HOME FORECLOSURE PROCEDURES ACT-(2014)
<u>HISTORY & CURRENT POLICY ISSUES</u>

> "It is well known in cognitive science that if you are a pessimist, you sound 'smarter'. That's why people are more likely to listen to and repeat pessimistic assessments. But pessimism…is mainly a failure of imagination. We can see all the problems but can't imagine the new possibilities." – **Phil Libin**

I. INTRODUCTION.

In 2013, in connection with the 'First Reading' of this Act, the Committee Chair prepared a memorandum entitled "Brief History and Policy Issues." This year, I've updated that memorandum to describe what has been accomplished – or not -in the three meetings of the Drafting Committee in the intervening year, how the 2013 issues look in 2014, and what new approaches we have developed in certain issues.

II. A BRIEF RESTATEMENT OF HISTORY.

In July, 2011 the President of the Conference appointed an expedited study committee to examine whether the Uniform Law Commission (the 'ULC') should create a drafting committee on mortgage foreclosure practices and procedures – a subject he characterized as a 'very important and timely issue.'

After completing its work, the Study Committee recommended that drafting go forward, and stated:

> <u>the overall thrust of any act should incorporate meaningful and substantial provisions addressing the concerns of borrowers in the current housing market crisis, and that the act should not be limited to expediting the foreclosure process, however warranted that may be in those circumstances where there is no practical remedy for the borrower.</u>

In last year's memorandum I listed the substantive issues that the Study Committee recommended for attention; the memorandum also stressed the importance of 'enactability' as a standard for our drafting. To refresh the Floor's recollection, I repeat this language from that memorandum:

A. Enactability. The issue of 'enactability' is posed by the following requirement, as stated in the ULC's "*2010 Statement of Policy Establishing Criteria and Procedures for Designation and Consideration of Acts*":

> (c) Every act drafted by the ULC must conform to the following requirements:
>
> ***
>
> (2) There must be a reasonable probability that an act, when approved, either will be accepted and enacted into law by a substantial number of states or, if not, will promote uniformity indirectly.

The issue of enactability continues to confront the Drafting Committee. This remains especially important, given (1) the states' collective unwillingness to date to enact any of ULC's previous acts in the foreclosure area; and (2) the broad array of legislation enacted in recent years in most states that supports debtor rather than lender interests.

B. Committee Membership; Observer Participation. Since its original appointment, the Drafting Committee's membership has been expanded by the felicitous additions of Commissioners Hawkins of Connecticut, Hortman of Minnesota and Kent of Hawaii.

The expanded Drafting Committee met three times in the past year with a broad range of individuals and groups representing lenders, borrowers and regulators.

The Drafting Committee continued to benefit from the insights of the same individual lawyer – Tom Cox - representing debtors and two law professors- Judith Fox and Kathleen Engel -who have engaged with us since the outset. However, as in the past, the major organizations that purport to represent the debtor community, including the Center for American Progress, the National Association of Attorneys General, The Center for Responsible Lending and the National Consumer Law Center have continued to ignore our efforts, refusing to participate in our meetings or offer comments on our drafts.

At the same time, we have been able to engage, to a limited degree, with certain stakeholders who had previously been absent from our deliberations, including representatives of the Consumer Financial Protection Bureau and the Mortgage Bankers Association.

Further, during the last two weeks of June, an informal and diverse network of activist homeowners and foreclosure defense lawyers has contacted Drafting Committee members; some have asked to participate in future Drafting Committee meetings, where they will be welcomed, while others propose demonstrations and protests at the Seattle meeting.

We continued to enjoy the active engagement of various representatives of the lending community and various related governmental and private sector stakeholders. Our most active lender stakeholders have been representatives of the Federal Housing Finance Agency ("FHFA") Fannie Mae and Freddie Mac (the two largest Government-Sponsored Enterprises or GSE's) and the American Bankers Association; the Chair of the Drafting Committee and our American Bar Association Advisor met with a group of ABA lobbyists and state bankers in October in Chicago, and participated in a conference call with national bank lawyers to discuss various provisions of the Act. Finally, we have been very well served indeed by the active participation of several able lawyers on behalf of various money center lenders and the secondary market.

III. POLICY ISSUES.

A. Scope. <u>Which properties and which foreclosure actions are covered?</u>

1. **One to Four Unit Residential Properties.** Section 103 provides that the act "applies to the foreclosure of a mortgage only on residential property in this state."

   In the 2014 annual meeting draft, "Residential property" is defined in Section 102 (23) as "real property improved with not more than four dwelling units" without regard to owner-occupancy or the amount of the mortgage loan. The hoped for result will be that a servicer or attorney can readily determine the applicability of the uniform Act based solely on the nature of the mortgaged property.

   Initially, the Drafting Committee had also concluded that foreclosure of commercial mortgages did not appear to create a problem under current practice, and therefore the act would not apply to a foreclosure of commercial property.

During the last year, on the recommendation of a lender to farms and other agricultural properties, the following language was added at the end of the definition:

> "The term does not include real property that was used or was intended to be used primarily for non-residential purposes such as farming, commercial, or industrial use when a mortgage was created."

2. **No 'owner-occupancy' Requirements.** In the past year, the Drafting Committee again discussed whether the act should apply only to owner-occupied units (as opposed to investor-owned units) or to larger –or smaller – properties but ultimately re-affirmed its decision that a 'bright-line' applicability standard was the preferable outcome.

3. **Applicability to all Mortgages but only to Post-Enactment Foreclosures.** Section 103 provides that "This [act] applies to foreclosure of a mortgage on residential property situated in this state." The Act's applicability is further clarified in Section 701, which now provides:

> (a) Except as otherwise provided in this Section, this [act] applies to the foreclosure of a mortgage within its scope, even if the mortgage was created before this [act] takes effect.
>
> (b) This [act] does not affect a foreclosure commenced before this [act] takes effect.

Taken together, the Act now makes clear that it applies only to the foreclosure of mortgages on 'residential property' in the enacting state, regardless of whether the mortgage was created before or after the effective date of this Act, but the Act would not apply if the foreclosure action was commenced before the Act takes effect.

4. **Applicability of Remedies to Post-Enactment Mortgages.** Finally, as discussed in more detail below, the Drafting Committee in the past year decided that certain potential remedies available to borrowers – including any potential amendments to the Holder In Due Course Doctrine - should apply only to mortgages signed after the effective date of the act in the state where the mortgaged property is located.

Further, as to Scope, the Committee has confirmed that, as a matter of policy, the Act would continue as an overlay to existing state foreclosure laws, and will not generally displace those existing laws. As a consequence, except as expressly repealed or changed. States may continue judicial foreclosure, non-judicial foreclosure, or a combination of both.

