

## FORECLOSURES: MORTGAGE MODIFICATIONS

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**House Bill 4453 as enrolled**  
**Public Act 29 of 2009**  
**Sponsor: Rep. Shanelle Jackson**

**House Bill 4454 as enrolled**  
**Public Act 30 of 2009**  
**Sponsor: Rep. Andy Coulouris**

**House Bill 4455 as enrolled**  
**Public Act 31 of 2009**  
**Sponsor: Rep. Bert Johnson**  
**Committee: Banking and Financial Services**

### **First Analysis (9-30-09)**

**BRIEF SUMMARY:** Together, the bills would create a mechanism by which borrowers who are behind on their mortgage payments could negotiate with the party holding the mortgage to modify the mortgage loan and stay a foreclosure for up to 90 days 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 this past March proclaiming “More than 1 in 10 Mich. mortgages past due” and that Michigan continues to be one of 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 those at risk of losing the family 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 mortgage holders and borrowers behind in their house payments are poor to nonexistent. Lenders expressed a desire to see foreclosures be avoided, but said they often had

repeated phone calls and letters to delinquent borrowers go unanswered. Borrowers, on the other hand, were often afraid or too ashamed to contact lenders, attempted to reach the mortgage holder but couldn't connect with an employee having authority to 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 decrease the number of homes entering foreclosure by encouraging better interaction and communication between mortgage holders and borrowers who fall behind on mortgage payments.

### ***THE CONTENT OF THE BILLS:***

The bills seek to stem the number of mortgage loans defaulting by encouraging communication between mortgage holders and servicers and borrowers who are 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 both parties in the negotiation process would be set forth.

The bills also: 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 mortgage holder did not fulfill certain requirements; require the Michigan State Housing Development Authority (MSHDA) to develop a list of housing counselors to assist borrowers; and address situations in which the notification process does not result in a loan modification. The provisions creating the new loan modification process would be repealed two years after the bills' effective date.

The bills each amend the Revised Judicature Act and are tie-barred to each other, meaning that none could take effect unless all three were enacted. The bills took effect on July 5, 2009 and will be repealed two years later on July 5, 2011.

### **House Bill 4454**

The bill adds two new sections (MCL 600.3205a and 600.3205b) to require a foreclosing party to serve written notice on the borrower before proceeding with a sale by advertisement of the borrower's principal residence. (See ***Background Information*** for more information on the types of foreclosures allowed under Michigan law.) The bill also specifies the duties and responsibilities of the borrower and housing counselor if the borrower wished to pursue negotiations to modify a loan.

**Notice to borrowers.** The bill requires two copies of a notice to be mailed to the borrower by the foreclosing party – 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 must contain:

**\*\* The reasons the loan is in default and the amount due.**

**\*\* The names and contact information of the mortgage holder, the mortgage servicer, or a designee along with a designation of which entity or person to contact that has the authority to make agreements under provisions of House Bill 4455 (hereinafter, *designated contact person*).**

**\*\* That the borrower can request a meeting to work out a loan modification with the designated contact person within 14 days after the notice had been sent. The borrower can also request that a housing counselor be in attendance.**

**\*\* That if a meeting is requested, foreclosure proceedings cannot be commenced until 90 days after the date the notice was mailed.**

**\*\* That if an agreement was reached, the mortgage will not be foreclosed as long as the borrower satisfies the terms of the modification agreement.**

**\*\* That if an agreement to modify the mortgage cannot be reached even though the borrower was eligible for a modification, that under certain conditions, the foreclosure would be before a judge instead of by advertisement.**

**\*\* That the borrower has the right to contact an attorney, along with the telephone numbers of the State Bar of Michigan's lawyer referral service and a local legal aid office in the area in which the property is situated.**

A list of HUD- or MSHDA-approved housing counselors prepared by MSHDA would have to be included with the notice. 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.

**Applicability.** The bill applies to a property claimed as a principal residence that is exempt from tax under the homestead property tax exemptions of the General Property Tax Act (MCL 211.7cc). (This is an owner-occupied primary residence.) A borrower who previously modified a mortgage loan under the bill would be eligible to have the loan modified again under the provisions of the bill and House Bill 4455 as long as he or she had complied with the terms of the previous loan modification for one year after the date of the modification.

**Responsibilities of a borrower.** A borrower who wishes to participate in negotiations to attempt to work out a mortgage modification must contact a housing counselor from the provided list within 14 days after the notice was mailed (not the date the notice was received). The borrower must also provide copies of any documents necessary to determine eligibility for a loan modification under provisions of House Bill 4455 if so requested by the mortgage holder.

