FORECLOSING A DREAM

State Laws Deprive Homeowners of Basic Protections

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I. Executive Summary

In recent months, a wave of foreclosures has swept millions of American families from their homes. The magnitude of this crisis defies easy comprehension: more than 8 million American families are expected to lose their homes to foreclosure in the next four years. Much has been written about the financial and economic causes of this disaster. Much less notice has gone to another factor that has accelerated and multiplied this grave loss of homes and savings: antiquated state laws that in some ways afford fewer protections to homeowners than to renters.

State foreclosure laws tilted against homeowners

This report examines the laws that govern mortgage foreclosures in the 50 states, and evaluates how well the laws of a given state protect homeowners facing foreclosure. Regulation of mortgage foreclosures has always been a fundamental province of state laws. Now, as families, communities and states face an onslaught of financial and social problems caused by the rising tide of foreclosures, states need to craft laws that can maximize the number of their residents who will be able to keep their homes.

Provisions in existing foreclosure laws that hurt homeowners include:

- In 30 states and the District of Columbia, mortgage holders who allege that homeowners have fallen behind in their payments **can bypass the courts and move directly to take away and auction off homes**. This denies homeowners due process protection comparable to that given many tenants. It also places upon homeowners the heavy burden to get a judge to review the mortgage holder's claims and stop the foreclosure.
- In every state but California and Connecticut, mortgage holders **can move directly to foreclosure without being required by state law to consider or discuss ways to avoid loss of the home** with homeowners, such as through modification of the terms of the loan.
- In every state but Massachusetts, New Jersey, and Pennsylvania, a mortgage holder who claims a homeowner has fallen behind in payments **can immediately impose default fees and costs** that reduce the chances that the homeowner can catch up by making the payments owed.
- In 29 states, a mortgage holder has **no obligation under state law to stop foreclosure even if the homeowner**, just before the house has been sold, **comes up with the money** to catch up on the owed payments and all incurred penalties and fees.
- In 33 states and the District of Columbia, there is **no requirement that homeowners be personally served** with a foreclosure notice or legal documents that start a court foreclosure case.
- In 36 states and the District of Columbia, mortgage holders **can pursue so-called "deficiency judgment" claims** against homeowners even after the foreclosed home has been sold at auction. These claims, seeking to re-

cover the difference between the amount owed on the loan and the amount collected from the foreclosure auction, can be pursued without conditions in 15 states and the District of Columbia, and only under certain conditions in the other 21 states.

States can and must do more to allow families to avoid foreclosure and preserve their homes and the wealth and savings embodied in them. By adopting the recommendations set out in this report states can level a playing field now tilted in favor of mortgage holders.

Recommendations

Action is urgently needed in these key areas to protect homeowners and restore basic fairness to the foreclosure process.

- **Mandate judicial supervision over foreclosures of all residential mortgages.** Many states now allow mortgage holders to bypass the courts and use non-judicial procedures to take away homes from their owners. These procedures create enormous barriers for homeowners who want to assert legal claims and raise defenses against lenders, servicers, and mortgage holders. States should either completely abandon the power of sale method and require judicial foreclosure, or they should incorporate essential due process protections into the existing non-judicial procedure.
- **Require mortgage holders to consider loss mitigation, including loan modification and other workout alternatives, as a condition to allowing the foreclosure of a home.** States have broad authority to set conditions upon a mortgage holder's right to foreclose. For example, states have always had the authority to require mediation in certain categories of disputes, and they can require mediation in home foreclosure cases. Several states, local governments and courts have already taken steps to implement these types of mediation systems. States should require that before a foreclosure may proceed, the mortgage holder must prove that it or its servicer explored all reasonable options to avoid foreclosure with the homeowner before the foreclosure was initiated. Mortgage holders who do not comply in good faith with these mediation procedures should not be permitted to use public officials, records, and services to enforce their claims.
- **Require that homeowners be given a right to cure a default by catching up on missed payments, without penalty, at least 60 days before a mortgage holder demands immediate full payment of the entire mortgage balance and before beginning any foreclosure proceeding.** Homeowners should be sent a notice that clearly informs them that before the end of the designated time period, they can stop the foreclosure by paying up the installments they are behind without payment of any default-related costs or fees.
- **Guarantee homeowners the right to reinstate the mortgage by paying the arrearage and costs up to the time of a foreclosure sale.** Nearly half of the states have enacted statutes that provide for this right to reinstate *after* the mortgage holder demands payment of the entire loan balance (acceleration). Such laws are cost neutral for the mortgage holder because borrowers typically pay all reasonable foreclosure costs incurred up to the time of reinstatement. State law should mandate a form of notice to homeowners that provides detailed information about the foreclosure process and steps the homeowner can take to avoid foreclosure, including the right of reinstatement and loan modification options.

- **Require that homeowners be personally served with the notice of sale or foreclosure complaint.** State laws should require that no matter which type of foreclosure proceeding is permitted, the mortgage holder must provide proof of personal service of the legal documents which both commence the foreclosure proceeding and schedule the sale, or the mortgage holder must document repeated good faith attempts to make personal service on the homeowners.
- **Create and adequately fund programs that provide emergency financial assistance to homeowners facing foreclosure.** At least eight states already have statewide programs offering such assistance to homeowners experiencing temporary financial difficulties such as loss of employment, illness, disability, death, divorce or legal separation. As the foreclosure crisis deepens and broader economic problems cause the unemployment rate to increase, more states should consider developing programs that 1) assist homeowners with monthly mortgage payments for a period of 12 to 24 months; 2) provide interest-free or below market rate loans to be repaid when the home is sold, transferred, or refinanced; and 3) are designed as revolving funds, with amounts replenished by loan repayment.
- **Provide homeowners with a statutory right to redeem and reacquire title to their home, for a fixed period of time after a foreclosure sale.** "Redemption" after a foreclosure sale allows a homeowner a fixed period of time in which to set the foreclosure sale aside and regain title to the home by paying the sale price, interest and costs of the sale. The payment compensates the mortgage holder or other purchaser for their financial outlay. Approximately half of the states have a law on the books allowing such post-sale redemptions. However, in a number of states the right to redeem is limited to certain types of foreclosures and applies only for certain outcomes of the sale. The right to redeem after sale should uniformly apply to all residential mortgage foreclosures.
- **Prohibit mortgage holders from pursuing homeowners for deficiency judgments after foreclosures.** Deficiency judgments can drive former homeowners into bankruptcy or burden them with an insurmountable debt obligation. Deficiency judgments can also create an unfair windfall for mortgage holders and reward them when their lack of marketing and publicity leads to a foreclosure sale at a winning bid far below market value. Ten states bar deficiency judgments after residential foreclosures and 21 other states substantially limit deficiencies by requiring lenders to calculate deficiencies with measures such as the property's fair market value rather than the artificially low foreclosure sale price. All states should simply enact outright bars on deficiency judgments after home foreclosures.
- **Require judicial supervision over the accounting of foreclosure sale proceeds and a prompt release of any surplus to the borrowers.** In many states, the accounting of sale proceeds and the distribution of any surplus left after payment of the mortgage debt are handled almost entirely by the mortgage holder or a private trustee, without any explicit procedures or formal court review. States should require that the proposed distribution of sale proceeds be reviewed and approved by a neutral public official and that any surplus funds be disbursed promptly to the borrower.

State Foreclosure Statutes at a Glance

Strengths and Weaknesses

	AL	AK	AZ	AR	CA	CO	CT	DE	DC	FL	GA	HI	ID	IL
Pre-Sale Protections														
Access to Court Review	●	●	●	●	●	◐	○	○	●	○	●	●	●	○
Loss Mitigation Requirement before Foreclosure	●	●	●	●	◐	●	○	●	●	◐	●	●	●	●
Right to Cure before Acceleration	●	●	●	●	●	●	●	●	●	●	●	◐	●	●
Right to Reinstate before Sale	●	◐	◐	◐	○	◐	●	●	◐	◐	●	◐	◐	◐
Personal Service Requirement for Complaint or Sale Notice	●	●	●	●	●	●	○	○	●	○	●	●	◐	○
Housing Emergency Assistance Fund	●	◐	●	●	●	●	○	◐	●	●	●	●	●	●
Post-Sale Protections														
Right to Redeem	◐	●	●	●	●	●	◐	●	●	◐	●	●	●	◐
Deficiency Judgments	●	○	◐	◐	○	◐	◐	●	●	◐	◐	○	○	●
Accounting of Sale Proceeds	●	●	◐	●	○	◐	○	○	●	○	◐	◐	◐	○
Prompt Return of Surplus	●	●	●	●	○	●	◐	◐	●	○	●	◐	●	○

	IN	IA	KS	KY	LA	ME	MD	MA	MI	MN	MS	MO	MT	NE
Pre-Sale Protections														
Access to Court Review	○	○	○	○	◐	○	●	●	●	●	●	●	●	●
Loss Mitigation Requirement before Foreclosure	●	●	●	●	●	●	●	●	●	●	●	●	●	●
Right to Cure before Acceleration	●	◐	●	●	●	◐	●	○	●	●	●	●	●	●
Right to Reinstate before Sale	◐	●	●	●	●	◐	◐	●	●	◐	◐	●	◐	◐
Personal Service Requirement for Complaint or Sale Notice	●	○	●	●	◐	○	○	●	●	○	●	●	●	●
Housing Emergency Assistance Fund	●	●	●	●	●	◐	○	●	◐	○	●	●	●	●
Post-Sale Protections														
Right to Redeem	●	○	◐	◐	●	◐	●	●	◐	○	●	◐	●	●
Deficiency Judgments	●	◐	◐	●	◐	◐	●	●	◐	○	●	●	○	○
Accounting of Sale Proceeds	◐	◐	◐	◐	◐	○	○	○	◐	◐	●	●	◐	◐
Prompt Return of Surplus	●	●	●	●	●	●	●	●	●	●	●	●	●	●

Key: ○ = strong ◐ = mixed ● = weak or nonexistent

State Foreclosure Statutes at a Glance *(continued)*

Strengths and Weaknesses

	NV	NH	NJ	NM	NY	NC	ND	OH	OK	OR	PA	RI	SC	SD
Pre-Sale Protections														
Access to Court Review	●	●	○	●	○	◐	○	○	◐	●	○	●	○	◐
Loss Mitigation Requirement before Foreclosure	●	●	◐	●	◐	●	●	◐	●	●	◐	●	●	●
Right to Cure before Acceleration	◐	●	○	●	●	◐	◐	●	◐	●	○	●	●	●
Right to Reinstate before Sale	●	●	○	●	○	●	●	●	●	○	○	●	●	●
Personal Service Requirement for Complaint or Sale Notice	●	●	○	●	○	●	○	●	○	○	○	●	●	○
Housing Emergency Assistance Fund	●	●	○	●	●	○	●	●	●	●	○	●	●	●
Post-Sale Protections														
Right to Redeem	●	●	◐	○	●	◐	◐	◐	◐	●	●	●	●	○
Deficiency Judgments	◐	●	○	◐	◐	◐	○	◐	○	○	◐	●	◐	◐
Accounting of Sale Proceeds	◐	○	○	◐	○	◐	◐	○	○	◐	○	●	○	○
Prompt Return of Surplus	●	◐	◐	●	○	◐	●	○	●	●	○	●	●	●

	TN	TX	UT	VT	VA	WA	WV	WI	WY
Pre-Sale Protections									
Access to Court Review	●	●	●	○	●	●	●	○	●
Loss Mitigation Requirement before Foreclosure	●	●	●	●	●	●	●	●	●
Right to Cure before Acceleration	●	◐	●	●	●	●	◐	●	●
Right to Reinstate before Sale	●	●	◐	●	●	○	●	○	●
Personal Service Requirement for Complaint or Sale Notice	●	●	●	○	●	●	●	○	●
Housing Emergency Assistance Fund	●	●	●	◐	●	○	●	●	●
Post-Sale Protections									
Right to Redeem	●	●	●	●	●	●	●	◐	◐
Deficiency Judgments	●	◐	○	◐	●	○	●	◐	●
Accounting of Sale Proceeds	●	●	◐	○	◐	◐	◐	○	◐
Prompt Return of Surplus	●	●	●	○	●	●	◐	◐	●

Key: ○ = strong ◐ = mixed ● = weak or nonexistent

II. Scope of the Foreclosure Crisis

We are facing the greatest foreclosure crisis since the Great Depression. The statistics are grim. For 2008, foreclosure filings nationwide were up 81% over 2007 filings.[1] Completed foreclosures in 2008 will likely exceed the one million mark.[2] That annual figure translates into more than 3,700 foreclosures every business day. As of July 2008, bank-owned property (REO) represented more than 16 percent of the inventory of existing homes for sale.[3] In some communities, bank-owned properties make up nearly 40 percent of existing inventory.[4]

In both the prime and subprime markets, seriously delinquent[5] loans have continued to rise at an alarming rate, increasing three-fold since early 2006.[6] The figures for adjustable rate mortgages (ARMs) are more shocking. Seriously delinquent ARMs have more than quadrupled in the past two and a half years.[7] By the third quarter 2008, nearly 3 out of 10 of subprime ARMs were more than 90 days late or in foreclosure.[8]

As of November, 2008 the FDIC had reported that 1.6 million loans were over 60 days delinquent.[9] The FDIC estimates that through the end of 2009, there will be an additional 3.8 million new loans over 60 days past due.[10] Nationwide it is estimated that 8.1 million mortgages will be in foreclosure over the next four years, through the end of 2012.[11]

The consequences of this foreclosure crisis are enormous, ripping through both Wall Street and Main Street. Abuses in the subprime market have undermined the efforts of hardworking families to acquire and maintain the dream of homeownership. Instead of building wealth, families are losing equity.[12] Worse yet, some foreclosed families are unable to find replacement shelter and become homeless.[13] Renters suffer too, as lenders quickly evict tenants from foreclosed homes.[14] More and more Americans are being driven into bankruptcy.[15] Neighborhoods are deteriorating as foreclosed homes are boarded up and left vacant.[16] Crime in high-foreclosure neighborhoods is on the rise.[17] Overgrown lawns and trash-strewn yards symbolize growing community abandonment and disinvestment.[18]

III. The Role of the Foreclosure Process in the Deepening Crisis

State Foreclosure Laws Escape Reform

Most Americans not well-versed in property law would assume that homeowners have greater rights than renters, or at least equal rights. The stark reality is that while most states updated their landlord/tenant laws decades ago to give renters basic due process protections in the eviction process, no similar reform effort has been made to assist homeowners in the foreclosure process.

Many state foreclosure laws were enacted in the 19th and 20th centuries and have gone largely unchanged since that time. These laws came into effect at a time when the residential mortgage industry, to the extent it existed at all, bore no relation to what exists today. Significantly, these laws pre-date the enormous changes in the mortgage market that began in the 1980s. The typical American pursuing the homeownership dream before the 1980s would have obtained a mortgage made by a bank using accepted underwriting guidelines which considered the homeowner's ability to repay the loan. Risks to the lender and the homeowner were kept in check by ensuring that the loan amount did not exceed an appropriate loan-to-value ratio, based on a sound property appraisal. Mortgage loans made before the 1980s were typically kept in the bank's own portfolio of loans and not assigned to another entity, and would have been serviced by that same bank.

The 1990s saw the increasing use of asset-based securities to fund an ever increasing supply of mortgage credit.[19] Creating capital flow in this way, subprime mortgage lending took off during this period.[20] Homeowners were encouraged, often through aggressive marketing campaigns that deceptively touted lower payments and tax benefits, to use their home equity to consolidate non-mortgage debts. Practices such as charging high points and fees and flipping loans through multiple refinancings often stripped homeowners of their most valuable asset, the equity in their homes, bringing many to the brink of foreclosure. The advent of today's more dangerous "exotic" subprime mortgages sealed the fate of many homeowners, spiraling the mortgage market downward into the current full-blown foreclosure crisis.

The securitization process also brought about significant changes in the way homeowners deal with their mortgage company. Servicing rights are often assigned independently of the mortgage. Homeowners have no choice about servicing companies when taking out the mortgage and have no ability to switch when problems arise.[21] Some servicers have been too aggressive in pursuing foreclosure without offering workout options. They may also be the cause of the homeowner's foreclosure problem due to negligent servicing or the imposition of excessive and unauthorized fees.[22]

MORTGAGE SERVICING ABUSES

Abusive servicing occurs when a servicer seeks to collect unwarranted fees or other costs from borrowers, engages in unfair collection practices or through its own improper behavior precipitates borrower default or foreclosure.[23] Some well documented examples include:

- misapplying payments;
- force-placing insurance for borrowers who have already provided evidence of insurance;
- failing to pay property taxes when due, triggering governmentally imposed late fees and penalties, or sometimes the forced sale of the home;
- charging late fees when borrowers are current on their payments
- engaging in coercive collection practices and falsely claiming amounts due;
- failing to offer and respond to requests for loss mitigation alternatives.

Despite the enormous changes in the mortgage market, our state foreclosure laws have remained frozen in the past. They have eluded modernization that would ensure homeowners their basic constitutional rights before they are deprived of their property and shelter.

States Should Act Now

The foreclosure crisis continues to spin out of control. Modernization and improvement of state foreclosure laws can significantly help blunt the impact of the crisis on individual homeowners and communities. The method by which homes are foreclosed in this country is almost exclusively controlled by state law. States have historically decided under what circumstances a homeowner can lose a home to foreclosure and what procedure a mortgage holder must follow. This traditional role for states presents a tremendous opportunity for state policymakers to take a fresh look at their foreclosure laws. While reform of state foreclosure laws will not end the current foreclosure crisis, it can significantly reduce the number of foreclosures. For example, research has shown that securitized mortgages in states with creditor-friendly foreclosure laws that permit quick foreclosure are less likely to be modified and are foreclosed at a higher rate than in states that afford protections to homeowners.[24]

Too often foreclosures occur because homeowners are not aware of the process itself and of the options to avoid foreclosure. Rather than adopt a triage approach in which homeowners with an interest and ability to retain their homes are given a serious opportunity to explore loan modification and other sustainable foreclosure avoidance options, state foreclosure laws often shunt borrowers into complicated legal proceedings that in many states lack oversight by a judicial officer or other basic due process protections. Rather than promote reconciliation and settlement, the arcane procedures in many states further isolate homeowners and create a sense of hopelessness. Importantly, states can take steps that will make it possible for large numbers of needless foreclosures to be avoided. This report points out the strengths and deficiencies in state laws and recommends ways they may be improved.

IV. Data and Methodology

For many years, the National Consumer Law Center has compiled and reported information about state foreclosure laws. One of our publications, *Foreclosures* (2d ed. 2007 and 2008 Supp.) contains an extensive discussion of foreclosure court decisions and a summary of each state's foreclosure laws. In preparing this report, we relied upon this data and supplemented it with research on recent state initiatives involving loan modification and foreclosure diversion programs.

To evaluate state foreclosure laws, we developed a set of questions designed to determine whether certain basic protections are provided for residential homeowners. Each state was reviewed based on the following questions:

1. Before losing their home to foreclosure, do homeowners have access to a court proceeding in which they can present objections and pursue options to avoid foreclosure?
2. Are mortgage holders required to engage in meaningful loss mitigation efforts before a home mortgage may be foreclosed?
3. Are homeowners given a right to cure a mortgage default for at least 60 days before the loan is accelerated and before any legal fees or foreclosure costs are incurred?
4. Are homeowners provided notice of the right to reinstate after acceleration but before sale, by bringing the loan current including foreclosure fees and costs?
5. Are homeowners provided personal service of the notice of sale or foreclosure complaint?
6. Does the state have a housing emergency assistance fund or similar program to assist homeowners in default due to temporary financial difficulties?
7. Are homeowners provided protections after the foreclosure sale, such as redemption rights, limitations on deficiency judgments, and procedures for accounting and return of surplus sale proceeds?

The answers to these questions for each state are compiled in Appendix A, Survey of State Foreclosure Laws. The results are based on laws in effect as of December 2008. While many states have rarely made changes to their foreclosure laws, as discussed earlier, we are pleased to report that a number of states have very recently enacted new laws in response to the foreclosure crisis. We are hopeful that many more states will follow this lead, perhaps after considering how they appear in this report. Thus, we hope to continue reporting on state law changes by regularly updating the Survey of State Foreclosure Laws and making it available on the Center's website at www.consumerlaw.org.

In Part V of this report we provide a detailed discussion of the homeowner protections addressed in the survey questions. Results of the survey are provided for each question. Finally, we conclude the discussion of each topic with a set of recommendations state policymakers might consider in reforming state foreclosure laws.

V. Findings and Recommendations

1. *Provide access to a court proceeding in which the homeowner has an opportunity to present objections and to pursue options to avoid foreclosure.*

Access to justice

A fundamental due process protection is the "opportunity to present objections" to an impartial decision-maker before an individual's property can be taken away.[25] Recognition and wide acceptance of this essential right led to reform of state eviction laws beginning in the 1960s and the elimination of "self-help" evictions in which landlords could physically remove a tenant's belongings and padlock the door without any court proceeding. In virtually every state, tenants are now given the right to a hearing before a judge in a proceeding initiated by the landlord before they may lose the right to possession of their residence and be evicted. Although firmly accepted in the rental context, our state laws have not embraced this fundamental right for all homeowners.

In **thirty states** and the **District of Columbia**, homeowners can lose their homes to foreclosure with no court oversight over the process and without an opportunity to be heard. In these states, foreclosures are accomplished by the mortgage holder's exercise of the "power of sale" contained in the mortgage or deed of trust. The mortgage holder does not need to initiate a court proceeding to foreclose and the homeowner has no clear access to a court hearing. The holder typically only needs to send a notice of sale to the homeowner, place a legal advertisement in a local newspaper, and hire an auctioneer to sell the property on the scheduled sale date.

