

# Part II: Litigating on Behalf of Reverse Mortgage Surviving Spouses

**Sarah Bolling Mancini**, Of Counsel at the National Consumer Law Center  
**Odette Williamson**, Staff Attorney at the National Consumer Law Center



**May 28, 2015**

**National Elder Rights Training Project for the National Legal Resource Center.  
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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.





## Moderator – Odette Williamson

- Odette has been a staff attorney at NCLC since 1999. Prior to this she was an Assistant Attorney General in the Massachusetts Office of the Attorney General where she concentrated on civil enforcement actions against individuals and businesses for violation of consumer protection and other laws.
- As an AAG she also served on the Elder Law Advocates Strike Force to combat unfair and deceptive acts against elderly citizens. She attended Tufts University and Boston College Law School.



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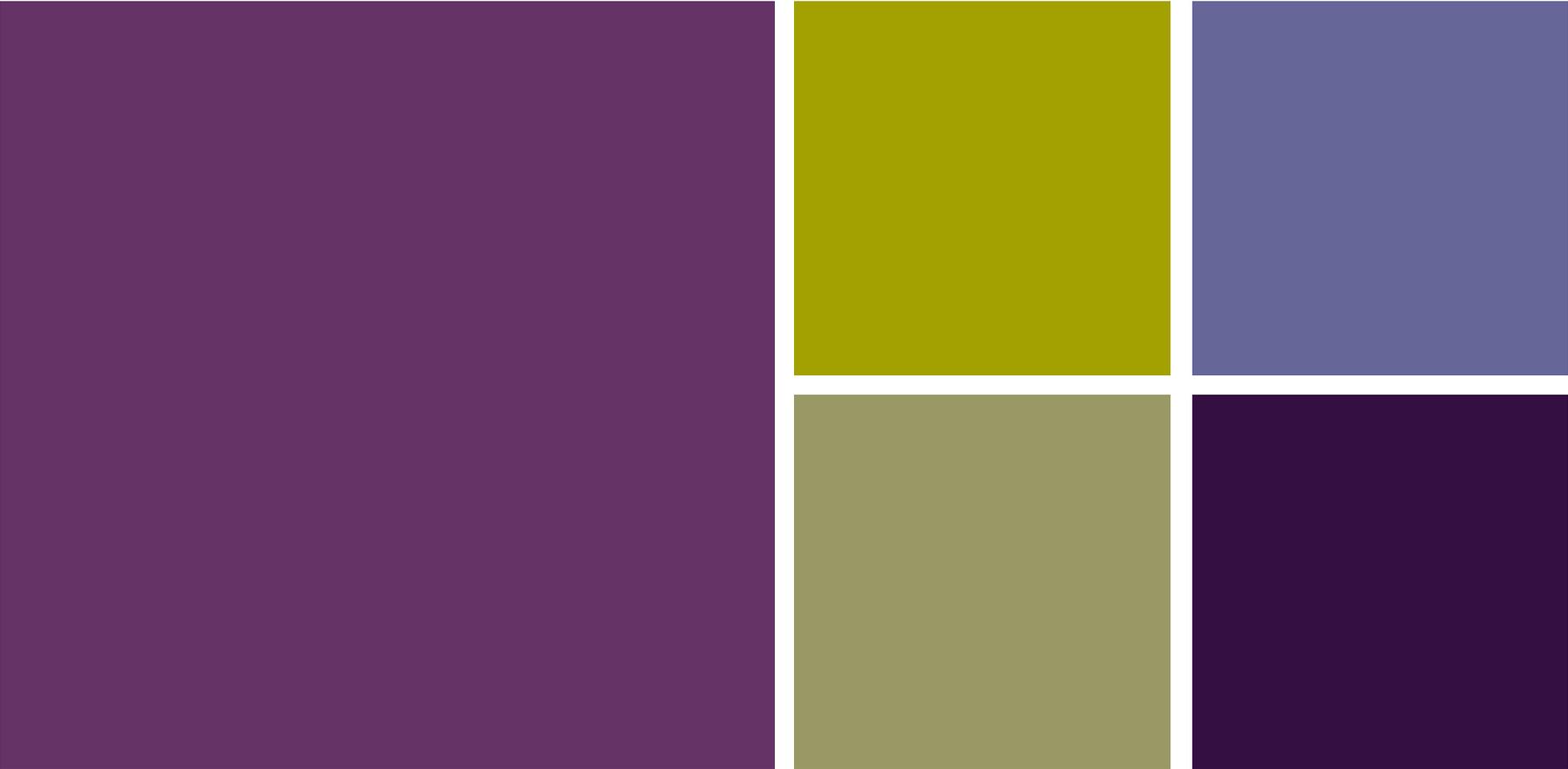
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**May 28, 2015**