**Duties of a housing counselor.** A housing counselor must inform, in writing, the designated contact person having authority to modify the loan within 10 days of a borrower's request to negotiate a mortgage modification. The counselor would be

required to schedule a meeting between the borrower and the designated contact person. If requested by the borrower, the housing counselor would also have to attend the meeting. All meetings would be held at a time and place convenient to all parties, or in the county where the property was situated.

**Responsibilities of the foreclosing party.** Before proceeding with a sale under Chapter 32 (Sale by Advertisement) of a principal residence, the foreclosing party must mail a notice as described above. Within seven days after mailing the notice to the borrower, the person who mailed the notice must publish a notice informing the borrower of his or her rights under the bill's provisions. The information must be published one time in the same manner as for foreclosures by advertisement. (The current requirement is that the notice must be published in a newspaper that is published in the county where the premises intended to be sold, or some part of them, are situated. If no newspaper is published in the county, the notice must be published in a newspaper published in an adjacent county. In every case within 15 days after the first publication of the notice, a true copy shall be posted in a conspicuous place upon any part of the premises described in the notice.)

This published notice is required to list the borrower's name and address and a statement informing the borrower that he or she has the right to request a meeting with the mortgage holder or servicer; the name of the designated contact person having the authority to modify the loan; the right to contact a housing counselor by calling MSHDA or visiting MSHDA's website; the web address and phone number for MSHDA; that requesting a meeting with the designated contact person will stay the foreclosure proceedings for 90 days from the date the other notice was mailed to the borrower; and that the borrower has the right to contact an attorney, along with the phone number of the State Bar of Michigan's lawyer referral service.

### **House Bill 4453**

The bill adds new language to the act (MCL 600.3204 and 600.3205) to specify situations under which a foreclosure proceeding by advertisement on a borrower's principal residence could not go forward.

Specifically, the bill prohibits a party from commencing a foreclosure by advertisement on a borrower's principal residence if one or more of the following apply:

- Notice has not been mailed to a borrower as required by House Bill 4454.
- The 10-day time period for a housing counselor to request a meeting with the designated contact person on behalf of the borrower has not expired.
- The borrower has requested a meeting with the designated contact person within the 14-day time period after the notice had been mailed, and the 90 days since the notice was mailed has not expired.
- The borrower requested a meeting with the designated contact person, provided requested documents to that person, but the contact person has not met or negotiated with the borrower.

- The borrower and mortgage holder or servicer have agreed to modify the mortgage and the borrower is not in default under the modified agreement.
- Calculations under provisions of House Bill 4455 show that the borrower is eligible for a loan modification, and foreclosure by advertisement is not allowed under a provision of that bill that restricts a foreclosure from proceeding unless certain conditions are satisfied.

The bill would only apply to foreclosure by advertisement proceedings 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," "mortgage holder," and "mortgage servicer."

### **House Bill 4455**

This bill would also add new sections to the act (MCL 600.3205c, 600.3205d, and 600.3205e). The bill addresses those situations in which the process established in House Bill 4453 does not lead to a mortgage loan modification, requires MSHDA to develop the list of housing counselors eligible to perform the duties under House Bills 4454 and 4455, and repeals the provisions of House Bills 4454 and 4455 two years after taking effect (July 5, 2011).

Specifically, if a borrower contacted a housing counselor under provisions of House Bill 4454, but the process established by that bill did not result in an agreement to modify the mortgage loan, the mortgage holder's or servicer's designated contact person would be required to work with the borrower to determine if he or she qualified for a loan modification. With some exceptions, the determination must be made using a loan modification program or process that includes all of the following features:

- The program or process targets a ratio of the borrower's housing-related debt to his or her gross income of 38 percent or less, on an aggregate basis. "Housing-related debt" includes mortgage principal and interest, property taxes, insurance, and homeowner's fees.
- In reaching the 38 percent target, the program or process includes an interest rate reduction (as needed) subject to a floor of three percent for a fixed term of at least five years; amortization term extension of the loan to 40 years or less from the date of the loan modification; deferral of some portion of the unpaid principal balance of 20 percent or less, until the loan matures or is refinanced or the property is sold; and/or late fees are reduced or eliminated.

