evaluate the adequacy of controls and governance over servicers' foreclosure processes and to assess servicers' authority to foreclose. The Board assembled a team from its Division of Banking Supervision and Regulation (BS&R), Division of Consumer and Community Affairs (DCCA), and Legal Division to oversee the horizontal review, with the assistance of staff from certain Reserve Banks.

In April 2011, the Federal Reserve System, the OCC, and OTS published a report describing the results of the horizontal review.⁵ The report outlined deficiencies and weaknesses in foreclosure processing, including inadequate monitoring and control of foreclosure activities and weak quality control and internal audit procedures. The report also identified that individuals employed by the servicers signed foreclosure-related affidavits filed in state courts, but they often did not personally check the documents for accuracy or possess the level of knowledge of the information they attested to in those affidavits.

On April 13, 2011, the Board, the OCC, and OTS issued consent orders to the following 14 mortgage servicers and their subsidiaries to address the issues identified during the horizontal review:

1. Ally Financial, Inc.; Ally Bank; Residential Capital, LLC; and GMAC Mortgage, LLC (hereafter, GMAC)
2. Aurora Bank FSB (hereafter, Aurora)
3. Bank of America Corporation and Bank of America (hereafter, Bank of America)
4. Citigroup Inc.; Citibank; CitiMortgage, Inc.; and CitiFinancial Credit Co. (hereafter, Citibank)
5. EverBank Financial Corp. and EverBank (hereafter, EverBank)
6. HSBC North America Holdings, Inc.; HSBC Bank USA; and HSBC Finance Corporation (hereafter, HSBC)
7. IMB HoldCo LLC and OneWest Bank, FSB (hereafter, OneWest)
8. JPMorgan Chase & Co., JPMorgan Chase Bank, and EMC Mortgage (hereafter, JPMorgan Chase)
9. MetLife, Inc., and MetLife Bank (hereafter, MetLife Bank)

5. Federal Reserve System, Office of the Comptroller of the Currency, and Office of Thrift Supervision, *Interagency Review of Foreclosure Policies and Practices*, April 2011, http://www.federalreserve.gov/boarddocs/rptcongress/interagency_review_foreclosures_20110413.pdf.

10. PNC Financial Services Group, Inc.; PNC Bank; and PNC Mortgage (hereafter, PNC)
11. Sovereign Bank (hereafter, Sovereign)⁶
12. SunTrust Banks, Inc.; SunTrust Bank; and SunTrust Mortgage, Inc. (hereafter, SunTrust)
13. U.S. Bancorp, U.S. Bank, U.S. Bank Home Mortgage, and U.S. Bank Consumer Finance (hereafter, U.S. Bank)
14. Wells Fargo & Company and Wells Fargo Bank (hereafter, Wells Fargo)

Of these 14 servicers, 4 had mortgage servicing subsidiaries supervised by specific Reserve Banks under delegated authority from the Board—GMAC, HSBC, SunTrust, and JPMorgan Chase.⁷ Additionally, in September 2011 and April 2012, the Board issued similar consent orders to Goldman Sachs and Morgan Stanley.⁸ Issuing these enforcement actions raised the total number of mortgage servicers subject to foreclosure consent orders to 16. These consent orders included provisions that required servicers to retain independent consultants to review foreclosure activity to identify whether mortgage borrowers with loans serviced by the respective institutions whose home was in the foreclosure process during 2009 or 2010 suffered financial injury due to servicer errors or deficiencies. The term *IFR* refers to the file review process combined with an outreach process designed to make borrowers aware of the opportunity for a file review. Board staff worked with dedicated teams from the Reserve Banks of Atlanta, Chicago, and New York to monitor compliance with the consent orders for servicers supervised by the Board.

Independent Foreclosure Review

The consent orders that established the IFR alleged that the servicers used unsafe and unsound practices to process mortgage foreclosures. Specifically, the orders alleged that servicers (1) filed or caused to be filed in state courts affidavits asserting that the affiant had personal knowledge of the facts contained, when in many cases he or she did not; (2) failed to sufficiently respond in a timely manner to the increase in foreclosures by increasing staffing and managerial resources; and (3) failed to have adequate internal controls, policies and procedures, compliance risk management, and training.

To address these issues, the consent orders required the servicers subject to the orders to make extensive changes in servicing and foreclosure processes. In addition, the orders required servicers to retain independent consultants to conduct a comprehensive foreclosure file review of each servicer's foreclosure activity in 2009 and 2010 to identify financial harm to individual borrowers that resulted from deficient foreclosure practices and to provide compensation or other remedy for that harm.

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6. Sovereign was acquired by the Santander Group in 2009 and changed its name to Santander in 2013.
 7. HSBC and JPMorgan Chase had residential mortgage operations that were supervised by the Board in addition to separate residential mortgage operations that were supervised by the OCC. The Board and the OCC issued separate consent orders and consent orders amendments for the relevant institutions.
 8. The mortgage servicing subsidiary of The Goldman Sachs Group, Inc., and Goldman Sachs Bank USA was Litton Loan Servicing LP (hereafter, Goldman Sachs). The mortgage servicing subsidiary of Morgan Stanley was Saxon Mortgage Services, Inc. (hereafter, Morgan Stanley).

One official explained that as a result of the horizontal review, Board officials knew that some borrowers may have been harmed, but they did not know the extent of the harm. The IFR process allowed borrowers who felt they were harmed by these servicing practices to submit a request for review. In response, the independent consultants would review the borrower's mortgage file to determine whether any harm occurred and to assess the extent of the potential injuries. In addition, the IFR consent orders required the independent consultants to perform look-back reviews to identify harmed borrowers who may not have submitted a request for review.

The IFR covered more than 4.4 million borrowers who had a mortgage on their primary residence in any stage of the foreclosure process in 2009 or 2010 that was serviced by one of the 16 financial institutions subject to the consent orders.⁹ The six mortgage servicing subsidiaries supervised by Reserve Banks serviced approximately 16 percent of the 4.4 million mortgage loans.

In June 2012, the Board and the OCC published a financial remediation framework to guide remediation for the IFR.¹⁰ The framework listed various categories of harm and suggested remedies, such as suspending foreclosures in process, correcting credit reports, and paying borrowers for the financial injury. Lump sum payments suggested in the IFR financial remediation framework ranged from \$500 to more than \$125,000.

Under the IFR, the Board and the OCC attempted to implement the corrective action and remediate harm at an individual-borrower level through a file review process for more than 4.4 million borrowers across multiple financial institutions. Board staff characterized the IFR as a "highly unusual undertaking," unlike anything the Board had previously undertaken, as enforcement actions typically address weaknesses and deficiencies in a financial institution's internal controls and risk management practices. Further, oversight of the IFR involved a shift from the Board's standard practice for overseeing a consent order. Board staff explained that typically, day-to-day oversight of compliance with consent orders is delegated to the Reserve Bank responsible for supervising the relevant institution. For the IFR, however, Board staff provided ongoing guidance to the oversight process, with staff at the three Reserve Banks interacting with the relevant servicers and their independent consultants on a regular basis.

As the supervisory process progressed from the interagency horizontal review to the IFR, the Board preserved the continuity of the team overseeing the project. The project team that supervised the horizontal review became responsible for overseeing the IFR and the work performed by the independent consultants.

By November 2012, the IFR had been ongoing for about 18 months, but no money had been provided to any of the borrowers. As of December 2012, the independent consultants for the IFR file reviews had billed about \$1.8 billion to the respective servicers.

9. "Any stage of the foreclosure process" included all foreclosure processing beginning with the borrower's mortgage loan being referred to the servicers' foreclosure department, which is sometimes referred to as initiating foreclosure, up to and including a foreclosure sale or the servicer rescinding the foreclosure. Servicers have different practices, but typically, mortgage servicers refer mortgages to their foreclosure departments after the borrower is more than 90 days in default.

10. Office of the Comptroller of the Currency and Board of Governors of the Federal Reserve System, *Financial Remediation Framework for Use in the Independent Foreclosure Review*, June 21, 2012, <http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20120621b2.pdf>.

