

Litigating and Other Strategies to Help Reverse Mortgage Surviving Spouses

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- See upcoming trainings, conferences, and webinars
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Presenter – Sarah Bolling Mancini

- Sarah is Of Counsel for NCLC half-time, focusing on foreclosures and mortgage lending, and works half-time as an attorney in the Home Defense Program of Atlanta Legal Aid.
- She has experience representing homeowners in bankruptcy cases and litigating in state, federal district, and bankruptcy courts.
- Sarah is a member of the Georgia Bar. She received her B.A. in public policy from Princeton University and her J.D. from Harvard Law School.





Presenter – Rachel Scott

- Rachel Scott is an attorney with the Senior Citizens Law Project of the Atlanta Legal Aid Society, focusing on foreclosures, mortgage lending, and real estate issues affecting seniors.
- She clerked for the Honorable Henry Coke Morgan, Jr., U.S. District Court for Eastern District of Virginia, Norfolk.
- Rachel received her B.A. in mathematics from Agnes Scott College and her J.D. from Atlanta's John Marshall Law School, where she graduated first in her class.





Moderator – Odette Williamson

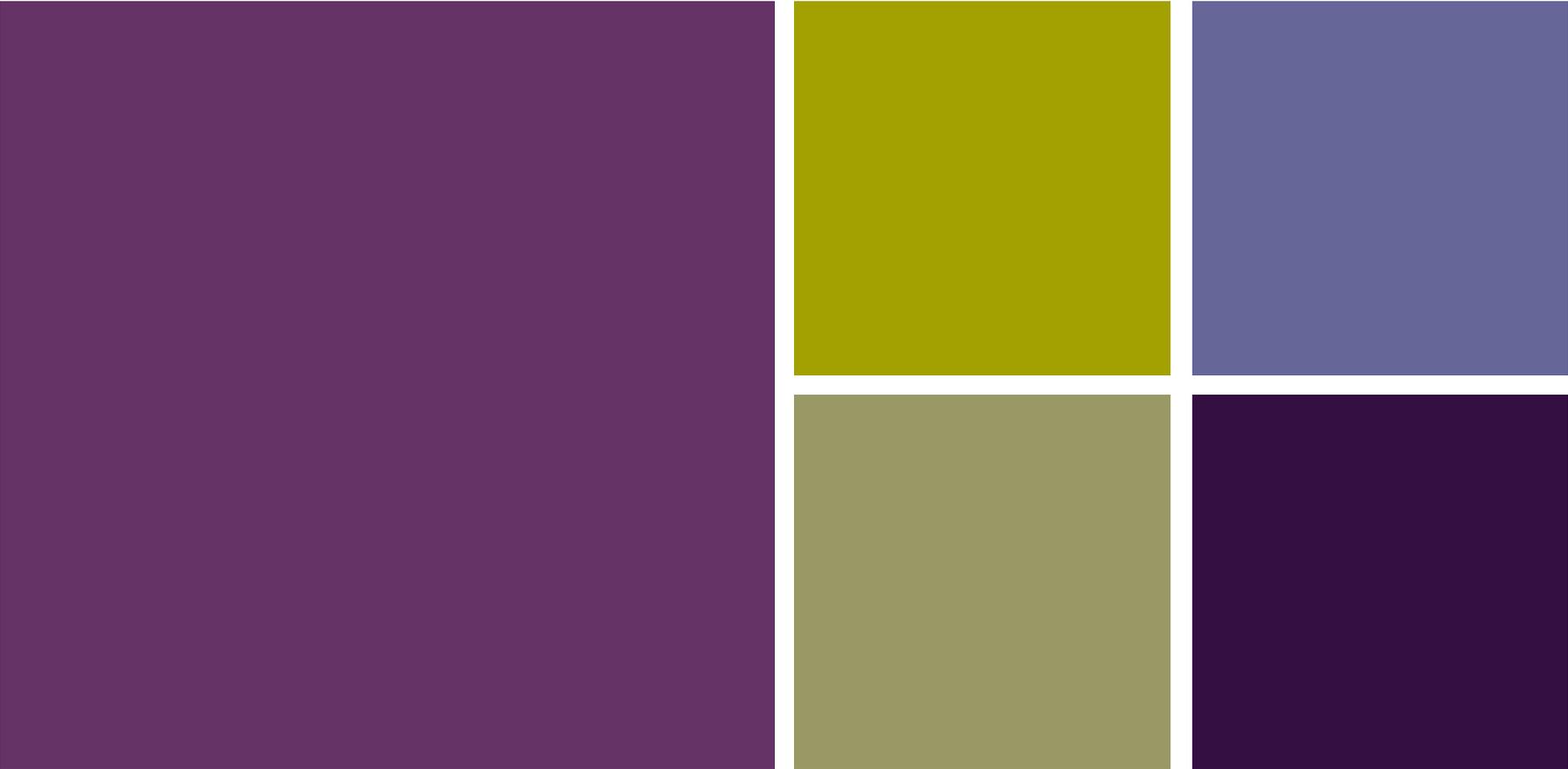
- Odette has been a staff attorney at NCLC since July, 1999. Prior to this she was an Assistant Attorney General in the Massachusetts Office of the Attorney General.
- As an AAG she also served on the Elder Law Advocates Strike Force to combat unfair and deceptive acts against elderly citizens. Odette attended Tufts University and Boston College Law School and is co-author of NCLC's Foreclosures, and Foreclosure Prevention Counseling.



