WRITTEN TESTIMONY OF RICHARD A. HARPOOTLIAN

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SENATE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

Mr. Chairman and Members of the Committee,

I thank you for the invitation to speak on behalf of my clients—Captain Jonathon Rowles of the United States Marine Corps and Sergeant George Holloway of the United States Army Reserve. I represent these fine men and women in uniform along with my co-counsel, William Harvey and Graham Newman.

As the committee is aware, our law firms have filed a class action complaint against subsidiaries of JPMorgan Chase alleging systematic violations of rights guaranteed to our men and women in uniform under the Servicemembers Civil Relief Act as it pertains to the financing of real estate. I am pleased to report that after intense negotiations we have reached a settlement with JPMorgan Chase and are currently undertaking the process of informing approximately 6,000 men and women in uniform of their entitlement under the settlement. With this case and settlement serving as a backdrop, I would like to discuss three topics: first, the facts and circumstances leading to the JPMorgan Chase litigation and the pending settlement; second, broader problems in the home finance industry revealed by the litigation; and third, suggestions as to how Congress might address these problems.

I. ***Jonathon Rowles and George Holloway vs. Chase Home Finance, LLC***

As I noted earlier, the litigation in which I and my co-counsel are representing Captain Rowles, Sergeant Holloway, and approximately six thousand military men and women stems from violations of the Servicemembers Civil Relief Act pertaining to home finance. The opening words of the Servicemembers Civil Relief Act establish that the purpose of the law is "to provide for, strengthen, and expedite the national defense through protection extended by this Act to servicemembers of the United States to enable such persons to devote their entire energy to the defense needs of the Nation." The venerable nature of these goals is undeniable. But to truly grasp the importance of the Act to our nation as a whole, one must examine the history of the legislation through the last two centuries.

a. History of the Servicemembers Civil Relief Act

The roots of the Servicemembers Civil Relief Act lie in the Constitution itself. Article I, Section 8 of the Constitution expressly grants to Congress the authority to build and maintain our Armed Forces in order to guarantee the security of this nation. With this in mind, as early as the Civil War Congress recognized the need to enact legislation placing certain restrictions on civil actions that would hinder the abilities of an individual soldier or sailor to dedicate all of his efforts to defending this country. In 1917, as the United States became embroiled in World War I, our government employed the services of Major John Wigmore—then Dean of the Northwestern University Law School and author of the famous treatise Wigmore on Evidence—

to draft the first modern version of the SCRA, then known as the "Soldiers' and Sailors' Civil Relief Act." This Act instituted many of the regulations that are central features of the modern law, including a stay of civil actions and a prohibition of foreclosures upon the homes of those on active duty.

Major Wigmore's Soldiers' and Sailors' Civil Relief Act expired six months after the end of World War I due to a sunset provision included in the law. Thus, in 1940, as conflicts throughout the globe again escalated into World War, Congress reenacted Major Wigmore's bill with some amendments. At the time, Congressman Overton Brooks of Louisiana reiterated the vital role the Act played in preserving the nation's defense and recognized the concerns the Act was intended to address.

> This bill springs from the desire of the people of the United States to make sure as far as possible that men in service are not placed at a civil disadvantage during their absence. It springs from the inability of men who are in service to properly manage their normal business affairs while away. It likewise arises from the differences in pay which a soldier receives and what the same man normally earns in civil life.

The Soldiers' and Sailors' Civil Relief Act has been in effect since it was reenacted by Congressman Brooks and others in 1940.

In April of 2003, as Operation Enduring Freedom in Afghanistan progressed, the 108th Congress styled a complete restatement of the Act. The bill received broad bipartisan support in the House Committee on Veterans' Affairs, boasting as its sponsors then-Chairman Christopher Smith of New Jersey and Ranking Member Lane Evans of Illinois. In its Report to the House, the Committee expressly noted the following:

> Congress has long recognized that the men and women of our military services should have civil legal protections so they can "devote their entire energy to the defense needs of the Nation." With hundreds of thousands of servicemembers fighting in the war on terrorism and the war in Iraq, many of them mobilized from the reserve components, the Committee believes the Soldiers' and Sailors' Civil Relief Act (SSCRA) should be restated and strengthened to ensure that its protections meet their needs in the 21st century.