This would not apply to a mortgage loan pooled for sale to an investor that is a governmental entity or a mortgage loan that has been sold to a government-sponsored enterprise (e.g., Fannie Mae or Freddie Mac). In either of those cases, the designated contact person must follow the modification guidelines dictated by the entity or enterprise when determining a borrower's eligibility for a loan modification.

The bill also permits the borrower and designated contact person to agree to a loan modification on other terms or other loss mitigation strategy instead of using modification.

The designated contact person must provide the borrower with a copy of any calculations made in determining the borrower's eligibility for a loan modification as well as, if requested by the borrower, a copy of the program, process, or guidelines under which the determination was made.

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 not eligible for a modification, the mortgage holder or servicer could foreclose by advertisement.

The mortgage holder or servicer could also foreclose by advertisement when a borrower was eligible for a modification if the designated contact person had in good faith offered the borrower a modification agreement prepared in accordance with the modification determination and, for reasons not related to any action or inaction of the mortgage holder or mortgage servicer, the borrower did not execute and return the modification agreement within 14 days after receiving the agreement.

If foreclosure proceedings began 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 court determined that the borrower participated in the negotiating process, a modification agreement was not reached, and the borrower is eligible for modification (and the above exclusion did not apply).

MSHDA would be required to develop the list of HUD-approved or MSHDA-approved housing counselors who could perform the duties of housing counselor under the provisions of House Bills 4454 and 4455.

Further, the bill would repeal Sections 3205a to 3205d (added by House Bills 4454 and 4455) two years after this bill's effective date (July 5, 2011).

#### ***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.

## ***BACKGROUND INFORMATION:***

### **Foreclosures in Michigan**

Under the Revised Judicature Act, two methods are used to foreclose on a property: judicial foreclosure (Chapter 31) and foreclosure by advertisement (Chapter 32). Both processes give the borrower an opportunity to recover, or “redeem,” the property after a foreclosure sale, by paying the redemption amount and required fees, but the procedures and timelines are different.

Judicial foreclosure (Chapter 31) involves the filing a foreclosure action in the circuit court. When a complaint is filed, the court determines the amount of the debt that is due and has the power to order a sale of the premises. The court may not order the sale within six months after the complaint is filed. The borrower then has six months after the sale to redeem the premises by paying the amount that was bid plus interest.

If a mortgage of real property defaults, it may be foreclosed by advertisement if the mortgage document contains a “power of sale.” This process requires the mortgage holder or servicer to post a notice conspicuously on the premises and publish it once a week for four successive weeks in a newspaper published in the county where the premises are located or, if there is no newspaper in that county, in a paper in an adjacent county. The notice must contain specified information including the amount claimed to be due and the length of the redemption period. If the property is sold at a foreclosure sale, the borrower may redeem the property by paying the redemption amount and required fees within the applicable period. The redemption period for a sale by advertisement varies from one month, three months, or six months depending on such factors as the size and type of the property, the percentage of the original debt still owed, and whether the property had been abandoned.

Both Chapter 31 and Chapter 32 allow a court to issue a deficiency judgment against the borrower for the amount of the debt not paid by the sale of the premises.

### **Federal loan modification programs**

FDIC Workout Program. The FDIC loan modification program was originally initiated for IndyMac Federal Bank to aid borrowers who occupy their home and who are financially unable to meet the current (or scheduled adjusted) terms of their mortgage by

providing an affordable and sustainable modification of the loan terms. The systematic and streamlined loan modification program, known as “mod in a box,” also provides a guide for other financial institutions in creating their own loan modification programs. The FDIC Workout Program is primarily based on two principles:

- 1) Determining a payment the borrower can afford by multiplying the borrower’s gross monthly income times the appropriate housing-to-income ratio, less taxes and insurance, to achieve a minimum payment reduction of 10 percent; and,
- 2) Protecting investor’s interests by requiring that the cost of the modification is less than the estimated cost of foreclosure.

The process includes reducing the interest rate to as low as three percent and extending, if necessary, the amortization and/or term of the loan to 40 years to reach a housing-to-income ratio of 31 percent to 38 percent. For more information, go to [www.fdic.gov](http://www.fdic.gov), click on Consumers and Communities under the Quick Link menu, then under Real Estate, Housing & Loans, click on Foreclosure Prevention.

Homeowner Affordability and Stability Plan. Created earlier this year, the affordability component seeks to provide access to low-cost refinancing for homeowners who have not defaulted on their loans but who have not been able to secure refinancing due to falling home prices that leave them with low to negative equity. The plan applies to mortgages on owner-occupied homes owned or guaranteed by Fannie Mae or Freddie Mac.