Reverse Mortgage

- Reverse Mortgage Survey
 - Non-borrowing surviving spouses
 - <https://www.surveymonkey.com/r/LL3MYCN>
- Send us your pleadings and other materials
- Advice and assistance
 - National Legal Resource Center
 - http://nlrc.acl.gov/index.aspx#service_dev





Litigation and Other Strategies to Help Reverse Mortgage Surviving Spouses

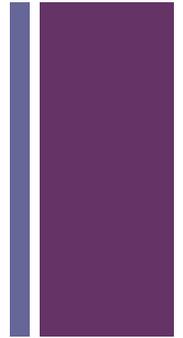
Sarah B. Mancini, Of Counsel, NCLC
J. Rachel Scott, Atlanta Legal Aid Society, Inc.

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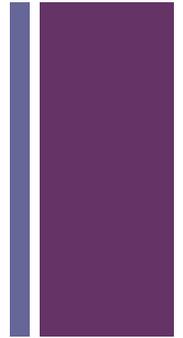
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Overview

- Status of Plunkett v. Castro
- Mortgagee Letter 2015-03
- Practical Case Selection Concerns
- The MOE and calculating the PLF test
- Litigating against HUD – claims, strategy, defenses, settlement



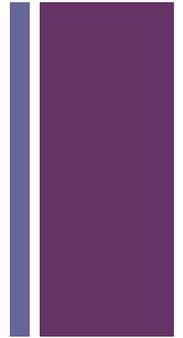
Reverse Mortgage Basics



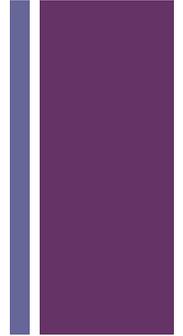
- FHA-insured Reverse Mortgages – the Home Equity Conversion Mortgage (HECM); borrower must be ≥ 62
- No monthly payments of principal or interest; interest and servicing fee is added to the loan balance each month
- Loan comes due upon a trigger event – death or non-occupancy
- Loan balance may grow to exceed value of the house (insurance; nonrecourse loan)
- Initial principal amount loaned is based on:
 - Appraised value of the house
 - Prevailing interest rates
 - Age of the youngest borrower (older = higher loan proceeds)

“Principal Limit Factor”

- Depends on the borrower’s age (rounded to the closest year) and the “expected interest rate.”
- Will be lower if the borrower’s age is lower; higher if the borrower’s age is higher (holding interest rate constant)
- Expected interest rate =
 - If the loan is a fixed rate, the note interest rate
 - If the loan is adjustable rate, the 10-year Constant Maturity Treasury (“CMT”) or LIBOR swap rate, plus the margin provided for in the note



Maximum Claim Amount



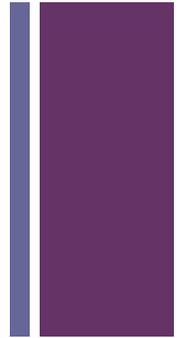
The lesser of:

- Appraised value of the house

OR

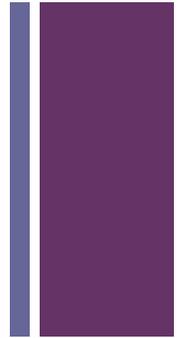
- \$625,500

Initial Principal Limit



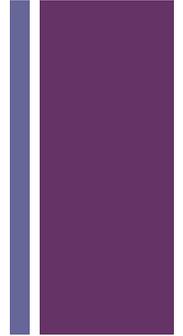
$$\text{Principal Limit} = \text{Principal Limit Factor} \times \text{Maximum Claim Amount}$$

The Non-Borrowing Spouse Problem



- Until recently, HUD allowed lenders to extend a Reverse Mortgage loan to one of two spouses and ignore the younger spouse in calculating initial Principal Limit
- Loan docs called the loan due and payable upon the death of the borrower – spouse was not protected
- This contradicted the HECM authorizing statute
- Many younger spouses were left off the loan because
 - Under 62
 - Or higher loan proceeds were needed to retire existing mortgage debt; needed to increase the age of the youngest borrower

Statutory Protection for Spouses

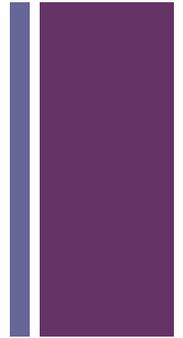


In a section titled, “Safeguard to Prevent Displacement of Homeowner,” the **statute** provides:

The Secretary may not insure a home equity conversion mortgage under this section unless such mortgage provides that the homeowner's obligation to satisfy the loan obligation is deferred until the homeowner's death, the sale of the home, or the occurrence of other events specified in regulations of the Secretary. *For purposes of this subsection, the term "homeowner" includes the spouse of a homeowner.*

12 U.S.C. § 1715z-20(j)

HUD's Regulation



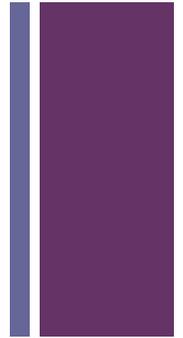
- However, HUD issued a regulation that provides:

“The mortgage shall state that the mortgage balance will be due and payable in full if a *mortgagor* dies and the property is not the principal residence of at least one *surviving mortgagor* . . .”

24 C.F.R. § 206.27(c)(1)

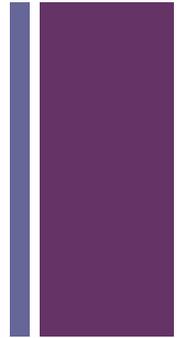
- HUD also required any HECM-insured lender to use a mortgage contract that says the death of the mortgagor (borrower) triggers the loan becoming due and payable.
- (This changed for new loans originated after August 2014)

Bennett and Plunkett litigation



- *Bennett v. Donovan*, 703 F.3d 582 (D.C. Cir. 2013) (surviving spouses had standing to sue HUD)
- *Bennett v. Donovan*, 2013 WL 54424708 (D.D.C. Sept. 30, 2013) (HUD's regulation allowing for foreclosure while surviving spouse still lived in the home was invalid)
- *Plunkett v. Castro*, 2014 WL 4243384 (D.D.C. Aug. 28, 2014) (holding that the HUD's creation of the MOE was not arbitrary and capricious; remanding to HUD to consider whether Hold Election should be extended to all surviving spouses; but refusing to certify a class action)
- HUD issues Mortgagee Letter 2015-03
- Amended Complaint, *Salera v. Castro* (D.D.C. Mar. 4, 2015)

Mortgagee Optional Election (MOE) vs. Hold Election (HE)



Mortgagee Optional Election: HUD created this option in its 6/24/14 Determination on Remand in the *Plunkett* litigation

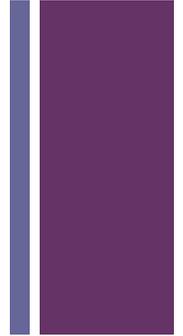
- Five factors – including the Principal Limit test
- If these five factors are satisfied, creditor may assign the loan to HUD and HUD will delay foreclosure until spouse's death

Hold Election: HUD took the position in one of its briefs in *Plunkett* that because the reg was invalid (as to these six plaintiffs), the foreclosure timelines were not triggered for their loans.

Therefore, creditor could delay foreclosure and simply assign the loan to HUD when it reaches 98% of the MCA. The Court called this the “Trigger Inapplicability Decision (TID)” in an Opinion entered 8/28/14.