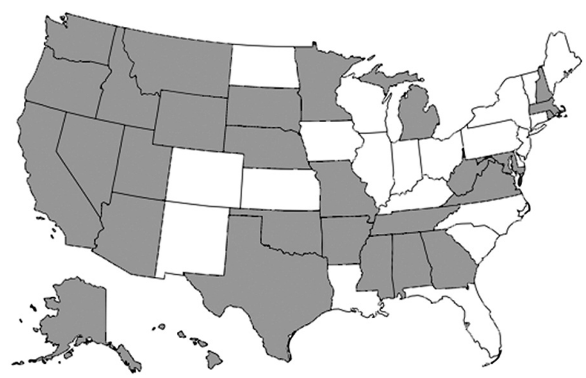
If the homeowner disputes that there has been a default in a non-judicial foreclosure state, there is often no one that a homeowner can turn to in the foreclosure process to resolve the dispute. To contest a foreclosure by power of sale, the homeowner must file an affirmative court action and request an injunction to stop the sale. If this step is not taken, there will be no judicial involvement at all in the foreclosure. The homeowner will need to satisfy the demanding pleading and proof requirements which courts impose before issuing injunctions, making it virtually impossible to obtain this relief without the assistance of an attorney. Most courts also require that a bond be posted prior to the issuance of any injunctive relief. In many cases, these bonds are set at an amount in excess of the amount that may be in dispute and effectively shut the courthouse doors to most homeowners.

Without some judicial oversight over the foreclosure process, mortgage servicer errors go unchallenged and homeowner defenses that could prevent foreclosure are not addressed. For example, a homeowner in Massachusetts spent several years trying to get a straight answer from her mortgage servicer while it continued to foreclose on her home.[26] Shortly after she received notice that the servicer had taken over servicing of her mortgage, she and a housing counselor assisting her made numerous attempts to get information about the account and an itemized payoff figure. The servicer first sent a letter stating that the total payoff amount was $264,603.13, but then one week later claimed it was owed $363,603.38. During the next two-year period, the servicer and its foreclosure attorneys quoted six different payoff figures on the mortgage ranging from a low of $121,948.38 to a high of $430,707.28. With no judge overseeing the power of sale foreclosure, the homeowner eventually had to file bankruptcy to stop the sale and try to sort things out. It was revealed in the bankruptcy court that the servicer had never obtained a payment history on the account from the old servicer and did not even have a copy of the original loan documents. The bankruptcy judge found that the servicer had "in a shocking display of corporate irresponsibility, repeatedly fabricated the amount of the Debtor's obligation to it out of thin air." None of this would have come to light if there had not been a court proceeding to compel disclosure by the servicer. And if there had been a judicial foreclosure proceeding, the homeowner could possibly have avoided filing bankruptcy.

> HOW JUDICIAL FORECLOSURE WORKS
>
> In less than half of the states, mortgages are always foreclosed by judicial action, either because of state law requirements or local custom. In these states the mortgage holder must file an action in court, usually in the county where the property is located, to obtain a judicial decree authorizing a foreclosure sale. Generally, to obtain a judgment, the party seeking to foreclose must prove that there is a valid mortgage between the parties, that it is the holder of the mortgage or proper party with authority to foreclose, that the borrower is in default, and that the proper procedure has been followed. The homeowner then has an opportunity to raise defenses to the foreclosure, such as the alleged default did not exist, the mortgage is invalid based on violations of state and federal consumer protection laws, or the servicer accepted but failed to process an application for a loan workout. The homeowner can also bring affirmative claims against the mortgage holder which may offset amounts claimed to be in arrears.
>
> If the homeowner and mortgage holder are unable to resolve the dispute, the court may accept the defenses, dismiss the foreclosure action, and award other relief based on the homeowner's affirmative claims. If the court concludes, after considering any defenses, that there has in fact been a default and that the mortgage holder has the legal right to foreclose, the court will determine the total amount owed. In some states the homeowner has the right to pay this amount to avoid foreclosure. If this amount is not paid by a deadline set by the court, the foreclosure will proceed, usually according to local rules or statutes governing foreclosure sales. Typically the sale is conducted by the sheriff or other public officer appointed by the court. In many states after the sale the court must review the sale procedures and confirm that the sale was conducted in accordance with the law. (Additional post-sale protections are discussed in Section 7, *infra*.).

Survey Results

As mentioned, in **thirty states and the District of Columbia**, the most common form of residential home foreclosure is by non-judicial power of sale.[27] In these states, homeowners generally do not have a meaningful opportunity for court review before their home is lost to foreclosure. After the auctioneer's hammer falls in most states, the sale itself is final and cannot be undone, regardless of any claims and defenses the homeowner might have been able to assert before the foreclosure.[28] Only after the foreclosure sale is there a court proceeding in these states to remove a homeowner who does not voluntarily vacate, but by then it is usually too late to contest the sale.



States Which Do Not Require Court Involvement in Foreclosures

Alabama	Montana
Alaska	Nebraska
Arkansas	Nevada
Arizona	New Hampshire
California	New Mexico
District of Columbia	Oklahoma
Georgia	Oregon
Hawaii	Rhode Island
Idaho	South Dakota
Maryland	Tennessee
Massachusetts	Texas
Michigan	Utah
Minnesota	Virginia
Mississippi	Washington
Missouri	West Virginia
Wyoming	

In all of these states foreclosure occurs without judicial involvement. Homeowners have no opportunity to present any claims or defenses to a judge unless they file an affirmative lawsuit in court.

Oklahoma is an exception as a power of sale state, offering a hybrid-type procedure. If an Oklahoma mortgage includes a power of sale, which most do, the mortgage document itself must contain a warning that the mortgage holder can "take the mortgaged property and sell it without going to court" upon default.[29] The mortgage document must also include a disclosure that if the homeowner sends a written notice by certified mail to the mortgage holder that a "judicial foreclosure is elected" at least ten days before the home is to be sold under the power of sale, the mortgage holder must stop the power of sale foreclosure and renew the foreclosure in a judicial proceeding.[30] This right to elect a judicial proceeding must also be prominently disclosed in the notice of sale which is personally served on the homeowner.[31]

Similar to Oklahoma, **South Dakota** also permits a homeowner to request that a power of sale foreclosure be converted to a judicial action.[32] However, this conversion is not automatic upon notification to the mortgage holder as the homeowner in South Dakota must first submit an application making the request to a court which handles foreclosures.

North Carolina is also unique in that several protections have been added to its power of sale procedure. The mortgage holder in North Carolina must first serve a "notice of hearing" on the homeowner and file it with the clerk of court.[33] A hearing is then held before a clerk who determines whether 1) there is a valid debt, 2) there has been a default, 3) the mortgage holder legally has the right to foreclose, and 4) proper notice has been given.[34] If the clerk finds that all of these conditions have been met, the clerk can authorize the issuance of a notice of sale and the mortgage holder can proceed under the power of sale. The clerk's decision can be appealed to a judge. North Carolina's procedure was enacted in response to a 1975 court decision which struck down the existing procedures on constitutional grounds because they did not provide minimum due process.[35]

Of the states which require judicial foreclosure, several have recently implemented mediation or diversion programs as part of their foreclosure process. In each of these states, **Connecticut, Florida, New York, New Jersey, Ohio,** and **Pennsylvania,** procedures implementing the programs have been developed by the court system. These programs are discussed more fully in the next section and summarized in Appendix B.

Recommendations for Homeowner Protections

The current foreclosure crisis, with its devastating impact on affected families, local communities, and property values, presents a call to action for state policy makers. Now more than ever states should consider bringing their foreclosure laws into the 21st century by ensuring that basic due process protections and foreclosure avoidance procedures are afforded to all homeowners. At a minimum, residential homeowners must be afforded a meaningful opportunity to present whatever grievances they may have to an impartial and disinterested court official. States should either completely abandon the power of sale method and require judicial foreclosure, or they should look to ways in which essential protections are incorporated into the existing non-judicial procedure. States which currently have judicial foreclosure procedures should consider innovations to facilitate foreclosure avoidance settlements, such as court-mandated mediation programs or settlement conferences. Specific recommendations include:

1. Require Judicial Foreclosure

The most obvious way to give homeowners access to justice is to require judicial foreclosure, as twenty-one states currently do. In most states that permit power of sale foreclosures, a mortgage holder currently has the option to bring a foreclosure action in court, so there already exists a structure and legal framework for judicial foreclosures in those states. Thus, this change would not require a substantial rewriting of a state's foreclosure laws.

2. Create a Hybrid System

States wishing to retain the power of sale structure can improve access to justice by enacting laws which create a hybrid procedure in which the process would begin as non-judicial but would convert to a court procedure if a homeowner seeks review of an unfavorable workout decision or responds by asserting foreclosure defenses. This process would require the mortgage holder to initiate a court action after some triggering event, such as receipt of a formal response from the homeowner to a notice invoking the power of sale. While many foreclosures would probably still proceed without court involvement under this regime, homeowners having legitimate foreclosure defenses and claims would not be deprived of an opportunity for court review.

3. Establish Streamlined Procedure for Homeowner to Invoke Court Review

Another approach to reform in non-judicial foreclosure states would be to establish a simple and low-cost alternative procedure for homeowners to seek judicial review of a mortgage holder's right to foreclose by power of sale. Borrowing from landlord/tenant procedures in many states, the law would create plain language legal forms that could be used easily by homeowners who are unrepresented by counsel. It is essential that homeowners have an opportunity for court review without having to post a bond, and that no other financial barriers to court access be imposed. Moreover, homeowners under this procedure should not be required to obtain a court injunction to stop the sale. The filing of the court action by the homeowner should come with an automatic stay of the sale issued by the court, similar to the automatic stay entered upon the filing of a bankruptcy case,[36] at least until some preliminary court hearing can he held. Similar to bankruptcy law, the procedure could include provisions to prevent abuse if the homeowner invokes the procedure more than once during a certain period of time such as one year.[37] While most homeowners would not avail themselves of the procedure, it would help eliminate wrongful foreclosures by providing a meaningful check on a mortgage holder or servicer's decision to foreclose.

4. Require Participation in Mediation Programs

Both judicial and non-judicial foreclosure states can improve their procedures by requiring that the parties confer and consider all options to avoid foreclosure. The hearing procedure in judicial foreclosure states should recognize and treat separately homeowners facing payment default who are seeking to negotiate a loan modification or workout agreement with the mortgage holder, or who wish to access other loss mitigation options. If a resolution is not reached by the parties on their own, they should be referred to a court mediation program. A similar program can be set up in non-judicial foreclosure states. This recommendation is discussed more fully in the next section.

2. Provide that mortgage holders must engage in meaningful loss mitigation efforts before a home mortgage may be foreclosed.

Loss mitigation reduces investors' losses

Loss mitigation was first developed by the Federal Housing Administration (FHA) as a way of balancing its purpose of facilitating homeownership with the need to be fiscally responsible with the federal government's funds.[38] In the context of pre-foreclosure practice, loss mitigation is essentially a mechanism that requires an evaluation of whether there is an alternative to foreclosure that will *reduce* the losses to the investor from the homeowner's default. The losses that are measured in this context are the investor's, rather than the homeowner's. Nevertheless, homeowners have traditionally benefitted from loss mitigation programs because they avoid the loss of the home.

Fannie Mae and Freddie Mac are both government sponsored enterprises (“GSEs”) created by federal charter as private, for-profit entities with the mission of facilitating and supporting homeownership.[39] In recognition of their public purpose, as well as the reality that loss mitigation efforts provide more income for the investor, Fannie Mae and Freddie Mac have followed the lead of the FHA in this regard. Both agencies have loss mitigation regulations which servicers are required to follow before initiating a foreclosure.

Investors and servicers of securitized, privately-held mortgages have also come to recognize the benefits of loss mitigation strategies, though such efforts are generally encouraged rather than mandated. The servicing contracts for loans held by private investors often include a loss mitigation plan and contain a standard clause allowing the servicer to modify seriously delinquent or defaulted mortgages, or mortgages where default is “reasonably foreseeable.”[40]

Despite widespread acceptance in the mortgage industry that loss mitigation efforts can reduce foreclosure rates, reduce investor losses, and save homes, most state foreclosure laws fail to incorporate any notice or opportunity for homeowners to access such options before or during the foreclosure process, and do not require that they be pursued by the mortgage holder as an alternative to foreclosure.

Loss mitigation options

Loss mitigation covers a range of measures to avoid foreclosure. For homeowners who wish to retain their homes, the common options include:

- **Repayment Plan**—which allows the homeowner to get current by making regular mortgage payments plus an amount on the arrears spread out usually over a period of less than six months;
- **Forbearance Plan**—which is also a payment plan that may reduce or suspend the homeowner’s payments for a period generally no more than twelve months;
- **Loan Modification**—which involves modifying the mortgage, such as by changing the interest rate or term of the mortgage, capitalizing arrears by adding them to the mortgage, and reducing the principal balance of the mortgage.

For homeowners who no longer wish to keep their homes, the options include:

- **Short Sale**—which allows the homeowner to sell the home before the foreclosure at an amount less than the mortgage balance;
- **Deed in Lieu**—which involves the mortgage holder or servicer accepting a deed for the home from the borrower in exchange for dropping the foreclosure process.

Voluntary efforts lacking

Among the loss mitigation options, loan modification has been identified as one of the preferred strategies for addressing the current foreclosure crisis.[41] In fact, because many of the loans in or soon to be in foreclosure were made without considering the homeowner’s ability to pay or were underwritten using inflated property appraisals, any plan to ameliorate the current crisis that does not include some form of loan modification as an essential component will fail. While the potential benefits of loan modifications are clear,[42] the response from the financial services industry has been lacking and is dwarfed by the magnitude of the foreclosure problem.

Since the start of the current foreclosure crisis, there have been several efforts to encourage loan modifications through voluntary measures. In September 2007, the federal and state banking regulators issued a joint statement on loss mitigation strategies, referencing earlier guidance and encouraging use of loss mitigation authority available under pooling and servicing agreements.[45] In October 2007, as part of the HOPE NOW program, Treasury Secretary Paulson sought voluntary commitments from servicers to contact borrowers and explore new loan modification approaches.[46] Then in December 2007, Secretary Paulson announced a plan for "fast track" loan modifications.[47]

WHAT IS A LOAN MODIFICATION?

A loan modification is a written *change* to the agreement between the mortgage holder (or its servicer) and the homeowner that alters one or more of the original terms of the note so that the loan will no longer be considered in default. The goal of a loan modification is to prevent foreclosure and facilitate the homeowner's ability to keep up with regular payments on the loan.[43] Loan modifications may be for short or long terms, or for the life of the loan. Modifications may do any or all of the following:

- capitalize the overdue amounts of interest, escrow items and fees in the mortgage amount (adding these amounts to the principal and making the payments higher than before);
- waive interest, late fees and other default related fees;
- reduce the interest rate and/or make it fixed (for the life of the loan or for a set period of time);
- reduce the principal of the loan;
- defer payment of loan principal for a period of time (resulting in a "balloon" payment at the end of the loan);
- extend the term of the loan, generally by re-amortizing the remaining amount due over a new 30-year term, or in some cases extending it to 40 years.[44]

Despite these efforts, the financial services industry has failed to implement a loan modification strategy to stop the foreclosure crisis. The HOPE NOW program issued its first data in early 2008, demonstrating that little progress had been made.[48] The Mortgage Bankers Association's report on loan modifications issued in January 2008 revealed similar results. The major finding was that, in the third-quarter of 2007, mortgage servicers worked out 183,000 repayment plans and 54,000 loan modifications, while starting 384,000 new foreclosures.[49] Both reports confirmed that servicers relied heavily during this period on repayment plans rather than loan modifications. Repayment plans require homeowners to make increased monthly payments to cure arrears. They do not address payment affordability problems caused by high interest rates and rate resets on adjustable rate mortgages.

A recent study illustrates that problems persist and that the industry has not yet engaged in meaningful loan modifications.[50] When loan level information from service remittance reports from July 2007 through June 2008 was analyzed, the conclusion was inescapable that:

> *[W]hile the number of modifications rose rapidly during the crisis, mortgage modifications in the aggregate are not reducing subprime mortgage debt. Mortgage modifications rarely if ever reduced principal debt, and in many cases increased the debt. Nor are modification agreements uniformly reducing payment burdens on households. About half of all loan modifications resulted in a reduced monthly payment, while many modifications actually increased the monthly payment.*

A report by Credit Suisse reaches similar results in finding that loan modification progress is slow and that plans with higher payments are more common than modifications with lower payments.[50] As of August 2008, Credit Suisse reported that modifications accounted for just 3.5 percent of the loans that are delinquent for sixty days or more. Moreover, after modifications that freeze the interest rate at the pre-reset amount, the most common form of modification was one in which the payment increased.

Mortgage modifications which do not reduce principal balances or interest rates generally also fail to reduce the monthly payments. This means that while there may be some delay, ultimately, these mortgage loans will still fail. Loan modifications with higher payments re-default almost half of the time.[52] Not surprisingly, modifications involving principal reduction are much less likely to default again.[53]

AFFORDABLE PAYMENTS NEEDED

A Massachusetts homeowner's failed attempt to get an affordable modification as reported in the *Boston Globe* helps illustrate that affordable payments are needed:

> *Ask LaWanda Fils. This single mother was behind on payments on her Dorchester two-family home when she asked for help from her lender, Option One Mortgage Corp. The solution Option One offered didn't seem to make sense—she would pay $800 a month more, after rolling in past-due principal, taxes, and insurance. Desperate to save her home, Fils agreed to the deal anyway in February.*
>
> *Two months later, she defaulted and now is again facing foreclosure.*
>
> *"I think it is more for them to pat themselves on the back to say at least they tried," said Fils. "It's not feasible and it doesn't work and they end up having people falling behind."*
>
> * * *
>
> *"I don't know why a lender would enter into that kind of agreement knowing what the outcome would be," said Kevin Cuff, executive director of the Massachusetts Mortgage Bankers Association. "Why would it not go into foreclosure? Why would it not fail?"*

Reworked Mortgages Not Working, Boston Globe, December 9, 2008.

Unless mandated, homeowners can't find the decision-maker

From the homeowner's perspective one of the biggest obstacles to loan modification is finding a live person who can provide reliable information about the loan account and who has authority to make loan modification decisions. Stories abound of exasperated homeowners attempting to navigate vast voice-mail systems, being bounced around from one department to another, and receiving contradictory information from different servicer representatives.[54] For example, a Neighborhood Housing Services of Chicago survey found that "countless counselors shared stories of having a client in the office ready to begin dealing with long-deferred financial problems, but then having to wait 30 minutes or more in order to talk to an appropriate loss mitigation staff person."[55] Unfortunately, things have only gotten worse as servicers struggle to keep up with the increased workload caused by the foreclosure crisis.[56] When asked to comment on the problems, one housing counseling agency stated the following about some mortgage servicers: "1. They do not return calls; 2. Take 30–60 days to give us a written answer; 3. Require their own authorization to release information forms; 4. Take too long to assign cases; 5. Keep changing officers when cases are assigned; 6. They give wrong information regarding the loan; 7. Always have to refax and explain the situation to different people; 8. Customer Service sends us to the wrong department; 9. They hang up; and 10. Never willing to work any details—they always have new personnel."[57]

Court-ordered mortgage modifications

While federal bankruptcy law generally permits claims of secured creditors to be modified in bankruptcy cases, it currently singles out home mortgage claims and shields them from modification, other than through a plan which cures a mortgage default. This provision in the Bankruptcy Code prevents homeowners from changing the interest rate, amortization, or term of mortgage loans in a chapter 13 case, the type of bankruptcy consumers often file to save a home from foreclosure. Several bills pending in Congress would repeal this provision and allow modification of home-secured loans in chapter 13 cases.[58] This change in the law would greatly assist homeowners and would complement state laws that encourage loan modifications outside of bankruptcy.

Survey Results

While loss mitigation in general—and loan modifications specifically—have gained acceptance as strategies for assisting all parties after mortgage defaults, clear requirements have not been incorporated into state foreclosure laws. No states have amended their foreclosure laws to require that mortgage holders engage in loss mitigation efforts before a home mortgage may be foreclosed. Although limited in scope, several states have taken steps in the right direction. **California** and **Connecticut** have enacted laws requiring notice of an opportunity for a meeting before a foreclosure. **New York** now has a law that mandates mediation in many home foreclosures. In addition, several judicial foreclosure states have implemented court-annexed mediation programs.

Mandated Contact. In a law which went into effect in September 2008, **California** now requires that before sending a notice of default, the mortgage holder or its servicer must contact the borrower in person or by telephone in order to "assess the borrower's financial situation and explore options for the borrower to avoid foreclosure."[59] During this initial contact, the holder or servicer must advise the borrower that he or she has the right to request a subsequent meeting. The law does not specify what should occur at the meeting or provide any clear enforcement mechanism if the holder or servicer does not offer any meaningful workout options or negotiate in good faith. Also, California is a non-judicial foreclosure state, and the law fails to add any process for court or some third-party review if the borrower is dissatisfied with the outcome. These significant limitations may cause the law to have a limited impact.