The IFR process received intense scrutiny from Congress and the U.S. Government Accountability Office (GAO). For example, one congressional hearing questioned the independence of the consultants hired to conduct the IFR. Additionally, members of Congress questioned the transparency surrounding the effort and sent various letters to the Board seeking additional information concerning the IFR. During our interviews, Board officials responsible for supervising the IFR explained that reviewing mortgage files was complex because of all the variables involved. A GAO report indicated that according to independent consultants, a mortgage file could comprise as many as 50 separate documents and consist of 2,000 pages or more to be reviewed.¹¹

Payment Agreement

In light of the delays associated with the IFR, Board and OCC staff began negotiating an agreement to end the IFR with the servicers subject to the IFR in late 2012. The agencies transitioned to the payment agreement to provide remediation to borrowers in a timelier manner than would have occurred under the IFR process. According to a GAO report, an OCC official estimated that the file reviews may have taken an additional two years to complete. Based on OCC data, the Board estimated that the servicers may have had to pay the independent consultants an additional \$2.0 billion to complete the file reviews. In our opinion, the IFR's lack of success in distributing remediation to borrowers resulted in a heightened sense of urgency to provide remediation to borrowers under the payment agreement.

Beginning on January 7, 2013, the Board and the OCC signed the payment agreement term sheets with 13 of the servicers.¹² The term sheets replaced the IFR mortgage file review requirements with an agreement to provide approximately \$3.67 billion in cash payments to borrowers.¹³ The deadlines contained in the term sheets between the Board and the OCC and the relevant servicers evidenced this urgency to act quickly. Under the terms of the payment agreement, the Board provided a 30-day deadline for the servicers to complete their validations and an additional 15 days for the Reserve Bank dedicated team reviews to be completed—that is, by February 21, 2013, for servicers that signed payment agreement term sheets in January 2013.

As the Board transitioned from the IFR to the payment agreement, the same Board staff who managed the interagency horizontal review and the IFR process became responsible for managing the payment agreement, including overseeing the remaining IFR consent order requirements, the check issuance process, and the paying agent. Board officials preserved the continuity of the oversight team due to the steep learning curve associated with this unique project. According to

11. U.S. Government Accountability Office, *Foreclosure Review: Lessons Learned Could Enhance Continuing Reviews and Activities Under Amended Consent Orders*, GAO-13-277, March 2013.

12. The 13 servicers were (1) Aurora, (2) Bank of America, (3) Citibank, (4) Goldman Sachs, (5) HSBC, (6) JPMorgan Chase, (7) MetLife Bank, (8) Morgan Stanley, (9) PNC, (10) Sovereign, (11) SunTrust, (12) U.S. Bank, and (13) Wells Fargo. In January 2013, EverBank, GMAC, and OneWest had not agreed to the payment agreement. In July 2013, the Board announced that GMAC had agreed to the payment agreement. Subsequently, EverBank agreed to the payment agreement, and remediation began for eligible OneWest borrowers under the original IFR.

13. The payment agreement also required the servicers to provide \$5.7 billion in other assistance, such as loan modifications and forgiveness of deficiency judgments. The amended consent orders left intact the requirements for the servicers to improve their foreclosure practices that were in the 2011 and 2012 consent orders.

Board staff, the Board has not undertaken enforcement actions of the size of the payment agreement. Also, similar to the IFR, the Board retained responsibility for overseeing compliance with the amended consent orders in addition to the oversight responsibilities typically delegated to the Reserve Banks.

Payment Agreement Borrower Slotting Process

The Board and the OCC issued the guidance defining the waterfall categories on January 8, 2013, and clarified that guidance 10 days later, on January 18, 2013. The guidance to the servicers defined 11 categories of potential borrower harm, known as the IFR waterfall. Definitions for the categories are in table 1.

Table 1: IFR Payment Agreement Categories

Number	Category description
1a	Servicemembers Civil Relief Act (SCRA) ^a sections 533 and 521
1b	SCRA section 527 interest rate protection
2	Borrower not in default
3	Foreclosure while in bankruptcy
6	Performing forbearance plan
4	Failure to convert trial plan
5	Performing trial period plan
10	Modification approvals
7	Denied modification
8	No decision
9	No loss mitigation engagement
11	Other

Source: OIG analysis of Board and OCC documents.

Note: The categories listed are not in numerical order. For the slotting, borrowers were to flow down through the waterfall in the order in which the categories appear in this table. Board staff explained that the Board and the OCC decided that all borrowers denied a modification would be slotted into category 7. Thus, the Board and the OCC combined two subcategories that had previously been listed separately in a draft of the IFR waterfall. For more information on the categories, see appendix B.

^aThe SCRA provides relief to active duty servicemembers so that members of the Armed Forces can focus their full attention on their military responsibilities. Some of the relief provided under the SCRA includes reducing the rate of interest for debts incurred before entering active duty to six percent and protecting servicemembers against default judgments, evictions, mortgage foreclosures, and repossessions of property.

The categories in the IFR waterfall were similar to those in the June 2012 financial remediation framework. The IFR waterfall guidance differentiated potential harm to borrowers by the stage of foreclosure (in progress, complete, or rescinded) and by whether the borrower had requested a review of his or her loan file under the IFR.

One Board official explained that for the payment agreement, the Board transitioned to a process that required no action to receive a check by most borrowers, unlike the IFR, which may have required a borrower to submit a request for review or be part of the look-back population to obtain remediation. Under the terms of the payment agreement, once the servicers submitted completed waterfalls that were validated by the servicer’s internal audit or compliance function and reviewed by the Reserve Bank, the borrower’s placement was deemed final and could not be appealed. The payment agreement prohibited servicers from requiring borrowers to waive any legal claims they may have against their servicer as a condition of accepting a payment.

After finalizing the terms of the payment agreement, the Board and the OCC published amended consent orders in February 2013, which replaced the IFR file review requirements in the original consent orders issued in 2011 and 2012. Table 2 shows the dates the Board, the OCC, and other agencies issued the IFR consent orders to the servicers and when the servicers agreed to the payment agreement.

Table 2: IFR and IFR Payment Agreement Participating Servicers

Banking institutions	Date the IFR consent orders were issued by the Board, the OCC, and other agencies	Month and year the servicer agreed to the payment agreement with the Board and the OCC
1 Aurora	April 13, 2011	January 2013
2 Bank of America	April 13, 2011	January 2013
3 Citibank	April 13, 2011	January 2013
4 EverBank	April 13, 2011	August 2013
5 GMAC	April 13, 2011	June 2013
6 Goldman Sachs	September 1, 2011	January 2013
7 HSBC	April 13, 2011	January 2013
8 JPMorgan Chase	April 13, 2011	January 2013
9 MetLife Bank	April 13, 2011	January 2013
10 Morgan Stanley	April 2, 2012	January 2013
11 OneWest	April 13, 2011	Did not participate in the payment agreement
12 PNC	April 13, 2011	January 2013
13 Sovereign	April 13, 2011	January 2013
14 SunTrust	April 13, 2011	January 2013
15 U.S. Bank	April 13, 2011	January 2013
16 Wells Fargo	April 13, 2011	January 2013

Source: OIG analysis of Board and OCC documents.

Note: Bolded institutions have a mortgage servicer subsidiary supervised by the Board, and shaded rows indicate the five servicers whose slotting process was within the scope of this OIG evaluation. HSBC and JPMorgan Chase also had separate mortgage servicing operations supervised by the OCC.

Of the 13 servicers that agreed to the payment agreement in January 2013, 5 were supervised by Reserve Banks—Goldman Sachs, HSBC, JPMorgan Chase, Morgan Stanley, and SunTrust. As required by the terms of the payment agreement, these servicers began slotting borrowers into the waterfall categories, the servicers' internal audit functions validated the slotting, and the responsible Reserve Bank dedicated teams reviewed the validation.

The Reserve Bank dedicated teams prepared, and the Board's team overseeing the initiative approved, guidance to the Reserve Bank teams called the *Complex Servicers Mortgage Foreclosure Supervisory Expectations (Supervisory Expectations)*. This guidance addressed monitoring the implementation of the payment agreement term sheets and sought to ensure, to the extent possible, consistency of the slotting review. The slotting, validation, and review processes were iterative and involved multiple meetings of the Board, the OCC, the Reserve Bank dedicated teams, the servicers, and the servicers' internal audit functions. Throughout this process, the Board had conference calls and meetings with Reserve Bank staff to ensure consistent results.