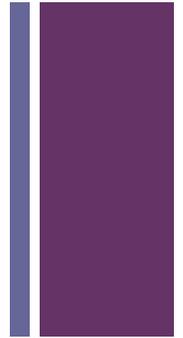
- HUD later began referring to the TID as the Hold Election (HE)

Risk of Foreclosure



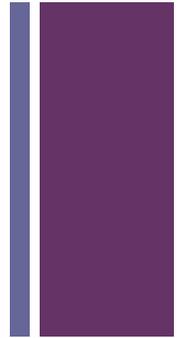
- Once the borrowing spouse dies, Creditor assumes the foreclosure timelines are triggered
- Creditor must initiate foreclosure within 6 months of the borrower's death, or HUD will impose **interest curtailment**
 - **Interest curtailment = lender not entitled to include later accrued interest in a claim it files with HUD**
- Temporary foreclosure delays (FHA Info 14-34)

Mortgagee Letter 2015-03



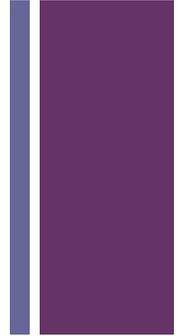
- HUD stated (with no explanation or supporting evidence) that extending the Hold Election to all surviving spouses would be too costly – this “imposes a financial risk to the insurance fund that is simply too great.”
- HUD offers mortgagees (creditors) the option to elect the Mortgagee Optional Election Assignment (“MOE” or “MOE Assignment” if all conditions are met)
- Mortgagee must make the election by the later of:
 - 90 days following issuance of ML 2015-03
 - 30 days following servicer receiving notice of the last borrower’s death
 - Such additional time as HUD may authorize in writing (in HUD’s sole discretion)

How to get the Hold Election?



- If a surviving spouse sues HUD and gets a judicial determination that the regulation is invalid, HUD is offering the creditor the Hold Election for that loan
- No logical reason to treat spouses differently simply because they are able to retain a lawyer and file suit against HUD
- Advocates intent on challenging HUD's decision
- For now, the question is:
 - Can this client qualify for the MOE Assignment?
 - If not, is this a case where it makes sense to sue HUD?

Practical Concerns in Case Selection



- Can the spouse afford the Taxes and Insurance (T&I)?
- Is there a T & I arrearage now? Can spouse cure promptly?
- Is the home in habitable condition (repair issues)?
- Does the spouse want to stay in the home?
- Is the spouse the heir or can she establish the right to stay?
How long will probate take?

Option to Refinance at 95% FMV



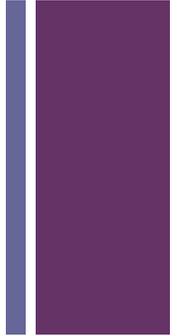
Is the home underwater?

Remember the option to refinance or sell the house (pay off the RM) for the lesser of:

- the current loan balance
- or
- 95% of the Fair Market Value.

Can the spouse qualify for a forward mortgage at 95% of the FMV? (income, credit score)

Housing Counselors: When to refer the homeowner to an attorney?



- As soon as possible
 - Provided the client wants to keep the home
 - Consider feasibility/ Case selection concerns
- Try calling your local legal aid/legal services office
- Use <http://www.consumeradvocates.org/find-attorney>
- Contact NCLC for help finding an attorney in your state who focuses on these kinds of cases
- Helpful for the counselor to stay involved/consult with attorney

Is the MOE an option?

Can Spouse Qualify for MOE?

- **Principal Limit (PL) test**
- Spouse was legally married to borrower at time of loan & remained married until borrower's death (allowance for same-sex couples who couldn't legally marry at time of the loan & became legally married before borrower's death)
- Home is spouse's principal residence from time of loan to the present
- Has title to the property (or legal right to remain for life), or can obtain such title or right within 90 days of the borrower's death
- Loan not in default for any other reason than death of borrower
- No claims that would invalidate the loan
- Balance can't exceed the Maximum Claim Amount

The Principal Limit (PL) Test

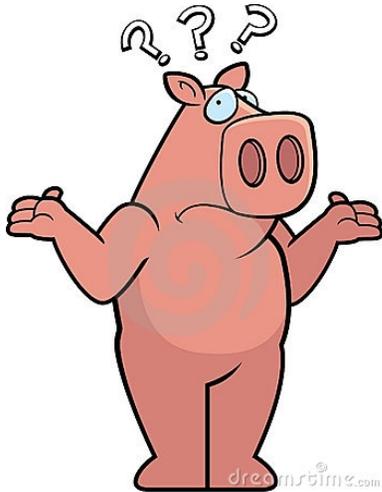
Part One: Principal Limit Factor Test

- Spouse would have had a PLF greater than or equal to the PLF of the borrower.
- i.e. Non-borrowing spouse was the same age or older than the borrower spouse (rounding to the nearest birthday if within 6 months)
- Rarely going to meet this

Principal Limit Test cont....