B. Study Committee Issues Not Addressed. Without detailing the rationale as presented in the 2013 memorandum, the Drafting Committee determined <u>not to address</u> in this Act a number of issues posed by the Study Committee. These include:

1. **Post - Redemption rights.** Law in the various States differs widely on whether the borrower should be entitled to a right of post-foreclosure redemption – that is, the right to regain title to property when title has already passed in foreclosure.

2. **Deficiency judgments.** A deficiency judgment is the recovery of a personal judgment against the borrower for a dollar sum equal to the difference between the total amount of the debt and the value of the borrower's home at foreclosure, either based on an auction sales price, a private sale or, far more commonly, the appraised value of the home as calculated by the lender's appraiser. This draft of the act bars recovery of deficiency judgments in the case of a negotiated transfer under Sections 501 through 504, but otherwise relies on existing state law regarding this subject.

3. **Use of private actors in foreclosure processes** The Drafting Committee has chosen not to risk engaging the lobbying interests of organized process servers and others in ways that might adversely affect the enactability of this Act.

4. **Post-sale confirmation, presumption of sale validity.** State statutes vary regarding post-sale confirmation- that is, requiring a court to confirm the lawfulness of a foreclosure sale. While earlier drafts had included sections addressing this subject, the Drafting Committee voted to delete all those provisions at our April 2013 meeting on the grounds that lenders and title insurers did not perceive a need for such a process.

   After considerable debate over the last year, the Drafting Committee opted to include an optional section addressing this topic in Section 407. The bracketed language as it appears in the annual meeting draft is followed by an extensive Legislative Note on the subject.

5. **Mandating judicial supervision over foreclosures of all residential mortgages, and over the accounting of foreclosure sale proceeds and a prompt release of any surplus to the borrowers.** After the Drafting Committee determined to draft an 'overlay' act rather than a completely new procedure for every state, it became clear that this proposal would be inconsistent with non-judicial procedures in all states that have them.

6. **Empower state foreclosure judges to temporarily restructure mortgage notes on principal residences.** Whatever the merits and practical utility of this concept might be, it became clear at our first meeting with stakeholders that such a concept would be vigorously opposed by the lending community and it was therefore abandoned.

C. POLICY ISSUES IN THE CURRENT DRAFT.

ARTICLE 1: GENERAL PROVISIONS

In 2013, the significant issues in Article 1 included:

- **Definitions** in Section 102,
- **Scope of the Act** in Section 103 [and discussed earlier], and
- **Substantive provisions** –
  - **Imposing the Duty of Good Faith** (Section 104) and
  - **Barring creditors** from engaging in acts that either **discourage** a reasonable borrower from participating in a

loss mitigation process **or misrepresent** any aspect of the foreclosure process to the borrower (Section 105).

During the past year, the Drafting Committee added these additional sections to Article 1:

Section 106. **Application Of Local Regulations**
Section 107. **Servicers**
Section 108. **No Waiver**.
Section 109. **Notices And Knowledge**.
Section 110. **Supplemental Principles Of Law**.

Section 102. Definitions. The 2013 issues memo noted that

> …most of the defined terms will be familiar to real estate practitioners. Care was taken to conform customary definitions to customary usage in our existing Uniform acts including the UCC, other statutes, and federal regulations.' Two definitions, however, will be unfamiliar. First is the term 'Facilitation'….and the second is 'Mortgage Registry' (Section 102(14).

Facilitation/Early Resolution - At the 2013 annual meeting, 'Facilitation' was the term used to describe the mediation or negotiation process mandated by the Act in Article 3.

In the past year, the Drafting Committee has discussed – ad nauseam in the Chair's view- the appropriate word or phrase to replace 'Facilitation' in the Act. Among the terms discussed by the Drafting Committee have been the following (and many others):

Facilitation
Mediation
Dispute Resolution
Early Resolution
Foreclosure Diversion
Foreclosure Avoidance

Currently, based on a shaky consensus achieved directly after a hearty Saturday lunch at the last drafting meeting, the Act substitutes the phrase 'Early Resolution' for the word 'Facilitation'. There is, however, a polite but heated rear guard action attacking that phrase as entirely inappropriate; some have observed its kinship to the unfortunate phrase 'Early Exit'.

In any case, the Chair is offering significant monetary compensation to that singular Commissioner, Observer or Stray Person on the Street who proffers the elusive word or phrase capable of securing a bare majority of votes at the next meeting of the Drafting Committee in November. Please forward your suggestions – and routing information for your bank account – to the Chair's home email address- billb7441@msn.com.

'Mortgage Registry' refers to the possibility discussed in Article 4 that a number of Federal agencies including the Federal Reserve Banking system, FHFA, and the US Treasury may create a new federally mandated system for the electronic recording of promissory notes, mortgages, and other related mortgage documents. The Drafting Committee has accommodated the possible creation of such a system in this Act; *see, e.g.*, Section 401(b)(2), which describes who is entitled to foreclose on a mortgage:

> (2) If the obligation is registered in a mortgage registry, the only person who may commence a foreclosure is the person designated as owner or holder of the obligation by the mortgage registry as of the time the foreclosure is commenced.

As a matter of interest to the Commissioners, the New York Federal Reserve Bank has moved forward in an effort to implement the registry. In March, 2014, it hosted a large reception, dinner and all-day meeting at its offices in New York City to which several persons associated with the Uniform Law Commission were invited; at that meeting, representatives of the Fed described what was it called a 'strawman' registry system, and sought input from a wide range of interest groups.

Then, in May 2014, The Senate Banking Committee reported out SB 1217, known as the Johnson/Crapo Bill. A bipartisan bill embraced by six Democrats and six Republicans – (but not supported by some liberal Democrats) Johnson/Crapo deals with a good many things, but would, if enacted, implement the registry.

I understand that recent amendments to SB 1217 would create a study of the proposed registry, and that representatives of the ULC will be part of that study effort. At the same time, for several reasons, it is not likely that SB 2117 will be enacted this year.

Meanwhile, there is a new Director of the Federal Housing Finance Agency ("FHFA"), former Congressman Mel Watt. While Alfred Pollard remains FHFA's general counsel, and while FHFA had previously supported creation of a registry where all notes that the GSEs would buy – some 60% to 70% of the entire mortgage market – Director Watt may have a different view than his predecessor regarding the registry.

Other Definitions While the Drafting Committee, with assistance from the Style Committee, amended a number of the remaining definitions, none of those changes represents a major policy choice.

Section 104. Good Faith Since the 2013 meeting, the Drafting Committee has approved significant amendments to the "Good Faith' provisions in Section 104.