Under the terms of the payment agreement, servicers had the option to use their IFR independent consultants to conduct mortgage file reviews to determine harm to borrowers who fit into categories 1a, 1b, and 2. Category 1 pertained to violations of the Servicemembers Civil Relief Act (SCRA), such as foreclosing on an active duty servicemember, and included a subcategory (category 1b) related to charging a servicemember interest rates above SCRA caps. Category 2 pertained to borrowers who were not in default at the time of the foreclosure actions.¹⁴ Servicers could slot borrowers into categories 1a and 2 using automatic system queries, or they could elect to have their independent consultant complete file reviews to slot borrowers into categories 1a or 2. If the independent consultant's file review determined that the borrower had not suffered harm as defined by categories 1a or 2, those borrowers were placed into the next highest applicable waterfall category.¹⁵ As one Board officer explained, the Board allowed the file review to continue for these categories because these situations involved some of the more egregious types of harm to borrowers. According to this Board official, IFR independent consultants reported that they had made significant progress reviewing files to determine these types of harm during the IFR file review process.

The payment agreement term sheets imposed an aggressive deadline for completing the slotting, validation, and review process. Under the payment agreement, the term sheets provided a 30-day deadline for the servicers to complete their validations and 15 additional days for the Reserve Bank dedicated team reviews to be completed—that is, by February 21, 2013, for servicers that signed payment agreement term sheets in January 2013. During this time frame, servicers requested more time to complete their waterfall submissions. Based on the documentation we

14. Under the Board's and the OCC's IFR waterfall guidance, a borrower was not considered to be in default if he or she was less than 60 days in default on his or her mortgage loan at the time the servicer referred the borrower to the servicer's foreclosure department.

15. Of the five servicers within the scope of our evaluation, one chose to slot borrowers into these categories without its independent consultant reviewing files, and four elected to have their independent consultants determine harm for these categories. Further, under the IFR waterfall guidance, for borrowers who potentially fit into category 1b, servicers could elect to have their independent consultant perform file reviews to determine the appropriate placement of those borrowers. Alternatively, for category 1b, the servicers could forgo having their independent consultant conduct the file review and instead slot those borrowers into the next-highest waterfall category for which the borrower was eligible. Two of the five servicers within the scope of this evaluation slotted borrowers into category 1b.

reviewed, the Board-supervised servicers submitted their final waterfalls to the Board during the March 11, 2013–April 3, 2013, time frame.

On April 9, 2013, after servicers had finalized their waterfalls, the Board and the OCC published a payment distribution plan for 11 of the 13 servicers.¹⁶ Payment amounts ranged from \$300 to \$125,000, and a few borrowers were eligible for additional variable payments—reimbursement for equity plus interest. Payments received under the payment agreement did not preclude borrowers from pursuing any legal actions against the servicer. Appendix B depicts the waterfall categories, the payment amounts, and the results of the servicers slotting exercises, with the total number of borrowers slotted into each category, for all 13 participating servicers that agreed to the payment agreement in January 2013, including the servicers supervised by the OCC.

Oversight of the Payment Agreement Check Issuance Process

The servicers selected Rust as the paying agent to administer the payment agreement, and the Board and the OCC did not object to the selection. The payment agreement term sheets and the amended consent orders identified Rust as the paying agent. Board staff based their nonobjection on Rust's prior knowledge of and possession of data regarding the borrower population and its familiarity with the servicers' systems given its role in serving as the administrator for the original IFR.

Board staff did not object to the statements of work (SOWs)¹⁷ between Rust and the Board-regulated servicers. Board and OCC staff provided the oversight for Rust's activities despite the fact that neither the Board nor the OCC were parties to those contracts. While the Board was not a party to the SOWs, the contracts described many tasks that Rust would conduct under the oversight and at the direction of the Board and the OCC. As required by the SOWs, Rust provided periodic reports to the Board and the OCC. Also, Rust submitted invoices to the servicers for payment, as the amended consent orders required the servicers to pay for the administrative costs associated with the payment agreement.

Rust functioned as the paying agent administering the payment agreement. To print and mail the checks, Rust hired a subcontractor, Quad/Graphics, Inc. (Quad/Graphics), and Rust selected The Huntington National Bank to manage the payment agreement Qualified Settlement Fund (QSF) accounts and clear the checks. Rust and the other third parties' activities in support of the payment agreement have included, among other activities, the following:

1. The Huntington National Bank maintained QSF accounts in which the servicers deposited funds, as required by the payment agreement's terms.
2. The servicers provided borrower data to Rust, such as borrower name, address, and waterfall categorization.

16. The payment distribution plan for the two other participating servicers, Goldman Sachs and Morgan Stanley, was published by the Board on April 29, 2013. This plan was similar to the plan for the other servicers, but it did not differentiate borrowers according to whether they had submitted a request for review under the IFR because Goldman Sachs and Morgan Stanley started their IFR processes later and borrowers did not have the same opportunity to submit such as request.

17. Typically, an SOW is written according to the terms of a master agreement between a client and its vendor. Examples of items generally delineated in SOWs include objectives, resources, the period of performance, roles and responsibilities, requirements, acceptance criteria, and deliverables.

3. Rust sent the borrower data to Quad/Graphics.
4. Quad/Graphics printed the checks and accompanying documentation, such as cover letters, envelopes, and tax reporting forms, as required.
5. Quad/Graphics delivered the checks and accompanying documentation to the U.S. Postal Service to be mailed.
6. Quad/Graphics monitored the check delivery process and provided related data to Rust.
7. Rust received and processed mail returned by the Postal Service as undeliverable.
8. The Huntington National Bank cleared the checks that borrowers cashed or deposited with various financial institutions and check cashing establishments.
9. Rust managed a call center to respond to borrower inquiries.

Beginning in March 2013, Rust mailed postcards to approximately 4.2 million borrowers alerting them that a payment agreement had been reached and that checks would be mailed. Rust mailed the checks in separate batches, and all checks had a 90-day expiration date. The vendor mailed the first batch of approximately 1.4 million checks on April 12, 2013. Rust sent most of the approximately 223,000 checks to Morgan Stanley and Goldman Sachs borrowers on May 3, 2013. For the initial 13 servicers, borrowers had cashed or deposited checks worth approximately \$3.15 billion, as of August 15, 2014.

Finding 1: The Board's Advance Planning Efforts Were Not Commensurate With the Agreement's Complexity

The Board staff's advance preparation and planning efforts for the payment agreement were not commensurate with the agreement's complexity. The Board was responsible for overseeing the corrective action at an individual-borrower level for more than 4 million borrowers on an interagency basis across multiple mortgage servicers supervised by three Reserve Banks. Nevertheless, the Board engaged in limited planning activities for this unprecedented enforcement strategy. When a financial institution is subject to an enforcement action involving significant corrective action, the enforcement action typically requires the relevant institution to submit a detailed implementation plan to its Reserve Bank or to the Board for approval. We attribute the Board's limited planning to the compressed time frame associated with the transition from the IFR to the payment agreement and the aggressive deadlines imposed by the term sheets so that remediation could be provided to borrowers as quickly as possible. The Board's limited planning activities represent a missed opportunity to assess the feasibility of implementing the payment agreement; to define the success measures for the payment agreement, such as the percentage of borrowers cashing or depositing a check; to assess whether the Board had the requisite skills and capabilities to oversee the exercise; to consider the possible risks associated with its chosen course of action, including measures to mitigate those potential risks; and to vet fully alternative courses of action.

The Board Prepared Limited Documentation Outlining Its Plans to Oversee This Unprecedented Enforcement Strategy

In general, there was limited formal documentation of the Board staff's planning activities for the payment agreement. Based on interviews, we understand that Board staff held meetings internally and with the servicers and OCC staff during the negotiation of the payment agreement and provided briefings to senior Board officials on the merits and risks associated with the proposed payment agreement. For some of these meetings, Board staff prepared briefing materials describing the proposed payment agreement, including the objectives, key terms, and potential risks of replacing the IFR with the payment agreement. We believe that planning activities should be commensurate with the complexity of the activity to be conducted. In our opinion, overseeing an unprecedented enforcement strategy such as the payment agreement should (1) involve vetting and planning activities prior to implementation to identify risks, (2) consider the costs and benefits associated with particular alternatives, and (3) anticipate foreseeable hurdles to successful implementation.

Board staff did consider some inherent limitations and challenges associated with the approach as they prepared to announce the payment agreement. For example, in briefings to senior Board officials regarding the proposed payment agreement, the team acknowledged that the payment agreement would not identify actual harm to borrowers. While identifying actual harm was the goal of the IFR, under the payment agreement, the servicers slotted borrowers into various categories based on possible, not actual, harm. Board staff explained that borrowers did not have to waive any legal rights they had against the servicer as a condition of accepting their payment.