Part Two: Principal Limit Test (i.e. “The Doozy”)

- “Non-borrowing spouse’s PLF would have resulted in a current principal limit that is greater than or equal to the current unpaid principal balance.”



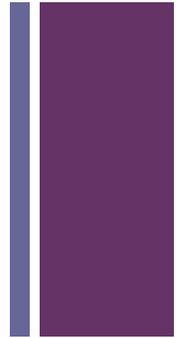
PL Test: as explained by HUD

Plunkett v. Castro, 1:14-cv-00326, Doc. 37 at 18-19;
HUD's brief dated July 21, 2014

A plaintiff with a lower principal limit factor can still satisfy the Principal Limit Test if the hypothetical principal limit he or she would have had if he or she had been a co-borrower would have grown to be greater than or equal to the unpaid principal balance of the existing mortgage loan at the time of loan assignment. . . To properly apply the Principal Limit Test, each plaintiff's initial principal limit first would be calculated using the principal limit factor. The principal limit continues to grow on a monthly basis, as set forth in the definition of "principal limit" in 24 C.F.R. § 206.3. . . . Under the Principal Limit Test, the surviving spouse's principal limit would be compared to the balance at the time of loan assignment.

FN 13: the principal limit grows each month at a rate of one-twelfth of the mortgage interest rate in effect in that month of the loan plus one-twelfth of one-half percent. 24 C.F.R. § 206.3. . . compounded monthly.

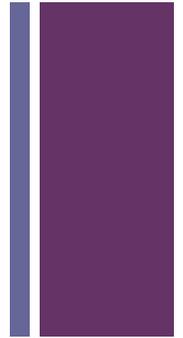
PL Test: Let's break it down



- Idea is to look back to see what the principal limit would be now if the spouse had been included on the loan at the outset

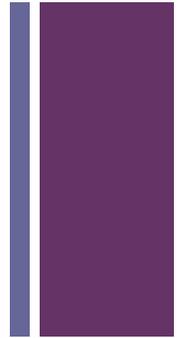
- Two steps (outlined by HUD):
 - (1) Determine spouse's initial principal limit at the time of origination
 - (2) Calculate how her principal limit would have grown to the present with the accrual of interest and mortgage insurance premiums

PL Test: docs/info you need



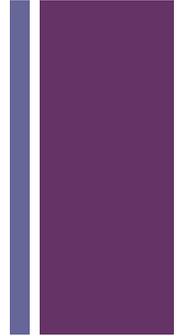
- Non-borrowing spouse's birthdate
- Complete loan docs, if available, but at a minimum, the Note
- HUD historic PLF tables
(http://portal.hud.gov/hudportal/HUD?src=/program_offices/housing/sfh/hecm)
- If adjustable rate mortgage, historic rates for the index:
 - For exact figures, request interest rate changes from lender;
 - Download historic rate data (mortgage-x.com/general/indexes/)
- Current balance of the loan

PL Test Step 1: Calculating Initial Principal Limit



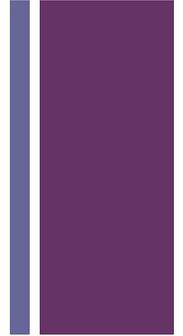
- Expected interest rate:
 - If fixed rate, expected rate = interest rate
 - If ARM
 - If you have complete loan docs, expected interest rate listed
 - EIR = rate for a constant maturity of ten years (10-year CMT or 10-year LIBOR swap rates) + loan margin
- Find PLF on historic table for the EIR & spouse's age (round to the nearest birthdate as of the first day of the month the loan is closed)
- Initial principal limit = $\text{PLF} \times \text{appraised value (max loan amount on mortgage/deed of trust} \div 1.5)$