During the initial contact under this new California law, the holder or servicer must also advise the borrower that a subsequent meeting, if requested, shall be scheduled to occur within 14 days and may be held telephonically. The notice must also give the borrower the Department of Housing and Urban Development (HUD) toll-free telephone number to find a HUD-certified housing counseling agency. The borrower may designate a housing counselor or attorney to discuss workout options with the holder or servicer. Assessment of the borrower's financial situation and discussion of options may occur during the first contact or at the subsequent meeting. Any notice of default may not be sent until 30 days after contact is made with the borrower and the notice must include a declaration that the holder or servicer contacted the borrower or diligently tried to make contact.

The California law applies only to loans on owner-occupied residences made between January 1, 2003 and December 31, 2007, and the law will remain in effect only until January 1, 2013 unless extended.

Court Sponsored Mediation Programs. A number of states and cities have adopted mediation programs in response to the current foreclosure crisis. Appendix B, *infra*. provides a summary of the known programs.

Philadelphia's program is the most ambitious and—by many informal accounts—quite successful. It is mandatory for all mortgage foreclosure cases in which the property is residential, owner-occupied and located in Philadelphia County. **Allegheny County, Pennsylvania courts** and those in **several Florida judicial districts** also have mandatory mediation programs.

The supreme courts of **New Jersey, New York,** and **Ohio** have established voluntary mediation programs for local courts to modify and use as each court determines is appropriate. Unfortunately, local courts are not required to use the programs in all instances. **New York** has added a notice to the foreclosure complaint which advises borrowers of the right to request a settlement conference.

Local advocates attribute the success of the Philadelphia mediation program in substantially reducing foreclosures to a number of critical factors:

- There are several parties at every conference: 1) the representative of the mortgage holder who is *required to have authority to modify the mortgage*; 2) an independent person (usually a local attorney unaffiliated with the mortgage industry) who acts as the mediator in the conference; 3) the homeowner, and 4) generally a trained housing counselor who is familiar with the dynamics of both the foreclosure process in the city and the different types of, and arguments in support of, the variety of loan modifications which will make the loan sustainable and affordable.

- The community group ACORN has been hired by the City to go door-to-door to personally explain the mediation process, its benefits and procedures to homeowners facing foreclosure.
- Housing counselors—with the permission of the homeowner—prepare and submit a written proposal to the holder's attorney before the conference outlining ways to mitigate the foreclosure.
- The program builds on the availability of the state Homeowners' Emergency Mortgage Assistance Program (HEMAP)[60] which has funds available to make modified loans more affordable to homeowners and acceptable to mortgage holders.

Recommendations for Homeowner Protections

The most effective way to ensure that mortgage holders and their servicers attempt in good faith to negotiate meaningful loan workouts with homeowners is to incorporate the requirement into the state's foreclosure laws and make it a condition precedent to foreclosure. The law should require that before a foreclosure may proceed, the mortgage holder must prove that it or its servicer explored all reasonable options to avoid foreclosure with the homeowner before the foreclosure was initiated.

States can employ a number of strategies to bridge the huge communication gap between mortgage holders and homeowners. These strategies include:

- Notice regarding the availability and benefits of loan modification and other loss mitigation programs should be provided to homeowners very early in the foreclosure process, and other outreach efforts required. Care should be taken to make the notice stand out from other notices, letters or solicitations (often from foreclosure rescue scammers) the homeowner might receive.
- Loan modifications and workouts must be considered before a foreclosure can proceed. The failure to satisfy this requirement should be treated in the foreclosure proceeding as a defense to foreclosure.[60]
- Diversion programs should be established and funded. If a resolution is not reached by the parties after considering options to avoid foreclosure, they should be referred to a mediation program under the supervision of the foreclosure court or an appropriate state agency. The procedure should ensure that the foreclosure process is stayed until a decision is made on any pending workout application and any further mediation efforts are concluded. To be effective the program must require that a representative of the mortgage holder with authority to approve a loan modification or other workout be present or readily available at the mediation sessions.

3. Provide notice of default and right to cure, with a cure period of at least 60 days, before acceleration and before any legal fees or foreclosure costs are incurred.

Pre-acceleration right to cure and notice

When a homeowner receives a letter from a mortgage holder declaring that a home mortgage has been accelerated, the impact can be devastating. A typical acceleration letter announces that the entire loan balance, along with an assortment of costs and fees, must be paid immediately. If the homeowner does not pay the full loan balance right away, the letter states that the mortgage holder will go ahead with the foreclosure and sale of the home. Essentially, an acceleration notice informs homeowners that they have lost the right to pay off the loan in monthly installments. Just making up the missed payments will not stop the foreclosure.

Upon receipt of such a notice, which is often sent by a lawyer who represents the mortgage holder, it is not surprising that many homeowners view their situation as hopeless. They do not know where to turn, do not seek out alternatives to foreclosure, and simply await the inevitable sale and eviction.

Neither mortgage holders nor borrowers have anything to gain from creating this premature sense of hopelessness, particularly when a foreclosure can be prevented by some relatively simple steps. State law requiring that the mortgage holder give the homeowner a notice of default *before* accelerating the loan and charging default fees provides an effective antidote to an uninformed borrower's impulse to lose hope and walk away from the mortgage obligation prematurely. Contrary to the unilateral fiat conveyed by many acceleration notices, there are often options short of full payment of the loan that can prevent foreclosure after a default in payments. A mandatory pre-acceleration notice informing the homeowner of these options ensures that homeowners receive accurate information about the means to avoid foreclosure.

Opportunity to cure when it can make a difference

It is critically important that homeowners be given an opportunity to cure early in the process before default fees accrue and the costly formal foreclosure proceedings begin. If the homeowner is not given this right, the amount needed to cure immediately before and after acceleration can dramatically increase, often adding several thousand dollars in legal fees, property appraisal fees, legal advertising costs, and auctioneer fees. While mortgage holders in all states typically send borrowers pre-acceleration notices of default as required by the FannieMae and FreddieMac uniform mortgage documents, default-related fees are assessed during the cure period. The uniform mortgage documents do not prohibit assessment of fees during the cure period.

ESCALATING FEES PREVENT CURE

Some temporary financial setbacks in the autumn of 2005 caused **Jennie Richards** of Columbus, Ohio, to fall behind on her monthly mortgage payments of $780. Anxious to save the modest, 1,200-square-foot house she had bought a decade earlier, Richards scrambled to get caught up. On Halloween she went in person to drop off an overdue payment to her lender, a subsidiary of Cleveland-based National City Corp., and left believing she had brought her account current.

But when Richards received her December statement from National City—whose website proclaims "We care about doing what's right"—she received a shock: a demand that she pay $3,300. A few days later she got another shock: a foreclosure notice.

Richards, a 47-year-old insurance claims examiner, managed to come up with the full $3,300 and paid National City a few days before its Jan. 16 deadline. But that wasn't enough. Instead, in early February the bank sent her another demand—this time for $6,800. And on Valentine's Day, the bank's lawyer asked a judge to order that Richards' house be sold in a foreclosure auction.

Facing the imminent loss of her house and unable to halt the inexplicably growing mountain of fees, Richards sought help from Rachel Robinson, a lawyer for the Equal Justice Foundation, a non-profit organization that provides legal representation to low-income people in the Columbus area.

"I worked hard to own a home and I do not want to lose my home," Richards wrote in an affidavit submitted to support Robinson's motion to overturn the foreclosure order. "I can afford my mortgage payments but I do not have the money to pay everything that National City has demanded in foreclosure fees and costs and the extra interest that National City has demanded."

As of November 2008, Richards remained in her home pending an appeals court's ruling on her bid to overturn the foreclosure. She also remained in limbo. "I can't move forward because my life is on hold, not knowing if I'm going to have a home or not with my kids," she said in an interview. "This has been a physical torment on me."

Particularly for low and moderate income homeowners, the inclusion of collection charges over and above the overdue installments can create insurmountable barriers to a cure.

Requiring a pre-acceleration notice before default fees may be imposed can provide positive incentives for both servicers and homeowners. Rather than allowing the mortgage holder to incur unnecessary fees and costs and then shift them to the borrower, a clear pre-acceleration cure right will encourage the holder or servicer to work with the homeowner. The pre-acceleration notice may also inform the borrower that if the cure is not made by the deadline date and foreclosure goes ahead, then fees and costs could be assessed against the homeowner in the future. This information gives an incentive to the homeowner to cure during the period when no fees and costs can be assessed.

Time period for cure

Homeowners should be given a period of at least 60 days to cure an alleged default before the mortgage can be accelerated and before default fees may be charged. In some cases, the mortgage servicer may be wrongly claiming that the account is in default due to its misapplication of payments or some other account error. If this occurs it can often take weeks if not months for the homeowner just to get an answer from the servicer after attempting to resolve the dispute. In addition to not prohibiting assessment of foreclosure fees during the cure period, the 30-day cure period provided under the FannieMae and FreddieMac uniform mortgage documents is not long enough.

The timing of the cure period should coincide with the important dispute resolution procedure for mortgages available under federal law. If the homeowner exercises legal rights under the federal Real Estate Settlement Procedures Act (RESPA) to dispute a mortgage account error or to seek account information, by sending a written "qualified written request," the servicer is given 60 business days (almost three months) to provide a response.[62] It makes no sense to give homeowners a pre-acceleration cure period which is significantly less than the time period servicers have to respond to a RESPA qualified written request.

Example from *Spencer Savings Bank, SLA v. Shaw,* 2007 WL 1964676 (N.J. Super. Ct. Chancery Div. July 6, 2007), *aff'd* 401 N.J. Super. 218, 949 A.2d 218 (N.J. Super. Ct. App. Div. 2008):

The Shaws were three months behind in their mortgage payments when they received a "Notice of Intention to Foreclose" from their lender. The Notice had been sent to them in accordance with the New Jersey statute which grants homeowners the right to cure a mortgage default for at least thirty days from the date of the Notice without liability for any fees and costs. (N.J.S.A. 2A:50-56). A related provision of New Jersey law allowed a lender to require a homeowner to pay fees and costs if the homeowner cured after a foreclosure lawsuit was started. However the statute was silent on the question of whether the lender could add fees and costs to the cure amount if the homeowner paid during the period between the end of the thirty-day notice period and the time the lender actually filed a foreclosure case in court.

The answer to this question made a significant difference for the Shaws. After the initial thirty-day cure period, but before the lender filed a foreclosure case in court, the Shaws offered the lender the three monthly payments due. The lender refused to allow the cure, demanding instead an additional $1,174.50 in fees and costs. These fees and costs included charges for an appraisal and legal fees incurred in anticipation of filing a foreclosure case in court.

The New Jersey trial and appellate courts ruled that the Shaws had effectively cured their mortgage default and the lender had no right to proceed with a foreclosure in court. The courts found that the state legislature intended that no costs and fees of any kind could be charged to homeowners if they paid up their missed payments before the lender filed a foreclosure action in court.

In some states the entire foreclosure process takes only three to four months. Allowing a 60-day period before acceleration and commencement of foreclosure gives homeowners the time to find the funds for repayment. The time can also be used to negoti ate, gather required financial information, and finalize a workout agreement, loan modification, or some alternative to foreclosure that is mutually beneficial to all parties.

> **TIME TO FIND SOLUTION**
>
> Texas has some of the quickest foreclosures in the country. Homeowners are initially given only a 20-day cure period before the process begins. Then they are given a 21-day advance notice of the intent to sell the property. If the homeowner is unable to cure the default within the 21 days, the property is sold at the county courthouse at a public auction held on the first Tuesday of the month. While the Texas non-judicial foreclosure process from default to foreclosure sale generally takes about three months to complete, it can be as short as 41 days.[63] This brief time period gives little opportunity for some homeowners to find a solution, as described in this *Dallas Morning News* story:
>
> *Mr. Brannon, a 78-year-old veteran, is running out of time to save his home after he got behind on his monthly payments, which almost doubled in recent months, from $379 to $700.*
>
> *Mr. Brannon said his finances were imperiled when he and his wife had to spend more money on health care, including a $3,000 bill for dental work. He got behind on his mortgage, then received a notice his home would be sold about a month ago.*
>
> *First Franklin Loan Services, his servicer, has agreed to work with him, Mr. Brannon said. But he has less than a month to find a solution, he said.*
>
> *"I can't hardly write, and now I've got to send bank statements and fax forms," said Mr. Brannon, a former postal worker who lives off disability from an injury he sustained on the job. "I feel I should have more time to get these mortgage payments together. The thing about it is, I could pay a little extra and get caught up."*
>
> *Texas' swift foreclosure process puts struggling homeowners in a bind*, Dallas Morning News, December 10, 2008.

Content of notice

An effective notice of default should inform the homeowner of the serious nature of the situation. It should go beyond a routine dunning letter and accurately describe the foreclosure proceedings that lie ahead if the homeowner does not pay the arrears within a time limit set by the statute. The notice should state the basis for the mortgage holder's claim of default, itemizing the payments and other charges allegedly due. The homeowner should be directed to appropriate individuals employed by the mortgage holder or servicer who can help to resolve any disputes over charges. The notice should inform the borrower of rights under the federal Real Estate Settlement Procedures Act and similar state laws to invoke formal dispute and information gathering procedures.

As discussed in the previous section, the notice should also provide information about the servicer's loss mitigation programs, again providing contact information that will direct the homeowner to someone who can effectively respond to a workout request. Information about state or local mortgage assistance programs, mediation programs and other resources should be included. The notice should also direct the homeowner to appropriate agencies for legal and housing counseling. A well-designed notice should stress the benefits of resolution of the default at an early stage, before an unmanageable arrearage in installments, costs and fees makes a cure of the default impossible.

> **WHERE TO TURN?**
>
> In 2005, Freddie Mac conducted a survey of homeowners to learn more about how they interact with their mortgage lenders and servicers.[64] The survey was updated again in 2007 after the foreclosure crisis had begun. Not surprisingly, most homeowners are not aware of options to avoid foreclosure:
>
> - The majority of homeowners (**57%** of borrowers in default and **65%** in good standing) were not aware of loss mitigation options
> - One-quarter (**25%**) of homeowners in default had not contacted their mortgage servicers to discuss their difficulties and nine in ten (**92%**) said they would be more likely to contact their servicers if they knew alternatives could be offered
> - More than half (**57%**) said they did not know about forbearance agreements

- Only **52%** said they knew their mortgage holder could extend the mortgage term
- More than half (**56%)** said they were unaware of foreclosure counseling, while **74%** indicated willingness to use such services once they became aware they existed

Survey Results

The vast majority of states do not have any laws mandating a pre-acceleration notice and a right to cure. Although servicers do send borrowers pre-acceleration default notices based on the uniform mortgage documents, these notices typically do not include the important protections described above. Most notably, without a state law requiring that the cure amount be limited to the monthly installments that the homeowner is behind, mortgage holders and their servicers typically demand costly property inspection fees, broker price opinion fees, legal fees and other fees related to the alleged default.

Massachusetts, **New Jersey,** and **Pennsylvania** are the only states that give all residential homeowners the right to cure a default before acceleration and before default fees may be charged. The **Massachusetts** statute prohibits the mortgage holder from accelerating the mortgage until the borrower is given a 90-day period to cure the default without being required to pay any charge, legal fees or penalty related to the default, except late fees. **New Jersey** and **Pennsylvania** law give the homeowner the right to cure without payment of default fees for thirty days before commencement of a judicial action to foreclose. The **Puerto Rico** statute also expressly prohibits mortgage holders from charging fees and costs as a condition to a cure before acceleration.

Although they do not place effective limits on costs and fees, the statutes of **Hawaii, Iowa, Maine, Maryland, Nevada, North Carolina, North Dakota, Oklahoma, Texas,** and **West Virginia** provide for a type of pre-acceleration notice of default that includes many of the protections described above. The required information typically includes an itemization of the amounts due and the identity of contact persons for dispute resolution and consideration of workout agreements. These statutes prohibit the lender from proceeding with acceleration and foreclosure until the notice period has passed without a cure. The **Maryland** and **New Jersey** statutes direct that proof of compliance with the notice requirement be included in later judicial foreclosure filings. **Massachusetts** requires that the notice be filed with the state division of banks.

States Which Mandate a Notice to Homeowners of Pre-Acceleration Right to Cure

Hawaii	New Jersey
Iowa	North Carolina
Maine	North Dakota
Maryland	Oklahoma
Massachusetts	Pennsylvania
Nevada	Puerto Rico
Texas	

Several states including **Florida, Illinois, Indiana, Kentucky, New Mexico, Tennessee,** and **Virginia**, have enacted laws extending a pre-acceleration right to cure to homeowners who have high-cost mortgages.[65] These cure and fee limitation provisions are generally included as part of more comprehensive legislation dealing with predatory lending. However, due to the limited definition of high-cost loans in many of these states, the protections are applicable only to a small percentage of home mortgages. These states should consider amending their foreclosure laws to include these rights for all homeowners, not just those with high-cost mortgages.

During 2008 a number of states enacted legislation requiring mortgage holders to give homeowners new pre-foreclosure notices. The notice gives homeowners contact information regarding the mortgage holder's loss mitigation office and refer the homeowner to housing counseling programs. Recent enactments in **Georgia,**

Minnesota, and **North Carolina** require that this type of notice specifically identify employees of the mortgage holder or servicer who have authority to negotiate workouts and loan modifications. A **California** law discussed earlier imposes new requirements for notice and a meeting with an authorized representative of the mortgage holder to "explore options for the borrower to avoid foreclosure" before the statutory notice of default leading to a sale may be sent. Recent **Colorado** and **New York** enactments require that mortgage holders give homeowners pre-foreclosure notices containing contact information to find out about housing counseling services. While this information can certainly be helpful to homeowners, the recent enactments do not establish a right to cure for a specific time without assessment of costs and fees.

States with Laws Mandating Limited Notice of Loss Mitigation And Counseling Options	
California	Minnesota
Colorado	New York
Georgia	North Carolina

Recommendations for Homeowner Protections

While no single law in effect in any state provides a truly comprehensive set of protections for homeowners before foreclosure, a combination of elements found in several of them can maximize these protections. The following items are required content in notices mandated by one or more of the laws in effect in **Hawaii, Maryland, Massachusetts, New Jersey,** and **North Carolina.** These items should be required content in the pre-acceleration notices mandated by each state's statute

1. A specific description of what the homeowner must do to cure, including an itemization of all cure amounts and directions on how to obtain updated statements of any additional sums coming due during the cure period (HI, MD, MA, NJ, NC);
2. A clear statement that fees and costs will not be charged to cure before the specific deadline date, with an indication that cure after that date could require payment of costs (MA, NJ);
3. Adequate time to cure, a minimum of 60 to 90 days (HI, MA);
4. Correct names, addresses and phone numbers, and state licensing numbers of the holder, servicer and the person authorized to approve workouts, loan modifications, or other options to avoid foreclosure (MD, MA, NJ, NC);
5. The name of the originating lender and any subsequent assignees (MD, MA);
6. A brief plain language description of the loss mitigation options that are alternatives to foreclosure (MD);
7. Referral information for housing counseling, legal services, and financial assistance programs that can help the homeowner avoid foreclosure (MD, MA, NJ, NY, NC);
8. A plain language description of the foreclosure procedures under state law (HI, NJ);
9. A plain language description of the dispute and information request rights under RESPA and applicable state law;
10. A requirement in each case to file a copy of the pre-foreclosure notice and proof of service with a state regulatory agency, court or county records office when the mortgage holder starts a judicial or non-judicial proceeding to foreclose (HI, MD, MA, NC (for subprime mortgages)).

4. Provide notice of the right to reinstate after acceleration but before sale, by bringing the loan current including foreclosure fees and costs.

Right to reinstate

The concept of allowing a borrower to "cure" a mortgage arrearage and avoid foreclosure has its roots far back in American and English property law. Traditionally, the courts looked at a foreclosure as a drastic remedy because it meant the irrevocable loss of an owner's interest in property.[66] The courts have always exercised broad discretion in applying principles of equity and fairness in foreclosure proceedings. When deemed appropriate, courts have construed legal rules strictly against the foreclosing creditor.

As an outgrowth of this historic reluctance of the courts to approve a forfeiture of property rights, many state legislatures crafted statutes that embody the same principles of fairness and equity in regulating foreclosures. A common type of statute that enforces these principles is one that allows the borrower to stop a foreclosure after acceleration of the obligation by curing the default at any time before the foreclosure has been completed, thus reinstating the mortgage and returning the homeowner to pre-default status. Many states have enacted statutes that require lenders to accept such a cure and terminate a foreclosure despite contrary terms in the mortgage documents.

Not only do many state statutes already codify a post-acceleration right to reinstate a mortgage, but many mortgages by their own terms allow the borrower to exercise this right. For example, Federal Housing Administration (FHA) regulations in effect since 1971 mandate a right to reinstate provision for all mortgages in FHA-insured programs.[66] The standard mortgage form approved by Fannie Mae and Freddie Mac contains a term allowing for termination of a power of sale foreclosure by payment of the arrears and costs up until five days before the sale.[68] The approved Fannie Mae and Freddie Mac form mortgage allows the borrower to reinstate after a default in a judicial foreclosure up until the entry of a court judgment in the foreclosure case.[69]

Time period for reinstatement

In the context of judicial foreclosures most statutes allow the homeowner to reinstate the mortgage at any time until the sale takes place. This cut-off is appropriate for sound policy reasons. It is the sale that significantly changes the nature of the relationship between the borrower and the mortgage holder. Once the sale takes place the rights of a potential third party, namely the purchaser at the sale, may come into play. Until the sale the rights of the borrower and the mortgage holder can be reinstated to their pre-default status quo without disruption of the rights of any third parties. Allowing the homeowner to reinstate only up until the time the court enters a judgment of foreclosure makes less sense, as the judgment of foreclosure merely authorizes the sale of the home to proceed at a later date.