Additionally, the briefing materials presented to senior Board officials also acknowledged that it may be difficult to verify the accuracy of the servicers' processes for slotting borrowers.

Board staff used their briefing materials during consultations with Board members. As the Board has explained in a letter to Congress, prior to agreeing to the payment agreement,

Board staff frequently consulted with Board members. These consultations included discussions with individual Board members subject to the Board member's availability. Based on these consultations, the Board's General Counsel approved entering into these actions, with the concurrence of the appropriate delegee of the Director of BS&R. Consistent with the General Counsel's approval, the Deputy General Counsel signed the documentation memorializing that approval.¹⁸

Despite acknowledging challenges and inherent limitations, we believe that the briefing materials did not contain additional information that would have proved useful in weighing the costs and benefits associated with the proposed approach. Specifically, the briefing materials did not

- detail how the Board team would oversee the slotting process or the payment process
- assess whether Board officials had the skills necessary to oversee this complex undertaking
- identify success measures or benchmarks for the exercise, such as an estimate of how many borrowers would likely obtain remediation
- indicate whether those success measures could be incorporated into the SOWs between the servicers and Rust as service-level agreements¹⁹ to incentivize performance under those agreements consistent with the Board's expectations
- address key assumptions underpinning the exercise, such as the impact that unreliable data in the servicers' systems would have on the project's results
- describe possible alternatives, such as a victims' relief fund, or outline the costs and benefits associated with such an approach
- estimate the length of time necessary to complete the payment process or outline options for distributing residual funds

While Board staff did hold planning meetings and consider some risks and possible alternatives as it negotiated the payment agreement, they did not record formal minutes of meetings or prepare a formal project plan. Board staff did, however, create a document to track progress on several project tasks, and approved the supervisory expectations document to guide the oversight of the slotting process. Board staff explained that the compressed time frame imposed by the payment agreement term sheets precluded formal planning activities and that engaging in such activities would have caused further delays in getting remediation to borrowers. Board staff said that they consulted with staff from other agencies familiar with these types of agreements, although the insights from these interactions were not formally documented. Given the lack of formal documentation, we could not determine the extent to which the knowledge gained from these other agencies informed the Board's oversight of the implementation phase of the payment agreement.

18. Ben S. Bernanke, letter to Senator Elizabeth Warren and Representative Elijah Cummings, December 16, 2013.

19. Service-level agreements are performance measures defining specific expectations for the vendor's performance.

In terms of planning for its oversight of the implementation phase, the Board considered the foreseeable challenge of locating addresses for some borrowers. At the outset of the implementation of the payment agreement, Board staff explained that Rust would be able to skip trace borrowers who had relocated to a new address by checking various databases, such as the U.S. Postal Service's national change of address database. The Board did not prepare an estimate of the likelihood that Rust's skip tracing process would be effective.

The Board Sought to Negotiate the Payment Agreement as Quickly as Possible

We attribute Board staff's limited advance planning to the narrow window of time between the decision to replace the IFR and the completion of the amended consent orders containing the payment agreement. Board officials emphasized providing remediation to borrowers in a timelier fashion than would have likely occurred had the IFR been allowed to continue. Therefore, timely action was a primary consideration underpinning the Board's decision to transition to the payment agreement.

Board staff began negotiating the payment agreement in late 2012. Beginning on January 7, 2013, the Board, the OCC, and the servicers signed the payment agreement term sheets, and the Board and the OCC announced the payment agreement. Board staff's primary focus during this compressed time frame was negotiating the payment agreement, which afforded little time for adequate planning. One member of the Board's oversight team explained that if the Board had stopped the IFR without an alternative that could be implemented quickly, the Board would have faced further stakeholder criticism. In this context, the Board prioritized replacing the IFR as quickly as possible with an alternative that provided payments to borrowers in a timelier manner than would have occurred under the IFR. This prioritization and sense of urgency limited the opportunity for advance planning.

As a result of limited planning, Board staff missed opportunities to assess the feasibility of executing the payment agreement, its likelihood of success, and whether Board staff had the requisite skills and capabilities to oversee the exercise. The Board also did not fully consider measures to mitigate the potential risks and vet possible alternative courses of action. In our opinion, the sense of urgency to transition to the payment agreement and the resulting limited planning and preparation placed the Board's oversight team in a position in which its approach to problem solving was more reactive and ad hoc than it otherwise might have been.

Summary

The Board sought to provide payments to borrowers as quickly as possible. The short time frame provided in the payment agreement term sheets afforded little time for adequate planning to oversee this complex, unprecedented initiative. Because of this limited planning, the Board staff did not identify project success measures, assess the project's likelihood of success, analyze alternative approaches to achieve the Board's desired objectives, or assess whether the Board had the right mix of skills and expertise to manage the payment agreement.

Recommendation

We recommend that the Directors of BS&R, DCCA, and the Legal Division

1. Develop a framework to guide planning, vetting, and approving activities for large, complex enforcement strategies that may involve multiple institutions, multiple Board divisions, or multiple Reserve Banks. This framework could include planning and risk assessment activities such as
 - a. identifying key risks and possible risk-mitigating activities.
 - b. assessing the feasibility of the intended corrective action.
 - c. vetting possible alternatives.
 - d. identifying documentation standards for the relevant initiative.
 - e. defining performance measures as indicators of success and creating key interim milestones to monitor progress.
 - f. assessing whether service-level agreements could be used to incentivize vendor performance consistent with expectations.
 - g. identifying key assumptions.
 - h. assessing whether the Board has the necessary skill sets and the resources available to oversee the intended corrective action.
 - i. defining roles and responsibilities among the Board team overseeing the corrective action.

Management's Response

The Director of BS&R, the Director of DCCA, and the Board's General Counsel agreed with our recommendation. In their consolidated response to recommendation 1, the Board officials indicated that they plan to leverage information learned throughout the IFR process and the implementation of the payment agreement to ensure an appropriate level of planning, vetting, and approving activities for similar enforcement actions in the future.

OIG Comment

In our opinion, the actions described by the Division Directors and the Board's General Counsel are responsive to our recommendation. We plan to follow up on the Board's actions to ensure that the recommendation is fully addressed.

Finding 2: The Board Did Not Use a Project Management Function to Support This Complex Initiative

The Board assigned three senior officials to oversee the project who, rather than serving exclusively in a support and guidance capacity, also engaged in time-consuming, day-to-day oversight, management, and implementation activities. We believe that this unprecedented interagency initiative would have benefitted from a project management function to assist in guiding the effort from planning through the execution phase with oversight and support provided by senior Board officials. Such an approach might have allowed the officers to delegate more of the daily oversight activities to the project management function, freeing the senior Board officials to focus more on other priorities. We attribute the significant allocation of senior Board officials' time to (1) the preference for maintaining the continuity of the initial team given the steep learning curve associated with this project; (2) the lack of project management resources available to support this large, complex initiative; and (3) the unique need for quick decisionmaking on implementation issues associated with the payment agreement given the Board's sense of urgency in providing checks to the borrowers as quickly as possible. The time these officers spent on this project minimized the time they could devote to other responsibilities.

Senior Board Officials Conducted Day-to-Day Oversight Activities for the Payment Agreement

To oversee the project, the Board assigned one senior official from each of three Board divisions: BS&R, DCCA, and Legal. In addition to serving in a leadership capacity for the project, however, these senior Board officials also engaged in day-to-day oversight, management, and implementation activities for the project. For example, these officers participated in multiple conference calls each week with their OCC counterparts, the Reserve Bank examiners assigned to the project, and Rust employees. In addition, in coordination with OCC staff, certain of these senior Board officials (1) reviewed and approved payment agreement correspondence to borrowers; (2) suggested changes to Rust's operating procedures for the call center scripts and processes to handle undeliverable mail; (3) resolved issues faced by borrowers, especially when the situation involved procedural adjustments for Rust's complaint resolution activities; and (4) monitored Rust's performance to confirm resolution of issues identified on the issues log.

Two of the senior officials noted that they spent as much as 50 to 60 percent of their time on this project, and the third reported spending 40 to 50 percent. According to an interviewee, one of the lessons learned from the IFR and a contributing factor in the significant allocation of officer time to this initiative was the importance of ensuring effective communication with the in-scope borrowers covered by the payment agreement. Another senior Board official explained that the direct senior official involvement allowed the oversight team to make quick decisions related to implementing the payment agreement.