Specifically, subsection (a) now imposes the duty of good faith on all parties – including homeowners - and the term's definition tracks precisely the definition of 'good faith' in UCC 1-201(20): "Good faith" means honesty in fact <u>and the observance of reasonable commercial standards of fair dealing</u> (emphasis added).

The current draft of 104(a) then continues with this bracketed language:

> ["This subsection does not create an independent cause of action for the failure of a person to act in good faith."]

As part of its re-examination of this section, the Drafting Committee then added new subsection (b), as follows:

> (b) A creditor or servicer shall proceed in a commercially reasonable manner in complying with the requirements of this Act.

The language in (b) is taken directly from UCC 9-607(c) and imposes on creditors and servicers, in addition to their duty of 'good faith' – that is, 'honesty in fact' and 'fair dealing', an obligation to proceed in a 'commercially reasonable' manner in complying with all the obligations imposed on them by this act.

Section 105. No Misrepresentations. The activities proscribed in Section 105 reinforce the importance of the 'early resolution' process, and is designed to minimize the likelihood that creditors or servicers would in any way misrepresent the rights granted borrowers in this act. The Drafting Committee made no changes to this section this past year.

New Sections

Section 106.Applicability of Local Regulations. As currently drafted, subsection (a), in the absence of specific state statute, would prevent local governments from regulating the foreclosure process or enacting ordinances at the local level to, for example, require lenders who have not foreclosed on a property to post a bond or pay for the property's clean-up.

The heart of the section lies in this excerpt from sub-section (a):

> ….no ordinance or regulation of a municipality, county or other political subdivision in this state may impose regulations, restrictions or limitations on the foreclosure process or add to or vary the rights and obligations of creditors, servicers, homeowners, or obligors set forth in this [act].

The section has been debated – and the outcome reversed – at every meeting of the Drafting Committee in the last year. In May, 2014, responding to a significant watering down of the section at our January 2014 meeting, the American Bankers Association and six state banking associations wrote an extensive memorandum to the Committee and concluded with the following:

> The Commenting Bankers Associations urge the HFPA Drafting Committee to include a strong and unequivocal preemption provision that precludes political subdivisions from acting with respect to foreclosure. Foreclosure regulation should remain a matter of law passed by the legislatures and federal regulation.

The entire letter appears on the Drafting Committee's website.
The subject is not free from controversy, since many states have strong Home Rule provisions that have arguably authorized the many existing local ordinances in the nation. In St. Louis, for example, Missouri state law on the subject is silent and the City has imposed what is reported to be a rigorous

bonding and repair obligation on creditors who hold mortgages on blighted and abandoned property, whether or not the creditor has commenced foreclosure. And in Massachusetts, there is litigation challenging the right of the city of Springfield to do the same thing. Community advocates argue that in the absence of local regulation, these abandoned and blighted buildings become 'zombie' properties, causing a ripple effect in the community, and that lenders should be obliged to take action with respect to them. The Act, of course, deals separately with the ability of creditors and governments to foreclose abandoned properties expeditiously (see Sections 505 through 510), but local governments – often financially unable to pay the cost of addressing thousands of these properties – seek an alternative means of addressing what is clearly a genuine issue for communities, even in the absence of an express authorization from the State.

The Drafting Committee would especially welcome comments from the Floor on this subject.

Section 107. Servicers. The principal purpose of this new section is to allow the Act to delete the words '…or servicer' that followed every recitation in the act of the obligations of a creditor. Thus, the section enhances the readability of the Act and accomplishes three other purposes:

First, to make clear that a creditor may delegate its duties to a servicer;

Second, to confirm that a servicer who acts for a creditor is subject to the same obligations that the Act imposes on the creditor; and

Third, in carefully considered language that avoids re-writing the law of principal and agent, to make clear that whether the creditor is responsible for the acts of its servicer is determined by other law.

Section 108. No Waiver. This new section makes clear that borrowers may not waive any rights conferred on them by the Act, with the sole exception of a waiver permitted in connection with a 'negotiated transfer' under 501.To the same effect, the Act provides that duties imposed on creditors may not be varied by agreement.

At its last meeting, representatives of the PEB/UCC suggested that the Drafting Committee might consider whether the 'no-waiver ' prohibition might be amended to allow a waiver in a separate writing after default. The Drafting Committee has not considered that subject in any detail.

Section 109. Notices and Knowledge. The Drafters' Note following new Section 109 provides in its entirety: "This Section incorporates without change those parts of Revised UCC § 1-202 that are relevant for this act."

Section 110. Supplemental Principles of Law. Again, this new language is commonly found in other uniform acts. The Drafters' note reads in part:

> 'The text above is taken verbatim from Revised UCC § 1-103(b) with one modification – this Section omits the § 1-103(b) reference to "the law merchant" on the basis that such principles are not likely to apply to our subject matter.

ARTICLE 2: NOTICE, RIGHT TO CURE

The Drafting Committee made few changes to Article 2 in the last year, and none were substantial.

A significant comment, however, was added following Section 201, in order to make clear that this Act has been drafted in contemplation of the foreclosure procedures which are part of the regulations adopted on January 10, 2014 by the federal Consumer Financial Protection Bureau. The lending community had initially resisted much of this Article on the grounds that the Act was layering time delays on top of the delays already mandated by the contemplated CFPB regulations. Comment 3 addresses that concern:

> 3. This Act refers in several sections to the 'foreclosure process'; *see, for example,* Sections 102(7), 104(a), 106 and this section 201. The notice of default under this Section is the beginning of the foreclosure process prescribed by this Act. However, the "first notice or filing" under federal regulations mandating a 120-day waiting period, 24 C.F.R. § 1024.41(f)(1), is the [Complaint or other first court filing in judicial state][Notice of Sale in non-judicial state]. Therefore the notice of default may be sent during the 120-day waiting period under the federal rule.

2013 Explanation The following text appeared verbatim in the 2013 Issues Memo and remains here in order to refresh the readers' collective recollections of what this Article seeks to accomplish:

The notice provisions establish a fairly detailed description of the pre-foreclosure notice for both judicial and non-judicial foreclosure processes. The content of the notice is drawn from two sources: the existing widely used Fannie Mae/Freddie Mac uniform mortgage instrument, and the national mortgage settlement, which is an agreement between certain large mortgage servicers, federal agencies and the state attorneys general.

The aim of the drafters has been to provide clear guidance so that the mortgage servicing industry can move towards a simple, standardized pre-foreclosure notice. However, states may still require some separate notices for programs unique to them.

The Act also specifies how and when a homeowner may cure a default, i.e. undo the acceleration of the mortgage debt and resume normal payments. This topic is governed by statute in some states, and only by contract in others. Uniform rules should also be helpful to mortgage servicers and attorneys working across state lines.