Among the protections recognized as necessary in modern society were three rights directly implicated in the pending litigation involving my clients: 1) a 6% cap of interest chargeable on debts incurred prior to military service; 2) a prohibition of derogatory reports to credit agencies due to eligibility of SCRA protection; and 3) limitations upon the ability to foreclose upon servicemembers' homes.

Once favorably reported to the House, the bill gained thirty-nine (39) co-sponsors from both parties and was passed by the full House by 425-0. The Senate passed similar legislation with the leadership of Senator Lindsey Graham from my home state of South Carolina and the differences between the two bills were negotiated without need of a conference committee. On December 19, 2003, President George W. Bush signed into law the now-restyled "Servicemembers Civil Relief Act."

b. Experiences of Captain Rowles and Sergeant Holloway

The litigation in which we are involved began after Jonathon Rowles and his wife, Julia, endured several years of frustration regarding their home mortgage with Chase Home Finance, LLC. Our law firms filed this lawsuit on behalf of Captain Rowles in July of 2011. Over the past several months, we have been contacted by numerous military personnel who have experienced similar denials of SCRA protection from Chase's subsidiaries. Last month, we filed an amended complaint, adding allegations on behalf of Sergeant Holloway.

Our research revealed what we believed to be systematic failures in the maintenance of SCRA protections pertaining to three classes of military men and women: 1) those denied the 6% maximum interest rate on debts incurred prior to military service; 2) those who received a blighted credit report as the result of their invocation of SCRA protection; and 3) those whose homes were foreclosed upon despite SCRA protection.

A review of the basic facts pertaining to each plaintiff is helpful in explaining how these violations came about.

In February of 2004, the Jonathon and Julia Rowles entered into a purchase money mortgage with BNC Mortgage, Inc. In May of 2004, Chase Manhattan Mortgage Corporation purchased this loan and, from that point in time, the Rowleses made all payments to Chase. After a year of making payments on this mortgage, Jonathon Rowles executed a United States Marine Corps Reserve contract on August 16, 2005 and received Assignment to Active Duty Orders which became effective on January 22, 2006. Shortly thereafter, Rowles requested in writing that Chase reduce the interest rate on the loan to 6% pursuant to the SCRA. In this letter, Rowles specified January 22, 2006 as the date he entered active duty and produced two sets of orders to verify his current status. Again on May 2, 2006, Rowles wrote to Chase to request the 6% rate protection under the SCRA. This letter also specified Rowles' active duty date and included additional copies of his orders and a copy of his previous letter.

On May 8, 2006, in response to this series of correspondence, Chase requested that Rowles provide "orders and/or an enlistment agreement showing the date of original call to duty." Again Rowles sent faxes to Chase customer service representatives that included handwritten cover sheets explaining his active duty orders as well as copies of his letters of April 14 and May 2. In a letter dated July 27, 2006—seven months after Rowles received his active duty orders—Chase informed Rowles that because he had qualified for the protection of the SCRA, the company had adjusted the interest rate on the loan to 6% effective with his May 1, 2006 payment. However, Chase failed to apply the statutory interest rate to the loan until August 17, 2006, which was the date of the first statement received by Rowles that reflected the 6% rate.

The July 27 letter also informed Rowles that his "loan is protected against late fees, adverse credit reporting, and default activities. These protections will remain in effect for 90 days following your return from active duty."

