

ALLOWABLE ATTORNEY FEES AND OUTSOURCING

1. Purpose. The purpose of this circular is to clarify VA's position on allowable attorney fees and costs of outsourcing foreclosure referral and management services.

2. Background. On February 1, 2008, VA published in the Federal Register (73 FR 6294) extensive changes to part 36 of the Code of Federal Regulations (CFR). In the preamble discussing the evolution of the final rules, VA included a paragraph describing its position on reimbursement for legal services on terminated loans, as follows:

“VA intends to reimburse only for attorney fees for services related to foreclosure of loans. Most of the attorneys commenting on the proposed rule reported that over the past 5 years many servicers have been outsourcing the foreclosure oversight process (i.e., hiring third parties to perform functions previously handled as part of the servicer's routine duties), and firms providing such outsourcing services are charging attorney firms a fee for providing the file needed to initiate the foreclosure action. While VA understands that servicers may find efficiencies in outsourcing certain functions, the cost for such outsourcing must be considered as an operating expense of the firm contracting for the outsourcing; i.e., the servicer. VA cannot consider outsourcing fees to be part of the cost of an attorney fee for completing a foreclosure. Consistent with our proposed rule, VA is establishing maximum amounts for legal services in each State, and those amounts are intended to reimburse for reasonable attorney fees. This is consistent with the position taken by Freddie Mac, which prohibits payment for referral fees, packaging or other similar fees, and new case start-up fees in its Single Family Seller/Servicer Guide, Volume 2, Chapter 71, Section 71.18. Fannie Mae also notes in its 2006 Servicing Guide, Part VIII, Chapter 1, Section 104.03, that it will not reimburse a servicer for legal fees and expenses related to actions that are essentially servicing functions.”

3. Fannie and Freddie Prohibitions. VA naturally looks to actions by large mortgage industry leaders such as Fannie Mae and Freddie Mac in determining best practices and reasonable expenses of loan servicing activities. As investors that own mortgage loans and sub-contract for their servicing, Fannie and Freddie have the ability to establish by contract what they will or will not pay for servicing activities, and also for loan terminations. Fannie and Freddie have separate guide sections to describe the amounts they will reimburse for actual legal services and necessary costs to terminate a delinquent loan. Though servicers often outsource various activities, such as preparation of a package for referral to an attorney for foreclosure, or oversight on the progress of a foreclosure, Fannie and Freddie view those activities as servicing functions covered by the servicing fee. Thus, Fannie and Freddie do not reimburse for outsourcing fees, whether paid by the servicer or by the attorney handling the loan termination.

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4. VA Prohibitions. VA may sometimes be termed an investor by the servicing industry; however, VA is actually a guarantor of loans to veterans. As such, VA does not reimburse for any servicing fees, as those are the responsibility of the loan holder, not a guarantor. VA does allow in a claim under guaranty the reasonable cost of legal services for the termination of a loan, but none of the amounts allowed for legal services are to be paid by either the servicer or the attorney for outsourcing services.

5. Attorney Invoices. Certain parts of a termination process may require the attorney to contract with an outside entity, such as a newspaper for advertising a sale. Similarly, actual out of pocket expenses may be incurred for recording documents related to the termination process. Such costs can be clearly displayed on the attorney's invoice for legal services and actual costs. In fact, general rules of professional conduct require that attorney invoices must itemize outside costs separately from the professional legal services that are billed. VA recognizes that professional legal services fees will naturally include allowances for normal office overhead expenses. However, VA does not consider outsourcing activities as part of those normal office overhead expenses, and will not reimburse for the cost of outsourcing activities, whether directly to the servicer, indirectly on an attorney's invoice for professional legal services, or when considering adjustments in the reasonable cost of legal services.

6. Technology Costs. VA is aware that many servicers are requiring attorneys to use specific technology providers to communicate about loans referred for termination. While the costs of such technology must be considered as office overhead expenses for attorneys, and should provide some benefit to attorneys in managing their caseloads, VA encourages servicers to work with their preferred providers to ensure technology costs are properly distributed based on the benefits received by servicers and attorneys.

7. Additional Information. For a complete copy of the new regulations, please refer to the VA Loan Guaranty website www.homeloans.va.gov/valeri.htm. Questions about this circular may be directed to Carl Wasson at carl.wasson@va.gov.

8. Rescission. This circular is rescinded July 1, 2010.

By Direction of the Under Secretary for Benefits

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