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A decorative graphic consisting of a large purple square on the left, and a 2x2 grid of smaller squares on the right. The top-left square in the grid is olive green, the top-right is blue-purple, the bottom-left is olive green, and the bottom-right is dark purple.

## Part II: Litigating on Behalf of Reverse Mortgage Surviving Spouses

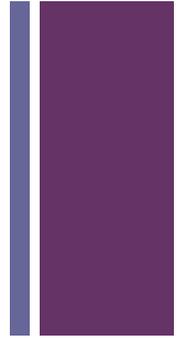
Sarah B. Mancini, Of Counsel, NCLC

May 28, 2015

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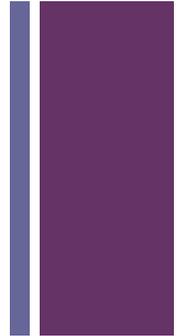
# Overview

- Status of ongoing litigation in D.C.
- Mortgagee Letter 2015-03
- Litigating non-borrowing spouse cases:
  - claims
  - defenses
  - strategy issues
  - settlement

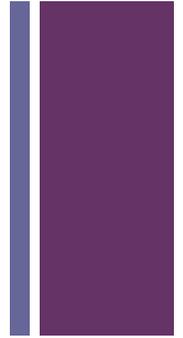


# Reverse Mortgage Basics

- FHA-insured Reverse Mortgages – the Home Equity Conversion Mortgage (HECM); borrower must be  $\geq 62$
- 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)

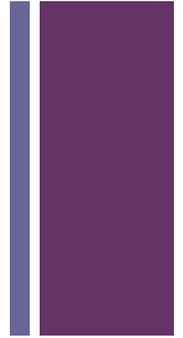


# Initial Principal Limit



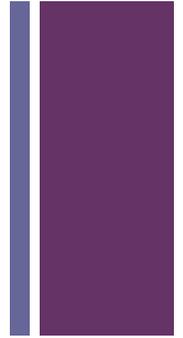
$$\text{Principal Limit} = \text{Principal Limit Factor} \times \text{Maximum Claim Amount}$$

# “Principal Limit Factor”



- Depends on the borrower's age (rounded up if next birthday is within 6 months) 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)

# Maximum Claim Amount



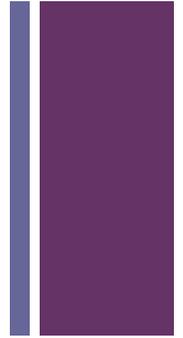
The lesser of:

- Appraised value of the house

OR

- \$625,500

# 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 borrow maximum amount possible

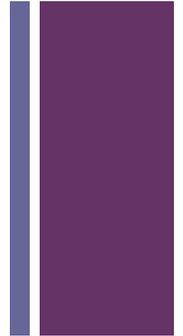
# Statutory Protection for Spouses

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



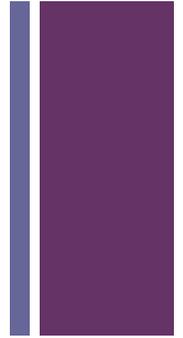
- However, HUD issued a regulation that provides:

“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)