A Project Management Function Could Allow the Board to Better Allocate Resources to Support Complex Projects

While the Board does not have a policy requiring the use of project management resources in support of large, complex initiatives such as the payment agreement, we believe that this unprecedented, interagency initiative would have benefitted from such support. Board staff on the payment agreement project team explained that project management resources were not available to the team. While we understand that the Board's senior management chose to keep the horizontal review and the IFR project team in place because of the team members' familiarity with the project and the steep learning curve associated with this project, we believe that the transition from the IFR to the payment agreement presented an opportunity for the Board to supplement the skills of the existing team on an as-needed basis.

Although both the IFR and the payment agreement involved Board staff oversight of Rust and the Reserve Bank dedicated teams, overseeing the payment agreement was different from overseeing the IFR. The IFR relied heavily on independent consultants to perform file reviews. The Board's oversight of the payment agreement, however, involved overseeing the dedicated teams at the three Reserve Banks conducting the reviews of the slotting processes. Further, for the IFR, the oversight of Rust's performance was primarily coordinated by a consortium of servicer officials. For the payment agreement, however, the Board and the OCC assumed the role of directly overseeing Rust's administration of the payment agreement involving the use of multiple third parties. As such, the team managing the payment agreement may have benefitted from additional resources to coordinate such a large, complex initiative.

Further, the Board did not have staff devoted solely to project management who could be available to support projects such as the payment agreement. One of the senior Board officials overseeing the payment agreement explained that additional resources could have been helpful to the project, but the Board does not typically expand staffing with temporary appointments or hire independent contractors to perform work. We believe that the Board should consider additional staffing approaches for monitoring large, complex initiatives, particularly those involving third-party vendor oversight.

Finally, Board staff explained that oversight of the payment agreement required direct involvement of senior Board officials because of the need to resolve issues quickly. As borrowers faced challenges cashing or depositing their checks, Board staff held almost daily conference calls and a few in-person meetings with Rust employees. For example, Board and OCC staff suggested revisions to Rust's operating procedures to improve processes for resolving borrowers' difficulties receiving checks, such as making it easier for borrowers to quickly provide their current address to Rust, and Rust updated its procedures and implemented the new processes accordingly. Our interviews revealed that the Board staff's scrutiny of Rust's performance during the payment agreement process exceeded the level of oversight Rust typically experiences.

Summary

The same Board staff who had been previously responsible for overseeing the horizontal review and then the IFR were responsible for managing the payment agreement. These officials devoted considerable time to day-to-day oversight of the project because the Board did not have project management resources available to them to whom certain tasks could be delegated. The Board's

oversight of the payment agreement is an example of how the Board could benefit from developing a staffing plan that includes project management resources. Such staff could be available to support large, complex Board projects, allowing the Board to better allocate resources, define project objectives and milestones, monitor project progress, and oversee vendor performance as necessary.

Recommendation

We recommend that the Directors of BS&R, DCCA, and the Legal Division

2. Identify the circumstances in which project management resources should be used and develop a staffing plan to include project management resources with appropriate subject-matter expertise for those situations.

Management's Response

The Director of BS&R, the Director of DCCA, and the Board's General Counsel agreed with our recommendation. In their consolidated response to recommendation 2, the Board officials indicated that they will integrate available project management resources with appropriate subject-matter expertise when staffing similar complex enforcement actions in the future.

OIG Comment

In our opinion, the actions described by the Division Directors and the Board's General Counsel are responsive to our recommendation. We plan to follow up on the Board's actions to ensure that the recommendation is fully addressed.

Finding 3: Data Integrity Issues With the Servicers' Systems Impacted the Reliability and Consistency of the Slotting Results

During the slotting, review, and validation process, Board staff identified weak or missing data in two servicers' systems.²⁰ Board staff determined that the data could not support the slotting of borrowers in specific categories. As a result, the two servicers could not complete the waterfall processes according to the categories defined by the Board and the OCC. To address these data reliability issues, Board staff directed these two servicers to move borrowers to higher categories or refrain from excluding borrowers from higher categories. Board staff explained that these solutions were a conservative approach that benefitted the borrowers affected by the data reliability issues by placing them into the highest possible waterfall category based on the available data. For example, one servicer reviewed a sample of its slotting results for 255 loans and identified 45 incorrectly slotted borrowers, or 18 percent of the sample. The servicer attributed the incorrect slotting to inaccurate system data. Board staff instructed this servicer to not slot any borrowers by manual intervention.

The guidance for the Reserve Bank dedicated teams' review of the slotting sought to ensure consistency to the extent possible. The servicers' internal audit functions sought to assess the completeness and accuracy of the servicers' waterfalls. In our opinion, consistency to the extent possible was a guiding principle for this exercise, although the scope of that principle was not clearly defined. Board staff directed servicers to move borrowers to higher categories or not exclude borrowers from higher categories because the Board (1) emphasized completing the payment agreement as quickly as possible and (2) sought to avoid repeating the file review process. As a result of the servicers' movement of borrowers into the highest possible category, some similarly situated borrowers may have received different payment amounts.

Board Staff Identified Weak or Missing Data in Two Servicers' Systems

During the Reserve Bank teams' reviews of the servicer's internal audit validation of the slotting process, Board staff identified weak or missing data in the systems of two servicers—hereafter referred to as Servicer A and Servicer B. Because the data were not sufficiently reliable to support moving borrowers out of specific waterfall payment categories, Board staff instructed these two servicers to move borrowers to higher waterfall categories or refrain from excluding borrowers from higher categories. Generally, borrowers in the higher categories received a higher payment amount.²¹ Moving borrowers into a higher waterfall category, or keeping borrowers in a higher waterfall category, benefitted those borrowers since they would likely receive higher

20. Board staff explained that the oversight of the slotting process was conducted jointly with the OCC. Board staff stated that they and OCC staff worked together to ensure consistency, to the extent possible, across all the servicers that participated in the payment agreement. According to Board staff, the determinations about the reliability of the servicers' data systems and the directions to servicers on how to address those issues were made in coordination with OCC staff.

21. As defined by the Board and the OCC, the waterfall categories are not in numerical order. For the slotting process, borrowers flowed down through the waterfall in the sequential order that the categories appear in waterfall guidance. For more information on the categories and the payment amounts, see appendix B.

payment amounts. Servicers completed the slotting process before Board and OCC staff determined the actual payment amounts associated with each of the categories. Therefore, the precise payment amounts did not affect the Board's or the OCC's decisionmaking with respect to options for addressing the data reliability issues.

Instances of Weak or Missing Data at Servicer A

Each Reserve Bank dedicated team drafted a conclusion memorandum to summarize the results of its review of the slotting process at each mortgage servicer. The Reserve Banks shared those memorandums with the Board to evidence completion of the review. According to the Servicer A Reserve Bank conclusion memorandum, Servicer A self-identified issues with the reliability of its servicing system data fields used to populate certain waterfall categories. To compensate for the data reliability issues, the servicer sampled 255 loans and performed a manual review of the system query results to confirm appropriate waterfall placement. As a result of the manual review, Servicer A reslotted a total of 45 accounts across multiple waterfall categories from the sample of 255 loans (18 percent). Out of the 45 incorrectly slotted borrowers, 36 were incorrectly slotted in what the Reserve Bank dedicated team referred to as lower-tier categories, categories 7 through 11. Thus, based on the sample, the bulk of the servicer's slotting errors were concentrated within lower waterfall categories.

The Reserve Bank dedicated team communicated to the servicer that the reslotting of accounts based on the servicer's manual intervention would not be consistent with the expectations set forth in the IFR waterfall definitions and the terms of the payment agreement. According to the Reserve Bank conclusion memorandum, the payment agreement terms required the servicer to slot borrowers using an objective and systematic process rather than a manual process. Board officials noted that the IFR was a time-consuming, manual process involving loan file reviews at the individual-borrower level, while the payment agreement sought to provide timelier remediation using an objective, systematic process. Therefore, slotting borrowers based on a manual process did not align with the terms of the payment agreement. As a result, the servicer was not permitted to slot borrowers to lower categories based on a manual review. Instead, the servicer revised its waterfall to reslot the 45 accounts back into the originally identified higher payment categories, even though manual intervention identified that those results were not reliable.

