

FTC Bans Up Front Fees for Loan Modifications

December 31, 2010 - Effective one month from today, the FTC will prohibit firms from charging up-front fees to homeowners seeking a loan modification from their lender. The ban will effectively shut down an industry that has grown up out of the housing bust. While there is no denying that there have been a number of fraud cases associated with loan modification firms, the FTC's ruling is so broad that it may be akin to throwing the baby out with the bathwater; banning consumers from even hiring attorney specifically to secure a modification. The FTC's action raises two concerns. First, who really benefits from the ban? And second, where can consumers turn for advice on securing a loan modification?

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There is no doubt that there have been problems with companies offering loan modification services. The largest complaint from consumers regarding these firms is that some of them charge fees up-front and then never provide any service. Since most firms involved in the loan modification business had little or no government oversight, and because the customers of these firms are often financially desperate, it is an area of the market that was bound to lead to fraud. But was killing the industry entirely really the answer?

The FTC's rule makes no exception to allow states require licensing of loan modification firms. Nevada, which is one of the states that has been most impacted by foreclosures, has such a licensing requirement already. The state also requires firms engaged in loan modifications to post a surety bond and to hold client funds in escrow accounts. The state's legal requirements for these firms have made fraud much more difficult and give the state recourse if it occurs; much the same way they hold real estate brokers, agents, attorneys, physicians, contractors, etcâ€¢ accountable. In fact, when people have an occupational licensing requirement, the remedies available to the state for investigation and prosecution of criminal activity are much better. The FTC didn't take this into account.

The FTC also could have allowed firms to charge up-front fees but required that those fees be held in an escrow account until a modification was completed. But the new rules don't allow for this either. As a result, firms that have done a good job for their clients and which have no complaints are being put out of business.

The rule does make an exception for attorneys involved in bankruptcy cases or other legal activity involving a loan, but it doesn't allow consumers to specifically hire an attorneyâ€¢ or anyone else for that matterâ€¢ to deal directly with lenders for the sole purpose of securing a mortgage modification. This seems excessive. What business is it of the FTC's if a consumer wants to hire a legal professional to negotiate on his or her behalf?

The rule also makes exceptions for some non-profit organizations. These may be the only place for consumers to turn for professional guidance however, the jury is out on what kind of a job these firms will do.

Unfortunately, the real beneficiaries of the FTC's decision may turn out to be lenders! That's because consumers will find it virtually impossible to hire a professional negotiator of any kind to work on getting a mortgage modification. It is very difficult to understand how this benefits consumers in any way and it makes one wonder how much input the banks actually had in the FTC's decision.

by Jim Malmberg

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