PL Test Step 2: Calculating Growth of Principal Limit to the Present



- Principal limit grows at the interest rate + mortgage insurance premium of .5% per annum, compounded monthly
- For ARM, get historic index data for the loan period:
 - <http://mortgage-x.com/general/indexes/>
 - For exact rate changes, request from servicer
- Use excel chart to calculate growth of principal limit from the time of the loan to the present
- Client passes if principal limit \geq current balance of the loan (or if client could pay down the balance to make this true)

Example

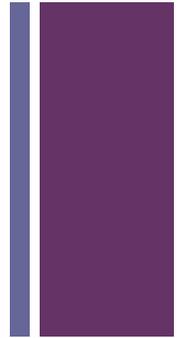


- Client's birthdate: February 9, 1941
- Date of the loan: October 11, 2006
- Appraised value: \$223,000
- Interest: intro rate of 6.1% for first 2 months, then US one-year constant maturity + 1.5%
- Current unpaid balance: \$179,000



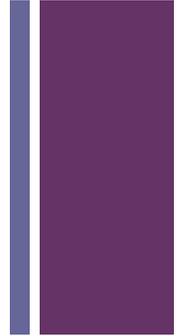
Questions?

My client passes! Now what?



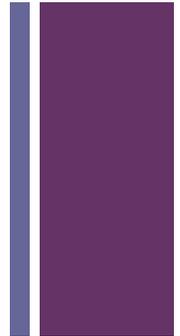
- Client qualifies for MOE (or could pay down principal to qualify), send a letter to the servicer requesting the MOE:
 - Include an explanation of the principal limit calculations providing a copy of the excel spreadsheet;
 - Good idea to cite to HUD brief explaining how the test should be run;
 - If you haven't already requested the actual change rates for each month of the loan, include a request for this to confirm the exact PL calculations.
 - Remember deadlines (ML 2015-03)

Litigation Options



- Spouse can't meet PL test, but can meet other criteria (married at time of loan, can obtain title, no other basis for default (or can be cured), principal residence)
- Consider bringing legal claims:
 - Administrative Procedure Act
 - Reformation/contract claims
 - Fraud/misrepresentation

APA Claims



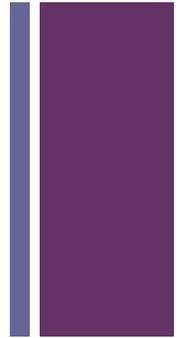
- HUD's regulation, 24 C.F.R. §206.27(c)(1), which requires the loan be called due and payable upon the borrower's death, violates the HECM statute, 12 U.S.C. § 1720z-20(j), which requires protection for the spouse.
- Because the reg is invalid where there is a non-borrowing surviving spouse, there is no due and payable event requiring foreclosure under HUD's regulations.
 - HUD has recognized this to be true and has stated it is the "automatic" result of a court holding the reg to be invalid as applied to a surviving spouse.
 - For plaintiffs who have obtained such a ruling, HUD has offered the "Hold Election", which allows the servicer to continue servicing the loan while the spouse is living in the home (and fulfilling the obligations of paying taxes and insurance).
 - Hold Election is at the lender's option.

APA claims cont.

Taking it one step further . . .

- If there is no due and payable event under the reg, there is also no basis for HUD to pay a claim based on foreclosure after the death of the borrower.
- HUD is still obligated compensate the lender under the HECM insurance and provide immediate payment if the lender wants to accelerate under the terms of the loan. 12 U.S.C. § 1715z-20(i).
- In order to fulfill both obligations of protecting the spouse from displacement and compensating the lender under the insurance policy, HUD should take immediate assignment of the loan (or develop another means of accomplishing both obligations).

APA – possible defenses



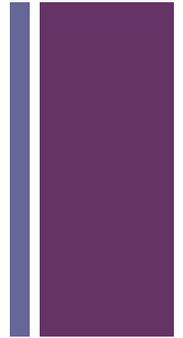
■ Standing

- Regardless of claims against HUD, lender has independent right to foreclose under the loan documents, so relief against HUD wouldn't redress the alleged harm. (Circuit Court of Appeals rejected this argument by HUD.)
- Lender – spouse doesn't have standing to interfere with its HECM insurance contract.

■ Mootness

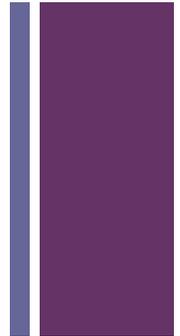
- HUD has already addressed the problem by providing the MOE relief, and cost of extending HE to everyone is too great.

