

Massachusetts Imposes Additional Restrictions on Residential Mortgage Foreclosures; May Now Require Loan Modification in Lieu of Foreclosure

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On August 3, 2012, **Massachusetts** became the latest state to impose additional restrictions on residential mortgage loan foreclosures when **Governor Deval Patrick** signed into law House Bill 4323, entitled “An Act preventing unlawful and unnecessary foreclosures” (“Act”). In doing so, Governor Patrick declared the Act “an emergency law, necessary for the immediate preservation of the public convenience.” Primarily, the Act (i) modifies the foreclosure process contained in Massachusetts General Laws, Chapter 244 and the ability to execute the statutory power of sale to foreclose contained in Chapter 183, Section 21, and (ii) imposes new affirmative obligations on creditors to attempt to avoid foreclosure arising from certain types of loans that many view as “risky” to consumers. The Act also imposes additional requirements for recording mortgage assignments and identifying ownership of mortgage instruments prior to foreclosure. These changes will generally become effective on November 1, 2012. Violating the Act may trigger violations under Massachusetts General Laws Chapter 93A (the Massachusetts Consumer Protection Statute), which affords consumers the ability to recover double or treble damages and attorneys’ fees, as well as seek class-wide relief for systemic violations of the law. Accordingly, creditors and their servicers will be well served to conform their practices to this new regime.

1. Mortgage Assignments Now Must Be Recorded Prior To Mailing Notice Of Foreclosure; Foreclosure Notice Now Must Reference Recording Information For All Recorded Assignments

With one exception, and notwithstanding certain stylistic changes, the Act leaves as is the current language contained in Chapter 244, Section 14, which describes the general foreclosure process in Massachusetts. The exception, however, is significant. Specifically, if a mortgagee holds a mortgage pursuant to an assignment, before mailing the required foreclosure notice under Section 14, (1) an assignment (or chain of assignments) evidencing the assignment of the mortgage to the foreclosing mortgagee must have been duly recorded at the appropriate registry of deeds, and (2) the recording information for all recorded assignments must be referenced in the notice of sale required by Section 14. Moreover, if a mortgage holder within a chain of assignments either changed its name or merged into another entity when it held the mortgage, the foreclosure notice must recite “the fact of any merger, consolidation, amendment, conversion, or acquisition of assets causing” a change to a

mortgage holder's name when it held the mortgage.

This requirement is a significant shift from the prior law in Massachusetts, which only required a foreclosing mortgagee to show that it held an appropriate interest in the mortgage and underlying debt obligation prior to the notice and sale. If those two interests had been split (in a MERS mortgage, for example), then the foreclosing mortgagee needed a proper assignment of the mortgage prior to the notice and sale. The mortgagee, however, did not have to record that assignment to exercise the power of sale under Chapter 183, Section 21. Indeed, in 2011, the Massachusetts Supreme Judicial Court expressly declined to require that a mortgage assignment be recorded prior to the notice and sale.¹

2. New Mandatory Pre-Foreclosure Loan Modification Analysis And Duties

Additional significant changes to the foreclosure process appear in two completely new sections created by the Act (Chapter 244, Sections 35B and 35C). These new sections are detailed and impose new compliance requirements.

A) Mandatory Weighing Of Loan Modification Versus Net Recovery Following Foreclosure For “Certain Mortgage Loans”

Section 35B requires creditors to consider loan modification over foreclosure when the mortgage loan at issue is a “certain mortgage loan.”

i) What Loans are Covered by the Act?

A “certain mortgage loan” is a loan (1) made to a natural person, (2) primarily for personal, family, or household purposes, (3) secured wholly or partially by a mortgage on an “owner-occupied residential property,”² that (4) has one or more of the following features:

- An introductory interest rate of 3 years or less and which interest rate is at least 2% lower than the fully indexed rate (e.g., “teaser” rates);
- Interest-only payments for **any** time period (with the exception of open-ended home equity credit lines or construction loans) (e.g., 3/1 interest-only ARMs);
- A payment option feature, where any one option is to pay less than the principal and interest fully amortized over the life of the loan (e.g., “payment option” loans);
- No requirement to document income or assets (e.g., “no-doc” loans, which also are governed by 940 C.M.R. § 8.06(15));
- Prepayment penalties exceeding the limits in Chapter 183, Section 56 or applicable federal law;
- Underwritten with a loan-to-value ratio at or above 90% and borrower having had a debt-to-income ratio higher than 38%;
- Underwritten as a component of a loan transaction in which the loan-to-value ratio exceeded 95%; or
- The creditor is unable to determine whether the loan has one or more of these characteristics after performance of reasonable due diligence.³

ii) What Else Must A Creditor Do When A Subject Loan Is In Default?