Though Rowles' SCRA protection had been in place for less than four months, Chase mailed Rowles a letter on December 1, 2007 which it characterized as a "required quarterly verification." The letter included a form which Rowles was instructed to complete and sign in order to continue to receive the protection of the SCRA. Rowles duly completed the form and returned the letter to Chase. Chase sent additional verification letters on December 17, 2008, March 25, June 22 and December 29 of 2009 and March 22, 2010. In addition to the periodic verification letters, no fewer than four times per year since July of 2006, Rowles has had to call various Chase customer service representatives after being verbally informed or receiving documentation indicating that the interest rate on the loan was going to be adjusted above 6% if he failed to do so. In March of 2008, Rowles was forced to request that his commanding officer at Training Squadron Eighty-Six in Pensacola, Florida, write to Chase on his behalf in order to confirm that he was in fact an active duty Marine.

In a letter dated January 16, 2007, Chase again informed Rowles that he had qualified for the protection of the SCRA and that the company had accordingly extended the adjustment on the 6% interest rate effective February 1, 2007. On April 2, 2008, Chase informed Rowles in writing that the company was "in receipt" of his "request for relief" under the SCRA and that he should allow three to four weeks for review of the request. A subsequent letter dated April 25, 2008, again informed him that his rate adjustment would be extended effective October 1, 2008.

From the time that Chase applied the 6% interest rate to the loan until April 2009, Chase would send loan statements to the Rowles family indicating the interest rate charged on their loan was, in fact, substantially above 6%. On information and belief, during this time Chase would use various formulas and accounting methods to reconcile the higher stated interest rates while effectively only charging Rowles at 6%.

This pattern of conduct by Chase caused Rowles to spend considerable time communicating with Chase via telephone, email and written correspondence. This time included leave from his unit which was spent traveling to meet with Chase representatives in an effort to preserve his 6% interest rate under the SCRA and to prevent Chase from taking threatened actions which are unlawful under the SCRA. Finally, in June of 2010, Chase denied Rowles electronic access to his account. Thereafter Rowles brought this suit.

The circumstances giving rise to Sergeant Holloway's allegations are much more brief, but gave rise to an injury perhaps worse than that of Captain Rowles and his family. On March 30, 2000, Holloway purchased a house located in Fountain Inn, South Carolina. At the time of the purchase, Plaintiff Holloway was not on active duty. The purchase was financed by NVR Mortgage Finance, but the loan was thereafter transferred to Chase for servicing. In 2008, Chase initiated foreclosure proceedings against Holloway's home which resulted in a foreclosure sale on May 4, 2009. Holloway was serving on active duty at the time of the sale. Today Sergeant Holloway is serving with the Army Reserve in the Afghanistan theater. His mail is addressed to his parents' home.

c. Details of the Proposed JPMorgan Chase settlement

After Captain Rowles brought to light the potential systematic failure of internal SCRA procedures at JPMorgan Chase, Chase began an extensive internal review to determine the extent of the mistakes made. That review, combined with the efforts of Captain Rowles and Sergeant Holloway, has resulted in a settlement that was reached after several months of intense negotiations that were supervised by a retired federal judge.

While this settlement is awaiting final approval of the District Court—the hearing of which has been scheduled for November 15, 2011—the details of the proposal have been made public. In sum, Captain Rowles, Sergeant Holloway, and Chase have agreed to a benefits package amounting to $48 million of relief to the military men and women who were denied SCRA benefits. This figure amounts to an estimated six times the actual damages suffered by the class members, including refunds of overcharges, full remediation of damage to credit, and remediation of all foreclosure actions.

To its credit, JPMorgan Chase has begun instituting many of these reforms even prior to the final approval of the settlement. Chase has also asked Captain Rowles to serve as an informal advisor to several of its senior officers, providing the company with a "boots on the ground" perspective of how its policies affect our men and women in the military.

II. Systematic Problems Revealed by the *Rowles* Litigation

The immediate effect of SCRA violations on our military men and women are obvious. Unlawful foreclosures force families from their homes. Derogatory reports to credit agencies damage the ability of our soldiers and sailors to enter into future financial agreement. Excessive charges of interest demand monies which are not owed.

Perhaps more damaging than these immediate effects, however, is the financial stress endured by military families while their loved ones serve on active duty. As the stories of Captain Rowles and Sergeant Holloway show, the spouses, parents, and children of our military men and women are those that inevitably bear the brunt of SCRA violations. While her husband was deployed to Korea, Julia Rowles was forced to negotiate with Chase representatives while caring for a small child and pregnant with another. While he was serving in a war zone, George Holloway was powerless to protect his home as foreclosure crept closer.