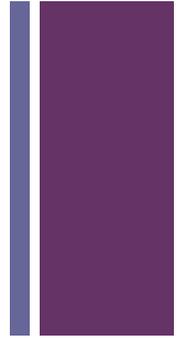
- HUD also required any HECM-insured lender to use a mortgage contract that says the death of the mortgagor (borrower) triggers the loan becoming due and payable.
- (This changed for new loans originated after August 4, 2014. See [Mortgagee Letter 2014-07](#))

# Risk of Foreclosure



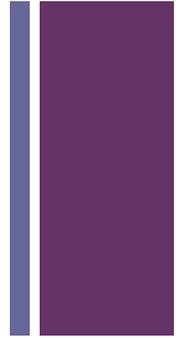
- Once the borrowing spouse dies, RM servicer assumes that HUD's required foreclosure timelines are triggered
- Servicer must initiate foreclosure within 6 months of the borrower's death, or HUD will impose **interest curtailment**
  - **Interest curtailment = lender not entitled to include later accrued interest in a claim it files with HUD**
- Servicers were allowed to grant temporary foreclosure delays in some circumstances while HUD was figuring out what to do (FHA Info 14-34)

# Bennett and Plunkett litigation



- *Bennett v. Donovan*: Initially, district court dismissed for lack of standing
- *Bennett v. Donovan*, 703 F.3d 582 (D.C. Cir. 2013) (holding that surviving spouses had standing to sue HUD because HUD could redress the harm)
- *Bennett v. Donovan*, 4 F.Supp.3d 5 (D.D.C. Sept. 30, 2013) (holding that HUD's regulation allowing for foreclosure while surviving spouse still lived in the home was invalid; remanding to HUD to fashion a remedy)

# 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

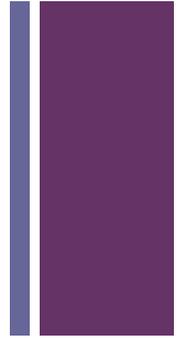
- Five factors – including the Principal Limit test
- If these five factors are satisfied, creditor may assign the loan to HUD and HUD will delay foreclosure until spouse's death

**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)

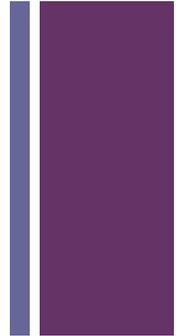
# Bennett and Plunkett Litigation



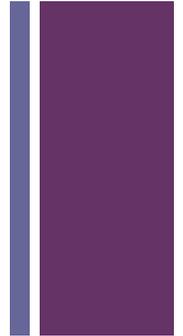
- HUD Determination Remand 6/24/14: extending MOE to named Plaintiffs in *Plunkett*
- *Plunkett v. Castro*, 2014 WL 4243384 (D.D.C. Aug. 28, 2014)
  - Holding that the HUD's creation of the MOE was not arbitrary and capricious
  - HUD's failure to consider the TID/HE was arbitrary and capricious; Remanding to HUD to consider extending this option for all non-borrowing spouses
  - Refusing to certify a class action at this time
- HUD issues Mortgagee Letter 2015-03 on Jan. 29, 2015
  - Extending MOE to all non-borrowing spouses
  - Extending the HE only to spouses who have obtained a judgment that HUD's regulation is invalid (6 named plaintiffs in *Plunkett* and one plaintiff in Georgia litigation)

# Mortgagee Letter 2015-03 (Jan. 29, 2015)

- 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 (later extended to 120 days after issuance – through April 29, 2015)
  - 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)



# Requirements for the MOE?

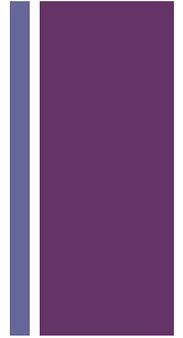


- **Principal Limit (PL) test (see March 19, 2015 webinar)**
- Spouse was legally married to borrower at time of loan & remained married until borrower's death (allowance for same-sex couples who couldn't legally marry at time of the loan & became legally married before borrower's death)
- Home is spouse's 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

