

Legislative Analysis



FORECLOSURES: MORTGAGE MODIFICATIONS

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House Bill 4453 (Substitute H-1)
Sponsor: Rep. Shanelle Jackson

House Bill 4454 (Substitute H-1)
Sponsor: Rep. Andy Coulouris

House Bill 4455 (Substitute H-1)
Sponsor: Rep. Bert Johnson
Committee: Banking and Financial Services

First Analysis (3-11-09)

BRIEF SUMMARY: Together, the bills would create a mechanism by which borrowers who are behind on their mortgage payments could negotiate with the lender (or the party holding the mortgage) to modify the mortgage loan and stay a foreclosure while the negotiations were in process.

FISCAL IMPACT: The fiscal impact of the bills would be indeterminate. A more detailed discussion follows later in the document.

THE APPARENT PROBLEM:

Announcements on the latest foreclosure statistics continue to dominate the media on an almost daily basis, such as a *Lansing State Journal* headline just a week ago proclaiming “More than 1 in 10 Mich. mortgages past due” and that Michigan continues to be one the five hardest hit states in the nation. Though foreclosures driven by subprime mortgages appear to be declining, families with prime rates are seeing increased foreclosure numbers as unemployment increases.

Regardless of the reasons for falling behind on house payments, foreclosures affect more than the family at risk of losing their home. Foreclosures impact neighborhoods – contributing to blight and lowering property values for surrounding homes; municipalities are affected as revenue from property taxes decrease; local businesses see decreased sales, and so the ripples spread. Obviously, if more people in danger of losing their homes could find a way to pay their mortgages, everyone would benefit.

During months of discussions and workgroups involving various stakeholders such as lenders and advocacy groups, one element stood out – communications between lenders and borrowers behind in their house payments are poor to nonexistent. Many lenders expressed a desire to see if foreclosure could be avoided only to have repeated phone calls and letters go unanswered. Borrowers, on the other hand, were often afraid to contact lenders, tried but couldn’t connect with the person who could help negotiate a

solution, or were inundated with foreclosure relief scams to the point that it became difficult to know who to trust.

From those discussions and workgroups, a plan was devised to encourage better interaction and communication between lenders and borrowers behind on mortgage payments.

THE CONTENT OF THE BILLS:

The bills would seek to stem the number of mortgage loans defaulting by encouraging communication between lenders and borrowers who were behind in their mortgage payments. Foreclosure proceedings would be postponed for 90 days upon a borrower requesting a meeting with the lender, written notices regarding foreclosure sales would have to be given via first-class mail, and the respective duties of borrowers and lenders in the negotiation process would be set forth.

The bills also would: require a foreclosure to go before a judge in some instances; allow a borrower to seek injunctive relief or to convert a foreclosure to a judicial foreclosure if the lender did not fulfill certain requirements; require MSHDA to develop a list of housing counselors to assist borrowers; and repeal the new process two years after the bills' effective date.

The bills would each amend the Revised Judicature Act (MCL 600.101 et seq.) and are tie-barred to each other, meaning that none could take effect unless all three were enacted.

House Bill 4453 would add new language to the act to specify situations under which a foreclosure proceeding by advertisement on a borrower's principal residence could not go forward. For instance, if a borrower requested a meeting with the mortgage holder or loan servicer, the proceeding would be stayed for 90 days from the date of service of a notice as required under House Bill 4454 from the foreclosing party.

The bill would only apply to those foreclosure proceedings under Chapter 32 (Foreclosure by Advertisement) in which the first notice in a newspaper had been published after the bill's effective date and before two years after the effective date. The bill would also define the terms "borrower," "FDIC workout program," "mortgage holder," and "mortgage servicer."

House Bill 4454 would add two new sections (Section 3205a and 3205b) to require a foreclosing party to serve written notice, as specified in the bill, on the borrower before proceeding with a sale by advertisement of the borrower's principal residence. The bill would require two copies of the notice to be delivered to the borrower – one by first-class mail and the other by certified mail, return receipt requested, both to the borrower's last known address.

Among other things, the notice would have to contain the names and contact information of the mortgage holder and the mortgage servicer along with a statement of which entity to contact with the authority to make agreements under provisions of House Bill 4455. Included with the notice would be a list of HUD- or MSHDA-approved housing counselors prepared by the Michigan State Housing Development Authority (MSHDA). A borrower who did not receive the required notice could bring an action in circuit court to enjoin the foreclosure if a foreclosure proceeding had been started.

The bill would also specify the duties and responsibilities of the borrower and housing counselor if the borrower wished to pursue negotiations to modify a loan. These provisions would not apply to a borrower who had previously agreed to a loan modification but had not complied with the modified loan terms for one year after the date of the modification.

House Bill 4455 would also add new sections to the act (Sections 3205c, 3205d, and 3205e). The bill would require a modified payment amount under the FDIC workout program to be calculated if the process established by House Bills 4453 and 4454 did not result in an agreement to modify the mortgage loan.

If the calculation showed the borrower was eligible for a modification, the foreclosing party could not proceed with a foreclosure by advertisement, but could proceed with a judicial foreclosure under Chapter 31 of the act. However, if the calculation showed the borrower was eligible for a modification without an exception, the mortgage holder or lender could foreclose by advertisement.

If foreclosure proceedings were begun in violation of the above provision, the borrower could file an action in circuit court to convert the foreclosure proceeding to a judicial foreclosure. A court would have to enjoin foreclosure by advertisement and order it to proceed as a judicial foreclosure if the borrower had participated in the negotiating process, a modification agreement could not be reached, and the borrower was eligible for modification under the FDIC workout program.