Both the servicer and its internal audit function agreed that no alternative data systems existed with data capable to slot borrowers more accurately into the waterfall. According to the Reserve Bank conclusion memorandum, the definitions set forth in the waterfall guidance state that all accounts are to begin at the top of the waterfall (category 1a) and then flow down into lower waterfall categories only when servicing system data evidence that they do not meet the definitions of each sequential category. Under Board staff's guidance, the Reserve Bank dedicated team communicated to the servicer that the data available in the servicing system were not sufficiently reliable to slot borrowers below category 7, and consequently, no accounts should be allowed to flow below that point in waterfall. Based on this directive, Servicer A truncated its waterfall at category 7, and approximately 83,000 borrowers who had been slotted into lower categories were moved to category 7, resulting in those borrowers being eligible to receive higher payment amounts.

Instances of Weak or Missing Data at Servicer B

During the review of Servicer B's slotting, the Reserve Bank dedicated team identified two instances in which the measures the servicer took "to compensate for weak or missing system data did not yield the most favorable outcome to the borrower." These instances also prevented movement of certain borrowers out of higher payment categories.

First, the Reserve Bank dedicated team recognized that the data used to place borrowers into the bankruptcy category, category 3, were weak or missing. Based on prior supervisory work performed during the IFR, the Reserve Bank dedicated team was aware that the servicer's system indicator for active bankruptcy was unreliable. After discussions among the Reserve Bank dedicated team, the servicer, and Board staff, the servicer agreed to purchase Public Access to Court Electronic Records (PACER) data and rely solely on this external data source to place borrowers into category 3.

The servicer extracted dates from PACER to identify borrowers in active bankruptcy at the time the foreclosure action occurred and determine whether the borrowers should be excluded from the category due to a court-granted motion for relief from stay on the borrower's mortgage loan, which would have permitted the foreclosure to proceed. Due to time constraints, however, the servicer was only able to extract the necessary PACER motion for relief from stay data for approximately 14,000 of 26,000 borrowers identified as having been in active bankruptcy. About 72 percent of those 14,000 were excluded from category 3 based on the motion of relief from stay data and moved to a lower category. Servicer B requested an extension to complete this process for the remaining borrowers. Board and OCC staff did not grant the extension, however, because it would have caused delays completing the overall payment agreement.

Granting an extension would have caused a delay because Board staff needed to know the total number of borrowers in each waterfall category before the Board and the OCC could finalize the payment amounts for each category. As such, the final waterfall payment amounts could not be determined until all the servicers submitted their completed waterfalls. Therefore, Servicer B slotted the remaining balance of approximately 12,000 borrowers for which it did not have time to extract PACER motion for relief from stay data in category 3, the bankruptcy category. Reserve Bank examiners were comfortable that the final number of loans in the bankruptcy category reflected a conservative approach to identifying borrowers in category 3 for this servicer based on the decision not to exclude borrowers.

The second instance of weak or missing data at Servicer B related to the modification status of borrowers' mortgages. In certain instances, Servicer B did not retain or could not determine the modification status of the borrower and slotted those borrowers into category 8.²² However, Board staff instructed the servicer that if it could not determine modification status, those borrowers should default to the highest applicable waterfall category, which was category 7. As a result of this directive, approximately 60,000 Servicer B borrowers were moved to category 7 from 8. Board officials considered the actions taken by the servicer to be the most conservative

22. Category 8 relates to instances in which the servicer received a borrower's modification request, but the servicer did not make an underwriting decision. Category 8 is further defined to exclude any customer in categories 1, 2, 3, 4, 5, 6, 7, and 10. As defined by the Board and the OCC, the categories in the waterfall were not listed numerically, and category 9 was lower in the waterfall than category 10. See appendix B for more details on the waterfall categories.

approach because the actions resulted in placing borrowers in the highest possible waterfall payment category given the available data.

Board Staff Provided Guidance to Ensure Consistency Among the Servicers

The Reserve Bank dedicated teams used the *Supervisory Expectations* as a project plan to monitor the servicers' implementation of the terms of the payment agreement. According to the overview section of the document, the *Supervisory Expectations* was "designed to outline the requirements of the exam teams and to ensure consistency, to the extent possible." We believe that consistency of results to the extent possible was a guiding principle for this exercise, although the Board's expectations for applying this principle were not clearly defined. Additionally, the scope of the document states that "the Dedicated Teams will direct the Servicers to have their waterfall independently reviewed by internal audit or independent compliance control function to assess the accuracy and completeness of the waterfall."

Board Staff Emphasized Speed and Provided Broad Objectives

We attribute the approaches taken to mitigate the data reliability issues to two contributing causes: (1) the Board had a sense of urgency to complete the process as quickly as possible and (2) the Board conveyed broad objectives as guidance to the Reserve Bank dedicated teams that did not consider how to address the impact of data reliability issues on the results of the slotting exercise.

First, the Board and the OCC emphasized speed in the design and execution of the payment agreement. Under the IFR, the precursor to the payment agreement, independent consultants conducted file reviews for about 18 months, but no money had been provided to borrowers. In response to the slow progress of the IFR, the payment agreement emphasized providing remediation to borrowers as quickly as possible. The payment agreement term sheets stipulated a narrow window of 45 days for completing the Reserve Bank dedicated team reviews of the servicer internal validation testing for the execution of the slotting process. Given the sense of urgency and narrow time frame, Board staff explained that the payment agreement was designed by Board and OCC officials to accurately slot borrowers using an objective, systematic process rather than a manual process.

Second, Board staff provided broad objectives to the Reserve Bank dedicated teams that did not specify detailed expectations and procedures. Specifically, the *Supervisory Expectations* document includes four objectives. The second objective outlined that "the process should also document and assess known system or data gaps/deficiencies and major assumptions associated with completing the Waterfall. In addition, it should document whether and how system gaps/deficiencies were addressed in preparing the Waterfall." Board staff sought to provide the dedicated teams with general guidance and provide specific responses to data reliability issues on a case-by-case basis. While the document provided instructions, it did not provide specific guidance concerning which approaches the Board would consider appropriate to resolve data reliability issues. Feedback on specific approaches was provided during frequent interaction between Board staff and Reserve Bank dedicated teams.

The *Supervisory Expectations* document provided detailed procedural steps to complete the review of categories 1 and 2 but not for the lower categories. The detailed procedures included several steps to be completed specifically to understand and assess the servicer's slotting processes for categories 1 and 2. For categories 3 through 11, however, procedures for reviewing the slotting are not specifically outlined; instead, a set of general instructions were provided. These instructions for the Reserve Bank dedicated teams included reviewing the servicer systems and developing an understanding of the process by which system queries were built. According to the *Supervisory Expectations*, the review may also include understanding which servicer systems were used in the slotting process and which data fields were accessed. The procedures to review categories 3 through 11 rely on analysis of automated system queries of the servicers' data. Moreover, the *Supervisory Expectations* document did not identify a threshold for when data systems would not be considered sufficiently reliable to support the slotting exercise. According to Board officials, a threshold was not used because decisions were made on a case-by-case basis based on discussions involving the Board and Reserve Bank staff.

Similarly Situated Borrowers May Have Received Different Payment Amounts

Because of the actions taken to mitigate data reliability issues and move borrowers into higher categories or refrain from excluding borrowers from higher categories, similarly situated borrowers may have received different payment amounts across the servicers. For example, per Board staff's instructions, Servicer A truncated its waterfall due to data that were not sufficiently reliable. As a result, approximately 83,000 borrowers originally slotted into lower-tier categories were slotted into a higher category and were eligible to receive a payment of \$2,000 to \$6,000. However, if those borrowers had not moved to the higher category, they would have received \$300 to \$800. Among the other 12 servicers, approximately 2 million borrowers were slotted into the lower-tier categories and were eligible to receive a payment of \$300 to \$800.

Because of the approach to resolving data reliability issues, borrowers at Servicer A and Servicer B may have received different payment amounts compared to borrowers at the other servicers. For example, at Servicer B, approximately 12,000 borrowers were included in the bankruptcy category (category 3) when they may have been appropriately excluded. Borrowers slotted in the bankruptcy category were eligible to receive a payment of \$3,750 to \$62,500. Servicer B's borrower population slotted into the bankruptcy category accounted for 56 percent of the total borrowers in category 3. Among the other 12 servicers, approximately 13,000 borrowers were slotted into category 3.

Board staff explained that it selected the actions taken to mitigate data reliability issues on a case-by-case basis to slot borrowers into the waterfall as accurately as possible. This approach sought to foster consistency by acknowledging the limitations associated with the available data. The Board and the OCC published the payment distribution plan after the servicers finalized their waterfalls. As such, the servicers and the Reserve Bank dedicated team members were not aware of the payment distribution amounts for the categories during the slotting process.

