

DRAFT
FOR DISCUSSION ONLY

RESIDENTIAL REAL ESTATE MORTGAGE FORECLOSURE PROCESS AND PROTECTIONS

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAW

For February 15-16, 2013 Drafting Committee Meeting

Without Prefatory Note and With Reporter's Drafting Comments

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ON UNIFORM STATE LAWS

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February 4, 2013

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FORECLOSURE PROCESS AND PROTECTIONS**

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RESIDENTIAL REAL ESTATE MORTGAGE FORECLOSURE PROCESS AND PROTECTIONS

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1 **RESIDENTIAL REAL ESTATE MORTGAGE FORECLOSURE PROCESS**
2 **AND PROTECTIONS**

3 **ARTICLE 1**

4 **TITLE AND DEFINITIONS**

5 **SECTION 101. SHORT TITLE.** This [act] may be cited as the Home Foreclosure
6 Procedures Act.

7 **SECTION 102. DEFINITIONS.** In this [act]:

8 (1) “Abandoned property” means mortgaged property with respect to which the borrower
9 and persons claiming through the borrower, including tenants, have relinquished possession.
10 Abandoned property does not include (i) a dwelling unit the initial construction of which is not
11 complete or (ii) a dwelling unit used or held for use by the borrower as a vacation home or
12 seasonal home.

13 (2) "Borrower" means a person owning an interest in the mortgaged property, other than a
14 mortgage, lien, servitude, or leasehold, whether or not the person is an obligor.

15 **Drafter’s Notes**

16
17 1. The Committee should compare the new definition of ‘Obligor’.

18
19 2. We need to consider to whom the Act requires ‘notice’ to be provided
20 to a ‘borrower’ v. an ‘obligor’ and how the creditor is able to identify each; see
21 the proposed amendments to Sec. 401.

22
23 3. At the November meeting, there were suggestions from several persons
24 for more expansive comments; to the extent these notes are inadequate, please let
25 the Reporters know of any desired additional comments.

26
27 (3) “Common interest community” means real property with respect to which a person,
28 by virtue of ownership of a unit, is obligated to pay for real property taxes, insurance premiums,
29 maintenance, or improvement of other real property ,or services described in a declaration or

1 other governing documents, however denominated. A common interest community includes
2 properties held by a cooperative housing corporation. In this paragraph, "ownership" includes a
3 leasehold interest if the period of the lease is at least [20] years, including renewal options.

4 (4) "Creditor" means a lender or other person who owns or has the right to enforce an
5 obligation. [The term does not include a person who extends no more than two mortgage loans in
6 the same calendar year as the mortgage at issue.]

7 **Drafter's Notes**

8
9 1. The last sentence of the definition of 'creditor' is an attempt to address
10 Dale Whitman's and other comments to exclude 'mom & pop' lenders or one-off
11 seller financing.

12
13 2. The alternative (i.e., the "or has the right to enforce" clause) is useful
14 for the time being due to the alternatives for section 401. We could define creditor
15 as a person who has commenced foreclosure, but that doesn't work because we
16 are imposing some duties on lenders before commencing foreclosure. We dropped
17 the language referring to agents, services, and assigns: It is now "buried" in "other
18 person"; to the extent we need to address issues involving services, agents, and
19 assigns, we think it belongs elsewhere.

20
21 3. We should consider the status of mortgage insurers, and other cases;
22 perhaps we can define guarantors separately and then include them in substantive
23 provisions only when appropriate.

24
25 4. The Reporters, Chair and ABA Advisor believe- subject to contrary
26 thoughts from the Committee – that we do not need to define the term 'servicer'.
27 That word is not used in any statutory text or comments; it appears only in the
28 discussion of facilitation standards and objectives.

29
30 (5) "Expenses of foreclosure" means the lesser of the reasonable expenses
31 incurred by a foreclosing creditor or the maximum amounts permitted by other law of this State
32 for expenses in connection with a foreclosure. These expenses include costs of transmission of
33 notices, advertising, title searches, inspections and examinations of the mortgaged property ,
34 management and securing of the mortgaged property, insurance, filing and recording fees,
35 attorney's fees and litigation expenses incurred to the extent provided in the mortgage or

1 authorized by law, appraisal fees, the fee of the person conducting the sale in the case of a
2 foreclosure by auction, fees of court-appointed receivers, and other expenses reasonably
3 necessary to the foreclosure.