Breach of Contract



- Three party HECM Loan Agreement for HECM insurance between the borrower, lender, and HUD, of which the spouse is an intended beneficiary:
 - Insurance policy is defined exclusively and expressly by reference to the HECM statute and regulations (no separate insurance policy or binder). 24 C.F.R. 203.251(j).
 - Agreement thus includes the spousal protection provision of the HECM statute, which makes the spouse an intended 3rd party beneficiary.
 - HUD and lender breach the agreement by attempting to foreclose in violation of the spousal protection provision.

Breach of Contract - Defenses

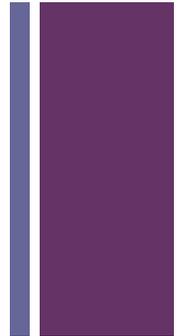


- Borrower not a party to the insurance contract
 - Cases saying borrower not a party or intended beneficiary to be able to enforce FHA insurance (not in HECM context)
 - But HECM insurance provides enforceable benefits to the borrower (guarantees payment by lender; non-recourse against borrower)

- Spouse not a 3rd party beneficiary
 - Cases creating presumption against 3PBs for gov't contracts (in context of large K's for general welfare)
 - But insurance K is specific to each loan, borrower and spouse are identified at the outset, and specifically contemplates protection for the spouse (intended beneficiary).

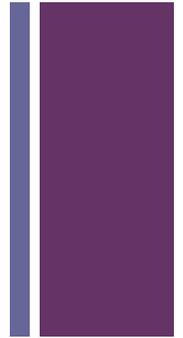
- Lender – statutory spousal protection provision only imposes an obligation on HUD, not the lender.

Reformation



- Mistake of law (check your jurisdiction's rule on this): parties intended to enter into a HECM loan that would be eligible for HUD insurance and understood the legal effect of the docs would be a loan that complied with the HECM statute, but by mutual mistake, the loan did not comply with the legal requirements for HECM insurance due to the exclusion of the spousal protection provision.
- Mistake of fact: parties intended for the loan to continue uninterrupted until the death of the borrower AND the non-borrowing spouse, but by mutual mistake the loan did not express this intent.

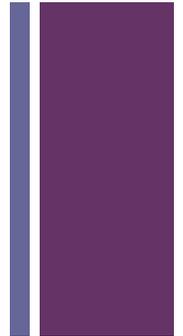
Reformation – Defenses



- Standing – spouse not 3rd party beneficiary of the loan
 - Consider whether spouse should so individually as alleged 3PB and as representative of the estate on borrower's behalf.

- Factual dispute
 - Lender likely to have documents signed by spouse indicating an understanding that loan might come due and payable at borrower's death (counseling certificate or spouse ownership interest certification).

Fraud / Misrepresentation

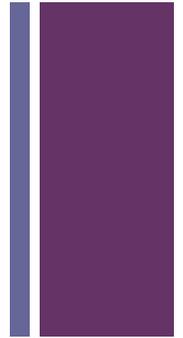


- Claim against original lender for fraudulent statements made about the spouse's ability to remain in the home in order to induce the spouse to give up a title interest and/or the borrower to sign the loan.
- Consider disclosure docs that spouse may have signed, and law of your jurisdiction as to how likely these claims are to prevail.
- If HUD grants Hold Election relief, claims that invalidate the loan will have to be resolved in favor of the lender or dismissed with prejudice.



Strategy Issues

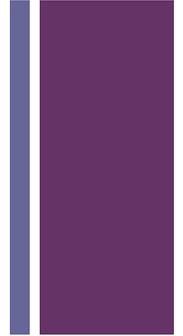
Judicial foreclosure states



- File a counterclaim against creditor and a 3d party complaint against HUD in the foreclosure action?
 - Benefit of consolidating these claims with the foreclosure action
 - Sovereign immunity issues
 - 5 USC 702
 - National State Bank of Elizabeth v. Gonzalez, 266 N.J. Super. 614 (1993)

- Affirmative suit against HUD in federal district court?
 - Filing fee
 - Need to seek a TRO