The above provisions would not apply to a borrower who had previously agreed to a loan modification but had not complied with the modified loan terms for one year after the date of the modification.

Further, the bill would repeal Sections 3205a to 3205d two years after this bill's effective date.

FISCAL INFORMATION:

The bills would have no fiscal impact on the Michigan State Housing Development Authority.

The bills would have an indeterminate fiscal impact on the judiciary. Although not all foreclosure proceedings go through a judicial process, the borrower's ability to delay

foreclosure proceedings may reduce the number of foreclosure proceedings in the circuit court, thereby reducing the caseload and associated costs. Reduction in the caseload could also reduce revenue received from filing fees paid to the local funding unit and civil filing fee fund.

Because it is not known which properties would benefit, the impact on tax revenue cannot be determined. To the extent that foreclosures and the corresponding reductions in taxable values are averted, property tax revenues (including revenue from the 6-mill State Education Tax that is dedicated to the School Aid Fund) would be higher than what would have otherwise occurred.

ARGUMENTS:

For:

The bill package would address one of the most troubling aspects of foreclosure – the inadequate communication between lenders and borrowers. Communication that perhaps would lead to negotiated loan modifications that would keep a family in their home. Too often, fear, shame, denial, or lack of knowledge regarding the foreclosure process keeps borrowers from contacting their lenders. For others, including trained housing counselors assisting borrowers to avoid foreclosure, trying to find the person who has the authority to negotiate a loan modification can be difficult at best and near impossible at worst.

The committee-passed bills attempt to address concerns of all stakeholders. For example, the bill would require lenders to notify a borrower in writing prior to advertising the home as a foreclosure. In addition to many pertinent pieces of information, the notice would also have to include the name of the business person, along with contact information, who had the authority to negotiate a loan modification. In addition, a MSHDA-prepared list of state and federal approved housing counselors, who can help borrowers navigate the loan modification process, would have to be provided with the notice. A notice could be delivered by mail instead of the more costly and slower personal service of process as in the introduced version.

Once the notice was mailed, the ball would be in the borrower's court to contact the lender. The foreclosure proceeding would be stopped for 90 days if the borrower requested a meeting with the lender in order to give time for discussions on alternatives to foreclosure. If the borrower failed to respond, the lender could go forward with the foreclosure proceeding.

The legislation would not mandate a lender to modify every delinquent loan. However, it would mandate communication between the lender and borrower and encourage lenders to use a federal model to determine if a loan modification would save the lender money over foreclosing on the property. A lender who opted to foreclose rather than modify the loan would have to use a slower and more costly court process if the model showed a loan modification would indeed save the lender money.

The bills are not expected to unduly increase the time that lenders would have to carry the debt from a delinquent loan - indeed, the requirement to proceed under a judicial foreclosure would only be triggered when a lender opts to ignore an FDIC model calculation that a loan modification would save the lender money over foreclosing. If the borrower cannot meet even a reduced monthly payment obligation, the lender is free to pursue foreclosure by advertisement.

It is important to note that this legislation, along with elements of the new federal plan to keep more homeowners in their homes, will not save every borrower from losing his or her home. The legislation will not help those who are unemployed, or who have large debts due to illness, gambling, or other reasons. If a person has insufficient monthly revenue to make even a lower, modified payment, no program can save their home from foreclosure. However, in conjunction with new federal programs, the bills may indeed help facilitate the communication that could successfully keep a significant number of borrowers in their homes.

Against:

Lenders still have some concerns that the bill package may unduly delay an otherwise unavoidable foreclosure, especially if forced to go through the courts. The bill is also silent as to when they can proceed with a foreclosure if the notice sent by certified mail is returned as undeliverable. In some instances, the borrower has simply walked away from the property and not left a forwarding address.

Consumer advocates have also expressed concerns that borrowers who previously entered into a loan modification within the last year and have since defaulted on that loan would be excluded from the bill's foreclosure protections. Some loan modifications may have been unworkable from the start, setting the borrower up for failure. Not all borrowers had the knowledge of or assistance from housing counselors, some may have entered into new terms under duress, and some may have fallen prey to foreclosure rescue scams. Each situation should be looked at on a case-by-case basis to see if under current circumstances, a workable loan modification can be achieved.

POSITIONS:

Michigan Legal Services (anti-poverty advocates) supports the bills. (2-26-09)

Michigan Advocacy Project supports the bills. (2-26-09)

A representative of the Michigan Credit Union League testified in support of the bills. (3-5-09)

A representative of the Michigan Municipal League testified in support of the bills. (3-5-09)

A representative of the Michigan State Housing Development Authority (MSHDA) testified in support of the bills. (2-26-09)

A representative of the Michigan Foreclosure Task Force testified in support of the bills. (2-26-09)

A representative of ACORN testified in support of the bills. (2-26-09)

The Community Economic Development Association of Michigan (CEDAM) indicated support. (2-26-09)

AARP indicated support for the bills. (2-26-09)

A representative of the Michigan Mortgage Lenders Association and Michigan Financial Services Association testified in support of the concept of the bill package. (2-26-09)

Michigan Association of Community Bankers testified that the association had a position of neutrality on the bill package. (2-26-09)

The Michigan Bankers Association indicated opposition to the bills in their current form. (3-5-09)

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.