# Litigation and ML 2015-03

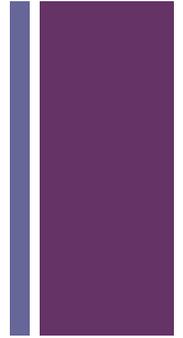
- Motion to Amend Complaint, *Plunkett v. Castro*, 14 CV 326 (D.D.C. Mar. 4, 2015) > if granted, case would become *Salera v. Castro*
  - Attacking Mortgagee Letter 2015-03 and the restrictions/deadlines HUD created for HE as arbitrary and capricious
  - Stayed until 6/1/15
  
- Also *Snyder v. Castro*, 15 CV 568 (D.D.C. Apr. 15, 2015)
  - Same claims as *Salera*, seeking TRO to stop 3 pending foreclosures
  - Court denied motion for TRO on 4/23/15
  - Administrative Record due 6/1/15, briefing schedule due 6/4/15
  
- HUD withdraws ML 2015-03 on April 30, 2015, issues 60 day stay of foreclosures pending HUD's next steps
  - Mortgagee Letter 2015-12 (rescinding ML 2015-03)
  - FHA Info # 15-33 (60 day stay of foreclosures involving N-B spouse)

# Practical Concerns: Pending MOE Request and/or Foreclosure Sale



- What if I requested the MOE for a client before April 30, 2015 and the creditor elected the MOE?
  - Not clear; all deadlines to complete the MOE assignment would seem to be on hold
  - Foreclosure hold for 60 days until HUD announces next steps
- What if my client is facing a pending foreclosure sale and I'm trying to evaluate the options?
  - Foreclosure hold for 60 days until HUD announces next steps
  - Send a letter to a high-up contact at servicer (reach out to NCLC if you need help getting in touch with the right person)

# HUD's Justification for Offering Only the MOE Assignment

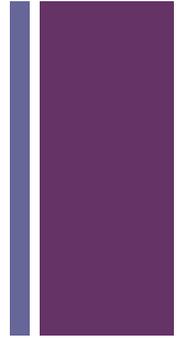


- Cost to the HECM Insurance Fund
- HUD estimates:
  - \$1.769 billion
  - Based on 20% of all RMs impacted (~ 100,000)
  - Based on assuming that all non-borrowing spouses are > 5 years younger
- Other estimates:
  - NRMLA: \$521 million, < 12,000 non-borrowing spouses impacted
  - HUD: \$397 million if normal age distribution of spouses
  - HUD: \$439 million for MOE Assignment Program



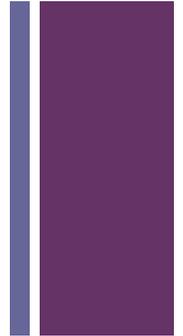
Questions?

# Litigation Options



- Spouse can't meet PL test, but can meet other criteria:
  - married at time of loan and stayed married until borrr's death
  - can obtain title or right to stay in the home until her death
  - no other basis for default – taxes and insurance are current (or can be cured)
  
- Consider bringing legal claims:
  - Administrative Procedure Act
  - Reformation/contract claims
  - Fraud/misrepresentation

# APA Claims

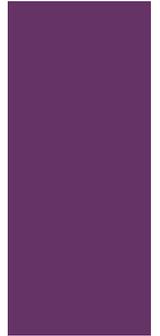


- HUD's regulation, 24 C.F.R. §206.27(c)(1), which requires the loan be called due and payable upon the borrower's death, violates the HECM statute, 12 U.S.C. § 1720z-20(j), which requires protection for the spouse.
- Because the reg is invalid where there is a non-borrowing surviving spouse, there is 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).