I began this written testimony by referring to the stated policy of the SCRA: "to enable [servicemembers] to devote their entire energy to the defense needs of the Nation." Violations such as those suffered by our clients directly defeat this purpose. While on active duty, our soldiers have limited time to so much as contact their families. Sadly, it appears that over the past few years several thousand men and women like Captain Rowles and Sergeant Holloway were forced to spend what personal time they did have on the phone with banking officials seeking an explanation why their families were being overcharged interest or why their home was being foreclosed.

Obviously companies like JPMorgan Chase need to do more to ensure that their internal procedures are refined to ensure that all servicemembers entitled to SCRA protection enjoy those rights. As Chase has shown with the settlement terms now pending in federal court, it has made the affirmative decision to lead the way in the financial industry in crafting more reliable SCRA policies and procedures. But based on my experience in this case over the past year, I believe there are measures that Congress can take to produce an atmosphere in which SCRA violations are greatly reduced. Below are three problem areas that can be addressed.

a. Lack of reliable information regarding servicemember status

As Captain Rowles' situation demonstrates, one of the primary problems with SCRA protection is that it can be difficult for the financial companies to determine when the "active duty" status of servicemen ends. As a result, account managers resort to calling the families of men and women in the military to obtain some sort of verification as to whether the borrower in question is, or is not, still "active duty." This repeated contact, however, violates the very spirit of the SCRA.

b. Lack of JAG manpower sufficient to protect civil rights

Many of the SCRA-protected individuals with whom I have spoken have emphasized two things: first, the staff at their bases or posts do an excellent job of educating them on their SCRA rights; but second, once a problem arose with their home mortgages, insufficient staff existed to help these servicemen negotiate resolutions with the various home finance companies.

Our clients and those servicemen I have spoken to all speak very highly of the JAG services that they receive. However, these attorneys are often heavily burdened with other tasks associated with their duty and do not have the ability to dedicate sufficient time to SCRA problems.

c. Lack of incentives to adjust mortgages that can be saved

After my testimony before the House Veterans' Affairs Committee in February, I received phone calls from hundreds of servicemen and women about problems they were experiencing with their mortgage. Some of these folks were entitled to SCRA benefits and some were not. But during my many conversations I noticed a disturbing trend of borrowers who had become no more than a handful of months delinquent on their loans only to be threatened with foreclosure.

There appears to be an atmosphere within the home finance market that incentivizes foreclosures and discourages modifications. Numerous servicemen I spoke with offered to increase their payments over a period of six months or less to become current on their loans. As a matter of routine, however, the financial institutions replied that these men and women immediately pay the balance of the loan—an option that is impossible for almost every American—or face accelerated collections or even foreclosure.

Within the State of South Carolina, this problem has reached epidemic proportions. In fact, on May 9, 2011, our State Supreme Court Chief Justice entered an administrative order dramatically altering the means by which foreclosures are litigated in this State. Now, before any foreclosure proceedings can proceed, a financial institution must certify:

> (a) that the Mortgagor has been served with a notice of the Mortgagor's right to foreclosure intervention for the purpose of seeking a resolution of the foreclosure action by loan modification or other means of loss mitigation;
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> (b) that the Mortgagee, or its designated agent, has received and examined all documents and records required to be submitted by the Mortgagor to evaluate eligibility for foreclosure intervention;
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> (c) that the Mortgagor has been afforded a full and fair opportunity to submit any other information or data pertaining to the Mortgagor's loan or personal circumstances for consideration by the Mortgagee;
>
> (d) that after completion of the foreclosure intervention process, the Mortgagor does not qualify for loan modification or other means of loss mitigation, in accordance with any standards, rules or guidelines applicable to the mortgage loan, and the parties have been unable to reach any other agreement concerning the foreclosure process; and,
>
> (e) that notice of the denial of loan modification or other means of loss mitigation has been served on the Mortgagor by mailing such notice to all known addresses of the Mortgagor; provided, that such notice shall also state that the Mortgagor has 30 days from the date of mailing of notice of denial of relief to file and serve an answer or other response to the Mortgagee's summons and complaint.