Congress has already adopted this principle for bankruptcy cases. A homeowner who files a chapter 13 bankruptcy case has the right to cure and reinstate a home mortgage after default as long as the bankruptcy case is filed before a foreclosure sale has been completed.[70] But this right only helps homeowners who file bankruptcy. Homeowners should not have to file bankruptcy in order to obtain the right to reinstate and prevent foreclosure.

A statute allowing the homeowner to reinstate after a mortgage default until the foreclosure sale occurs typically provides that the homeowner must pay all costs and fees associated with the acceleration and foreclosure. These costs may include court filing fees, advertising fees, recording fees, title search charges, and attorney fees. However, an appropriate statutory provision should limit assessment of attorney fees and other charges against the homeowner to reasonable fees and costs actually incurred by the mortgage holder.

Content of notice

A right to reinstate after acceleration has little value if homeowners do not know about the option. In many cases homeowners' initial lack of knowledge about their legal rights is not the only problem. When state law does not require a specific form and content for a notice, homeowners rely on information received from the mortgage holder or servicer. National mortgage servicers often use generic forms and notices that fail to take into account the special features of a particular state's foreclosure laws. Unless a state statute mandates otherwise, homeowners may receive only notices and dunning letters that are silent as to many important rights under their state's laws. In some cases the notices from mortgage holders blatantly contradict the provisions of state law. This can be especially true when an extended right to cure is involved.

Like the pre-acceleration notice discussed previously, a meaningful post-acceleration notice should summarize simply and accurately the steps a mortgage holder must follow in order complete a foreclosure under state law. The notice should explain alternatives available to avoid foreclosure and direct the homeowner to individuals who can provide assistance, both legal and, where available, financial. The amounts claimed to be in arrears and any fees and costs should be itemized in distinct categories. It is particularly important that the notice identify individuals from whom the homeowner can obtain clarifying information. The notice should also inform the borrower of the right under the federal Real Estate Settlement Procedures Act (and any similar state law) to send a qualified written request to dispute account errors and request information, and the servicer's address where such requests should be sent.

Because the notice of right to reinstate is often combined with the notice of acceleration (and notice of sale in non-judicial foreclosure states), it is often sent by the attorney who represents the foreclosing mortgage holder. Attorneys that specialize in this area typically handle large volumes of foreclosures and have little ability to explore options that take them outside the scope of their routine paperwork. These attorneys often claim to be unable to obtain basic information about an account from their clients. In this era of multiple assignments of mortgages and securitization of debt obligations, it is not unusual for foreclosing attorneys to be unsure who their clients really are. This problem has been noted by the courts with increasing frequency. Recently a number of courts have denied foreclosure relief or threatened and imposed sanctions upon attorneys when they could not establish their purported clients' ownership of the mortgages and notes at issue.[71]

Given the widespread problems in identifying the entity ultimately responsible for a particular mortgage, it is not surprising that individual homeowners are often frustrated in their attempts to find a human being authorized to review a workout proposal or clarify a disputed charge. It is therefore essential that a notice informing the homeowner of the right to cure disclose the identity of the servicer and the holder of the note and mortgage. The notice should contain the phone numbers and addresses of individuals with authority to implement a cure and consider other workout options, including loan modifications. Local housing counseling agencies often assist homeowners facing foreclosure, and these agencies also need to know the identity of the relevant staff of the lender and the borrower's recent payment history. Providing this contact information with the notice of a right to cure will allow the counselor to review account information and promptly begin to assess how best to help the homeowner.

Proof of compliance

In addition to requiring that the mortgage holder serve a clear and accurate notice of the right to reinstate, the statute should contain a provision which ensures that the mortgage holder complies with the requirement to serve the notice. The most appropriate means to enforce compliance is to require that the mortgage holder file copies of the pre- and post-acceleration notices in land records as a condition to completion of a valid power of sale foreclosure. Similarly, the statute should mandate that the mortgage holder include a sworn statement in a judicial foreclosure complaint to the effect that the notices of the right to cure were timely served, with copies of the notices attached to and incorporated into the foreclosure complaint.

Survey Results

In **twenty-eight states**, there is no state law which guarantees that a homeowner may cure a default and reinstate the mortgage after acceleration.

States Which Do Not Require Right to Reinstate after Acceleration

Alabama, Connecticut, Delaware, Georgia, Iowa, Kansas, Kentucky, Louisiana, Maine, Massachusetts, Michigan, Missouri, Nevada, New Hampshire, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Vermont, Virginia, West Virginia, and Wyoming.

Twenty-two states, the District of Columbia, and **Puerto Rico** provide by statute that the homeowner can reinstate by paying the amount due, plus any permissible costs and fees, by a time certain before the sale. If the homeowner becomes current by the deadline, the foreclosure is stopped and the mortgage is reinstated.

States with Laws Giving Right to Reinstate after Acceleration

Alaska *(until sale)*
Arizona *(in judicial foreclosure until sale, in non- judicial foreclosure until day before sale)*
Arkansas *(until sale)*
California *(until five days before sale)*
Colorado *(until 15 days before sale)*
District of Columbia *(until five days before sale)*
Florida *(until entry of judgment in judicial foreclosure)*
Hawaii *(until three days before sale)*
Idaho *(until 115 days after recording of notice of default)*
Illinois *(within 90 days of service of summons and complaint)*
Indiana *(until judgment with further stay conditioned on making timely payments)*
Maryland *(until one day before sale)*
Minnesota *(until sale)*
Mississippi *(until sale)*
Montana *(for "small tract" properties, until time of sale)*
Nebraska *(within one month of filing of notice of default in non- judicial foreclosure)*
New Jersey *(until entry of judgment in judicial foreclosure)*
New York *(until entry of judgment with further stay upon continued payments)*
Oregon *(until five days before sale)*
Pennsylvania *(until one hour before sale)*
Puerto Rico *(by full payment within 30 days after initial court review of foreclosure documents)*
Utah *(within three months of filing of notice of default)*
Washington *(until eleven days before sale)*
Wisconsin *(until entry of judgment with further stay subject to continued payments)*

Several states which do not grant a reinstatement right, such as **Oklahoma** and **Massachusetts**, do however have pre-acceleration right to cure laws. While these states should retain those laws for the reasons stated in the earlier section, they should consider providing homeowners with a post-acceleration right to cure and reinstate.

Some states place limits on the number of times a homeowner can take advantage of the right to cure and reinstate. For example, the **Oklahoma** statute provides that the homeowner cannot reinstate more then three times in twenty-four months, and the **Pennsylvania** law limits exercise of the right to three times in one year. **Alaska, the District of Columbia**, **Illinois**, and **New Jersey** also place limits on the frequency with which homeowners may reinstate after a foreclosure has been initiated.

As mentioned above, if the state law does not grant a more generous time period, borrowers generally have the right under the standard Freddie Mac and Fannie Mae mortgage documents to cure up until five days before the foreclosure sale in non-judicial foreclosure states. With respect to judicial foreclosures, there is a split between state statutes that permit a cure until the foreclosure sale and those that allow a cure only until entry of judgment in the foreclosure lawsuit. Several statutes allow for a more limited stay of proceedings after the entry of judgment in a judicial foreclosure case, with the continuation of the stay dependent on the homeowner's making future payments on schedule.

To be effective, a statute granting the homeowner an extended right to reinstate must require that the mortgage holder provide the homeowner with a notice of this right. Unfortunately, several of the states which grant this right, such as **Arizona, Arkansas, the District of Columbia, Iowa, Idaho, Minnesota, Mississippi, Nebraska, Nevada, New York, North Dakota, Utah,** and **Wisconsin** do not require that mortgage holders inform borrowers of the right.

Several state statutes contain specific language to be included in the notice of the right to reinstate. The **California** statute mandates a form of notice with a clear explanation of rights and requires the lender to identify staff who can respond to requests for information. **Maryland's** statute describes the relevant time frames, provides contact information, and requires that the foreclosure documents attest to compliance with the notice provision. The form mandated by the **Washington** statute requires a clear itemization of amounts due and categories of charges. The **Hawaii** and **New Jersey** statutes also require specific information about homeowner rights in the text of the notice. Statutes from other states, such as **Oregon, Pennsylvania, Texas,** and **Utah**, do not contain a precise model text to be incorporated verbatim into a notice, but instead list the general items to be included in the notice.

Georgia and **Tennessee** have enacted laws that apply special cure provisions to loans that are defined as "high cost" under their statutes. These statutes allow cure and reinstatement of these particular loans until the time of sale or within a few days of the sale. As mentioned in the previous section, these high cost loan statutes apply to only a small portion of all loans being foreclosed today. States should expand the scope of covered loans to include all loans secured by a primary residence.

Recommendations for Homeowner Protections

The reinstatement statutes in several states include one or more elements that can be very helpful for homeowners seeking to avoid an ongoing foreclosure. An effective statutory scheme should incorporate as many of these protective terms as possible. They include:

1. A right to reinstate until the date of the foreclosure sale;
2. A limitation on fees and charges to those reasonably and actually incurred, or a strict monetary cap on fees;
3. A requirement that the foreclosing mortgage servicer or holder respond promptly and in writing to requests for an itemized statement of the reinstatement amount;
4. A requirement that the mortgage servicer or holder serve the homeowner with a plain language written notice which gives such essential information as:
    a. The duration of the right to cure and reinstate, and the acts which must be performed in order to do so;
    b. The names, addresses and phone numbers of legitimate agencies providing foreclosure counseling and related financial assistance;
    c. The name, address and phone number of the mortgage servicer's or holder's staff who can provide written updated statements of amounts due and authorize workout and loan modification agreements;

d. The right to make a formal request under RESPA and the name (or office) and address to whom the request should be sent;

5. A requirement that the mortgage holder file of record a proof of service and copy of the notice with any judicial foreclosure complaint and notice of non-judicial sale.

6. A requirement that the mortgage holder file of record all prior assignments of the mortgage before any judicial foreclosure complaint is filed and notice of non-judicial sale is sent.

5. *Provide personal service of the notice of sale or foreclosure complaint.*

Due process requires adequate notice

Foreclosure irrevocably deprives individuals of what is typically the most important property interest they have. Beyond the immeasurable emotional value the home holds for many consumers, home equity may also represent the consumer's sole savings and security for retirement. Laws must operate with the greatest possible care to ensure that homeowners have notice of ongoing proceedings and can make informed decisions in response to them. Non-judicial sales raise the most significant concerns about notice.

Unfortunately, when homeowners fall into default and suspect that a foreclosure proceeding is imminent, they often believe there is nothing they can do to avoid loss of their home. Many homeowners who are in default, almost one-half of those surveyed in a 2007 Freddie Mac survey, describe their contacts with their mortgage holder or servicer as "embarrassing" or "frustrating."[72] About one in four of these homeowners also considered their discussions with mortgage servicers as "scary," "intimidating," "confusing," and "pointless."

It is therefore not surprising that many homeowners ignore initial letters they receive from mortgage servicers. This understandable "head in the sand" approach might also cause some homeowners to not claim certified letters. They may also incorrectly assume, perhaps based on knowledge of judicial landlord/tenant proceedings in their state, that they do not need to act until personally served with legal papers by a court official. Others who are most intimidated by the process or find their situation to be hopeless may move out abruptly. And there will always be cases in which mistakes will be made by mortgage servicers and notices will be sent to the wrong address. For a variety of reasons then, homeowners may not receive or review notices of ongoing proceedings that are simply mailed to the foreclosed property.

Gary Holden, a retired purchasing contract negotiator for the state of Arkansas who lives in the tiny town of Glenwood, remembers that it was "scary" when a man in a uniform came to his door in the early evening in late autumn of 2007. The man, a deputy sheriff, handed Holden a "notice to vacate" the house he lived in ever since it was built 20 years earlier. In an affidavit, Holden said he was "shocked, scared, sick to my stomach and absolutely terrified that I was going to lose my house."

Unbeknownst to Holden, his house had been sold in a foreclosure auction a month earlier. The lawyers for the holders of his mortgage had complied with the state's notice requirements for a non-judicial foreclosure by sending letters to an address for his home which had not been used since street numbering changes related to a new emergency 911 telephone system went into effect a decade earlier.

Not that Holden was so hard to find. Monthly mortgage payment notices were being sent by the mortgage servicer to Holden's current, correct address.

Kathy Cruz, Holden's lawyer, says that she was able to save her client's house despite an Arkansas law that precludes legal challenges to a foreclosure unless those challenges are raised prior to a foreclosure sale. Fortunately for Holden, documents from another court case showed that Holden's mortgage servicer knew and used his current address, Cruz says.

Still, Holden remained in limbo during months of legal wrangling required to persuade the holder of Holden's mortgage to agree to give him back his house. And he and his family had to endure a summer thunderstorm season without insurance coverage because he couldn't demonstrate an insurable interest in the property. Only after a judge issued an order that the title be returned to Holden was he able to buy property insurance.

Many states' non-judicial foreclosure laws require mortgage holders to do nothing more than mail a notice of an upcoming sale to the borrowers at the property address, usually by regular and certified mail. Mortgage holders can comply with this service requirement even when they know that key documents such as the notice of sale have been returned as undeliverable or unclaimed. Curiously, many of these same states provide greater notice when a consumer is being sued on an unpaid personal debt. In those cases, the debt collector is typically required to have a court summons personally served on the consumer; a court official will go to the consumer's home and hand the summons to the consumer or leave it with an adult member of the household.

THE MARYLAND EXPERIENCE

Excerpt from brief on behalf of Joyce Griffin before the Maryland Court of Appeals in Griffin v. Bierman, 941 A.2d 475 (Md. 2008):

Joyce Griffin, and her children, lost their home because Ms. Griffin did not receive notice until it was too late to contest the foreclosure. Following the death of her fiancé, Ms. Griffin had difficulty making payments on her home mortgage, which she had refinanced with Ameriquest, a now-defunct predatory subprime lender. Without Ms. Griffin's knowledge, the company, through its trustees, initiated foreclosure proceedings. Ms. Griffin did not learn of the foreclosure until after her house was sold for $223,000 at an auction on the courthouse steps, and then only because the purchaser took it upon herself to tack a handwritten notice on Ms. Griffin's door.

The trustees responsible for prosecuting Ms. Griffin's foreclosure did the bare minimum under the Maryland rules: They published notice in a newspaper and sent letters by certified and regular mail, once after docketing the action and again in the weeks immediately preceding the sale. Even though each one of the certified letters were returned as unclaimed, the trustees did nothing in response during the eight months preceding the sale. They took no additional steps to notify Ms. Griffin and instead held the foreclosure sale just one day after one of their certified letters was returned unclaimed. The trustees did not even wait to see whether the official notice of the foreclosure sale itself was delivered; that notice was promptly returned unclaimed fifteen days after the sale had already taken place. Indeed, the trustees testified that their official policy is to do nothing in response to certified-mail foreclosure notices that are returned unclaimed by the post office.

The trustees' practices leave Maryland homeowners in Ms. Griffin's position in a much worse position than the defendants in tax foreclosures, summary eviction proceedings, small-claims disputes, and even routine debt collection actions where the stakes are far, far lower. If she had been a defendant in virtually any other type of legal proceeding in the State of Maryland, in fact, the procedures employed would have been better calculated to provide notice to Ms. Griffin than they were in the proceedings to foreclose on her home.

* * *

Sadly, the Maryland Court of Appeals rejected Ms. Griffin's attempt to get her home back. In finding that the Maryland procedure satisfied minimum due process requirements, the Court of Appeals noted that "[p]erhaps some changes in the foreclosure process would be beneficial to the citizens of the State of Maryland." Aware that several bills were pending in the Maryland Legislature that would reform the foreclosure process, the Court said it would defer to the legislative process. In fact, soon after the case was decided, a new law was enacted in Maryland requiring personal service of the foreclosure sale notice. However, in many states there is still no requirement of personal service.

Survey Results

Among the states that rely primarily on judicial foreclosure, **nine** allow service of the foreclosure complaint by mail or by means other than personal service. Of the judicial foreclosure states **Connecticut, Delaware, Florida, Illinois, Iowa, Maine, New Jersey, New York, North Dakota, Pennsylvania, Vermont,** and **Wisconsin** require personal service of the legal documents that start a foreclosure case.

Of the thirty states and the District of Columbia where non-judicial foreclosures predominate, **twenty-six** allow service of the notice of sale upon the borrower by mail or means other than personal service. **Maryland, Minnesota, Oklahoma, Oregon,** and **South Dakota** now require that mortgage holders serve the notice of sale personally upon the homeowner in all non-judicial foreclosures. This practice creates the greatest likelihood that homeowners will receive actual notice and act to protect their rights. The **Oregon** statute requires three attempts at personal service of the notice of sale before the mortgage holder can rely on mail service and posting. The **Maryland** law requires at least two attempts to serve the "order to docket the complaint" for the sale. If these two attempts fail, the mortgage holder must file an affidavit describing the efforts at personal service and send the order by first class and certified mail to the property as well as post it at the property.

Recommendations for Homeowner Protections

Repeated efforts at personal service of the foreclosure complaint and the notice of sale have the greatest chance of impressing upon the homeowner the seriousness of the situation. It should be in the mortgage holder's interest to have the homeowner actively engaged in the process. State laws should require that before a sale of a home is allowed to take place under any type of foreclosure statute, the mortgage holder must file proof of personal service of the notice of sale or else document repeated good faith attempts to make personal service on the borrowers. Alternatively, states may consider a procedure which provides for service by mail with an acknowledgement form to be filled out and returned by the homeowner. If the form is not returned, then personal service would be required.

Judicial foreclosure actions proceed through a state court system subject to the rules that apply to most civil cases. To the extent personal service of a summons and complaint is required under the state's rules of civil procedure, the judicial foreclosure complaint is served in the same way. However, some added protections must apply to documents related to a foreclosure sale. Homeowners who did not file a written "answer" or response to the foreclosure complaint with the court should not be treated the same as other defendants who have defaulted in a civil lawsuit. The default should not be deemed as a waiver of service of all future documents related to the case, such as a later notice of sale. The requirements for personal service of the notice of sale, similar to those under the Oregon and Maryland statutes described above, should apply to judicial foreclosure sales as well.

6. Provide a state housing emergency assistance fund or similar program to assist homeowners in default due to temporary financial difficulties.

Housing assistance fund programs

Several states have programs to provide small emergency loans or assistance to homeowners who are facing foreclosure. Most of these programs are aimed at assisting homeowners who are experiencing temporary financial difficulties such as loss of employment, illness, disability, death, divorce or legal separation. Homeowners are usually required to have a good payment history prior to the delinquency, and they must be able to resume the mortgage payments after the assistance.

Typically the programs provide short term loans ranging from \$3,000 to \$60,000, either interest-free or at rates less than 6%. Generally, there are two types of loans: 1) a continuing loan which pays the homeowner's delinquent balance and assists the homeowner with his or her monthly payments for a period of time that ranges from 12 months to 24 months, or 2) a non-continuing loan with a one-time disbursement which permits the homeowner to pay off the delinquent mortgage balance.

These rescue fund programs can help homeowners avoid foreclosure, especially when they are combined with state laws which give the homeowner the right to cure defaults before acceleration and the imposition of excessive fees and costs. Since rescue fund programs are generally most effective in helping homeowners who have experienced a temporary loss or reduction in income, they work best in conjunction with traditional loss mitigation options such as forbearance or repayment plans. However, these programs alone are inadequate to deal with foreclosures caused by mortgage loans which were unaffordable for the homeowner when made or which have become unaffordable due to a change in the monthly payment on an adjustable rate mortgage. Homeowners in foreclosure because of oppressive loan terms affecting their ability to pay will need a loan modification in addition to any assistance provided by a rescue fund program. Still, these programs can play a valuable role as part of a comprehensive solution for foreclosure avoidance.

Survey Results

At present, a small number of states have created emergency assistance programs to assist homeowners who are at risk of foreclosure. Statewide programs currently exist in **Connecticut, Delaware, Maryland, Michigan, Minnesota, New Jersey, North Carolina, Pennsylvania, Vermont,** and **Washington**. There are also several local programs that provide small emergency funds, such as in **St. Louis, Missouri; Syracuse, New York; Waco, Texas;** and **New York City**. Appendix C, *infra*, provides details about the requirements for some of these programs.

Recommendations for Homeowner Protections

As the foreclosure crisis deepens, more states may wish to consider developing such programs. Due to the escalating unemployment rate caused by the housing crisis and broader economic factors, a second wave of foreclosures over the next few years will likely fall upon homeowners with prime mortgages whose payment problems were not caused by the mortgage terms. These unemployed homeowners could greatly benefit by a loan program which would help them get through tough times until the economy rebounds and they can find new jobs. States should consider programs that:

- assist homeowners with monthly mortgage payments for a period of 12 to 24 months;
- provide interest-free or below market rate loans to be repaid when the home is sold, transferred, or refinanced;
- are designed as revolving funds, with amounts replenished by loan repayment;
- provide that foreclosure is stopped pending application for funds.

7. Provide protections for homeowners after the foreclosure sale, such as redemption rights, limitations on deficiency judgments, and procedures for accounting and return of surplus sale proceeds.

A. Post-Sale Right of Redemption

Some states have enacted laws that allow a homeowner to undo the effect of a foreclosure for a set period of time after a foreclosure sale by paying the amount of the winning bid at the sale. The right to set aside a foreclosure sale in this manner is typically created under a state statute and is often referred to as a "statutory" right to redeem. Unlike the right to cure discussed in Section 3 and the right to reinstate discussed in Section 4, *supra*, the statutory right to redeem comes into play only after a foreclosure sale. It allows the borrower a final opportunity to save the home.