ARTICLE 3: ~~FACILITATION~~ EARLY RESOLUTION

A Commissioner comparing the 2014 version of Article 3 with the 2013 version will find considerable rewriting of the text, including these substantive changes, most of which are intended to encourage greater lender support for the process:

- In Section 303 [compared to former 304], the Drafting Committee reduced from 60 days to 30 days the period of time within which a borrower or homeowner may request a meeting with a third party neutral.

- Section 304 of the 2014 Act permits the creditor to commence the foreclosure action, but prohibits the creditor from proceeding to judgment or filing any dispositive motion until the Resolution process has been completed. The 2013 version of the Act did not allow commencement of the action until after the facilitation process had been completed.

Note – at least one consumer advocate asserts that this is a statutory validation of the much criticized 'dual tracking' procedure, where lenders are simultaneously foreclosing on the borrower and engaged in a process designed to avoid foreclosure.

- Section 302 (a) of the 2014 Act exempts abandoned properties from the Early Resolution process; this was not a part of the 2013 Act.

- In addition, Section 304 (c) provides in part that:

  "To be eligible for early resolution, the mortgaged property must not be abandoned property <u>or rented to a person other than the obligor or homeowner [or an immediate family member of either].</u> If the mortgaged property contains more than one dwelling unit, early resolution is available only if at least one dwelling unit is occupied by the homeowner or obligor [or an immediate family member of either]" (emphasis added).

The policy issue which the Drafting Committee must still resolve is whether the Early Resolution process should be available only to owner occupants, to owner occupants and their families, or also to investor-owned property.

- Further, the lending industry has urged the Drafting Committee to fashion some means of avoiding or severely limiting the process in 'hopeless cases' – that is, conceptually, cases where the borrower has no realistic prospect of retaining ownership of the home. Borrower advocates, including 'third party neutrals' who regularly conduct these proceedings, assert that no case is so hopeless that some form of relief – even if a 'graceful exist' – cannot be achieved in the process, and therefore, no such cases should be excluded. The Drafting Committee to date has not acceded to the lenders' requests.

- Finally, Sections 303(e) and 304(c) contemplate the possibility that the agency may develop a range of fee payment obligations, including fees to fund the agency's actions or mandatory payments of some reduced sum by the borrower to the lender as a condition of participation in the process. Consumer advocates generally oppose the imposition of fees on borrowers as a condition of participation in this process.

- Appendix 3 to Article 3 immediately follows the text of Article 3 and contains very substantial changes to the draft 'Model Rules' and 'Best Practices' which appeared in much more rudimentary form in the Comments to Section 302 of the 2013 Act.

The Drafting Committee would welcome comments from the Floor on any of the matters described above.

2013 Explanation Again, the following text appeared verbatim in the 2013 Issues Memo and remains here in order to refresh the readers' collective recollections of what Article 3 seeks to accomplish:

> "In the wake of the 2007 foreclosure crisis the states have passed dozens of new laws aimed at preventing unnecessary foreclosures. Seventeen states have adopted statewide mandatory mediation programs either by statute or court initiative. Other states, like California, have enacted laws requiring mortgage servicers to offer homeowners the chance to apply for all available foreclosure avoidance programs, such as loan modifications and short sales. These mediation programs have broad support and a record of success in preventing avoidable foreclosure sales.
>
> At the federal level, the Consumer Financial Protection Bureau (CFPB) has adopted regulations that will take effect in January 2014 that will require mortgage servicers to notify homeowners of foreclosure alternatives prior to foreclosure sales.[1]
>
> The current draft would establish a uniform basic structure for facilitation/mediation programs, leaving many details to a court or agency rulemaking process, and deferring to the CFPB rules as to servicer duties to notify homeowners about foreclosure alternatives and handle homeowner applications appropriately.
>
> The draft Act would establish a facilitation process but leaves to the responsible state agency broad latitude in designing the program.
>
> The term "facilitation" is used because the term "mediation" may unduly constrain the role of a third-party neutral.

[1] 78 Fed. Reg. 10695 (Feb. 14, 2013).

The committee first considered a detailed set of mediation provisions modeled on a Washington State statute. After a robust discussion at the November 2012 meeting, the chair, reporters and ABA representative met with several observers and experts on state mediation programs in December of 2012 and formulated a set of best practices for foreclosure mediation programs.

At its February and April 2013 meetings the Drafting Committee approved the framework in the current draft, which establishes a basic facilitation program and requires notice to the homeowner and a temporary hold on foreclosure for homeowners who participate. The current draft omits detailed requirements that appear in many existing state laws, and instead authorizes the state court or agency responsible for supervising the program to issue rules governing the facilitation program.

However, the draft includes in the comments the complete set of best practices developed at the December meeting as guidelines for the court or agency rules.

Clearly, there are significant policy issues embedded in this process.

For example, in all our discussions, FHFA's consistent focus has been on the extraordinary length of time is required to foreclose in some states, and the resulting cost that delay imposes on Fannie Mae, Freddie Mac and Federal Home Loan Banks and other lenders and on those who have purchased interests in Residential Mortgage Backed Securities or RMBSs - bonds secured by pools of residential mortgages.

The Drafting Committee has discussed this issue at length, but has not yet reached a consensus on how to integrate the time frame for facilitation with the existing practices of the lending community and with recently adopted regulations of the Consumer Financial Protection Bureau. The Drafting Committee recognizes that, in some considerable portion of all 'facilitated' foreclosures, the lender will still be required to proceed to foreclosure; in those instances, the lender may view the facilitation process as an additional expense with no offsetting value other than allowing the debtor an additional period of uncompensated residency.

At this time, it seems clear that a state statute that meaningfully reduces that aggregate time frame would necessarily be a part of any ULC drafting effort if ULC expects to secure FHFA/GSE support for such an effort. During the next year, it may be that other appropriate elements may be incorporated into the facilitation process to secure broader support from both the consumer and the lender stakeholders.

Other policy issues include the insistence of consumer representatives that any facilitation process much necessarily have recourse to judicial oversight to remedy what these advocates unanimously assert to be delaying or non-cooperative strategies employed by lenders and creditors.

Further, to the Drafting Committee's knowledge, there is no precedent in the Uniform Laws process for the suggestion of a set of 'best practices' without statutory mandate that they be used.

The draft's approach represents a compromise between leaving all issues of mediation and facilitation to non-uniform state laws and rules, on the one hand, and adopting a detailed uniform model mediation statute, on the other hand.

Reporters' memoranda on foreclosure mediation and the new federal mortgage servicing regulations are available on the committee's web site, which is

http://www.uniformlaws.org/Committee.aspx?title=Home%20Foreclosure%20Procedures%20Act."