Before publishing a notice of foreclosure sale upon default in performance under a “certain mortgage

loan,” a creditor⁴ must first take “reasonable steps” and make a “good faith effort to avoid foreclosure.” This means that a creditor must consider (1) an assessment of the borrower’s ability to make an “affordable monthly payment,”⁵ 2) the net present value of receiving payments under a “modified mortgage loan”⁶ as compared to the anticipated net recovery following a foreclosure, and (3) the interests of the creditor, including (but not limited to) the interests of investors.

The Act establishes specific requirements for servicers of pooled residential mortgages:

Except as otherwise specified in a contract, a servicer of pooled residential mortgages may determine whether the net present value of the payments on the modified mortgage loan is likely to be greater than the anticipated net recovery that would result from foreclosure to all investors and holders of beneficial interests in such investment, but not to any individual or groups of investors or beneficial interest holders.

A servicer acts in the best interest of all such investors if the servicer agrees to or implements a modified mortgage loan or takes reasonable loss mitigation efforts to comply with Section 35B. The Act further provides that a modified mortgage loan must comply with current federal and state law pertaining to mortgage loans **and** the borrower shall be able “to reasonably afford to repay the modified mortgage loan according to its scheduled payments.”

iii) What Constitutes Good Faith Under The Act?

The Act provides further that a creditor “shall be presumed to have acted in good faith” and to have complied with Section 35B if, before publishing the notice of a foreclosure sale, the creditor:

- 1) Determines a borrower’s current ability to “make an affordable monthly payment”;
- 2) Identifies a modified mortgage loan that achieves the borrower’s affordable monthly payment, which may include one or more of the following: (a) reduction in principal, (b) reduction in interest rate, or (c) increase in the amortization period (so long as the amortization period is not increased by more than 15 years and the total amortization period does not exceed 45 years);
- 3) conducts an analysis comparing the net present value of the modified mortgage loan with the creditor’s anticipated net recovery following foreclosure (which analysis shall be deemed compliant if in accordance with the formula presented in at least one of various enumerated state and federal loan modification programs); *and*
- 4) *either* (a) “in all circumstances” where the net present value of the modified loan exceeds the creditor’s anticipated net recovery at foreclosure, the creditor agrees to modify the loan in a manner that provides for the “affordable monthly payment,” or (b) “in circumstances where the net present value of the modified loan is less than the creditor’s anticipated net recovery at foreclosure (or does not meet the borrower’s affordable monthly payment), the creditor notifies the borrower that no modified loan will be offered and provides a written summary of the creditor’s net present value and analysis and the borrower’s current ability to make monthly payments.”

B. Mandatory Notice Of Right To Pursue Loan Modification; Time Frames For Process

Also, concurrently with the notice already required by Chapter 244, Section 35A(g) (concerning a borrower’s right to cure), a creditor must send notice of a borrower’s rights to pursue a modified mortgage loan under Section 35B and file a copy of that notice with the Massachusetts Attorney

General. The notice must also include the appropriate contact information for modification assistance within the Attorney General's Office and shall be similar in substance and form to the notice promulgated by the Massachusetts Division of Banks under Section 35A. The process of determining whether to offer a modified mortgage loan "shall take no longer than 150 days." The borrower must respond to the notice within 30 days of receipt and inform the creditor of the borrower's intent (1) to pursue a modification and a statement of the borrower's income and "complete list of total debts and obligations, as requested by the creditor," (2) to pursue an alternative to foreclosure, including a short sale or deed-in-lieu of foreclosure, (3) not to pursue a modified mortgage loan and pursue the right to cure period described in Section 35A, or (4) to waive the right to cure period and proceed to foreclosure. If a borrower fails to respond within 30 days, the borrower shall be considered to have forfeited the 150-day right to cure period and shall be subject to a right to cure period of 90 days.