To exercise a statutory right to redeem, the borrower pays the amount of the successful bid at the foreclosure sale. The borrower must make this payment during the time defined by the state's statute. In addition to the bid amount, the borrower usually must compensate the buyer for any costs it incurred as a result of the purchase. These costs may include interest at a statutory rate, taxes and insurance premiums paid, as well as maintenance and repair expenses. The purchaser at the sale, whether it be the mortgage holder or a third party, should be made financially whole through this payment.

Purposes behind the statutory right to redeem

The statutory right to redeem after a foreclosure sale serves two important purposes. First, it gives the borrower a realistic period of time within which to seek alternative financing to pay the sale price and keep the home. Reemployment, recovery from illness, or the availability of assistance from government programs may come into play during this time. The personal and social costs of subjecting a family to eviction and permanent loss of a home are significant. Providing a final opportunity to save the home and avoid these consequences is clearly a goal that many state legislatures have considered important. The borrower may also sell the property during the redemption period. With the benefit of a longer period to arrange a private sale, the borrower is much more likely to pay off all or a substantial part of the mortgage holder's original claim (if the mortgage holder is the purchaser at sale) and potentially recover the value of any equity lost at the sale.

A second purpose in allowing borrowers to redeem after sale is to deter mortgage holders from strategically offering low bids at foreclosure sales. A mortgage holder should not be encouraged to acquire a property at a foreclosure sale, then resell it for a significantly higher price at a later date by using more effective marketing techniques. By means of intentionally low bids, mortgage holders can acquire a former homeowner's equity in the property as a windfall. Even when the borrower has no equity in the home, the mortgage holder's purchase of the property through an unreasonably low bid can have detrimental effects. An artificially low foreclosure sale price can saddle the borrower with a much higher than appropriate deficiency debt in the future. By contrast, when mortgage holders know that borrowers can redeem after sale by paying the amount of the winning bid, they will be more likely to avoid letting the sale end with a bid so low that it allows for an easy redemption.

Arguments against redemption rights are based on stereotypes and unsupported claims

Exercise of the statutory right to redeem ultimately causes little concrete harm to mortgage holders. The statutory formulas for redemption require payment of sums that compensate either the holder or the third party purchaser for all costs they incurred as a result of the foreclosure and sale. Because it sometimes preserves any secondary liens, the redemption may also protect the rights of junior lienholders who might otherwise lose their interests in the property if the sale were not set aside.

Objections to the statutory right to redeem have often focused on a presumed uncertainty created in the minds of bidders when there is a possibility of redemption after a sale. This "chilling effect" has never been documented. If they choose to use them, mortgage holders can always employ an array of truly effective practices that will encourage competitive bidding at foreclosure sales. Mortgage holders can always invest in basic advertising and marketing strategies that will lead to substantially higher bids. Despite the cost effectiveness of these marketing tools, mortgage holders routinely ignore them and end up buying the properties with their own low bids. The low bid problem is nationwide and appears in all forms of foreclosures. Simply blaming post-sale redemption statutes for this phenomenon is not a serious attempt to address the need for truly effective solutions that would allow foreclosure auctions to benefit from market forces.

In some respects, the lack of a right to redeem after sale is just as likely to cause uncertainty as does the existence of the right. Absent a right to redeem after sale, borrowers will be more likely to challenge irrevocable sales through other means, such as lawsuits alleging a gross inadequacy of sale price or non-compliance with foreclosure procedures. Because of the lack of judicial supervision, power of sale foreclosures and other non-judicial sales are particularly susceptible to this kind of attack. Allowing the right to redeem after sale will direct borrowers to concrete measures designed to allow them to keep their homes and compensate creditors, rather than pursue time consuming and expensive litigation over sale procedures.

Finally, some critics have pointed to the borrower's right to continue to reside in the property during the post-sale redemption period as a factor that possibly leads to lower bids at foreclosure sales. Mortgage holders argue that homeowners will vandalize properties or deliberately cause waste during redemption periods. Again, this supposed chilling effect on bidding has not been documented. Most often, this claim is simply the product of a demeaning stereotype of debtors. Property inspections can determine whether, in fact, homeowners are deliberately destroying property. Purchasers can seek equitable remedies from the courts to prevent waste in the rare instances when this type of conduct truly occurs. Moreover, it is possible to draft statutes that allow the shortening or termination of redemption rights upon a verified showing that borrowers are causing deliberate damage to a property during a redemption period. These statutory provisions can adequately address the mortgage holders' and sale purchasers' concerns about property condition during a statutory redemption period.

Survey Results

Approximately half the states have enacted laws that allow a homeowner to set aside a foreclosure sale by redeeming for a set period of time after the sale has taken place. These laws vary a great deal from state to state in how they operate and when they apply. Some states have more than one redemption law. For example, a state may have one statute that applies to judicial foreclosures, another that applies to non-judicial foreclosures, and a third one that regulates execution of judgment liens against real property.

The following states which rely primarily upon judicial foreclosures have a statutory right to redeem after a foreclosure sale:

Illinois *(redemption until later of seven months after service of complaint or three months after judgment with additional thirty days for a home mortgage if the mortgage holder is the purchaser at sale and the sale price was less than specified amount)*
Iowa *(one year under general sale provision)*
Kansas *(twelve months from date of sale)*
Kentucky *(one year from date of sale if sale did not bring at least two-thirds of property's appraised value)*
North Dakota *(sixty days after sale)*
South Dakota *(one year for judicial foreclosures and 180 days for certain power of sale foreclosures if provided in loan documents)*

The following states in which mortgage holders predominately use non-judicial foreclosure have a right to redeem after foreclosure sale:

Alabama *(one year from date of sale)*
Michigan *(varies from one month to one year depending on size of parcel, number of units, percentage of original loan outstanding)*
Minnesota *(one year from sale)*
Missouri *(twelve months from date of sale, but only if mortgage holder acquired the property at sale and homeowner posts bond)*
Montana *(twelve months from sale)*
New Mexico *(nine months from sale)*
Tennessee *(two years, but may be waived by loan documents)*
Wyoming *(three months)*

A number of states have statutes allowing post-sale redemption after judicial foreclosures, but these laws rarely help homeowners because non-judicial foreclosures are the predominate method of foreclosure:

Alaska *(twelve months for judicial foreclosure and none for power of sale unless loan document authorizes it)*
Arizona *(twelve month redemption from sale after court judgment, none after power of sale foreclosure)*

Arkansas *(one year after judicial foreclosure, none for power of sale)*
California *(two year redemption applies in certain judicial foreclosure, if plaintiff seeks deficiency; none for non-judicial foreclosure)*
Michigan *(six months for judicial foreclosure, varying times for non-judicial foreclosure)*
Utah *(six months after judicial foreclosure, none after non-judicial foreclosure sale)*
Washington *(eight months after judicial foreclosure sale, none for deed of trust foreclosure)*

Several states allow a very limited right to "redeem" for a short period after a judicial foreclosure sale and until certain post-sale formalities are completed. These states include **North Carolina, Florida, Ohio,** and **South Carolina**. Because the time periods to redeem under these statutes typically run for a matter of weeks, these laws differ significantly from the statutory right to redeem discussed generally in this section.

Although many states have statutes on the books that allow a property owner to redeem after a foreclosure sale, most allow a homeowner to redeem only in limited circumstances. An array of factors set conditions on the right to redeem and otherwise limit its effectiveness. Some of these limitations may have been based upon what appeared to be reasonable policy grounds. However, in practice the rationales routinely ignore the real needs of most homeowners who face the threat of home loss.

For example, the length of time allowed to redeem varies under some statutes depending on factors such as the percentage of the underlying debt that the borrower has paid, the extent of any equity the homeowner has in the property, and the intent of the mortgage holder to sue the borrower for a deficiency in the future. In **Michigan** and **North Dakota**, borrowers have more time to redeem the greater the portion of the underlying debt they have paid. In **Illinois, Kansas,** and **Kentucky**, the relation of the foreclosure sale price to the current market value of the property affects the time allowed to redeem. Finally, under statutes such as those in effect in **California, Iowa,** and **New Jersey**, the intention of the mortgage holder to pursue a deficiency claim against the homeowner after the sale triggers greater redemption rights.

In states that allow both judicial and non-judicial foreclosure a fairly common development has been to retain the right of redemption as part of the traditional judicial foreclosure practice, but preclude redemption after non-judicial foreclosure sales. Other states, such as **Illinois** and **Missouri**, allow more extensive redemption rights if the mortgage holder, rather than a third party, purchases the property at the sale. In a further variation, under some redemption laws, such as those in **Illinois** and **California**, homeowners with mortgages used to purchase the property receive greater protections than do homeowners with other types of mortgages.

Recommendations for Homeowner Protections

1. Make redemption applicable to all types of foreclosure sales involving a primary residence

Restrictions that limit redemption based upon the identity of the purchaser at sale, the method of foreclosure used, or whether the mortgage was from a purchase money transaction or a refinancing, deny effective relief to many homeowners without regard to their need. Similarly, limitations based on the value of the property or the percentage of the debt paid can be arbitrary, complex and expensive to apply. Nor should the right to redeem depend on a factor such as whether the mortgage holder will later claim a deficiency.

In most jurisdictions, foreclosure legislation has developed over time and in a piecemeal fashion. Over the years, the laws have allowed mortgage holders to rely more extensively on non-judicial and power of sale foreclosures. This trend has left behind some of the significant borrower protections that were available to homeowners under traditional judicial foreclosure systems. The need today is for a comprehensive approach to borrower protections, and the right to redeem for a set period of time after a foreclosure sale has typically been one of the core rights of homeowners under judicial foreclosure systems. Many states recognize this right in one form or another and have done so for many years. A simple redemption statute that applies across the board to all home foreclosures in a state works best to protect homeowners in foreclosures. For example, the **Iowa** redemption statute is straightforward and avoids some of the unnecessarily complex variations and exceptions that have developed under other states' laws.[73]

2. Allow the homeowner to continue residing in the property during the redemption period

Most statutes that authorize redemption after sale permit the borrower to live in the home during the redemption period. This is consistent with the goal of allowing the borrower an opportunity to refinance or otherwise take advantage of an improved financial situation during the extended redemption period. Burdening the homeowner with relocation and moving expenses during the redemption period only diminishes the likelihood of a successful redemption.

3. Allow the homeowner to redeem and satisfy the mortgage obligation by paying the sale price with interest and costs of sale

A typical redemption statute permits the borrower to redeem upon payment of the foreclosure sale purchase price plus the costs of the sale and any interest accrued on the sale price. This payment, particularly when the sale has been confirmed by a court order, should satisfy all the homeowner's obligations under the mortgage. **California's** statute applicable to redemption from judicial sales recognizes this effect of redemption.[74] The stated purpose of this statutory provision is to discourage mortgage holders from letting private auctions end in low sale prices when the foreclosing lender is the only bidder. Provisions like those in the California law require mortgage holders to look at the auction as the ultimate source of payment of their debt. With this understanding they should take appropriate steps to maximize bid amounts. This result is fair in view of the mortgage holder's election to foreclose and liquidate the property under what purports to be a competitive bidding auction.

Not all states follow this rule. For example, the **South Dakota** statute requires payment of any deficiency as a condition to redeeming.[75] The better rule, as under the California law and the Iowa statute referred to above, recognizes that the payment of the sale price satisfies the borrower's obligation under the mortgage.

4. Declare the right to redeem to be non-waivable by any terms of loan documents

One provision that invariably undermines the right to redeem is a statutory authorization for the waiver of the right. The **Alaska** and **Tennessee** statutes expressly allow the waiver of the right to redeem. If a statute allows redemption rights to be forfeited by contract language, then it is inevitable that boilerplate language to this effect will appear in all loan documents developed for use in the state. An effective statutory redemption provision must declare that any purported waiver of redemption rights by contract terms is unenforceable.

B. Limitations on Deficiency Judgments

Destructive effect of deficiency judgments

A mortgage foreclosure can be one of the most traumatic experiences that an individual or family ever endures. The dream of homeownership ends in eviction, forced relocation, and loss of the family's most significant investment. Yet this may not be the end of the hardships. Months or years later, after sustaining these losses, the former homeowners may encounter what seems like the ultimate cruelty. They discover that the mortgage holder is suing them to recover a substantial money judgment. This lawsuit, called a deficiency action, seeks to recover the difference between the price the house sold for at the foreclosure sale and the total debt that was due under the mortgage and note at the time of foreclosure. To make matters worse, the mortgage holder may have bought the property at the foreclosure sale for a fraction of its real market value, then garnered a substantial profit by selling it to a third party for a price much closer to its true value. Now the mortgage holder is suing the former homeowners for the same shortfall it recovered in the sale to a third party. Under many state foreclosure laws, this double recovery is perfectly lawful.

Foreclosed homeowners have good reason to feel outraged by this turn of events. If the property was located in an area with depressed home prices, or if the loan originator made the loan based on an overly optimistic or deliberately inflated appraisal, the deficiency amount is likely to be very high, easily in the tens of thousands of dollars. If the mortgage holder obtains a money judgment for the deficiency against the former homeowners, the judgment will be listed on the borrowers' credit report for seven years, jeopardizing their financial recovery. With statutory interest, the unpaid judgment amount could double over a decade. Unless they are fully protected by exemption laws, the borrowers' property and income will be exposed to collection actions and wage garnishments until the judgment is paid in full.

Example from *American General Financial Services, Inc. v. Brown*, 376 S.C. 580, 658 S.E. 2d 99 (S.C. 2008):

Kimberly Dawn Brown bought a mobile home in 1999. She signed a mortgage in the amount of $53,600. After making payments for several years she fell behind. Her lender filed a judicial foreclosure action in 2005. The court entered a foreclosure judgment, ordered the property sold at sheriff's sale, and found the total debt due to be $61,763.90.

A third party bid $25,001 at the sale and acquired the property. The lender then requested a deficiency judgment against Ms. Brown personally. The lender asked the court to enter judgment in the amount of $39,087.99, the difference between the high bid and the full amount of the debt.

The judge hearing the foreclosure case refused to grant the deficiency judgment. According to the judge, the result would be inequitable and a judge hearing a foreclosure case could exercise discretion to deny a deficiency judgment on equitable grounds. The lender appealed the decision. On appeal, the South Carolina Supreme Court reversed the trial court judge. According to the Supreme Court, under existing state law, the trial judge had no discretion to refuse to enter the deficiency judgment in the full amount of $39,087,99. Thus, Ms. Brown would not only lose her home, but she would remain personally liable for this $39,087.99 debt.

The only limitation on foreclosure deficiency claims allowed under South Carolina law is the debtor's right to submit evidence of an appraisal of the property in an attempt to lower the deficiency claim. The debtor must submit the request for an appraisal to the court within 30 days of the foreclosure sale. The statutes do not require any form of notice to homeowners of the right to seek this appraisal.

One of the major inequities resulting from the diversity in state foreclosure laws is that the events in this scenario would never occur if the borrower lived in a state that barred deficiency judgments after a home foreclosure. In the wake of a foreclosure, depending upon the laws of the state where it took place, homeowners can face a remarkable variety of consequences. These range from complete immunity, to deficiency judgments, to full enforcement of creditor judgments.[76]

State statutes that limit holders' rights to pursue former homeowners for a deficiency judgment have been in effect in many parts of the county since the 1930s. The courts upheld these state laws against creditor claims that they were unconstitutional infringements of contract rights.[77] The United States Supreme Court has ruled that a state statute which limited a lender's recourse to a post-foreclosure deficiency claim passed constitutional muster even though the statute had been enacted *after* the borrower and lender entered into the loan transaction.[78]

State legislatures have enacted anti-deficiency statutes in response to a number of unfair practices that have been endemic in the home lending industry. First, anti-deficiency statutes discourage lenders from overvaluing property when they originate a mortgage loan. This practice has contributed significantly to the current foreclosure crisis. When lenders know that if they foreclose they will never be able to recover more than the foreclosure sale price, or at most the property's fair market value, they have less incentive to overvalue the property at the beginning of the transaction. When deficiencies are outlawed, recovery of an inflated debt that is unrelated to any real value in the property is not an option. Second, anti-deficiency statutes prevent the windfall scenario in which the holder purchases the home at a foreclosure sale for an artificially low price, sells it later for a much higher price, then seeks a double recovery by pursuing a deficiency claim based on the low forced sale price.

Anti-deficiency statutes can also play a role in mitigating the regionwide effects of an economic downturn and a depressed real estate market.[79] The likely result of mortgage holders' pursuit of deficiency judgments will be to drive many individuals into chapter 7 bankruptcies when they would not otherwise have sought bankruptcy relief. While discharging the mortgage deficiency may be the driving force behind the bankruptcies, the borrowers' local creditors will be dragged into the bankruptcy discharges as well. If not for the overwhelming deficiency debts, the borrowers may have gone ahead and paid the debts owed to their other creditors. Similarly, if the borrowers refrain from seeking bankruptcy relief and struggle to pay the deficiency debts owed to mortgage holders, their payments toward the deficiency claims typically flow to distant holders of securitized loan obligations rather than providing needed stimulation for the distressed local economy.

Anti-deficiency statutes encourage mortgage holders to make greater efforts to avoid foreclosure in the first place, but also to maximize the bids made at foreclosure auctions if the sale proceeds. Under prevailing practices, whether the sales are judicially supervised or take place under power of sale provisions, mortgage holders often do little to attract bidders to an auction. Relatively small expenditures by mortgage holders for advertising and marketing could yield significantly higher bids. Mortgage holders have access to title and appraisal information they could use for more effective marketing. They could encourage more lucrative bids by setting flexible bid or payment terms. Mortgage holders have the ability and, one would think, the financial incentive to encourage vigorous bidding. Yet, as is true for many of the entrenched practices of the home mortgage lending industry, rationality and common sense do not necessarily prevail. Rather than make the efforts to maximize bids, mortgage holders typically go through the motions of complying with the bare minimum steps required under existing state foreclosure laws in order to obtain title to the properties as quickly as they can. They rarely engage in any of the marketing practices associated with home sales outside of the foreclosure context. Because many of the deficiencies resulting from low foreclosure sale prices are really self-imposed by lenders, statutory restrictions on their ability to pursue borrowers for deficiencies is an appropriate response.

Survey Results

In the following **fifteen states** and the **District of Columbia**, mortgage holders are free to pursue collection of deficiencies against foreclosed homeowners without limitation:

Alabama	Mississippi
Delaware	Missouri
District of Columbia	New Hampshire
Illinois	Rhode Island
Indiana	Tennessee
Kentucky	Virginia
Maryland	West Virginia
Massachusetts	Wyoming

Many state legislatures have enacted statutes that substantially restrict mortgage holders' ability to pursue deficiency claims. These statutes take two basic forms. Some prohibit pursuit of deficiency claims outright. Other states do not prohibit deficiency claims after foreclosures, but impose significant limits upon them. The most common limitation is to require that the fair market value of the property be substituted for the foreclosure sale price when calculating the amount of a deficiency. The debt owed after foreclosure is then reduced by the larger of the foreclosure sale price or the fair market value of the property.

While the prohibitions do not apply across the board in all foreclosures, the following ten states have enacted laws that completely bar deficiencies claims after most home foreclosures:

Alaska *(bars deficiency after power of sale foreclosure)*
Arizona *(no deficiency for most home purchase mortgages)*
California *(no deficiency after power of sale foreclosure on home mortgage)*
Hawaii *(no deficiency after power of sale foreclosure of mortgages executed after 1999)*
Minnesota *(no deficiency after power of sale foreclosure if six-month redemption applicable)*
Montana *(no deficiency after power of sale foreclosures)*
North Dakota *(no deficiency for most residential properties)*
Oklahoma *(no deficiency after power of sale foreclosures)*
Oregon *(no deficiency after power of sale foreclosure or after judicial foreclosure of home)*
Washington *(no deficiency after power of sale foreclosure of residential properties)*

Statutes creating a clear prohibition against deficiency actions offer the most effective protection for homeowners. Two uniform foreclosure laws, the Uniform Land Security Interest Act (ULSIA) adopted in 1985 and the Uniform Nonjudicial Foreclosure Act promulgated in 2002, contain provisions that bar deficiency actions.[80]

The following **twenty-one states** have enacted laws that require mortgage holders to use the fair market value as the basis for calculating a deficiency debt after a foreclosure sale in most home foreclosures:

Colorado *(non-judicial)*
Connecticut *(judicial)*
Georgia *(non-judicial)*
Idaho *(non-judicial)*
Kansas *(non-judicial)*
Louisiana *(executory process)*
Maine *(judicial)*
Michigan *(non-judicial)*
Nebraska *(non-judicial)*
Nevada *(non-judicial)*
New Jersey *(judicial)*
New York *(judicial)*
North Carolina *(non-judicial)*
Oklahoma *(barred in non-judicial, limited to fair market value in judicial)*
Pennsylvania *(judicial)*
South Carolina *(judicial)*
South Dakota *(non-judicial)*
Texas *(non-judicial)*
Utah *(non-judicial)*
Vermont *(judicial)*
Wisconsin *(judicial)*

Using a property's fair market value rather than the sale price to calculate the deficiency can reduce the borrower's net debt owed to the lender by a substantial amount. Unfortunately, all states do not apply the fair market value limitation on deficiencies in a uniform way. In a few states, the fair market value calculation may be used to reduce a deficiency only in non-judicial foreclosures. **Nebraska** and **Utah** restrict use of the fair market value standard in this way. Other states apply the limitation when the mortgage holder purchases the property at the foreclosure sale. This is the case in **Arizona, Maine, Michigan, North Carolina, Pennsylvania,** and **South Dakota**.