ARTICLE 4: RIGHT TO FORECLOSE; SALES PROCEDURES.

Section 401 – Who has the right to foreclose? Section 401 addresses the foundational question of identifying the person who has the right to commence foreclosure of a mortgage.

In 2013, the Drafting Committee sought to address the basic question of what the proper fit should be between foreclosure law and Article 3 of the UCC.

Most residential mortgage loans are documented using promissory notes that are ‘negotiable instruments’ and are thus governed by UCC Article 3.

For such loans, the 2013 version of Section 401 authorized foreclosure by the “person entitled to enforce” the instrument under Article 3. In most cases, the “person entitled to enforce” is a holder of the note, who has possession of the note with any necessary endorsements. Section 401 (2013) served to unite the right to collect mortgage loan payments, which under existing law is specified by Article 3, with the right to foreclose on the collateral. Because the purpose of collateral is to ensure payment of the obligation, the two rights normally are bundled together; this idea is reflected in the legal maxim, “the mortgage follows the note.” Separating those two rights, although conceptually possible, would create – and has created in recent years - a number of problems that proved difficult to solve.

By deferring to Article 3, Section 401 (2013) recognized the traditional importance of a person qualifying as a holder of a negotiable instrument under Article 3, and sought to protect borrowers by ensuring that proceeds of foreclosure sales will flow to the holder, thereby discharging the obligation.

During the past year, the Drafting Committee’s 2013 version of Section 401 was substantially rewritten at the behest of representatives of the Permanent Editorial Board for the UCC.

Concerned that the language of 401 may not have been interpreted by courts to precisely track the outcome under UCC3, the PEB representatives urged that the section be rewritten to confirm that, except in the case of a note registered with a mortgage registry, ‘only a person entitled to enforce’ (a “PETE”) the obligation – that is, the note secured by the mortgage - ‘under other law” – read ‘UCC3’- could also be a person entitled to foreclose the mortgage.

The Drafting Committee observed that the decision to defer to ‘other law’ in all cases comes at a cost in the case of non-negotiable instruments.

It is likely that some residential mortgage loans are not documented using negotiable instruments. For example, the borrower may sign a promissory note, but that note may contain a provision that disqualifies the note from being classified as negotiable under Article 3; or the parties may use other documents, such as an installment land contract, which in some states is considered to be an equitable mortgage.

In the absence of a negotiable instrument, Section 401 (2013) expressly authorized foreclosure by the owner of the mortgage obligation. In some cases – likely not a large number – it will not be easy to tell whether a particular promissory note is negotiable. If the holder of the note and the owner of the note are the same person, the uncertainty would not present a substantial problem under Section 401 (2013), since the person could establish both bases.

But if they are not the same person, there might have been uncertainty as to who is the proper person to foreclose, the resolution of which may require cooperation between the two persons or a judicial determination.

Whatever the limitations of the 2013 version of 401 as regards non-negotiable instruments, that language did have the advantage of setting a default rule that would likely apply in most cases.

Notwithstanding, the Drafting Committee chose to defer to the PEB/UCC's request that the same standard apply to both negotiable and non-negotiable instruments – that is, the PETE 'under other law". This rule works smoothly for negotiable instruments, since UCC3, as more fully articulated in the JEB's 14 page memorandum on the subject, makes clear who the PETE is for negotiable instruments. But UCC3 is entirely silent on who the PETE is for non-negotiable instruments, leaving the question of 'what' "other law" applies unanswered in Section 401(2014).

A complicating factor in a particular instance, as pointed out in Comment 7 to Section 401 (2014), may be that there are multiple persons entitled to enforce a note 'under other law'. The new language under 401 carries that possibility over into the law of mortgage foreclosure, but it is likely that such confusion would occur regardless of this language.

Recent foreclosure litigation has often struggled not only with defining the person with the right to foreclose, but also with related issues detailing what evidentiary proof that person must submit, and at what point in time. When there is a negotiable instrument, Section 401 (2014) – unchanged from (2013) - requires the creditor to produce a copy of the instrument when commencing foreclosure. A few courts have required the physical presentation of the original promissory note to the court – the so-called “show me the note” rule.

Section 401 does not require production of the original note as a general matter. Such a rule imposes substantial costs because original notes are often held by custodians and stored at locations distant from where the property is located; in most cases the cost of securing the original note – while traditional in pre-securitization practice - produces no benefit. However, if during the course of foreclosure an issue arises as to the authenticity of the copy or the whereabouts of the original instrument, then a court may choose to require production of the original.

Section 402 – Transfers of Mortgages – This section was stylistically re-drafted during the last year to simplify but not change its essential result – that mortgage assignments need not be recorded on the land records.

Most residential mortgage loans are sold after origination, and therefore the foreclosing creditor is often a person other than the original mortgagee. In many states, assignments of mortgages are recorded in the county land records to reflect a transfer of the mortgage to the purchaser of the loan. State law presently conflicts as to whether a creditor must hold an express assignment of the mortgage in order to have the right to foreclose; and if so, whether that assignment must be recorded in the county land records prior to foreclosure.

Section 402 adopts the position that an express assignment of mortgage is unnecessary. Requiring that the foreclosing person also hold a recorded assignment adds costs, without an appreciable benefit for the borrower.

The interests of third parties are better handled by other mechanisms. For example, when a foreclosure ends in a foreclosure sale, instruments must be recorded to document title in the foreclosure purchaser, and those instruments must be satisfactory to title insurance companies. The nature and content of those instruments are left to local practice.

Notwithstanding the position taken by the Draft, it is likely that those states that presently require recorded assignments, and some consumer advocates, will object to this provision, especially when the effects of 402 combine with the results available under Section 403 concerning lost notes.

In any event, subsection (a) of the 2013 version of the Act simply recited the Restatement provision that a transfer of the note is also a transfer of the mortgage securing that note. In the re-write, that language was deleted as surplusage.

Subsection (b) of the 2013 Act essentially provided that if the holder of the note received a separate written assignment of the mortgage, the holder could record it but need not in order to foreclose.

The 2014 version of 402 simply provides in its entirety that "[a] person entitled to foreclose a mortgage pursuant to Section 401 does not have to obtain or record an assignment of mortgage from the initial holder of the obligation."

It may be appropriate to expand this language to make clear that a PETE need not obtain or record an assignment from either the initial or any subsequent holder of either the obligation or the mortgage – but this is an issue for the next Drafting Committee meeting.

In any case, the Floor should know that while the consensus of all those participating in the Committee's drafting process is that 402 as drafted is the only practical outcome under current securitization practice, it remains a volatile topic among some consumer groups and may well be a subject of controversy in the states at the time of enactment.