Summary

Data integrity issues impacted the reliability and consistency of the slotting results for two servicers. These data issues resulted in those servicers moving borrowers into the next-highest category or not excluding them from a higher category. As a result of these actions, some similarly situated borrowers at the other servicers may have been slotted into dissimilar categories and received different payment amounts.

Recommendation

We recommend that the Directors of BS&R, DCCA, and the Legal Division

3. Assess the potential impact of data reliability issues as part of the complex enforcement strategies framework described in recommendation 1. Specifically, consider how data availability or reliability issues may impact the feasibility of the exercise or the consistency of its results. As part of this analysis, consider whether alternative enforcement strategies can be adopted that mitigate or eliminate these challenges. As appropriate, these strategies should be developed, vetted, and approved as part of the planning process.

Management's Response

The Director of BS&R, the Director of DCCA, and the Board's General Counsel agreed with our recommendation. In their consolidated response to recommendation 3, the Board officials indicated that they plan to leverage information learned throughout the IFR process and the implementation of the payment agreement when planning for similar complex enforcement actions in the future. This effort would include addressing the potential impact of any data reliability issues as warranted.

OIG Comment

In our opinion, the actions described by the Division Directors and the Board's General Counsel are responsive to our recommendation. We plan to follow up on the Board's actions to ensure that the recommendation is fully addressed.

Finding 4: The Board Has Not Finalized a Strategy to End the Payment Agreement

Board officials have not finalized a strategy to end the payment agreement, although the Board has developed and discussed with the OCC alternatives to conclude the payment agreement and distribute any remaining funds. As of August 15, 2014, borrowers of the 13 servicers that joined the payment agreement in January 2013 have cashed or deposited checks totaling about \$3.15 billion of the total \$3.67 billion paid into the QSF accounts by those servicers.²³ As there will likely be money remaining in the QSF accounts—possibly as much as \$500 million or more—an approved plan is necessary to address any claims on remaining funds and to administer the residual. The Board and the OCC intentionally deferred resolving this issue in order to initiate the payment agreement as quickly as possible. The lack of an approved plan or strategy creates uncertainty about how the remaining funds will be distributed and may subject the Board to further stakeholder criticism.

Board Officials Acknowledged That It Is Unlikely That All Checks Will Be Cashed or Deposited

Board officials have not finalized a strategy to end the payment agreement process because the Board's limited advance planning efforts did not involve preparing for the eventuality that all borrowers would not be located and that all checks would not be cashed or deposited. Board officials have acknowledged that it is unlikely that all borrowers will cash or deposit their check. As of August 15, 2014, borrowers of the 13 servicers that joined the payment agreement in January 2013 had cashed or deposited checks totaling about \$3.15 billion, or about 86 percent, of \$3.67 billion that those servicers paid into the QSF accounts for those borrowers. Therefore, as of August 15, 2014, approximately \$520 million in funds were remaining in those QSF accounts. Borrowers may not have cashed or deposited checks for varying reasons, including failure to locate the borrower or, in limited cases, fraud. For instance, some borrowers were difficult to locate due to changes in residence, divorce, name changes, and deaths. As Board staff concluded, it is unlikely that they or Rust will be able to locate addresses for all borrowers, and as such, funds will be remaining in the QSF accounts. Thus, the Board must determine its strategy to eventually wind down this activity.

Board officials anticipated challenges locating every borrower. Interviewees indicated that the Board's primary focus during the term sheet negotiation process was providing remediation to borrowers as quickly as possible. As a result, we understand that Board officials chose to defer developing and finalizing the plan for distributing any residual funds until the execution phase of the payment agreement. The lack of an approved strategy to address how the remaining funds will be distributed creates uncertainty. As the Board has not yet finalized a plan to end the payment agreement, the Board exposes itself to additional stakeholder criticism and reputational risk.

23. The QSF 1 account holds funds allocated for borrowers whose mortgage was with 11 servicers. These 11 servicers are (1) Aurora, (2) Bank of America, (3) Citibank, (4) HSBC, (5) JPMorgan Chase, (6) MetLife Bank, (7) PNC, (8) Sovereign, (9) SunTrust, (10) U.S. Bank, and (11) Wells Fargo. The QSF 2 account holds funds allocated for borrowers whose mortgage was with Morgan Stanley or Goldman Sachs. The QSF 3 account holds funds allocated for borrowers whose mortgage was with GMAC.

Management Actions Taken During Evaluation

Board officials have discussed with the OCC alternatives for finalizing the payment agreement. During the course of our evaluation, the Board addressed the need to develop a plan to complete the payment agreement and distribute any remaining funds, although as of September 18, 2014, it had not finalized a plan. Board officials have held meetings internally and with their OCC counterparts. Separately from the OCC, the Board has started to consider the pros and cons and evaluate the feasibility of various alternatives for completing the payment agreement and distributing any remaining funds.

Recommendations

We recommend that the Directors of BS&R, DCCA, and the Legal Division

4. Finalize an approach to end the payment agreement, including developing, in coordination with the OCC, a strategy to appropriately allocate any funds remaining in the QSFs that have not been cashed or deposited by borrowers, and continuing efforts to locate uncompensated borrowers.
5. As part of future agreements involving payments to harmed consumers, identify potential options for distributing any residual amounts as part of the planning process.

Management's Response

The Director of BS&R, the Director of DCCA, and the Board's General Counsel agreed with our recommendations. In their consolidated response to recommendation 4, the Board officials indicated that the agency has begun working on a plan to end the process for paying in-scope borrowers, including continuing efforts to locate uncompensated borrowers and to appropriately allocate any funds remaining in the QSFs. We understand that the Board has discussed its plans with the OCC. In their consolidated response to recommendation 5, the Board officials indicated that they plan to consider potential options for distributing any residual amounts as part of the planning process in similar complex enforcement actions in the future.

OIG Comment

In our opinion, the actions described by the Division Directors and the Board's General Counsel are responsive to our recommendations. We plan to follow up on the Board's actions to ensure that these recommendations are fully addressed.

Appendix A

Scope and Methodology

The scope of our evaluation includes the Board's oversight of the slotting process for the five servicers supervised by the Board that had agreed to the payment agreement in January 2013, including Goldman Sachs, HSBC, JPMorgan Chase, Morgan Stanley, and SunTrust. Our scope did not include the Board's oversight of the payment agreement as it related to GMAC, another Board-supervised servicer, because that servicer did not agree to the payment agreement until June 2013. Additionally, our scope comprises evaluating the Board's approach to overseeing the mortgage foreclosure consent orders and the Board's oversight of the payment process by Rust and other third parties.

To accomplish our objectives, we interviewed officials from BS&R, DCCA, and the Legal Division who were assigned to oversee this project. We developed interview questions and interviewed officials from the Federal Reserve Banks of Atlanta, Chicago, and New York who were assigned to dedicated teams to assess specific servicer compliance with the consent orders. Additionally, we interviewed staff from third parties involved in implementing the payment agreement, including Rust, Quad/Graphics, and The Huntington National Bank.

We reviewed in detail the Board's guidance to the servicers, to the independent consultants, and to each of the Reserve Bank teams. We also analyzed the slotting for each of the servicers and conducted testing related to the borrower slotting and supporting documentation, including internal audit validation and the review performed by the Reserve Bank dedicated teams. Finally, we reviewed documentation related to Rust's activities as the paying agent, including its issues log and correspondence with borrowers.

We conducted our fieldwork from February 2013 through April 2014. We performed this evaluation in accordance with the *Quality Standards for Inspection and Evaluation* issued by the Council of the Inspectors General on Integrity and Efficiency.