The Homeowner Stability Initiative component targets at-risk homeowners by financially sharing in loan modification programs offered by mortgage lenders and servicers in order to reduce interest payments, provide financial incentives to both servicers and borrowers, create clear and consistent guidelines for loan modifications, require participation by Financial Stability Plan participants, allow judges to modify mortgages during bankruptcy, strengthen other federal programs such as the Hope for Homeowners Program, and support local communities and help displaced renters. Additional information can be found at [www.makinghomeaffordable.gov](http://www.makinghomeaffordable.gov) or [www.treas.gov](http://www.treas.gov) and typing in “Homeowner Affordability and Stability Plan” in the search window.

Michigan State Housing Development Authority (MSHDA). For more information on help for struggling homeowners, visit the MSHDA web site at [www.michigan.gov/mshda](http://www.michigan.gov/mshda) and click on the Save the Dream icon, or call toll-free 866-946-7432.

## ***ARGUMENTS:***

### ***For:***

The bill package would address one of the most troubling aspects of foreclosure – the inadequate communication between mortgage holders and borrowers; communication that perhaps could 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 the foreclosing party. For those who do try, trying to find the person who has the authority to negotiate a loan modification can be



difficult at best and near impossible at worst. With the current practice of mortgage loans being bundled and sold as investments many times over, even experienced housing counselors, who assist borrowers in avoiding foreclosure, can have difficulty determining the owner or servicer of a particular mortgage loan.

For borrowers, the legislation makes it easier to know who to contact to discuss a loan modification and the time period in which contact must be made. It slows the foreclosure process to no more than 90 days from the date the notice to foreclose was mailed by the mortgage holder to provide time to seek a loan modification agreement. The borrower would be provided with a list of state and federal housing counselors approved by MSHDA and the phone number of the State Bar of Michigan's lawyer referral service. A borrower could also sue to stop a foreclosure by advertisement and move the proceedings before a judge if a mortgage holder violated the bills' notification and modification requirements. In addition, a borrower who had a mortgage loan modified under provisions of House Bill 4454 could do so again as long as the terms of the modified mortgage loan had been complied with for at least one year. These are important information and protection pieces that should encourage more delinquent borrowers to seek assistance rather than just giving up or walking away from their properties.

For mortgage holders, the legislation allows the notice to be mailed rather than paying a process server to personally serve the notice on the borrower, and allows the foreclosure proceedings to go forward if the borrower does not respond within 14 days of the notice being mailed. Most foreclosure proceedings would still be by advertisement; the requirement for judicial foreclosures would be limited to those instances in which a borrower was eligible for a loan modification under criteria outlined in House Bill 4455, but the mortgage holder or servicer did not agree to a modification. Moreover, if the borrower is not eligible for a loan modification because he or she cannot meet even a reduced monthly payment obligation, the mortgage holder would be free to pursue foreclosure by advertisement. Therefore, the bills are not expected to otherwise unduly increase the time that mortgage holders would have to carry the debt from a delinquent loan.

It is important to note that this legislation, along with the new federal plans 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 a home from foreclosure. However, by facilitating communication between mortgage holders and borrowers before foreclosure proceedings are begun, and basing loan payments on a reasonable housing-related debt to income ratio, the legislation could successfully keep a significant number of borrowers in their homes.

***For:***

The bill package represents several important compromises that balance the needs of borrowers with fairness towards financial institutions and mortgage holders. For example, consumer advocates have expressed concerns that borrowers who previously

entered into a loan modification and have since defaulted on that loan would be excluded from the bill package'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. By being silent in regards to loan modifications between borrowers and mortgage holders that predate the legislation, it would appear that a struggling borrower who had previously modified his or her mortgage loan under some other program or policy would not be disqualified from inclusion in the legislation's notice and negotiation provisions.

However, House Bill 4454 specifically restricts the ability of a borrower who enters into a mortgage loan modification under the legislation from re-modifying that loan to only those who were able to comply with the terms of the first modification for a year. Thus, those engaging in the business of home mortgages would not be unduly burdened with a seemingly endless attempt by some borrowers to prolong an inevitable foreclosure.

In addition, though new federal programs also provide struggling homeowners with relief, they primarily target borrowers who have not yet defaulted on their mortgage loans. Therefore, this legislation provides needed help for those who are beyond what other programs can offer.

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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.