A copy of this order has been attached to my testimony for your review. (**Exhibit A**)

III. Suggestions for More Diligent Enforcement of SCRA

The systematic failure of SCRA protections in the Rowles litigation is evidence that the enforcement provisions of the SCRA deserve reconsideration. In our review of the law and its application over the last six months, we believe that there are three areas Congress may improve to strengthen the SCRA in hopes of preventing such failures in the future.

a. Cooperation between the Department of Defense and financial institutions

As noted above, much of the strain suffered by Jonathon and Julia Rowles was the result of continuous contact from JPMorgan Chase officials seeking written verification that Captain Rowles was still on active duty and thus entitled to SCRA protection. There is no provision of the SCRA that permits a financial institution to demand such verification and the Rowles believe that Chase was overly aggressive in pursuing it. At the same time, however, JPMorgan Chase and other financial institutions undoubtedly wish to protect themselves from the potential of fraud, namely a servicemember continuing to receive SCRA benefits long after he or she has been deactivated.

A solution for this quandary could be found in the creation of a liaison office within the Department of Defense designed to work with financial institutions to certify when servicemembers are—or are not—on active duty. Such an office would provide the financial institutions with the information needed to determine whether to apply SCRA protections while relieving the servicemembers and their families from the burden of continuously updating their status.

b. Stronger emphasis on legal support for servicemembers

Every single class member with whom I have spoken has noted his or her gratitude for the assistance they have received from JAG officers. However, it appears that JAG is often unable to render remedial SCRA support to servicemen that experience problems with their home loans.

This could be due to several reasons. Obviously lack of manpower hinders any ability to respond to this type of situation. But also, JAG officers may not be licensed to practice in the civilian courts in which their fellow soldiers are experiencing difficulty. For example, a JAG officer assigned to Fort Jackson, South Carolina may receive an SCRA question from a solider about to lose his home to foreclosure in California. It would be highly unusual for that South Carolina-based officer to be licensed to appear on behalf of the soldier in the State of California to contest the foreclosure. Even if the officer was licensed to do so, transporting him or her across the country for this one event may not be practical.

In my opinion, Congress should examine two possibilities that may alleviate this situation. First, determine whether JAG possesses sufficient manpower to adequately address remedial needs of servicemen who need to assert their SCRA protections. Second, examine partnership efforts that can be formulated between JAG and State bar associations who would be, I am sure, willing to offer pro bono services to the military in order to help enforce SCRA rights.

c. Incentivize mortgage modification and discourage foreclosure

Congress should reexamine the incentives in place that either encourage, or discourage, loan modifications. As I noted above, many servicemen have offered to accelerate their loan payments over a series of months in order to become current on their obligations to the various financial institutions. Yet they report what seems to be a disturbing trend of preferring foreclosure and/or collections to preserving the terms of a loan.

Federal insurance of mortgages may contribute to this reverse incentive. While the specifics of mortgage finance are not my professional specialty, it appears that the guaranteed payment financial institutions receive from entities such as FHA may be encouraging foreclosure rather than loan modification. While I in no way suggest that such programs be terminated, I do think that considering modifications to these programs that would incentivize loan modification could alleviate many of the problems that servicemembers are now facing with their mortgages. Consideration of several prerequisites to foreclosure as instituted by the South Carolina Chief Justice (see **Exhibit A**) may serve as a useful starting point.

CONCLUSION

I would again like to thank the Committee for the opportunity to speak on behalf of our clients and on behalf of the thousands of servicemen and servicewomen who have fallen victim to SCRA violations in the last several years. As the SCRA recognizes, its protections are essential to our national defense. It is my hope that Congress will take all steps necessary to ensure the continuing vitality of this law.