Appendix B

Results of the Servicers' Slotting and the Payment Amounts

No. ^a	Category description	Stage of foreclosure	11 servicers ^b				Goldman Sachs and Morgan Stanley		Total borrowers
			Borrowers who requested a review		All other borrowers		Number of borrowers	Payment amount	
			Number of borrowers	Payment amount	Number of borrowers	Payment amount			
1a	Servicer foreclosed on borrower eligible for SCRA protection ^c	Rescinded	8	\$15,000	108	\$15,000	14	\$15,000	1,261
		Completed	123	\$125,000	959	\$125,000	49	\$125,000	
1b	Servicer charged servicemembers interest rates that exceed SCRA section 527 limits	In process	33	>=\$300	317	>=\$300	101	>=\$300	525
		Completed	11	>=\$300	63	>=\$300	0	>=\$300	
2	Servicer initiated or completed foreclosure on borrower who was not in default ^c	In process	46	\$5,000	543	\$5,000	55	\$5,000	747
		Rescinded	8	\$15,000	29	\$15,000	10	\$15,000	
		Completed	8	\$125,000	45	\$125,000	3	\$125,000	
3	Servicer initiated or completed foreclosure on borrower who was protected by federal bankruptcy law	In process	2,401	\$7,500	19,860	\$3,750	1,069	\$4,650	29,531
		Rescinded	28	\$7,500	160	\$3,750	67	\$4,650	
		Completed	763	\$62,500	5,075	\$31,250	108	\$38,750	
6	Servicer completed foreclosure on borrower who was meeting all requirements of documented forbearance plan	Rescinded	50	\$6,000	185	\$3,000	45	\$3,900	1,174
		Completed	162	\$24,000	684	\$12,000	48	\$15,600	
4	Servicer failed to convert borrower to permanent modification after three successful payments under a written trial-period plan	In process	461	\$6,000	2,436	\$3,000	312	\$3,900	4,482
		Rescinded	31	\$6,000	91	\$3,000	44	\$3,900	
		Completed	239	\$50,000	718	\$25,000	150	\$32,500	
5	Servicer completed foreclosure on borrower who was performing all requirements of the written trial-period plan	Rescinded	29	\$6,000	126	\$3,000	77	\$3,900	1,209
		Completed	163	\$50,000	477	\$25,000	337	\$32,500	
10	Modification request approved	In process	118,177	\$500	746,894	\$300	62,927	\$300	1,191,516
		Rescinded	2,617	\$500	9,229	\$300	869	\$300	
		Completed	39,368	\$500	195,448	\$300	15,987	\$300	
7	Modification request denied ^d	In process	62,557	\$2,000	432,595	\$1,000	41,912	\$1,300	942,116
		Rescinded	1,539	\$2,000	6,007	\$1,000	1,016	\$1,300	
		Completed	60,251	\$6,000	309,597	\$3,000	26,642	\$3,900	
8	Modification request received but no underwriting decision made	In process	21,153	\$800	200,596	\$400	13,090	\$520	449,266
		Rescinded	709	\$800	3,757	\$400	324	\$520	
		Completed	27,152	\$800	168,479	\$400	14,006	\$520	
9	Servicer did not engage with borrower in a loan modification or other loss mitigation action	In process	16,679	\$600	312,881	\$300	5,825	\$300	918,392
		Rescinded	350	\$600	4,549	\$300	96	\$300	
		Completed	36,564	\$600	531,912	\$300	9,536	\$300	
11	All other loans	In process	21,459	\$500	334,630	\$300	13,780	\$300	633,435
		Rescinded	450	\$500	4,161	\$300	304	\$300	
		Completed	24,959	\$500	218,737	\$300	14,955	\$300	
Total borrowers			438,548		3,511,348		223,758		4,173,654

Source: OIG analysis of Board and OCC documents.

^a The categories listed are not in numerical order. For the slotting, borrowers were to flow down through the waterfall in the sequential order that the categories appear in this table.

^b The 11 servicers were Aurora, Bank of America, Citibank, HSBC, JPMorgan Chase, MetLife Bank, PNC, Sovereign, SunTrust, U.S. Bank, and Wells Fargo. This chart includes borrowers whose mortgage was serviced by Board- and OCC-supervised servicers.

^c The amount received by borrowers in these categories may be different because of offsets resulting from other settlements.

^d According to Board staff, the Board and the OCC decided that all borrowers denied a modification would be slotted into one category. Thus, the Board and the OCC combined subcategories (7a and 7b) that had been listed separately in a draft of the IFR waterfall.

Appendix C

Management's Response



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

ADDRESS OFFICIAL CORRESPONDENCE
TO THE BOARD

September 29, 2014

Mark Bialek
Inspector General
Board of Governors of the Federal Reserve System
Washington, D.C. 20551

Dear Mr. Bialek:

Thank you for the opportunity to comment on your draft report evaluating the Board's oversight of the payment agreement reached by the Office of the Comptroller of the Currency (OCC) and the Board with several large mortgage loan servicers that replaced the Independent Foreclosure Review (IFR) process required by enforcement actions. As the report recognizes, as of August 15, 2014, borrowers of the 13 servicers covered by the report have cashed or deposited checks totaling approximately \$3.15 billion, which represents approximately 86 percent of the value of checks issued to borrowers of those servicers. In negotiating the payment agreement, the Board coordinated with the OCC, which regulated most of the servicers participating in the IFR. The Board entered into the agreement to provide monetary compensation, in a timelier manner than was experienced with the IFR, to millions of borrowers affected by the foreclosure crisis.

The draft report contains five recommendations relating to the Board's oversight of the payment agreement and similar complex enforcement actions in the future. We are in general agreement with the recommendations and have begun taking steps to implement them, as outlined below.

The first recommendation is that the Division of Banking Supervision and Regulation (BS&R), the Division of Consumer and Community Affairs (DCCA) and the Legal Division (Legal) (collectively, the Divisions) develop a framework to guide planning, vetting, and approving activities for large, complex enforcement strategies that may involve multiple institutions, multiple Board divisions, or multiple Reserve Banks. Board staff significantly expanded its planning and monitoring efforts during the course of the payment agreement and will continue to devote resources to overseeing the remaining requirements of the enforcement actions. Staff is also working on planning documents for possible steps to end the process for paying in-scope borrowers. We expect that this documentation will address the appropriate planning and risk assessment factors set out in recommendation one. We plan to leverage information learned throughout the IFR process and implementation of the payment agreement to

ensure an appropriate level of planning, vetting, and approving activities for similar complex enforcement actions in the future.

The second recommendation is that the Divisions identify the circumstances in which project management resources should be used and develop a staffing plan to include project management resources with appropriate subject-matter expertise for those situations. Although project management resources were not available to assist Board staff in planning and implementing the IFR and the transition to the payment agreement, BS&R recently assigned staff with project management expertise to help finalize and implement our plan to end the process for paying in-scope borrowers. We agree that project management resources can add value and we will integrate available project management resources with appropriate subject-matter expertise when staffing similar complex enforcement actions in the future.

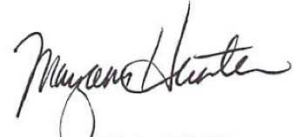
The third recommendation is that the Divisions assess the potential impact of data reliability issues as part of the complex enforcement strategies framework described in recommendation one. As the report noted, to provide timely relief to borrowers, the terms of the payment agreement contained tight timeframes that did not permit intensive advance planning. However, these terms did include provisions to address data integrity issues without disadvantaging individual borrowers. As stated in response to recommendation one, we plan to leverage information learned throughout the IFR process and implementation of the payment agreement when planning for similar complex enforcement actions in the future, which would include addressing the potential impact of any data reliability issues as warranted.

The fourth recommendation is that the Divisions finalize an approach to end the payment agreement, including developing, in coordination with the OCC, a strategy to appropriately allocate any funds remaining in the qualified settlement funds (QSFs) that have not been cashed or deposited by borrowers, and continuing efforts to locate uncompensated borrowers. We have already begun working on a plan to end the process for paying in-scope borrowers, including continuing efforts to locate uncompensated borrowers and to appropriately allocate any funds remaining in the QSFs, and have been in discussions with the OCC. As stated in response to recommendation two, we have engaged project management resources to help finalize and implement our plan.

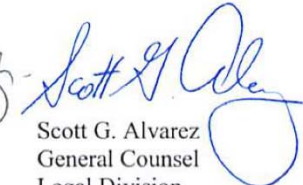
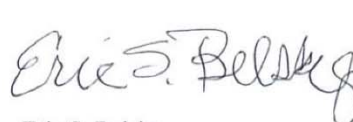
Finally, you recommended that the Divisions, as part of future agreements involving payments to harmed consumers, identify potential options for distributing any residual amounts as part of the planning process. In similar complex enforcement actions in the future, we plan to consider potential options for distributing any residual amounts as part of the planning process.

Thank you, again, for the opportunity to provide comments to this report.

Sincerely,



Michael S. Gibson
Director
Division of Banking
Supervision and Regulation



Eric S. Belsky
Director
Division of Consumer and
Community Affairs

Scott G. Alvarez
General Counsel
Legal Division



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