Section 403 – **Lost Note Affidavits** – This section treats the frequently litigated topic of lost, stolen or destroyed notes, made notorious by the "robo-signing" practices of lenders and servicers.

A lost note creates the risk for the borrower that a person other than the foreclosing creditor may present the promissory note and demand payment. Following UCC Section 3-309, Section 403 gives the borrower the right to adequate protection, and extends that right by requiring an express indemnity from the creditor in all cases in which it uses a lost note affidavit.

In Section 403 (2013), the Act contained alternative versions of subsection (a) of this section: one of which was based on the 2002 amendments to UCC 3-309, and the second of which was based on UCC 3-309 before those amendments.

The Drafters' Notes in the 2013 version stated the policy choice clearly:

> The policy choice facing the Drafting Committee…is the extent to which this act should give license to foreclosing creditors who sign 'lost' or 'destroyed' note affidavits without ever having possessed either the original or certified copy of the note, and without any evidence of a written assignment of the underlying mortgage to that creditor….[I]f one is to speak of 'moral hazard', there is little doubt that a liberal 'lost note' affidavit policy offers a powerful incentive to the first note holder intentionally to discard the original note and thereby avoid the cost and uncertainty of maintaining original paper notes.

There is a split of authority as to whether the successor may execute a lost note affidavit when it never had possession of the note. While revised Article 3-309 (2002) expressly allows such a person to enforce a lost note, only 10 states have adopted Revised Article 3. Under old Article 3, courts are split as to whether a note can be enforced by a successor to the person who lost the note.

The policy choices are stark: sometimes the promissory note has legitimately been lost or destroyed by a predecessor of the creditor who is seeking to foreclose and it is not always possible for the foreclosing creditor to get the predecessor to execute an appropriate lost note affidavit. The 2013 alternatives related to the specific content of the affidavit and the degree to which the affiant should have personal knowledge of facts. Under the 2002 amendments – now reflected in the 2014 version of the affidavit, a general statement that the note was "lost or destroyed" before a given date is sufficient and does not require that the affidavit specify particulars as to when, where, and how the loss or destruction took place.

In any event, at the suggestion of representatives of the PEB and in order that the UCC rules for enforcement of a note track the rules for enforcement of a mortgage which provides security for a note, the Drafting Committee has elected to track the 2002 amendments to UCC 3-309.

In the Chair's view, the ULC should recognize the exposure we face to consumer criticism. As a result of the Act as now drafted, a person who possesses only a faxed copy of a note endorsed in blank- that is, a person who possesses neither an original note, a copy of a note endorsed to that person, nor any written assignment of the mortgage- recorded or otherwise - may lawfully foreclose on a borrower's home solely on the basis of an affidavit from that same person that she (or her appointed agent) is the person entitled to enforce a note that she cannot find. As the model form of affidavit appearing in the Act after Section 403 (2014) makes clear, the affiant's obligation of due diligence in determining that the note is lost is limited to a search of the lender's own records; a statement that "I looked and the note could not be found' would suffice.

Finally, in states that allow non-judicial foreclosure, that creditor - who possesses no documentation of its right to foreclose - may nevertheless proceed to foreclose without oversight by any judge, unless the borrower institutes a separate lawsuit to prevent the foreclosure- a rare occurrence indeed.

One of the principal goals of the electronic registry of notes proposed by the Federal Reserve Bank of New York is to eliminate the continued litigation over enforcement of missing original 'paper' notes. If the registry were implemented, the controversy posed by the Conference's policy reflected in UCC 3-309 (2002) and the 2014 version of Section 403 of this Act would end.

Until then, however, the combined effect of Sections 402 and 403 of this Act with existing provisions of UCC 3 and 9 enabling such a facile loss of a borrower's home in the absence of any judicial scrutiny is likely to be a major focus of consumer opposition to this Act.

Section 404 – **Public advertisement and notice of foreclosure sale**

The 2013 Issues Memorandum stated:

> "Existing law generally requires the advertisement of foreclosure sales in local print newspapers, with no alternatives and no additional requirements except, in some states, posting of a sign at the location of the property being foreclosed. Section 404 replaces this rule with a more flexible standard, requiring a commercially reasonable advertisement of a foreclosure sale, which depends upon the particular facts. A local newspaper advertisement is no longer mandatory in all cases. In many communities, newspaper advertisements are no longer an effective means of informing the public about upcoming foreclosure sales. Under these circumstances, a creditor's decision not to publish in a newspaper benefits both the creditor and the homeowner by saving the expense.

> In recognition of the growing importance of Internet advertising, <u>Section 404 authorizes Internet advertising of foreclosure sales and creates a safe harbor, which deems an advertisement commercially reasonable when published in both an appropriate Internet website and a local newspaper</u> (emphasis added).

The principal change in the last year – but a significant one - is that the Drafting Committee, in Section 404 (a)(2), voted to expand its safe harbor of commercial reasonableness by providing that publication is commercially reasonable if published in <u>either</u> a newspaper for the prescribed period, <u>or</u> on an internet site "that is reasonably expected to be viewed by persons having an interest in purchasing the mortgaged property at least 21 days before the sale and the Internet posting remains regularly available between the time of posting and the time of sale."

Without a doubt, this policy change will be welcomed by the lending industry and vilified by the newspaper publishing industry.

The remaining three sections of Article 4 do not pose any substantial policy issues. Section 407 is now an optional section which a State may choose to adopt in those instances where, most likely for title purposes, the affected parties would seek judicial confirmation of a foreclosure sale.

ARTICLE 5: ACCELERATED DISPOSITIONS

In the past year, the Drafting Committee sought to enhance the effectiveness of two devices – Negotiated Transfers and Accelerated Foreclosure of Abandoned Property – which both the lending industry and consumer advocates agree could enhance the interests of both lenders and borrowers and, in the case of the communities where abandoned property is located, the neighborhoods that are adversely affected by what have come to be called 'Zombie Properties'.

In the case of 'Negotiated Transfers', The Drafting Committee was happy to accept the helpful recommendations of the Style Committee, but there have been no significant policy changes in Sections 501-504.

In the case of Abandoned Property, the major changes made were these:

- Significant re-styling of these provisions resulted in the addition of three new separate sections.

- Several of the criteria by which a court might conclude that the property in question is abandoned have been tightened and made more objective. For example, Section 505(a)(4) in its 2013 version provided that one criteria was

  > (4) the property is deteriorating so as to constitute a serious threat to public health or safety.

  That language was replaced in the current version by:

  > (4) A governmental entity has issued an order or finding declaring that the property is unfit for occupancy or constitutes a serious threat to public health or safety.