Another practice that allows courts in judicial foreclosures to limit deficiency liabilities is the use of an "upset bid" as a threshold to bidding at a foreclosure sale. Under this practice, the court requires a fair market value appraisal before the foreclosure sale and sets an "upset bid," or required minimum bid, based on the appraised value.[81] **Arkansas, Louisiana,** and **Ohio** use variations of this practice.

Additional limits on deficiencies come in the form of short statutes of limitations for filing a deficiency lawsuit. Several states, including **Idaho, Nebraska, New Jersey, Oklahoma,** and **Utah,** set three-month limitation periods for filing mortgage deficiency claims with a court. If the mortgage holder does not begin legal action within this time, its deficiency claim is permanently barred. Under the **Montana, Nevada,** and **New York** procedures, the lender must seek the deficiency when it forecloses or in the confirmation of sale proceedings. These timing restrictions effectively prevent lenders from waiting until years later to bring a collection action. Under **Iowa's** statute the lender must waive any deficiency claim if it wishes to enforce the borrower's waiver of the post-sale redemption right.

New Mexico enacted a unique provision that bars deficiency claims from deeds of trust securing residential loans made to low-income households. The law applies to households whose income was lower than 80% of the state median for the family's size at the time of the loan application. **Florida's** statute gives the courts a general discretion to regulate deficiency claims, but does not mandate application of any particular guideline or rule.

California laws provide some of the broadest protections against deficiency claims. California statutes allow holders to use either a judicial or non-judicial foreclosure procedure. Mortgage holders overwhelmingly favor the non-judicial procedures. Deficiency actions are prohibited in both judicial and non-judicial foreclosures in California when the loan was secured by a residential property containing four or less units. No deficiencies are allowed in connection with power of sale foreclosures, regardless of the type of property involved. An exception to this broad rule applies only to junior mortgagees. A junior mortgagee may bring a lawsuit to recover a money judgment against the borrowers if its lien has been voided through foreclosure of a senior lien. The bottom line in California is that deficiency claims are available only with certain junior mortgages or after judicial foreclosures, and these are limited by the fair market value rule and cannot involve loans for purchase of residential properties.[81]

Recommendations for Homeowner Protections

1. Bar all deficiency actions after foreclosure on residential properties

Upon analysis, many of the limitations on the scope of anti-deficiency statutes for consumer borrowers prove to be arbitrary. For example, applying the protection against deficiencies solely to purchase loans for residential properties fails to protect borrowers whose loans involved refinancings and other loans secured by a home. Similarly, the inconsistent treatment of judicial and non-judicial foreclosures does not stand up to scrutiny. Creditor conduct that results in low bids in non-judicial foreclosures occurs just as routinely in judicial foreclosures. Competitive bidding is largely a fiction in both contexts. The best protection for consumers against future deficiency actions is to bar them for all loans secured by a residence and to apply the prohibition equally to judicial and non-judicial foreclosures. This will achieve the goals of protecting both individual borrowers who are seeking better futures for themselves and the communities that are reeling from the cumulative impact of a multitude of foreclosures.

2. To extent deficiency actions are allowed, make them subject to fair market value and time limitations

If deficiency actions are allowed, the calculation of the deficiency amount should be based on the greater of the fair market value of the property or the sale price at foreclosure. However, there are several drawbacks to reliance on the fair market value calculation as the primary means to protect borrowers from deficiencies. In many instances the rules require a timely property appraisal. Paying for an appraisal is often beyond the means of a homeowner facing imminent foreclosure. At the time of foreclosure the borrower's attention is understandably focused on essential survival and relocation options. In addition, the rule presumes a degree of knowledge and sophistication on the part of unrepresented borrowers that is simply unrealistic. As discussed above, borrowers are often surprised years after a foreclosure when they first learn about the concept of a deficiency claim. This typically happens when they are served with the legal papers starting the deficiency lawsuit.

A few modifications of procedures would make application of the fair market value limitation a more effective protection for homeowners. One option would be to set a strict time limit on raising deficiency claims. Requiring the holder to raise the claim during or immediately after the foreclosure would encourage production of a timely appraisal. Under **New York's** statute, the mortgage holder must have the court establish a deficiency claim during the proceeding to confirm the foreclosure sale, otherwise the claim is barred. This limitation is preferred, at least in judicial foreclosure states. Alternatively, a ***three-month*** time limit after the sale should be set for bringing a deficiency claim, as required now in several states.

Another protection in judicial foreclosure states would be to have the court order an appraisal after a foreclosure judgment and before any judicial sale. The court could use a system for selecting neutral appraisers and require the mortgage holder to pay for the appraisal as part of its costs of foreclosure. The current **Ohio** practice follows a version of this procedure. If the court does not order the appraisal, a minimally protective alternative would be to place the initial burden of producing an appraisal showing fair market value on the mortgage holder. The court could then review the appraisal in the context of a timely deficiency action and the borrower would have the opportunity to present contrary evidence, including an opposing appraisal. In power of sale states, the mortgage holder could be required to obtain an appraisal before the foreclosure sale and attach it to any legal papers filed against the homeowner seeking a deficiency judgment.

Finally, the fair market value limitation on deficiencies must apply to all home foreclosures. The limitations that many states place on the rule, such as those based on the type of foreclosure or the identity of the purchaser, did not develop out of any comprehensive legislative plan and are arbitrary in practice.

C. *Accounting of Foreclosure Sale Proceeds and Return of Surplus*

Accounting of foreclosure sale proceeds

In the typical foreclosure auction the mortgage holder submits the highest or often the only bid and buys the property. Because the borrower's debt usually exceeds the amount of the mortgage holder's bid, the bid is simply treated as a credit toward the borrower's deficiency debt. Occasionally the sale brings in a bid that is high enough to pay off the mortgage debt and the costs of the sale. During periods of a robust real estate market, this is more common. When this happens, most state laws require that the remaining proceeds be applied to pay off any junior mortgages and judgment liens recorded against the property. Finally, if all these claims are paid in full and a surplus still remains, the final surplus is paid over to the borrower.

Regardless of which of these scenarios occurs at the auction, the borrower has significant interests at stake throughout the foreclosure sale process. A remaining surplus represents the borrower's equity from the home, possibly the sole investment of a lifetime. The surplus can provide a source of funds that allow a family to relocate and start on the road to financial recovery. For this reason, when there is any surplus from a foreclosure sale, the borrower needs to be sure that the amount is calculated accurately and that the funds are available promptly.

Even in the more common case, when the borrower does not receive any surplus, the manner in which proceeds from a foreclosure sale are applied can have a significant impact on the borrower's financial future. For example, if other creditors receive more from the sale proceeds than is lawfully due to them, a potential surplus that would otherwise go to the borrower can disappear. If the mortgage holder includes exorbitant foreclosure charges and other "junk" fees in the loan balance, these bogus charges will similarly eat away at a potential surplus. Bad accounting, whether the result of negligence or deliberate calculation, can erase a surplus or leave the borrower with a highly inflated deficiency debt.

Despite the clear need for a system that imposes strict oversight over the distribution of foreclosure sale proceeds, many state laws are surprisingly lax in the supervision they provide. Homeowners are not familiar with the procedures and seldom know that they have any rights to protect. Often they do not receive documents and critical notices, such as the report of the sale. Reported court decisions give an indication of the nature of these problems. For example, a **Massachusetts** homeowner never found out that she was entitled to a $21,000 surplus from a non-judicial foreclosure sale until one year after the sale, when she received a notice from the Internal Revenue Service (IRS) informing her that her former lender had reported the surplus to the government as income to her.[82] A **Maine** appellate court has held that a seventeen month delay in filing an accounting and report of sale was reasonable given the lack of any express statutory time frame under the state's foreclosure laws.[84]

"Surplus retrieval" consultants

It is not surprising that during the current foreclosure epidemic a cottage industry of "surplus retrieval" consultants has emerged. These scammers offer a "service" of assisting distressed homeowners through the maze of procedures surrounding a foreclosure sale. The consultants typically end up with a lion's share of any surplus, or simply take money from financially strapped homeowners when there is no likelihood there will ever be a surplus. Some states, including **Nevada** and **Maryland**, recently enacted statutes drafted specifically to regulate the practices of "surplus purchasers."[85] Other states, including **California, Colorado,** and **Florida**, include surplus purchasers and their practices within the definition of "foreclosure consultants" who are now subject to state regulation.[86] Homeowners turn to these unscrupulous enterprises out of sheer desperation. This desperation is a clear indication of the need for stronger judicial supervision and control over the entire foreclosure sale process, including the turnover of any surplus proceeds.

Comparing judicial and non-judicial foreclosures

When it comes to protecting the borrowers' interests in an accurate and timely distribution of foreclosure sale proceeds, judicial foreclosure systems always provide more safeguards than the non-judicial procedures. Unlike non-judicial foreclosures, which involve little or no court supervision, judicial foreclosures require, or at least permit, court intervention at the important stages in the foreclosure process. When a court enters a foreclosure judgment, whether by default or after litigation, a judge signs an order approving the claims of the various parties who will be paid out of the proceeds from a sale. This order directs an official, typically a sheriff, to conduct a sale of the property. In most cases the judgment order itself tells the official how to distribute proceeds from the sale. If the order does not expressly do so, the order will likely direct the official to make a distribution of proceeds according to priorities set forth in a state statute.

After the sale in a judicial foreclosure, the mortgage holder or the officer who conducted the sale must file a report describing how any proceeds have been disbursed. If a surplus remains after paying off the mortgage debt and the costs of the sale, the report will give notice of this sum. The report is a public document filed with the court or county clerk. If there is a surplus to be distributed, the officer pays the surplus funds into court or retains them pending a further order from the court.

A judicial foreclosure typically includes a post-sale motion procedure in which the court must "confirm" the sale. In some states this court review and a hearing are automatic after all foreclosure sales. In other states the matter is set for court review and a hearing only if someone disputes the officer's report, including its proposed distribution of a surplus. When a judge rules in a proceeding to confirm a sale, the judge's order addresses the distribution of any remaining surplus.

In sum, most judicial foreclosures provide the homeowner with notice and an opportunity to dispute claims on two occasions. First, the homeowners can dispute the claims of interested parties by responding to the summons and complaint that begin the lawsuit. Second, in the post-sale confirmation proceedings the homeowner can challenge a proposed distribution of proceeds, as well as any other defects in the conduct of the sale.

A non-judicial foreclosure proceeds along a very different track. When a non-judicial sale takes place there will have been no prior court ruling that established the amounts owed to the mortgage holder or any other entities claiming shares in the sale proceeds. If the sale results in a deficiency rather than a surplus, a private trustee or the mortgage holder plays a large role in determining the costs of the sale and the extent of any credit against the borrower's debt. When state law allows the mortgage holder to pursue the borrower for a deficiency judgment, this assessment of the borrower's debt by the mortgage holder or trustee will be the initial basis for the deficiency claim. It will also be the amount the mortgage holder reports to the IRS as taxable income to the borrower. The consequences of this initial assessment of the borrower's debt can be difficult to undo at a later time.

If a third party purchases the home at a non-judicial foreclosure sale, it will again be the private trustee or the mortgage holder who applies all payments received toward the borrower's debt and to foreclosure charges. In some jurisdictions the individual mortgage holder or trustee has authority to complete the distribution of any available proceeds to junior lienholders and to judgment creditors. If there is any final surplus left, the trustee or mortgage holder pays this surplus to the borrower. Thus, in a non-judicial proceeding, the entire foreclosure, including the accounting and distribution of all proceeds, usually takes place outside the supervision or control of a neutral judicial official.

Survey Results

Accounting of sale proceeds—judicial foreclosure states

Judicial foreclosure systems work most effectively to protect the interests of homeowners when they require that a court review all aspects of the sale. The foreclosure procedures should mandate close scrutiny over disbursements for any charges that were not included in the court's earlier foreclosure judgment. For example, payments for new post-judgment foreclosure costs and fees should not be paid from the proceeds unless the court has explicitly approved them. The following **thirteen states** require this type of formal court review after all judicial foreclosure sales:

Connecticut	New York
Delaware	North Dakota
Illinois	Ohio
Indiana	Oklahoma
Kansas	South Dakota
New Jersey	Vermont
Wisconsin	

In addition to these states, both **Puerto Rico** and the **Virgin Islands** use judicial foreclosure systems that require court approval of sales and distribution of surplus proceeds. Of the states in which judicial supervision of foreclosures occurs, only **Colorado** and **Iowa** do not routinely provide for court review of distribution of proceeds following foreclosure sales.

In the states that require a court to conduct a formal post-sale review, either the official who conducted the sale or the mortgage holder must file a formal request with the court to ratify the sale and approve the proposed distribution of any surplus. In some states, such as **Connecticut, Illinois, New York, Ohio,** and **Vermont**, requests to confirm a foreclosure sale are treated as distinct legal proceedings, following specific court rules. The procedures include the opportunity for a hearing and a decision in writing from a judge. In **Connecticut** the ruling is designated as a "supplemental judgment" and is a separate, appealable court order distinct from the court's earlier foreclosure judgment.

New York follows this type of formal procedure for surplus money proceedings. In one published decision, a New York trial court reviewing a foreclosure sale discovered that the mortgage holder had made a claim for $88,000 in attorney's fees connected with the foreclosure, a charge not included in the court's earlier foreclosure judgment.[87] The court determined the reasonable attorney fee charge to be only $5,000. When a state's laws provide for court procedures to confirm a sale, abuses such as these can be remedied effectively.

An alternative but slightly less protective system for review of judicial foreclosure sales exists in several other states. In **Florida, Kentucky, Maine,** and **Pennsylvania,** the officer who conducted the sale files a report of the sale. The report is a matter of public record. The homeowner or any other interested party may then request a court review. Under this practice, a court does not routinely review the conduct of the sale or the distribution of proceeds unless a party has formally objected to the officer's report of the sale. Absent objection, the official will distribute proceeds from the sale as described in the report of the sale.

Accounting of sale proceeds— non-judicial foreclosure states

In non-judicial foreclosures, there is typically no court involvement in the period leading up to the sale. A neutral public official will not have reviewed the extent or validity of the mortgage holder's claim or the claims of any junior lienholders. Therefore, after a non-judicial foreclosure sale, it is critical that there be judicial scrutiny of the disbursement of proceeds. Unfortunately, under most non-judicial procedures, the opposite is true. Despite the need, the majority of non-judicial foreclosure states do not have any explicit procedures or protections for homeowners that apply routinely to accounting of sale proceeds.

Non-Judicial Foreclosure States Lacking Routine Sale Accounting Homeowner Protections

Alabama, Alaska, Arizona, Arkansas, District of Columbia, Idaho, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, Oregon, Rhode Island, Tennessee, Utah, West Virginia, and Wyoming

Under most non-judicial foreclosure systems, borrowers' access to court procedures that can hold a trustee accountable often proves to be costly and time consuming. To the extent that avenues for court review after a non-judicial foreclosure exist at all, the procedures appear designed primarily for the benefit of the trustee or mortgage holder. The procedures authorize trustees or mortgage holders to wash their hands over troublesome cases involving conflicting claims of junior lienholders and refer those disputes to the courts to settle.

In the realm of non-judicial foreclosures, there are a few general schemes that allow for limited judicial review of the conduct of sales. Those that do the best job of protecting homeowners require that in all cases in which there is a surplus left after payment of the foreclosing mortgage holder's claim and the costs of sale, the surplus must be transmitted to the local court for further action. Under the non-judicial foreclosure statutes of **New Hampshire**, **South Dakota** and **Washington**, all cases involving a surplus are directed to court review. **Maryland's** court rules apply the same judicial review procedure to both judicial and non-judicial foreclosure sales.

Several other states provide some limited judicial review of non-judicial foreclosure sales. In **Virginia**, the trustee reports to a county commissioner of accounts who reviews the report and sends it on for court review. A judge can confirm or reject the account over a 15-day period. **North Carolina's** law requires the trustee to file a report of the sale with the court within five days of the sale and pay a surplus into court under specific circumstances defined by statute, such as when claims are disputed. Similarly, **California** and **Massachusetts** require the trustee to make a report and, under conditions set forth in the statutes, refer certain questions of proposed distribution of proceeds to a court. **Michigan** requires that the trustee refer the disbursement of the surplus to the court if a junior lienholder makes a claim. **Georgia's** non-judicial foreclosure statute mandates court confirmation of a sale, but only if the mortgage holder intends to seek a deficiency judgment.

Most other states give a private trustee or the lender substantial discretion in determining when to refer a question over distribution of proceeds to a court. The trustee makes the initial distribution from sale proceeds to cover the foreclosing mortgage holder's claim and the costs of the sale. Then, to the extent proceeds remain, the trustee has the discretion to complete the distribution, including payments to junior lienholders and to the borrower.

The statutes in **Arizona, Montana, Nevada, New Mexico,** and **Utah** expressly give the trustee the authority to file an "interpleader" type of legal action in a court. In an interpleader case, the trustee pays the sale proceeds into court so that a judge can decide how the funds should be disbursed. Under most non-judicial foreclosure systems, starting such a proceeding is left to the trustee's discretion. Although a state's foreclosure statutes may not expressly provide for a trustee's authority to start an interpleader action, trustees have the option of resorting to this general type of court proceeding in any jurisdiction when they face disputed or complex claims related to a specific sum of money.

Ostensibly, a homeowner who has the requisite sophistication and financial resources could initiate a lawsuit to stop an inappropriate distribution of a surplus in any non-judicial foreclosure. However, this remedy is almost always illusory. As a practical matter, homeowners find themselves in much the same position after a non-judicial foreclosure sale as they do at the commencement of the proceeding—they must file a lawsuit with a court in order to stop proceedings that will otherwise forge ahead without any court oversight. In both situations time constraints and the unavailability of affordable legal help effectively bar homeowners from access to the courts.

Finally a number of state statutes simply direct the trustee to follow the state's general ranking of priorities in distributing proceeds from a non-judicial foreclosure sale. The distribution takes place entirely outside of court supervision. The priorities are set by statute, or otherwise are part of the state's common law. The statutes in **Arkansas, Idaho, Minnesota, Oregon, West Virginia,** and **Wyoming** operate in this manner. Absent a controlling statute defining priorities for distribution, trustees in some states, such as **Texas**, follow common law rules for distribution of proceeds.

Timely access to surplus sale proceeds

Thirty-two states and the **District of Columbia** do not require a surplus to be released by a certain date to the homeowner after a foreclosure sale.

States Which Do Not Require Prompt Release of Surplus Funds

Alabama, Alaska, Arkansas, Colorado, District of Columbia, Delaware, Florida, Georgia, Idaho, Indiana, Iowa, Kansas, Kentucky, Maine, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Jersey, New Mexico, North Dakota, Oklahoma, Oregon, Rhode Island, South Carolina, Tennessee, Texas, Utah, Washington, and Wisconsin

Many states allow a certain period of time for the official who conducted the foreclosure sale to file a report and accounting of the sale. Because the filing of this report is often a prerequisite to release of a surplus to the homeowner, states should require that the report be filed promptly. However, the states' responses to this need for prompt release of the report vary significantly. The **Illinois** statute simply requires that the report be filed "promptly." The **Maine** statute does not set any time limit at all, and this caused a Maine court to find that a 17-month delay was not unreasonable.

Many states, however, do set a time limit for the filing of the report of sale after a foreclosure. **North Carolina** requires that the report be filed within five days of the sale.[88] **New York** requires that the surplus be paid to court within five days of the sale and the report must be filed within 30 days.[89] **Vermont** and **Wyoming** require reports of surplus and an accounting to be served within 10 days of the sale.[90] In **New Hampshire**, the accounting must be filed within 10 days of the sale. **Arizona** requires notification to the borrower of any available surplus within 15 days of the sale.[91] There are no sound reasons to justify periods longer than 15 days for filing a report of a sale, as these statutes allow. However, many states permit significantly longer times. These range from 30 days in **California, Pennsylvania, and Maryland**, to 45 days in **Hawaii**, 60 days in **West Virginia**, and six months in **Virginia**.[92] Under the California procedure, the trustee has 30 days from the execution of the trustee's deed to notify parties of a surplus remaining after the initial payment to the lender. Parties then have 30 days to file claims. At the end of 30 days, assuming no disputes require court intervention, the surplus is released.

Once homeowners receive a report of the sale, they can decide whether to challenge the report or accept it. Again, local statutes vary in the time limit they set for filing objections. Once an objection is filed, court calendars may have more to do with the time frame in resolving the objection than do the statutory provisions. The most efficient procedures will again be those in jurisdictions such as **Connecticut** and **New York** which follow standard motion rules for reviewing the conduct of foreclosure sales and issuing orders for disbursement of proceeds. When the accounting for a surplus is not disputed, these motions proceed with little delay.

Recommendations for Homeowner Protections.

1. Require effective means to notify the borrower of the proposed distribution and an explanation of basic rights under the sale procedures

Homeowners often move away abruptly in reaction to a looming foreclosure. Default judgments are common in judicial foreclosures, and defaulted parties typically do not receive notices of ongoing events in a lawsuit. Therefore, foreclosure sale procedures must provide extra protections to ensure that borrowers receive notices of key events related to the sale. As discussed in Section 5, *supra*, a requirement that the notice of sale be served personally on homeowners is a much needed reform. In addition, the notice should contain a description of the state's procedures related to disbursement of proceeds from the sale. The notice should include language urging the borrowers to submit an updated mailing address so they will be kept informed of further proceedings related to any surplus.