4 (x) “Facilitation” means the assistance of a third-party neutral at an in-person meeting or
5 meetings between the parties with the objective of achieving a commercially reasonable
6 alternative to foreclosure, resulting in sustainable outcomes for the creditor and borrower.

7 **Barry’s Note:** Does this preclude telephone conferences, and to whom does ‘in-
8 person’ apply?
9

10 (6) “Foreclosure” means any process, proceeding or other action by a creditor to
11 terminate the borrower’s interest in the mortgaged property or to obtain possession of the
12 mortgaged property for the creditor. [Foreclosure does not include a voluntary transfer by the
13 borrower and does not include an action to recover possession of the property after a completed
14 foreclosure sale.]

15 (x) “Good Faith” – In November, Commissioner Ring recommended that we consider
16 defining ‘good faith’ in this Act; the Reporters, Chair and ABA Advisor, after discussion,
17 concluded that this should not be done.

18 (7) “Individual” means a natural person.

19 **Drafter’s Note**
20

21 This definition was used only in section 503; that section has been amended to
22 avoid the need for the definition.
23

24 (9) “Instrument” means a negotiable instrument as defined in [U.C.C. § 3-104].

25 (10) “Loss mitigation” means any program that the creditor offers to borrowers in default
26 or facing imminent default, as an alternative to a foreclosure sale.

1 **Drafter's Note**

2
3 The comments will be expanded to make clear that 'loss mitigation' includes such
4 actions as a repayment plan, forbearance agreement, loan modification, short sale,
5 partial mortgage insurance claim, negotiated transfer and deed in lieu of
6 foreclosure.

7
8 (11) "Facilitation agency" means [the administrative or judicial agency designated by the
9 state to supervise foreclosure facilitation.]

10 (12) "Mortgage" means a consensual interest in residential property that secures payment
11 of an obligation, created by a mortgage agreement.

12 **Drafter's Note**

13
14 The Committee should determine whether it wishes to address the status of land
15 installment contracts within the act and if so, how.

16
17 (13) "Mortgage agreement" means a mortgage instrument, deed of trust, security deed, or
18 other record that creates or provides for a mortgage.

19 **Drafter's Note**

20
21 The Reporters acknowledge the circular nature of the definitions of 'Mortgage'
22 and 'Mortgage Agreement' and welcome further discussion.

23
24 (14) "Mortgaged property" means residential property, together with any personal
25 property held or used in connection with the real property, which is subject to a mortgage.

26 (15) "Obligor" means a person that, with respect to an obligation secured by a mortgage,
27 (i) owes payment of the obligation, (ii) has provided property other than the mortgaged property
28 to secure payment of the obligation, or (iii) is otherwise accountable in whole or in part for
29 payment of the obligation.

30 (16) "Obligation" means a debt or other liability that is secured by a mortgage.

31 (17) "Person" means an individual, corporation, business trust, estate, trust, partnership,
32 limited liability company, association, joint venture, government; governmental subdivision,

agency, or instrumentality; public corporation, or any other legal or commercial entity.

Drafter's Note

The Reporters, Chair and ABA Advisor believe that the definition of 'real property' is unnecessary and, by deleting it, we avoid several issues which were debated in November.

(18) "Record", used as a noun, means information that is inscribed on a tangible medium or is stored in an electronic or other medium and is retrievable in perceivable form.

(19) "Residential property" means real property improved with, one- to four-dwelling units, including structures ancillary to such dwelling units and including attached single-family dwelling units and single-family manufactured housing units placed upon permanent foundations. Residential property includes single-family units in a common interest community.

(20) "State" means a State of the United States, the District of Columbia, Puerto Rico, the United States Virgin Islands, or any territory or insular possession subject to the jurisdiction of the United States.

Reporters' Drafting Notes

1. Many of the definitions are taken from the Uniform Non-Judicial Foreclosure Act, while the drafters have also added several new definitions, including 'Borrower', 'Lender', 'Loss Mitigation' and 'Facilitation Agency'.

2. In some states, a land sale installment contract does not constitute a 'mortgage', with all the attendant consequences for borrowers and creditors, until a specified percentage of the original principal amount has been paid to the creditor. In Illinois, for example, that percentage is 50% of the original principal amount. In those States where the issue arises, statutory drafters should make appropriate amendments to this act to track existing practice in that state.