- Section 505(b) creates a procedure for filing of affidavits supporting the proposed determination of abandonment, in anticipation of a summary proceeding in those instances where the homeowner or obligor fails to appear at the hearing.

- New Section 506 details the procedures for service of a complaint seeking a determination of abandonment, and setting a prompt hearing. This is coupled with the possibility of commencing the foreclosure process by filing a Section 201 notice. Importantly, building on Section 505(b), Section 506(f) directs the court to enter a determination that the property is abandoned if the homeowner fails to appear at the hearing.

- Section 509 creates two alternative means of passing title to abandoned property: in the first, the court may order a sale within 30 but not more than 45 days. In the second, akin to strict foreclosure, if the court on the foreclosing creditor's motion, determines that there is no equity in the property in excess of the foreclosing creditor's lien, the court may order transfer of title directly to the creditor and extinguishment of junior liens.

- Section 509(e) also extinguishes any rights of redemption of the borrower, and holds the foreclosing creditor or purchaser at the sale immune from any borrower claims for abandoned property.

2013 Explanation Again, the following text appeared verbatim in the 2013 Issues Memo and remains here in order to refresh the readers' collective recollections of what Article 5 seeks to accomplish:

> Sections 501 through 504 address what this Act calls a 'negotiated transfer,' while Sections 505 through 510 deal with the foreclosure of abandoned property. Taken together, the Drafting Committee considers these two significant devices to enable lenders to secure title quickly when there are no homeowners who would be adversely affected by the sale.
>
> ***Negotiated transfer in satisfaction of debt*** Existing law in most states recognizes a "deed in lieu of foreclosure" transaction, in which the parties agree to a conveyance of the property to the lender as an alternative to a standard foreclosure. In recent years, such negotiated transfers have been called "cash-for-keys" agreements, reflecting the practice of lenders offering cash payments to homeowners in exchange for their relinquishing possession and agreeing not to contest the foreclosure. Under existing law, the presence of junior liens or other junior interests often prevents a deed in lieu of foreclosure, because the lender as grantee under the deed in lieu of foreclosure takes subject to the junior interests. The only way to terminate the junior interests is by formal foreclosure.
>
> Sections 501 to 505 provide a statutory framework that recognizes and enhances existing workout arrangements, including "deed in lieu" transactions. If a homeowner faced with foreclosure cannot afford to retain the home after exploring all possible options to keep possession of the property, then it is often in the best interests of all concerned if the parties can negotiate a transfer to the lender as an alternative to the completion of a foreclosure sale.
>
> One policy consideration, reflected by a charge given to the Drafting Committee, is whether to include a statutory "minimum sum" paid to the borrower in a negotiated transfer. After preliminary drafting and discussion, the decision was made not to specify a minimum

consideration based upon a concern that a substantial minimum consideration would chill use of the procedure, and that given the wide variety of mortgage loans and individual circumstances, it is very hard to say what minimum should be required in all cases. The main borrower protection set forth in the negotiated transfer provisions, other than requiring proper documentation and notices, is that the negotiated transfer results in full satisfaction of the mortgage debt. In other words, a deficiency judgment is barred.

Another policy issue that some have discussed is the negative reaction that junior creditors may have to being forced to abandon their position quickly in those states where their rights under a judicial foreclosure procedure may offer them greater leverage in dealing with a senior creditor.

A final issue that has been discussed is whether to make the benefits of this statutory procedure available in all 'deed in lieu' situations, whether or not the signed agreement provides that the agreement is made pursuant to this Act. To date, the Committee's position is that a requirement that the agreement confirm to the substantive and procedural requirements of these sections will quickly become conventional practice in the states, without incurring the uncertainty as to which 'agreements' qualify for accelerated foreclosure, and which do not.

Accelerated foreclosure of abandoned property Foreclosures of abandoned or vacant homes raise special issues. Those properties often become derelict and remain empty for long time periods, creating substantial problems for the surrounding neighborhood. Sections 505 and 506 authorize an expedited foreclosure procedure for abandoned properties for both judicial foreclosure and for nonjudicial foreclosures. Practically, this is of greater importance in judicial foreclosure states, as timelines for foreclosure in most nonjudicial foreclosure states are already relatively rapid.

An accelerated timeline is appropriate for two reasons. First, the homeowner is no longer using the property for shelter. A foreclosure sale will not result in a family being forced to relocate to other housing. Second, vacant properties that are in foreclosure have significant negative impacts on neighborhoods and the surrounding communities. Vacancies reduce the market values of neighboring properties. Neighborhood crime increases. The vacant properties tend to suffer from lack of repair and maintenance, creating public health risks. There are fiscal impacts on local governments, who find property taxes on vacant properties often become delinquent; yet the governments are faced with added expenses to provide essential services to blighted neighborhoods, such as police and fire protection. The objective of the Act's expedited procedure is to return abandoned properties to the housing stock, occupied by families, as soon as reasonably possible.

A second main feature of the abandoned property provisions is to require maintenance of abandoned properties by lenders pursuant to the standards set forth in Section 507. This is a quid pro quo – the lender gets accelerated foreclosure, but has to take care of the property. The trigger for the duty to maintain is a judicial determination that the property is abandoned, which authorizes expedited foreclosure. In a judicial foreclosure, the court makes the determination as to whether a particular home is abandoned, guided by statutory criteria set forth in Section 505. In a nonjudicial foreclosure, the act enables a government official, such as a building code department, to make a determination that a home is abandoned. Also, in addition to a lender seeking a determination that the home is abandoned, the city or a homeowners' association will have the right to request the determination, thereby triggering a lender's duty to maintain the property.

ARTICLE 6: REMEDIES

Section 601 – Effect of Violation – The Drafting Committee has made these significant changes to this section in the last year:

- Last year's version required that any dismissal of a foreclosure action must be without prejudice 'unless the court determines that a new foreclosure action would unfairly burden the homeowner due to a creditor's repeated violations or other aggravating circumstances.' In 2014, the standard is changed to read: "unless the court determines that a new foreclosure action should be barred because of egregious misconduct by the creditor or servicer or other good cause."

- In the 2013 version of this section, the Act provided statutory damages of a bracketed amount for each violation of the Act, regardless of any actual damage. That provision has been deleted in this version of the Act.

- Further, in revising Section 601(e), the award of statutory damages is now limited to those circumstances where the lender is guilty of what the statute describes as a 'pattern or practice' of non-compliance with the Act.

Section 602. Defense or Remedy under Other Law. The Drafting Committee made no changes to this section.

Section 603. Procedure for Asserting Defense in Nonjudicial Foreclosure. The only substantive change to this section is the proposed addition of bracketed language requiring that an action to enjoin a foreclosure sale must be brought before the sale.