Another protection, as is provided in **Ohio**, is to require additional steps to give notice after mail sent to the homeowners has been returned as unclaimed. There are many inexpensive and effective methods for locating individuals who have moved. Trustees and mortgage holders should be required to pursue these measures.

After the foreclosure sale is completed, the trustee or mortgage holder should be required to prepare and serve on the borrower a final report and accounting which lists all of the proposed distributions of the sale proceeds, including an itemization of all amounts to be paid to the mortgage holder for principal, interest, escrow charges, late fees, foreclosure costs, and other fees. The report would also specify the amount of any surplus. State law should require that this report be prepared and served within 15 business days of the foreclosure sale.

2. Require review and approval by a neutral public official of all distributions of proceeds before they take place

This protection is essential for non-judicial foreclosures, whether or not there is a surplus. Private, interested individuals should not play this critical role in using the borrower's property to pay their own debts as well as debts the borrower owes to others. In judicial foreclosures, the laws must require that a court approve payment of any claims not already fixed by an earlier foreclosure judgment. In both types of foreclosure, the review must occur through an independent judicial proceeding with a record and right to review.

3. Require that surplus funds be disbursed promptly to the borrower

State law should set a deadline for distribution of surplus funds. This deadline should be soon after a final report and accounting is approved by the court, generally no more than 10 business days after any time to appeal the approval to a higher court has passed.

4. Provide that surplus funds are exempt from creditor collection actions and that homeowners get notice of exemption rights

Many state laws allow borrowers to claim a homestead exemption in surplus proceeds from a foreclosure sale. The surplus represents the borrower's exempt equity in the home and can be a resource to use for replacement housing in the future. Since creditor claims, even those which are judgment liens, typically cannot be enforced against exempt homestead property, a borrower should be able to protect surplus funds in the same way by claiming them as exempt. States should amend their laws to allow for the exemption of surplus funds.

Whenever government officials assist private creditors in seizing property from debtors there is a great risk that the debtors will lose exempt property without knowledge of their right to claim an exemption and keep all or part of the property. Many courts have recognized this risk. They have ruled that basic due process law mandates that government officials give notice of exemption rights to debtors before they lose property involuntarily and permanently to a creditor. Notices of exemption rights should be required prior to any judicial foreclosure sale and in any non-judicial proceeding in which government officials play a significant role. Notices of exemption rights must include information about the procedures available under state law that the debtor may use to claim the homestead exemption in proceeds from a foreclosure. State law should ensure that surplus proceeds held by a trustee or mortgage holder's attorney, or held in the court registry, should not be released to other creditors until there is a determination made that the proceeds are not exempt.

APPENDIX A

SURVEY OF STATE FORECLOSURE LAWS

Appendix A provides a detailed analysis of each state's law based on a set of questions designed to determine whether certain basic protections are provided for residential homeowners. Because of its length, it is found as an appendix to this report only at www.nclc.org.

APPENDIX B

Court Mediation Programs

Philadelphia's Residential Mortgage Foreclosure Diversion Pilot Program

This program is mandatory and applies to all mortgage foreclosure cases where the property is residential, owner-occupied and located in Philadelphia County.

How Does a Homeowner Participate in the Philadelphia Mediation Program?

When a foreclosure Complaint is filed, the court schedules a mandatory Conciliation Conference. Both the homeowner and the mortgage holder's servicer are required to attend. However, the servicer may appear by telephone.

Are There Any Special Requirements?

The court will require the homeowner to immediately call the Save Your Home Philly Hotline. The Hotline will then direct the homeowner to a housing counseling agency. The court further requires the homeowner to cooperate with the housing counselor and provide financial information necessary to complete loan resolution proposals. The court also requires the homeowner and the mortgage holder to exchange information.

What Is the Role of the Housing Counselor?

The housing counselor will meet with the homeowner to explore the homeowner's options. They include: bringing the mortgage current; paying off the mortgage; a repayment plan; agreeing to vacate the premises in exchange for the mortgage holder not contesting the matter and a monetary payment; offering the holder a deed in lieu of foreclosure; filing bankruptcy; paying the mortgage default over 60 months; requesting a loan modification; opposing the foreclosure.

With the homeowner's permission, the housing counselor will prepare and submit a written proposal addressing the mortgage delinquency to the holder's attorney as soon as possible; or at least 10 days before the Conciliation Conference. The holder must evaluate and respond to the homeowner's proposal before the Conciliation Conference.

What Happens If the Homeowner and the Mortgage Holder Do Not Reach an Agreement Before the Conference?

Unless an agreement has been reached before the Conference, a representative of the holder who has authority to modify the mortgage, to enter into an alternate payment agreement or to otherwise resolve the action must attend the Conference or be available by telephone. If the holder does not attend the Conference, the Conference is rescheduled and the sheriff sale is postponed. If the homeowner does not attend the Conference, the court will issue an order allowing the sale of the property.

What Happens at the Conciliation Conference?

The Conciliation Conference is conducted by a person designated by the court who possesses experience in the area or by a trial judge. The parties address the following issues: whether the homeowner is represented, and if unrepresented whether volunteer counsel is available to represent the homeowner; whether the homeowner met with a housing counselor; whether the housing counselor prepared a loan work-out report; homeowner's income and expense information; homeowner's employment status; homeowner's qualifications for any of the available work-out programs; assistance with preparation of the work-out plans; the need for another Conciliation Conference; whether the case should proceed to sheriff sale since there is no prospect for an agreement.

What Happens After the Conference?

Unless an agreement is reached at the Conference, the sale of the property will proceed. If an agreement is reached, the court will issue an order memorializing the agreement.

Ohio's Foreclosure Mediation Program Model

The Supreme Court of Ohio designed a model mediation program for courts throughout Ohio to modify and use for their own needs. It is unknown how many counties in Ohio have adopted the foreclosure mediation program. Under the Ohio model program, mediation is not mandatory.

How Does It Work?

The mortgage holder sends to the homeowner along with the Summons and foreclosure Complaint filed with the court a Request for Foreclosure Mediation form and mediation and foreclosure brochures. The homeowner has 28 days after service of the Summons to answer the Complaint and send in the Request for Foreclosure Mediation form to the court's Mediation Department. If the homeowner sends in the Request for Foreclosure Mediation, the Mediation Department sends a letter to the holder along with the holder's Mediation Questionnaire for Foreclosure Cases. The holder has 14 days to complete the questionnaire and return it to the Mediation Department.

The Mediation Department then reviews the homeowner's Request form and the holder's Mediation Questionnaire to determine if mediation is appropriate. The program does not set any specific criteria for determining when a case is appropriate for mediation.

If the case is not appropriate for mediation, the Mediation Department notifies the parties and the case continues on the trial docket. If the case is sent to mediation and an agreement is reached, the parties memorialize the agreement by: having a written agreement signed by all the parties, having the agreement read into the record by a court reporter, or tape recording the agreement with all parties stating their consent to the agreement. If no agreement is reached, the case continues on the trial docket.

Is the Model Program in All Counties?

The Ohio model program is designed for use in its current form or with modifications where appropriate. Counties may implement changes that include: making the program mandatory, creating a role for housing counselors and attorneys, and establishing a set of criteria for the Mediation Department. Also, before implementing a mediation program, the model program recommends that counties have a meeting with the stakeholders to discuss foreclosure mediation. Franklin County (Columbus), Clark County (Springfield) and Ashtabula County have or are currently implementing programs. Cuyahoga County has implemented a program and a description appears at www.cp.cuyahogacounty.us/internet/CourtDocs/ForeclosureMediation.pdf.

Connecticut's Foreclosure Mediation Program

Does the Foreclosure Mediation Program Apply to All Cases?

Connecticut's Foreclosure Mediation Program applies to mortgage foreclosure actions that have Summons return dates on or after July 1, 2008. The homeowner must also occupy the home as his or her primary residence.

How Does It Work?

The mortgage holder is required to attach to the front of the foreclosure Complaint a notice about the availability of foreclosure mediation and a Foreclosure Mediation Request form. Upon receiving the notice, the homeowner may request mediation by filing the form with the court within 15 days after the return date on the Summons. A homeowner's participation in the mediation program does not suspend his or her obligation to respond to the foreclosure and answer the Complaint. No judgment of foreclosure will be entered until the mediation period has expired.

How Long Is the Mediation Period?

The mediation period begins when the court notifies the parties that the homeowner submitted a Mediation Request form. It ends no more than 60 days after the return date for the foreclosure action. The court may extend the mediation period for 10 days.

Who Should Attend?

The mortgage holder and the homeowner must attend in person and have authority to agree to a proposed settlement. If a holder is represented by an attorney, the attorney may appear without the holder, but the attorney must have authority to agree to the proposed settlement. The holder must be available by telephone. If the homeowner is represented by an attorney, both the attorney and homeowner must be present.

What Happens at the Conference?

During mediation, the parties are expected to address issues such as: reinstatement of the mortgage, restructuring of the mortgage debt, assignment of sale date, and foreclosure. The mediators are judicial employees who are trained in mediation and foreclosure law.

Have There Been Any Reports Issued?

In a report issued by the Superior Court Judicial Operations Branch reviewing cases filed from July 1, 2008 through October 31, 2008, 7,063 foreclosure cases were filed statewide during the period. Of the 5,513 eligible for mediation, 1,553 defendants (28% of those eligible) sought mediation, and 680 mediations were completed. Of the 680 cases mediated, 40% (or 270 cases) were reported as resulting in loan modifications; 53% as "staying in home"; 17% as "moving from home; and 30% as "not settled." The report does not give information on nature of loan modifications.

Other Programs:

New York's Residential Foreclosure Program

The Chief Judge of the New York State Unified Courts issued report in June 2008 establishing a Statewide Program for Residential Owner Occupied Foreclosures. The plan anticipates amending local court rules to include mediation procedures for foreclosures. The initial pilot program was to operate in Queens, then expand statewide. Under general guidelines, notice of availability of mediation is to be served with the complaint. A second notice is to be sent by the court, notifying the homeowner that a conference can be held within 60 days. In order to schedule a conference, the homeowner is required to confirm by sending in a request for conference and indicating that he/she scheduled an appointment for legal assistance or housing counseling, or explain why this has not been done. The request for a conference does not relieve the homeowner of the obligation to file an answer. Further case management scheduling will be made at the initial court conference. The homeowner can request an extension of time to complete mediation. Information is available at www.courts.state.ny.us (under "What's New).

New York Civil Practice Rule 3408, effective September 1, 2008, requires mandatory settlement conferences for residential foreclosure actions involving high cost home loans originated from January 1, 2003 through September 1, 2008, as well as certain subprime non-traditional loans (including payment option, adjustable rate mortgages) and loans defined by the Real Property Actions and Procedures Law (RPAPL) § 1304. Mortgagees are required to give 90 days notice to homeowners before filing a foreclosure action involving these types of loans. The conference must be scheduled within 60 days of service of the complaint or as continued by the court. At the conference, the parties will review payment revisions and other options to avoid foreclosure. The court may appoint counsel for unrepresented homeowners. The foreclosing party must appear for the conference with an attorney authorized to settle and the mortgagee must be available by phone or video conference.

Florida Circuit Court Mandatory Mediation Programs

During late 2008, the chief judges of several circuits, including the 12th judicial circuit (DeSoto, Manatee, Sarasota counties) and the 18th judicial circuit (Seminole County) of Florida, authorized mediation for foreclosure cases in their courts. The chief administrative judge of a circuit may issue administrative orders related to court procedures under Florida Rule of Judicial Administration No. 2.215(b)(2).

The 12th Judicial Circuit order requires mortgage holders to attempt to set up a single phone conference without a mediator. The conference is to occur no later than 45 days after service of process. The parties can agree to a longer time frame for completion of the discussion. Homeowners are notified of the availability of mediation with service of the summons and complaint. The court proceeding is stayed pending the mortgage holder's certification that the mediation is completed. The conference may take place by phone. *See* www. 12circuit.state.fl.us.

The 18th Circuit requires a referral through the court's formal mediation process, using certified court mediators. All foreclosure cases involving residential properties are referred to mediation. The foreclosing party pays in advance the costs of $200 for a 1.5 hour session. Fees can be taxed as costs in a final judgment. The court proceeding is stayed until the mediation is completed. The foreclosing party may enter defaults and waive mediation only upon filing a motion certifying there has been communication with the homeowners and the foreclosure is truly uncontested. The mortgage holder may appear by phone, with attorney present. *See* www.flcourts18.org/foreclosures.php.

New Jersey Court Mediation Program

On October 16, 2008, the Chief Justice of New Jersey Supreme Court announced a program to require mediation in foreclosure cases. The program was to begin in selected counties with the intention to expand statewide. A request for mediation does not stay or otherwise delay a foreclosure action. The homeowner can request mediation up to the time of sale, but the homeowner must file a motion with the court to stay the sale if time is inadequate to complete mediation. The homeowner can request mediation if he/she did not file an answer. Information and instructional material on mediation must be served on the homeowner with the summons and complaint. This information includes the notice of mediation availability, mediation financial worksheet, and a HUD-certified housing counselor information form and recommendation sheet. These documents must also be served on the homeowner when a foreclosing party requests judgment. A further notice of availability of mediation must be given 60 days after the filing of the complaint. Mediation is not scheduled until a complete financial packet, including tax returns, pay stubs, and bank statements, is returned along with a housing counselor recommendation. The homeowner is required to formulate a proposal with a housing counselor when counseling services are available. These requirements apply to one to four unit owner-occupied properties. Mediation is to be "free." In January 2009, the legislature appropriated $12 million to pay for mediations. Information, notices, and forms are available at www.judiciary.state.nj.us.

APPENDIX C

State Rescue Funds Programs

State	Program	Loan Terms	Eligibility Requirements
Connecticut	Emergency Mortgage Assistance Program (EMAP), administered by Conn. Housing Finance Authority (CHFA)	*Continuing loan:* ▪ Initial disbursement paid to homeowner's mortgage holder to bring mortgage current. Homeowner pays portion of regular monthly mortgage payment to CHFA while receiving EMAP assistance, based on his/her income. CHFA then pays the total required monthly mortgage payment to the homeowner's mortgage holder for up to five years. ▪ Total amount of EMAP assistance paid by CHFA to the current mortgage holder is repaid by homeowner as a 30-year, fixed-rate, fully amortizing mortgage loan.	▪ EMAP is not available to borrowers who have FHA-insured loans. ▪ Homeowner must have had a significant loss of income beyond his or her control and be able to resume full mortgage payments in the future. ▪ Homeowner not eligible if behind in payments at least twice for more than 30 days during prior two years, though CHFA may waive this provision if owner can show this was due to circumstances beyond his or her control.
Delaware	Delaware Emergency Mortgage Assistance Program (DEMAP)	▪ Short term loan up to $15,000 with a fixed 3% interest rate. **Two Types of Loans:** *Continuing loan:* ▪ Pays the delinquent balance and assists the homeowner with his or her monthly payments for a period of 12 months. *Non-continuing loan:* ▪ Makes a one-time payment of the delinquent balance. ▪ Homeowner must be able to resume monthly mortgage payments after delinquent balance is paid.	▪ Homeowner must be 90 days or more delinquent in his or her monthly mortgage payments. ▪ Homeowner must have a good credit history prior to the delinquency. ▪ Homeowner must be experiencing financial hardship beyond his or her control. ▪ Homeowner must have a reasonable prospect of being able to make monthly mortgage payments in the near future. ▪ Homeowner must have no more than two mortgages on the property.

State	Program	Loan Term	Eligibility Requirements
Maryland	Bridge to Hope Loan Program	▪ Short term loan up to $15,000. **Terms:** ▪ Pays homeowner's delinquent payments and subsidizes home-owner's monthly mortgage payment up to 24 months. ▪ Loan is repayable at the time home is resold, transferred or upon refinancing of the existing mortgage.	▪ Homeowner must be in delinquency or imminent risk of delinquency because a subprime or exotic mortgage or an adjustable rate mortgage has or is about to reset. ▪ Homeowner must have stable employment. ▪ Homeowner must have a good mortgage/credit history prior to the reset.
Michigan	HELP Loan	▪ Short term loan up to $3,000 and is non-interest bearing. **Terms:** ▪ Pays delinquent amount or cost of non-recurring event that created the temporary financial difficulties. ▪ Loan is repayable when property is sold, transferred or otherwise conveyed or when homeowner defaults on the MSHDA mortgage.	▪ Homeowner must already have a Michigan's Save the Dream Mortgage Refinance Programs (MSHDA) mortgage and be experiencing temporary non-recurring difficulty paying the monthly MSHDA mortgage payments.
Minnesota	Foreclosure Prevention Assistance Program	▪ Short term loan up to $5,500. **Terms:** ▪ Provides one-time financial assistance towards mortgage payment or other financial assistance.	▪ Homeowner must be facing foreclosure because of temporary financial crisis.
New Jersey	Homelessness Prevention Program	**Terms:** ▪ Provides limited financial assistance. ▪ Payments are made either as loans or grants to the mortgage companies on behalf of the homeowner.	▪ Homeowner must have low or moderate income. ▪ Homeowner must be in imminent danger of foreclosure because of a temporary financial setback beyond his or her control.

State	Program	Loan Term	Eligibility Requirements
North Carolina	Home Protection Pilot Program	▪ Short term zero interest loan that is: lesser of $20,000 or 18 months of monthly mortgage payments; or the minimum amount required to bring the mortgage current. **Terms:** ▪ Loan is deferred for 15 years, unless the home is sold, refinanced or is no longer the principal residence. ▪ Once homeowner's application is approved, foreclosure is stayed for 120 days.	▪ Homeowner must be a worker who has lost his or her job in a designated county even if he or she does not live in that county. ▪ Homeowner must have had a stable employment and credit history before losing his or her job. ▪ Homeowner must be able to resume mortgage payments after the assistance ends.
Pennsylvania	Homeowners' Emergency Mortgage Assistance Program (HEMAP)	▪ Loan amount limited to the maximum of 24 months of mortgage payments from the date of the mortgage delinquency or a maximum of $60,000 whichever comes first. **Two types of loans:** *Continuing loan:* ▪ Pays delinquent mortgage balance and subsidizes monthly mortgage payments to mortgage holder. *Non-continuing loan:* ▪ Pays delinquent mortgage balance; homeowner is required to make all monthly payments to mortgage holder along with monthly payments to HEMAP.	▪ Homeowner must be at least 60 days delinquent on mortgage. ▪ Homeowner must have a favorable mortgage credit history prior to the delinquency during the past five years. ▪ Homeowner must be experiencing financial difficulty due to loss of job, illness, divorce, or other circumstances beyond his or her control. ▪ Homeowner must have a reasonable prospect of resuming full mortgage payments within 24 months.

Local Programs

- **Beyond Housing, St. Louis, Missouri**—To receive these funds, homeowners must face short-term problems beyond their control.
- **Home Headquarters, Syracuse, New York**—Homeowners can receive up to $2,000 towards the amount owed on their mortgages. However, homeowners must have a good credit history, must be financially stable, and the reason for the delinquency must be as a result of extenuating circumstances such as medical problems, divorce, death, or loss of employment. Homeowners are required to contribute 25% of the total loan amount from their own funds. The loans are forgiven if homeowners attend quarterly budget and credit counseling sessions for a year.
- **Foreclosure Emergency Assistance Program (FEAP), Waco, Texas**—FEAP funds are available to homeowners who have received a foreclosure notice. Homeowners are eligible if their delinquency was a result of illness, divorce, job loss or unforeseen circumstances that caused a temporary disruption in the ability to pay. Homeowners can receive funds up to $3,000. Counseling is required.
- **Neighborhood Housing Services, New York City, New York**—Offers small loans to assist homeowners who have predatory loans or who are delinquent because of financial hardship.
- **Michigan's Department of Human Services**—Homeowners facing foreclosures can receive up to $2,000.