Seeking a TRO to Stop Foreclosure Sale



- Difficulty of enjoining the creditor, when contractually, they have a right to foreclose
- Focus on HUD
- Concern about ordering HUD to take a particular action
 - Court may be inclined to remand to HUD so that HUD can have the first attempt at fashioning relief (subject to review)
- But, Court can compel agency action unreasonably delayed
 - 5 USC 706
- Focus on maintaining the status quo and preventing irreparable harm
- Enjoin HUD from imposing interest curtailment; Order HUD to send a letter to lender saying no interest curtailment (no due and payable event, because reg is invalid)

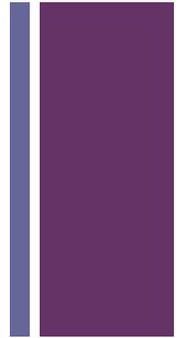
Sample language: injunctive relief

- Enter preliminary and permanent injunctions requiring HUD to **use its authority** under the reverse mortgage statute to **protect Mrs. Smith from foreclosure and displacement**;
- Enter an order enjoining HUD from imposing interest curtailment;
- Enter an order requiring HUD to send Creditor a letter acknowledging that foreclosure timelines do not apply;
- Enter an order that 24 C.F.R. § 206.125 **has not been triggered** by the death of Mr. Smith, and therefore foreclosure timelines do not apply, and **there shall be no interest curtailment**;
- Enter an order that because 24 C.F.R. § 206.125 has not been triggered by the death of Mr. Smith, HUD would not have a basis to pay an insurance claim based on foreclosure;
- Enter an order requiring HUD to **specifically perform its obligations under the HECM insurance contract** to protect Mrs. Smith from displacement and to ensure payment to Creditor.

Using Bankruptcy to Stop a Foreclosure?

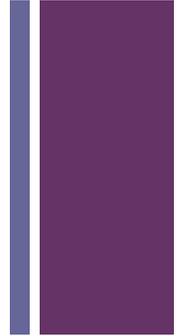
- Basic principle in bankruptcy that a “claim” includes a debt secured by the debtor’s home, even if debtor has no personal liability on the note.
- Non-borrowers must be allowed to de-accelerate the note and cure arrearage in a chapter 13 plan.
 - See *In Re Jordan*, 199 B.R. 68 (Bankr. S.D. Fla. 1996); *In Re Curinton*, 300 B.R. 78 (M.D. Fla. 2003); *Citicorp Mortg. v. Lumpkin*, 144 B.R. 240 (Bankr. D. Conn. 1992); *In Re Alexander*, 20 Fla. L. Weekly Fed. B 463 (Bankr. N.D. Fla. 2007); see also *Johnson v. Home State Bank*, 501 U.S. 78 (1991).
- Servicer required by bankruptcy court to engage with debtor in bankruptcy loss mitigation procedures, even though bankruptcy debtor was not on the note and mortgage. *In Re Smith*, 469 B.R. 198 (Bankr. S.D. N.Y. 2012).

Defendants: Just HUD, or Creditor too?



- You want injunctive relief that impacts the Creditor's rights
- May be a necessary party (Rule 19)
- Creditor will incur attorney's fees, which may be added to the loan balance (watch out for 98% of the MCA!)
- If Creditor has an attorney and a stake in getting the matter resolved, much easier to get the Hold Election done

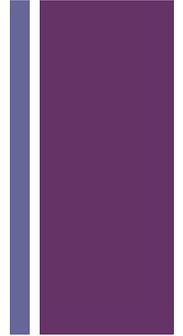
What is your litigation goal?



- Getting a judgment stating that the regulation is invalid
 - Motion for TRO or Preliminary Injunction?
 - Motion for Partial Summary Judgment?
- Discovery not likely very important
- Get HUD to extend the Hold Election to Creditor:
- Get Creditor to elect the Hold Election
- Be ready to meet all criteria



Other strategies



- Media outreach
 - Story in your local newspaper or on the nightly news
- Policy advocacy
 - Talk with elected officials about your client's situation
 - Keep up with ongoing advocacy efforts by other groups; share your client's story

Settlement

Implementing the Hold Election

- 30 days for servicer to make the election
- 30 days (from election deadline) to meet criteria:
 - All property charges must be paid
 - Must have ownership or right to remain, and reside in the home
 - Must provide proof of the marriage
 - Any asserted claims that could invalidate the loan must be judicially resolved in favor of lender (i.e. dismissed with prejudice)
- Certification signed by spouse
- Tolling/modification agreement with lender
- Attorney's fees against HUD under APA?

Questions?