If a creditor receives notice from a borrower that the borrower intends to pursue a modified mortgage loan, a creditor must then provide (within 30 days following receipt) the borrower with its assessment (in writing) under Section 35B(b), which shall include, without limitation, (1) a statement of the borrower's income, debts, and obligations as determined by the creditor, (2) the creditor's net present value analysis of the mortgage loan, (3) the creditor's anticipated net recovery at foreclosure, (4) a statement of the interests of the creditor, and (5) a modified mortgage loan offer or notice that no modified mortgage loan will be offered. If a modification is offered, the creditor must assign the borrower no more than two representatives to negotiate and approve the modified loan, and it must provide the borrower with those representatives' first and last names and telephone numbers.

If a borrower responds to an offer for a modified mortgage loan within 30 days of receipt, the borrower may (1) accept the offer, (2) make a reasonable counteroffer, or (3) state that the borrower wishes to waive the borrower's rights as provided by Section 35B and proceed to foreclosure. The borrower's response must be in writing and any counteroffer shall include substantiating and supporting documentation. If a counteroffer is proposed, the creditor shall accept, reject, or propose a counteroffer to the borrower within 30 days of receipt. The right to a modified mortgage loan shall be granted once during any 3-year period.

C. Mandatory Recordation Of Section 35B Affidavit Of Compliance Prior To Notice Of Foreclosure Sale

In addition, before publishing a notice of foreclosure sale, the creditor (or duly authorized agent if the creditor is not a natural person) *must record an affidavit with the appropriate registry of deeds* certifying compliance with the requirements of Section 35B based on a review of the creditor's business records. This affidavit shall be conclusive evidence (in favor of an arm's-length third-party purchaser for value) that the creditor has complied fully with Section 35B and that the mortgagee is entitled to foreclose under the power of sale conveyed in the mortgage and any one or more foreclosure procedures authorized by Chapter 244.

D. Mandatory Bi-Annual Reporting To Massachusetts Divisions Of Banks; Regulations

The Act also requires creditors, on a bi-annual basis, to report to the Massachusetts Division of Banks the "final outcome" of all loans for which the creditor sent the required notice of right to pursue a modification to a borrower. The Division of Banks is charged with adopting, amending, or repealing regulations to aid in the administration and enforcement of Section 35B, including minimum requirements that constitute a good faith effort by the borrower to respond to the notice required under Section 35B(c), as well as requirements for reasonable steps and good faith efforts of the

creditor to avoid foreclosure and additional safe harbors for compliance. The Division shall also make any available net present value models accessible to all creditors.

3. Certifying That The Mortgagee Is The Note Holder Or Authorized Agent; Unlawful Acts Under Section 35C

Section 35C, which (unlike 35B) does not exclude in its definition of “creditor” the Massachusetts Housing Finance Agency and the Massachusetts Housing Partnership Fund, provides that a creditor shall not publish a notice of foreclosure required by Section 14 when the creditor knows “or should know” that the mortgagee is neither the holder of the mortgage note nor the authorized agent of the note holder. Prior to publishing notice, the creditor (or duly authorized agent if the creditor is not a natural person) must certify compliance with this subsection in an affidavit based upon review of the creditor’s business records and *record that affidavit with the applicable registry of deeds*. The affidavit shall be conclusive evidence (in favor of an arm’s-length third-party purchaser for value) that the creditor has complied fully with Section 35C and the mortgagee is entitled to foreclose under the power of sale conveyed in the mortgage and any one or more foreclosure procedures authorized by Chapter 244. The Act’s definition of “residential property” in Section 35C differs than the definition in 35B in that the Section 35C definition does not exclude residential property subject to condemnation or receivership.