Section 604. Attorney's Fees And Costs. No changes are proposed.

Section 605. Enforcement By [Attorney General]. No changes are proposed.

Section 606. Effect of The Holder In Due Course Rule. Last year in Boston, the Floor passed a nearly unanimous 'sense of the house' resolution directing the Drafting Committee to propose some 'compromise' regarding the Holder In Due Course doctrine.

Commissioners seeking more background on the topic are urged to review the Sub-Committee Report on that topic by Commissioners Lisman, Miller and Walters, which can be found beginning at page 15 of the 2013 Issues Memorandum, on the Drafting Committee's website. You may also wish to review the several letters, comments and other communications on this subject appearing on the same website, bearing dates from July 2013 through November 2013.

In response to the Floor resolution, the Drafting Committee spent an extraordinary amount of time and effort in an attempt to identify various alternatives that would be acceptable to both the lending industry and consumer advocates. That effort included creation of a sub-committee on the subject that met separately from the entire Drafting Committee on two occasions, once in Washington DC and a second time in New York City.

The three alternatives in Section 606 are no more than 'works in progress' that the Drafting Committee presents to the Floor for its consideration.

A note on the structure of the Section as it appears in the Act may be helpful.

Subsection (a) states the fundamental rule that a holder in due course is subject to the defenses identified in subsection (b), despite UCC 3-305 (which otherwise insulates the holder in due course from such claims) and despite any waiver of such claims that the borrower may have signed.

Subsection (b) then allows a claim or defense against a holder in due course based on any one of three bases: (i) fraud; (ii) material misrepresentation; or (iii) fundamental breach of promise in connection with the original loan transaction – that is, unless any such claim would be barred by some other statute of limitations or other preclusion.

Subsections (c) and (d) - The three alternatives are all contained in three alternative variations of subsections (c) and (d) of Section 606. All three assume that subsections (a) and (b) would remain constant. The following descriptions of the three Alternatives are verbatim quotes taken directly from the Drafters' Notes**.**

> **Alternative A –** In this alternative, the obligor or homeowner may assert as either a defense to a foreclosure or in a declaratory judgment, any claim or defense she may have under subsection (b), in addition to whatever rights she may have under UCC3-305. However, this right is limited to a period of 3 years from the date of the original transaction or, if longer in the case of an interest rate adjustment or prepayment fee, an additional one year after the date of the adjustment. Further, the maximum amount of borrower's recovery in that case would be the balance owing on the note.
>
> **Alternative B -** Under this alternative, there is no time limit on when an obligor or homeowner may raise a defense in a foreclosure action. However, no declaratory judgment is authorized under this alternative, and therefore no relief is

> available to the borrower unless the creditor initiates foreclosure after the borrower's default. This alternative imposes the same limits on the economic recovery attributable to the defense as in Alternative A.
>
> **Alternative C -** Under this alternative, as in Alternative B, there is no time limit on when an obligor or homeowner may raise a defense in a foreclosure action, and the same prohibition on affirmative claims applies. However, unlike Alternative B, any relief is limited to protection from a deficiency judgment.

As the Reporters' Notes following this section make clear, "this section represents a middle-ground position between preservation of the status quo and complete abrogation of the HDC doctrine, along the lines of the Federal Trade Commission Regulation (16 CFR Part 433) that protects consumers who finance the purchase of goods or services.

The most vigorous proponents of abolishing the HDC doctrine entirely have been the general counsel and chief economist of the Federal Reserve Bank of Cleveland; nonetheless, those gentlemen, in an effort to reach some consensus on this subject, have supported Alternative A. Lenders, while not seeking any diminution of their insulated position, also seem to have gravitated to Alternative A if there is to be any change, since the three year period coincides with the time frame now set by FHFA within which the GSEs will be allowed to surrender their rights to require repurchase of notes by the sellers of the notes if no claim of invalidity of the notes and no monthly payment failure has occurred.

The Chair observes that from an economic perspective in the 21st century, there is little reason to impose on borrowers – for no economic benefit - the risk that their claims against the original creditor would be barred against subsequent holders of the same note. Standard economic models suggest several devices by which the secondary market could – and likely would – protect itself from the possibility of such claims. In the auto loan field, the principal model would be to 'overfund' the trust that holds auto loans sold by dealers, with any balance remaining in the trust after the loans have matured (and claims having been adjudicated) being returned to the dealer/sellers.

Since this overfunding device tends to reduce profits, a less expensive model – and the one which triggered the downfall of AIG during the recent melt down – would be the purchase of 'credit default swaps' – a form of insurance against the possibility of Section 606 claims being successful. While the initial pricing of such swaps could be speculative in the first years, the Chair is informed that over time, the market would find the appropriate return necessary to compensate the counterparties to such 'swaps' for the risk they are incurring.

Notwithstanding the availability of such more or less traditional devices to shift risk to the appropriate parties, it is clear that the secondary market is strongly resistant to such a proposal, and the compromises suggested by the Drafting Committee are an effort to reach a presently unattainable consensus.

2013 Explanation Again, the following text appeared verbatim in the 2013 Issues Memo and remains here in order to refresh the readers' collective recollections of what Article 6 seeks to accomplish:

> In preparing the sections (of Article 6) as they currently appear in the draft, the Chair and reporters were in some respects guided by analogous provisions for foreclosure of personal property in Article 9 of the UCC. These provisions represent tentative decisions reached at that April meeting and are almost certain to be the object of continued discussion between lenders and borrowers.
>
> The fact is that, in all these regards, industry and consumer positions are inherently difficult to reconcile.
>
> Consumers naturally advocate full assignee liability, mandatory attorney's fees, liquidated damages, and similar remedies for all violations, as well as a full panoply of defenses and defensive remedies including dismissal with prejudice of a judicial foreclosure or injunction against a non-judicial foreclosure. At the same time, their advocates insist that these enhanced consumer remedies and restrictions on foreclosure practices should not result in higher creditworthiness standards, reduced availability of mortgage loans, or higher interest rates. Indeed, they threaten that if any such practices result in a 'disparate impact' on the poor and minority populations, those lenders who precipitate such impacts should be subject to liability for discrimination.

Lenders naturally oppose these remedies, and seek safe harbors, damage caps, no or limited assignee liability, and materiality and cure standards for violations. They also claim that these remedies are certain to result in higher costs for all borrowers and will preclude potential borrowers with marginal credit from buying homes.

Ultimately the Act will need to strike a balance in providing remedies adequate to insure compliance by lenders, as well as support from consumer advocates, but not creating excessive litigation exposure for “gotcha” violations that would provoke vigorous mortgage industry opposition, and hopefully not adversely affecting the ability of the citizenry to purchase homes.