Notes

[1] RealtyTrac, Inc., Foreclosure Activity Increases 81 Percent in 2008 (Jan. 15, 2009), *available at* http://www.realtytrac.com/ContentManagement/pressrelease.aspx?ChannelID=9&ItemID=5681&accnt=64847.
[2] RealtyTrac, Inc., Foreclosure Activity Up 14 Percent in Second Quarter (July 25, 2008), *available at* http://www.realtytrac.com/ContentManagement/pressrelease.aspx?ChannelID=9&ItemID=4891&accnt=64847 (reporting 222,391 REO properties for the quarter); HOPE NOW, Loss Mitigation National Data July 2007 to November 2008, *available at* http://www.hopenow.com/upload/data/files/HOPE%20NOW%20Loss%20Mitigation%20National%20Data%20July%2007%20to%20November%2008.pdf.
[3] RealtyTrac, Inc. has reported more than three quarters of a million properties are in its active REO database. *See* RealtyTrac, Inc., Foreclosure Activity Increases 8 Percent in July (Aug. 14, 2008), *available at* http://www.realtytrac.com/ContentManagement/pressrelease.aspx?ChannelID=9&ItemID=5041&accnt=64847; *see also* National Association of Realtors, July Existing-Home Sales Show Gain (Aug. 25, 2008), *available at* http://www.realtor.org/press_room/news_releases/2008/july_ehs_show_gain (reporting total housing inventory at the end of July at 4.67 million existing homes for sale).
[4] Kelly Bennett, Local Prices Down 30 Percent from Peak (Aug. 27, 2008), *available at* http://www.voiceofsandiego.org/articles/2008/08/27/housing/869dataparty082708.txt (reporting 135 of 337 properties listed for sale in San Diego area on Aug. 21 and 22, 2008, were bank repossessions).
[5] Seriously delinquent loans include loans that are at least ninety days delinquent, plus the loans-in-foreclosure inventory.
[6] The seriously delinquent rate for subprime loans in the first quarter of 2006, both fixed and adjustable, was 6.22%. By the third quarter of 2008 that number had grown to 19.56%. Similarly, in the prime market the number of seriously delinquent loans has climbed from .77% in the first quarter of 2006 to 2.87% in the third quarter of 2008. Mortgage Bankers Association, National Delinquency Survey, 2006–2008.
[7] Mortgage Bankers Association, National Delinquency Survey, 2006-2008.
[8] *Id.*
[9] Press Release, Federal Deposit Insurance Corp. , FDIC Announces Availability of IndyMac Loan Modification Model (November 20, 2008).
[10] *Id.*
[11]Credit Suisse, Credit Suisse Fixed Income Research, Foreclosure Update: Over 8 Million Foreclosures Expected (Dec. 4, 2008).
[12] Ellen Schlomer, et al., Center for Responsible Lending, Losing Ground, Foreclosures in the Subprime Market and Their Cost to Homeowners at 3 (Dec. 2006) (estimating that foreclosures will cost homeowners as much as $164 billion, primarily in lost home equity).
[13] *See* Erlenbusch, et al., National Coalition for the Homeless, Foreclosure to Homelessness: The Forgotten Victims of the Subprime Crisis (Apr. 15, 2008); Connie Paige, *Foreclosures Bring Rising Tide Of Homelessness*, Boston Globe, Jan. 4, 2009, at S1.
[14] It is estimated that 18% of the foreclosures started in the third quarter of 2007 were not occupied by the owners. *See* Jay Brinkmann, An Examination of Mortgage Foreclosures, Modifications, Repayment Plans and other Loss Mitigation Activities in the Third Quarter of 2007, Mortgage Bankers Association, at 10 (Jan. 2008), *available at* http://www.mortgagebankers.org/files/News/InternalResource/59454_LoanModificationsSurvey.pdf.*see also* Hearings Before the H. Comm. on Financial Services, 110th Cong. (Apr. 10, 2008) (statement of Sheila Crowley, discussing the affects of the foreclosure crisis on renters), *available at* http://www.house.gov/apps/list/hearing/financialsvcs_dem/crowley041008.pdf; John Leland, *As Owners Feel Mortgage Pain, So Do Renters*, New York Times, Nov. 18, 2007.
[15] Bankruptcy filings for 2008 were just under 1.1 million, as compared to 827,000 in 2007. The 2008 figure represents the highest number of filings since the 2005 amendments to the Bankruptcy Code. *See* Posting of Robert Lawless, Bankruptcy Filings Rise 32% in 2008, to http://www.creditslips.org/creditslips/2009/01/bankruptcy-filings-rise-32-in-2008.html#more (Jan. 5, 2009).
[16] *See* Letter, Senator Chris Dodd to Senator Harry Reid (Jan. 22, 2008), *available at* http://dodd.senate.gov/multimedia/2008/012308_ReidLetter.pdf (describing cycle of disinvestment, crime, falling property values and property tax collections resulting from foreclosures); Brad Heath & Charisse Jones, *Mortgage Defaults Force Denver Exodus*, USA Today, Apr. 1, 2008 (in some Denver neighborhoods as many as one-third of residents have lost their homes).
[17] *See, e.g.,* J.W. Elphinstone, *After Foreclosure, Crime Moves In*, Boston Globe, Nov. 18, 2007 (describing Atlanta neighborhood now plagued by house fires, prostitution, vandalism, and burglaries).

[18] *See* Daphne Sashin & Vicki Mcclure, *Foreclosure Leave Painful Ripple Effect*, Orlando Sentinel, Oct. 15, 2007 (describing a once safe neighborhood now dotted with empty homes and overgrown lawns).
[19] The Asset-Back Securities Market: The Effects of Weakened Consumer Loan Quality, FDIC Regional Outlook (Second Quarter, 1997).
[20] By the end of 1997, the volume of subprime mortgage-backed securities had leaped to about $90 billion, and by 2002, more than $134 billion were issued. Inside Mortgage Finance Publications, The 2003 Mortgage Market Statistical Annual (2003); Glenn B. Canner, Thomas A. Durkin & Charles A. Luckett, Recent Developments in Home Equity Lending, 84 Fed. Res. Bull. 241, 250 (Apr. 1998).
[21] Servicers are responsible for handling a variety of mortgage account activities. They send monthly statements, handle interest rate changes on adjustable rate mortgages, accept payments, keep track of account balances, process escrow accounts, engage in loss mitigation, and prosecute foreclosures. They also collect and report information to national credit bureaus, and issue reports and remit monies to the owners of the loans. In effect, servicers provide the link between mortgage borrowers and mortgage owners.
[22] *See* Kurt Eggert, Limiting Abuse and Opportunism by Mortgage Servicers, 15 Housing Policy Debate 753, 756–58 (2004).
[23] For a more detailed discussion of mortgage servicing abuses, see National Consumer Law Center, Foreclosures Ch. 6 (2d ed. 2007 and Supp.); *see also* Islam v. Option One Mortgage Corp., 432 F. Supp. 2d 181 (D. Mass. 2006) (servicer continued to report borrower delinquent even after receiving the full payoff amount for the loan); Hukic v. Aurora Loan Servicing, 2006 WL 1457787 (N.D. Ill. May 22, 2006) (servicer's clerical error in recording amount of payment left homeowner battling with subsequent servicers and fending off foreclosure for nearly five years); Vician v. Wells Fargo Home Mortgage, 2006 WL 694740 (N.D. Ind. Mar. 16, 2006) (servicers have forced-placed insurance in cases where the borrowers already had it and provided evidence of it); Dowling v. Select Portfolio Servicing, Inc., 2006 WL 571895 (S.D. Ohio Mar. 7, 2006) (servicers have forced-placed insurance in cases where the borrowers already had it and provided evidence of it); Barbera v. WMC Mortgage Corp., 2006 WL 167632 (N.D. Cal. Jan. 19, 2006); Rawlings v. Dovenmuehle Mortgage, Inc., 64 F. Supp. 2d 1156 (M.D. Ala. 1999) (servicer failed for over seven months to correct account error despite borrowers' twice sending copies of canceled checks evidencing payments); Choi v. Chase Manhattan Mortg. Co., 63 F. Supp. 2d 874 (N.D. Ill. 1999) (home lost to tax foreclosure after servicer failed to make tax payment from borrowers escrow account and then failed to take corrective action to redeem the property); Norwest Mortgage, Inc. v. Super. Ct., 85 Cal. Rptr. 2d 18 (Ct. App. 1999) (kickbacks available in force-placed insurance encourage placement); Monahan v. GMAC Mortgage Co., 893 A.2d 298 (Vt. 2005) (affirming $43,380 jury award based on servicer's failure to renew flood insurance policy and subsequent uninsured property damage).
[24] Tomasz Piskorski, Amit Seru, and Vikrant Vig, Securitization and Distressed Loan Renegotiation: Evidence From the Subprime Mortgage Crisis, Dec. 2008.
[25] Mullane v. Cent. Hanover Bank & Trust Co., 339 U.S. 306 (1950).
[26] Maxwell v. Fairbanks Capital Corp., 281 B.R. 101 (Bankr. D. Mass. 2002).
[27] New Mexico will soon become the thirtieth state in which non-judicial power of sale will be the most common form of residential home foreclosures. In 2006, New Mexico removed a statutory ban on power of sale clauses in residential deeds of trust. Since then, power of sale clauses have become standard in residential deeds of trust and will soon outnumber those without such clauses.
[28] In some states, a completed sale of the home to a good faith purchaser will cut off the homeowner's ability to challenge the sale even if there has been some irregularity in how the sale was conducted.
[29] Okla. Stat. tit. 46, § 43.
[30] *Id.*
[31] Okla. Stat. tit. 46, § 45.
[32] S.D. Codified Laws § 21-48-9.
[33] N.C. Gen. Stat. § 45-21.16.
[34] N.C. Gen. Stat. § 45-21.16(d). Recent legislation enacted in North Carolina, which will expire on October 31, 2010, requires that a mortgage holder foreclosing a "subprime" loan as defined in the law must include in the initial foreclosure notice either a statement of compliance with the subprime pre-foreclosure notification requirement or a statement that the loan is not "subprime." If the court clerk determines that the certification is "materially inaccurate" it may be grounds for dismissal of the foreclosure action without prejudice and for payment of borrower costs defending the action.
[35] Turner v. Blackburn, 389 F. Supp. 1250 (W.D.N.C. 1975). Many power of sale statutes are probably constitutional under federal law due to the lack of state action. Flagg Brothers, Inc. v. Brooks, 436 U.S. 149 (1978).
[36] *See* 11 U.S.C. § 362.
[37] *See* 11 U.S.C. § 362(c)(3).
[38] The FHA is one of the federal agencies that ensures mortgage lenders against loss when a loan is made in accordance with FHA regulations.
[39] On September 7, 2008, the Federal Housing Finance Agency (FHFA) announced that the two GSEs, Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation) had been placed into a conservatorship run by the FHFA.
[40] *See* American Securitization Forum, Streamlined Foreclosure and Loss Avoidance Framework for Securitized Mortgage Loans (Dec. 6, 2007) (revised July 8, 2008).
[41] *See, e.g.,* Sheila C. Bair, Chairwoman, Federal Deposit Insurance Corp. (FDIC), Remarks to the American Securitization Form (ASF) Annual Meeting (June 6, 2007) ("The immediate task is to sustain homeownership by ensuring the servicers have the flexibility they need to make prudent loan modifications.").

[42] *Id.* (stating that loan modifications that provide sustainable mortgages for borrowers are generally the best option for investors and borrowers).
[43] Some mortgage programs, such as the FDIC program instituted for mortgages owned and serviced by IndyMac Savings Bank, have requirements that the new loan be sustainable, by requiring that the payments be no greater than—for example—38% of the homeowner's gross income.
[44] Extending a mortgage term to forty years is only a benefit when the interest rate on the mortgage is very low (for example, 4% or less); otherwise, the benefits derived from extending the payback period over a longer term are outweighed by the extraordinarily large excess interest that is due.
[45] Statement on Loss Mitigation Strategies for Servicers of Residential Mortgages (Sept. 2007), *available at* http://www.occ.treas.gov/ftp/bulletin/2007-38a.pdf.
[46] Associated Press, Paulson to Mortgage Industry: Help Curb Defaults (Oct. 31, 2007), *available at* http://money.cnn.com/2007/10/31/real_estate/paulson_housing.ap/.
[47] Press Release, Statement of Treasury Secretary Henry M. Paulson, Jr. at Press Conference to Announce Framework to Help Preserve Communities by Preventing Foreclosure (Dec. 6, 2007), *available at* http://www.treas.gov/press/releases/hp716.htm.
[48] *See* HOPE NOW: Results in Helping Homeowners (Feb. 2008) (data covers eighteen servicers representing two-thirds of the industry), *available at* http://www.fsround.org/hope_now/pdfs/JanuaryDataFS.pdf; *see also* HOPE NOW, Alliance Servicers, Prime and Subprime Residential Mortgages: 2007 Loss Mitigation Activities (Feb. 2008), *available at* http://www.fsround.org/media/pdfs/NationaldataFeb.pdf.
[49] Of the 384,000 foreclosures, the MBA reports that 235,000 of the foreclosure filings fell in one of three categories: property was investor-owned, the subject of a previous broken payment plan, or the homeowner could not be reached by the servicer. Jay Brinkmann, Mortgage Bankers Association, An Examination of Mortgage Foreclosures, Modifications, Repayment Plans and other Loss Mitigation Activities in the Third Quarter of 2007 (Jan. 2008), *available at* http://www.mortgagebankers.org/files/News/InternalResource/59454_LoanModificationsSurvey.pdf.
[50] *See* Alan M. White, Rewriting Contracts, Wholesale: Data on Voluntary Mortgage Modifications from 2007 and 2008 Remittance Reports (Aug. 27, 2008). Fordham Urban Law Journal, Forthcoming.
[51] Rod Dubitsky, et al. , Credit Suisse Fixed Income Research, Subprime Loan Modifications Update at 1-2 (Oct. 1, 2008).
[52] *Id.*.
[53] *Id.* (while 80% of principal modifications were delinquent prior to modification, only 23% were delinquent eight months after modification).
[54] *See, e.g.,* Miller v. Mccalla, Raymer, Padrick, Cobb, Nichols, & Clark, L.L.C., 214 F.3d 872, 875 (7th Cir. 2000) (describing the process of trying to get through to an 800 number as a "vexing and protracted undertaking"); Gretchen Morgensen, *Can These Mortgages Be Saved?,* New York Times, Sept. 30, 2007 (describing one homeowner who identified 670 calls relating to her home foreclosure in the previous three months and who received nine different answers about how best to proceed from fourteen different people at the company).
[55] Neighborhood Housing Services of Chicago, Inc., Lessons from the Front Lines: Counselor Perspectives on Default Intervention, at 6 (Oct. 29, 2007).
[56] *See* Kate Berry, *The Trouble with Loan Repayment Agreements*, Am. Banker (Jan. 9, 2008) (noting that servicers push repayment plans instead of modifications because they "need twice the staff, and in part they can't manage the volume").
[57] California Reinvestment Corp., The Growing Chasm Between Words and Deeds (Dec. 2007).
[58] Information about these bills can be found on NCLC's website, www.nclc.org.
[59] Cal. Civ. Code § 2923.5 (West).
[60] *See* Appendix C, *infra*.
[61] This is exactly what the Maryland Supreme Court held was the effect in that state when a mortgage servicer failed to provide loss mitigation as required by the FHA guidelines. *See* Wells Fargo Home Mortgage Inc. v. Neal, 398 Md. 705, 922 A.2d 538 (Md. 2007).
[62] 12 U.S.C. § 2605(e).
[63] Texas Department of Housing & Community Affairs, Division of Policy & Public Affairs, An Examination of Residential Foreclosures in Texas, at 32 (Sept. 29, 2006).
[64] Freddie Mac, Foreclosure Avoidance Research, 2005, *available at* http://www.freddiemac.com/service/msp/pdf/foreclosure_avoidance_dec2005.pdf; Freddie Mac, Foreclosure Avoidance Research II, 2007, *available at* http://www.freddiemac.com/service/msp/pdf/foreclosure_avoidance_dec2007.pdf.
[65] Fla. Stat. § 494.00794 (forty-five-day notice of right to cure); 815 Ill. Comp. Stat. § 137/105 (thirty-day notice of right to cure); N.M. Stat. § 58-21A-6 (thirty-day notice prior to acceleration or commencement of any type of foreclosure proceeding).
[66] *See, e.g.,* Bisno v. Sax, 175 Cal. App. 2d 714, 346 P.2d 814 (1959);Reynolds v. Ramos, 188 Conn. 316, 449 A.2d 182 (1982); Savarese v. Schoner, 464 So.2d 695 (Fla. Dist. Ct. App. 1985); Fed. Home Loan Mortgage Corp. v. Taylor, 318 So.2d 203 (Fla. Dist. Ct. App. 1975); Crane v. Bielski, 15 N.J. 342, 104 A.2d 651 (1954); Associated East Mortgage Co. v. Young, 163 N.J. Super. 315, 384 A.2d 899 (N.J. Super. Ct., Ch. Div. 1978); Graf. v. Hope Bldg Corp., 254 N.Y.1, 171 N.E. 884 (N.Y. 1930) (Cardozo, C.J., *dissenting*); Germania Life Ins. Co. v. Potter, 109 N.Y.S. 435 (App. Div. 1908); Casper v. Anderson Apartments, 196 Misc. 555, 94 N.Y.S. 2d 521 (Sup. Ct. 1949); Murphy v. Fox, 278 P.2d 820 (Okla. 1955); United States v. Loosley, 551 P.2d 506 (Utah 1976).
[67] 24 C.F.R. § 203.608.
[68] Federal National Mortgage Ass'n/Federal Home Loan Mortgage Corp. (FNMA-FHLMC), Clause 22, Mortgage Documents Security Instruments, *available at* www.efanniemae.com/singlefamily/forms_guidelines/mortgage-documents/sec- instr.jhthl?role,ou); Federal National Mortgage Ass'n/Federal Home Loan Mortgage Corp. (FNMA-FHLMC), Clause 18, Uniform Mortgage–Deed of Trust Covenant-Single Family.

[69] *Id.*
[70] 11 U.S.C. § 1322(c)(1).
[71] *See e.g., In re* Foreclosure Cases, 521 F. Supp. 2d 650 (S.D. Ohio 2007); *In re* Parsley, 384 B.R. 138 (Bankr. S.D. Tex. 2008); *In re* Maisel, 378 B.R. 19 (Bankr. D. Mass. 2007); Everhome Mortgage Co. v. Rowland, 2008 WL 747698 (Ohio Ct. App. Mar. 20, 2008); DJL Mortgage Capital, Inc. v. Parsons, 2008 WL 697400 (Ohio Ct. App. Mar. 13, 2008).
[72] Federal Home Loan Mortgage Corp., Foreclosure Avoidance Research II, 2007, *available at*http://www.freddiemac.com/service/msp/pdf/foreclosure_avoidance_dec2007.pdf.
[73] Iowa Code § 628.3, provides: "The debtor may redeem real property at any time within one year from the day of sale, and will, in the meantime, be entitled to possession thereof; and for the first six months thereafter such right of redemption is exclusive. Any real property redeemed by the debtor shall thereafter be free and clear from any liability for any unpaid portion of the judgment under which said real property was sold."
[74] Cal. Civ. Proc. Code § 729.080 (West).
[75] S.D. Codified Laws § 21-49-31.
[76] Conflict of law issues governing which state's laws apply in a situation when the former homeowner has moved to a different state after foreclosure add a further layer of uncertainty and unfairness to the operation of deficiency laws. *See generally* Robert A. Brazener, *Conflict of Laws: Application of statutes Proscribing or Limiting Availability of Action for Deficiency After Sale of Collateral Real Estate,* 44 A.L.R. 3d 922 (1972).
[77] Gelfert v. Nat'l City Bank of N.Y., 313 U.S. 221 (1941); Honeyman v. Jacobs, 306 U.S. 539 (1939); *see also* Lester v. First Am. Bank, Bryan, Tex., 866 S.W. 2d 361 (Tex. App. 1993) (upholding Texas deficiency limitation against state constitutional challenge).
[78] Gelfert v. Nat'l City Bank of N.Y., 313 U.S. 221 (1941).
[79] *See generally* Joseph E. Gotch, Jr., *Creditors' vs. Debtors' Rights Under Alaska's Foreclosure Law: Which Way Does the Balance Swing?*, 14 Alaska L. Rev. 77, 105-106 (1997); Georgina W. Kwan, *Mortgagor Protection Laws: A Proposal for Mortgage Foreclosure Reform in Hawaii*, 24 U. Haw. L. Rev. 245, 265-66 (2001); John Mixon & Ira B. Shepard, *Antideficiency Relief for Foreclosed Homeowners: ULSIA Section 511(b)*, 27 Wake Forest L. Rev. 455, 474-75 (1992).
[80] *See* John Mixon & Ira B. Shepard, *Antideficiency Relief for Foreclosed Homeowners: ULSIA Section 511(b)*, 27 Wake Forest L. Rev. 455 (1992); Grant S. Nelson & Dale A. Whitman, *Reforming Foreclosure: The Uniform Nonjudicial Foreclosure Act*, 53 Duke L.J. 1399 (2002).
[81] *See, e.g.*, Ohio Rev. Code Ann. § 5721.19 (West).
[82] Cal. Civ. Proc. Code § 580(b),(d) (West); Georgina W. Kwan, *Mortgagor Protection Laws: A Proposal for Mortgage Foreclosure Reform in Hawaii*, 24 U. Haw. L. Rev. 245, 259-62 (2001).
[83] Duclersaint v. Fed. Nat'l Mortgage Ass'n, 427 Mass. 809, 696 N.E. 2d 536 (1998).
[84] Brickyard Ass'n v. Auburn Venture P'ship, 626 A.2d 930 (Me. 1993)
[85] Md. Code Ann., Real Prop. §§ 7-301(h), 7-314 (West); Nev Rev. Stat. § 40.463.
[86] Cal. Civ. Code § 2945.1(e)(8) (West) (defining surplus recovery as a regulated "service" subject to restrictions under statute applicable to foreclosure consultants); Colo. Rev. Stat. § 6-1103(4)(a)(IX) (including surplus retrieval consultants in scope of regulated foreclosure consultant activities); Fla. Stat. §§ 45.032, 45.034 (regulating contracts to assign sale surpluses).
[87] NYCTL 1998-1 Trust v. Oneg Shabos, Inc., 800 N.Y.S.2d 808 (Sup. Court. 2005).
[88] N.C. Gen. Stat. § 45-21.26.
[89] N.Y. Real Prop. Law §§ 1354, 1355 (McKinney).
[90] Wyo. Stat. Ann. § 34-4-104(b); Vt. R. Civ. P. 80.1.
[91] Ariz. Rev. Stat. Ann. § 33-812(B).
[92] Cal. Civ. Code § 2924j (West) (report due within thirty days of issuance of trustee's deed); Haw. Rev. Stat. § 667-33; Va. Code Ann. § 26-15; W. Va. Code § 38-1-8; Md. Civ. R. 14-305; Pa. R. Civ. P. 3136; .