A creditor violates Chapter 244 if the creditor:

- 1) Imposes upon a third party the cost of correcting, curing, or confirming documentation relating to the sale, transfer, or assignment of a mortgage loan;
- 2) Makes statements to a state or federal court related to foreclosure or compliance with Chapter 244 (orally or in writing) that it knows “or should know” are false, including statements about the offering of a loan modification, the borrower’s history of payments, the validity of assignment of the mortgage loan, whether the creditor is the record holder of the mortgage, or the creditor’s compliance with any other requirements of Chapter 244; or
- 3) Imposes a fee upon a borrower for goods not rendered or services not performed in connection with a foreclosure.

Section 35C also provides that no person shall give or accept any portion, split, or percentage of any charge made or received for the rendering of a service in connection with a transaction involving a foreclosure upon a mortgage loan other than for services actually rendered. Finally, as to offers to purchase a mortgage loan or residential property by a charitable 501(c)(3) entity or an entity controlled by a 501(c)(3) entity, no creditor shall require as a condition of sale or transfer to any such entity any affidavit, statement, agreement, or addendum limiting ownership or occupancy of the residential property by the borrower.

4. Delay to Reverse Mortgage Loan In-Person Counseling

The Act also extends, until August 1, 2014, the effective date of in-person counseling requirements for reverse mortgage loans under Massachusetts General Laws Chapter 167E, Section 7A(b), and Chapter 171, Section 65C1/2.

5. Foreclosure Prevention Task Force and Loan Modification Tracking

Beyond these statutory changes, the Act creates a task force to study ways to prevent “unnecessary vacancies following foreclosures.” For example, the Act suggests that the task force consider whether a foreclosed homeowner should be allowed to remain in the home until a third-party purchases the property. The task force is also charged with evaluating options for mediating issues that arise between borrowers and creditors and the possibility of creating a state mediation program. The task force’s findings and recommendations are due by December 31, 2013.

Finally, the Act requires the Massachusetts Division of Banks to track annually the “final outcome of the loan modification process on all certain mortgage loans” and to provide a report within 90 days of each calendar year end from 2012 to 2017.

Conclusion

These changes to the foreclosure environment in Massachusetts are far-reaching and will likely affect significant numbers of mortgages (and their respective borrowers, creditors, and servicers) when they take effect in November. Creditors and servicers should start preparing now for the new responsibilities (and potential sources of liability) they will face at that time.

¹ U.S. Bank Nat’l Ass’n v. Ibanez, 458 Mass. 637, 651, 941 N.E.2d 40, 53 (2011).

² The Act defines “residential property” as real property “on which there is a dwelling house with accommodations for 4 or few separate households and occupied, or to be occupied, in whole or in part by the” mortgagor so long as the property is the principal residence of the mortgagor. “Residential

property” shall not include (i) investment property or a residence other than a primary residence, (ii) residential property taken in whole or in part as

collateral for a commercial loan, or (iii) property subject to condemnation or receivership. Therefore, commercial loans and residential loans for

investment purposes are outside of the Act.

³ The Act excludes from the definition of “certain mortgage loans” any loans financed by the Massachusetts Housing Finance Agency or originated by programs administered by the Massachusetts Housing Partnership Fund board (both of which are also excluded from the definition of “creditor” for the

purposes of the new Section 35B).

⁴ The Act defines “creditor” as a “person or entity that holds, partially, wholly, indirectly, directly or in a nominee capacity, a mortgage loan securing and owner-occupied residential property, including, but not limited to, an originator, holder, investor, assignee, successor, trust, trustee, nominee holder,

[MERS] or mortgage servicer, including the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation[.]”

⁵ The Act defines “affordable monthly payment” as “monthly payments on a mortgage loan, which, taking into account the borrower’s current circumstances, including verifiable income, debts, assets and obligations[,] enable a borrower to make the payments.”

⁶ The Act defines “modified mortgage loan” as a “mortgage loan modified from its original terms including, but not limited to, a loan modified under 1 of the following: (i) the Home Affordable Modification Program; (ii) the Federal Deposit Insurance Corporation’s Loan Modification Program; (iii) any

modification program that a lender uses which is based on accepted principles and the safety and soundness of the institution and authorized by the

National Credit Union Administration, the division of banks or any other instrumentality of the commonwealth; (iv) the Federal Housing Administration; or (v) a similar federal loan modification plan."

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