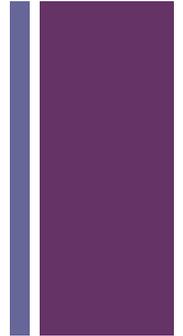


# APA – possible defenses

## 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.
- *Bombet v. Donovan*, 2015 WL 1276569 (M.D. La. Mar. 19, 2015) (finding no standing because of ML 2015-03) – appeal pending to 5<sup>th</sup> Circuit
- See *Bennett* (D.C.Cir.) and *Plunkett* (D.D.C. Aug. 28, 2014), both finding standing
- Probabilistic benefit is enough to confer standing

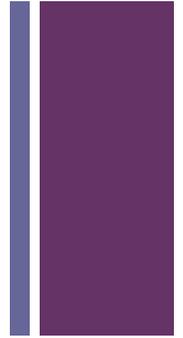
# APA – possible defenses



## Mootness

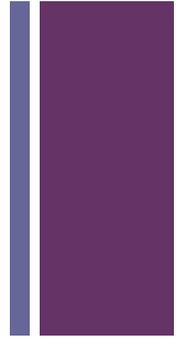
- The argument: HUD has already addressed the problem by providing the MOE relief.
- Requisite personal stake that must exist at commencement of the lawsuit and throughout its pendency
- See *Plunkett* (D.D.C. Aug. 28, 2014)
- Currently ML 2015-03 has been rescinded
- If same policy is reissued, a challenge to that policy as arbitrary and capricious should not be moot
- A challenge to the regulation as to this plaintiff is not moot

# APA - remedy



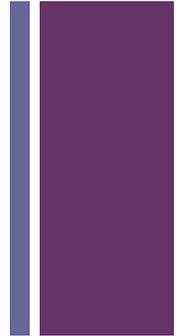
- Declaration that the regulation is invalid
- Remand to agency to fashion relief
- Generally the Court cannot order HUD to take a particular action
- However, once the Court enters an order that the reg is invalid as to this Plaintiff, you can ask HUD to extend the Hold Election for this loan

# Breach of Contract



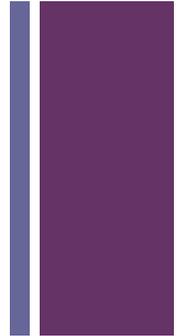
- Three party HECM Loan Agreement for HECM insurance between the borrower, lender, and HUD, of which the spouse is an intended 3<sup>rd</sup> party beneficiary:
  - Insurance policy is defined exclusively and expressly by reference to the HECM statute and regulations (no separate insurance policy or 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 3<sup>rd</sup> party beneficiary.
  - HUD and lender breach the agreement by attempting to foreclose in violation of the spousal protection provision.

# Breach of Contract



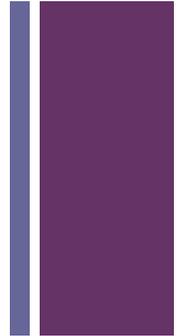
- Paragraph 17 of the Mortgage/ Deed of Trust specifically provides that the instrument is “governed by Federal law” and any provision conflicting with Federal law can be severed.
- Unusual facts in a case out of N.C.: both spouses signed the mortgage/ deed of trust (even though only H signed the note).
  - Great argument for breach of contract on these facts!
  - No right to foreclose under the mortgage/deed of trust so long as there is a surviving **borrower**.
  - If mortgage defines both H and W as borrowers, there is no right to accelerate (para 9) or foreclose (para 20).

# Breach of Contract - Defenses



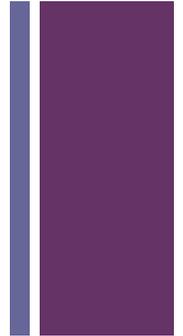
- Borrower not a party to the insurance contract
  - Cases saying borrower not a party or intended beneficiary to be able to enforce FHA insurance (not in HECM context)
  - But HECM insurance provides enforceable benefits to the borrower (guarantees payment by lender; non-recourse against borrower)
- Spouse not a 3<sup>rd</sup> 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.

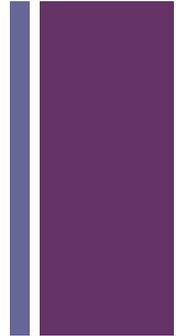
# Reformation – Defenses



- Standing – spouse not 3<sup>rd</sup> party beneficiary of the loan
  - Consider whether spouse should sue 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

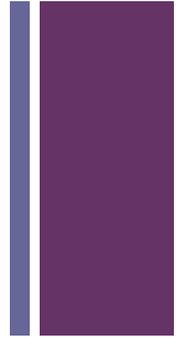


- Claim against original lender for fraudulent statements made about the spouse's ability to remain in the home in order to induce the spouse to give up a title interest and/or the borrower to sign the loan.
- Consider disclosure docs that spouse may have signed, and law of your jurisdiction as to how 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

# Forum and Sovereign Immunity Issues

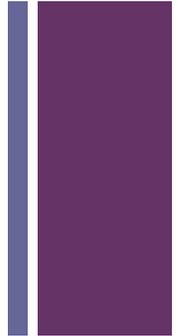


Judicial foreclosure states:

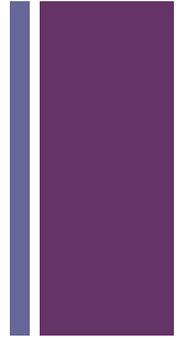
- Affirmative suit against HUD in federal district court?
  - Filing fee
  - Need to seek a TRO
  
- File a counterclaim against creditor and a 3d party complaint against HUD in the state court foreclosure action?
  - Benefit of consolidating these claims with the foreclosure action
  - But... sovereign immunity issues
  
- Waiver of sovereign immunity for APA claims **in federal court**:
  - 5 USC § 702; see National State Bank of Elizabeth v. Gonzalez, 266 N.J. Super. 614 (1993)

# Sovereign Immunity and Jurisdiction

- Other source for non-APA claims: 12 USC § 1702 (National Housing Act)
  - “The Secretary shall, in carrying out the provisions of this subchapter and subchapters II, III, V, VI, VII, VIII, IX-B, and X, be authorized, in his official capacity, to sue and be sued in any court of competent jurisdiction, State or Federal.”
  - Subchapter II includes HECM authorization, 12 USC 1715z-20
  - Breach of contract and equitable claims based on HUD’s “carrying out” of the HECM program; but not claims for judicial review of agency actions (APA) – see Nat’l State Bank of Elizabeth v. Gonzalez, 266 N.J. Super. at 619.
- Even if HUD doesn’t raise it, the Court may raise subject matter jurisdiction sua sponte. Removal to federal court doesn’t fix the problem.
- Breach of contract claims < \$10K must go to U.S. Court of Federal Claims
  - The Tucker Act 28 USC 1346(a)(2), 1401(a)(1)



# Seeking a TRO to Stop Foreclosure Sale

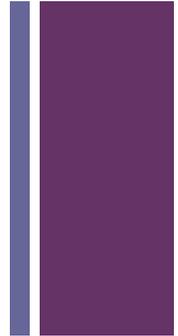


- Difficulty of enjoining the creditor, when contractually, they have a right to foreclose
- Focus on HUD
- Concern about ordering HUD to take a particular action
  - Court may be inclined to remand to HUD so that HUD can have the first attempt at fashioning relief (subject to review)
- But, Court can 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)
- Good case: *Hill v. Generation Mortgage Co.*, Case No. 56-2014-447789 (Super. Ct. Cal., Ventura County Dec. 17, 2014)

# Sample language: injunctive relief

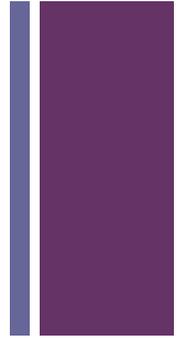
- Enter preliminary and permanent injunctions requiring HUD to **use its authority** under the reverse mortgage statute to **protect Mrs. Smith from foreclosure and displacement**;
- Enter an order enjoining HUD from imposing interest curtailment;
- Enter an order requiring HUD to send Creditor a letter 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

# Part II: Litigating on Behalf of Reverse Mortgage Surviving Spouses

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- I will email you the PowerPoint and recording in a few days
- Thank you to our speakers!



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