3. Whether mortgaged property is "abandoned property" is determined by the facts of each case. The factors listed in Section 505(a) are not exclusive. The core question is whether the borrower is presently in possession of the property. The question must be answered by evaluating the facts related to the borrower's use of the property. The subjective intention of the borrower to maintain or continue ownership of the property, whether or not communicated to the creditor, is irrelevant.

1
2 4. The definitions of “mortgage” and “obligor” refer to the payment of an
3 obligation, and do not use the phrasing found in UCC Article 9 definitions that
4 includes “payment or other performance” of obligations. Almost always the basis
5 for a residential mortgage foreclosure is the failure to pay a monetary obligation.
6

7 **SECTION 103. [Alternative #1] SCOPE.** This Act applies to the foreclosure of every
8 mortgage on residential property that commences on or after the effective date of this [act], even
9 if the mortgage was created before the [act] takes effect.

10 **Drafter’s Note**

11
12 From a style perspective, it may be that all the language after ‘real property’
13 should be deleted and the issue of which foreclosure actions are governed by the
14 act would be dealt with at the end of the act in an ‘Effective Date’ section.
15

16 **SECTION 103. [Alternative #2] SCOPE.** This Act applies to the foreclosure of every
17 mortgage on residential property occupied by the borrower for personal, family, or household
18 purposes at the time the mortgage is granted or when the creditor commences a foreclosure
19 proceeding.

20 **Reporters’ Drafting Notes**

21
22 1. This Act applies whenever a creditor forecloses on a mortgage on
23 residential property, whether by judicial process or by non-judicial measures. The
24 definition of “foreclosure” in Section 1-102 must be consulted to determine which
25 actions taken by creditors have the legal effect of making the Act applicable to the
26 parties to a mortgage.
27

28 2. The Reporters, Chair and ABA Advisor believe this Act applies to the
29 foreclosure of mortgages created before the effective date of this Act, unless the
30 creditor has taken action to foreclose before the effective date; the Style issue is
31 whether to state that outcome in the ‘Scope’ section or the ‘Effective Date’
32 section
33

34 3. Under Alternative #1 this Act applies whenever a mortgage covers one-
35 to-four dwelling units, regardless of whether the borrower occupies or intends to
36 occupy one or more of the units as a principal residence or other residence.
37 Alternative #2 limits the scope of the Act to owner-occupied residential property.
38 In both cases, the Act does not apply if the mortgage covers five or more dwelling

1 units, even if the borrower personally occupies one or more of those units.

2
3 4. The Drafting Committee may well wish to expand the ‘scope’ section to
4 address the question of how this Act is to be blended with existing state law.

5 6 **ARTICLE 2**

7 **NOTICES, RIGHT TO CURE**

8 **SECTION 201. PRE-FORECLOSURE NOTICE.** Before any creditor may
9 commence foreclosure, the creditor shall give each borrower [and obligor?] both a notice of
10 default, intent to accelerate and the right to cure pursuant to Section 202 and a notice of
11 facilitation pursuant to Section 301.

12 **Reporters’ Drafting Notes**

13
14 1. We debated a threshold policy issue raised by these notice provisions
15 [201 and 202] and by the mandatory provisions of Article 3 on facilitation. That
16 issue is whether this act should apply to enforce the obligation’ (that is, to any
17 creditor action seeking recovery of the debt) or, as it is presently drafted, only to
18 actions that would have the effect of depriving the borrower of the right to occupy
19 the home – primarily, a foreclosure. The issue is posed most directly in those
20 cases where the creditor may choose to sue, either first or exclusively - on the
21 note rather than to foreclose the mortgage.

22
23 2. As drafted, the notices and mandatory facilitation would apply only to
24 foreclosure and not to other actions that a lender might theoretically take, such as
25 seeking a receivership in the case of, for example, an owner-occupied 3 family
26 house. Those advocating for a narrower rule would argue that the primary purpose
27 of this act is to keep the borrower in the house and a suit on the note is no
28 different than a suit by any other unsecured creditor.

29
30 The matter becomes even more complicated when one considers those states that
31 have a ‘one action’ rule, where a suit on the note would have the effect of barring
32 a subsequent action to foreclose on the mortgage.

33
34 3. The notices required by this section are separate and distinct from the
35 notice of foreclosure sale required by Section 405. The notices need be sent by
36 only one of the persons or entities defined as “creditor,” but must be separately
37 sent to all persons who come within the definition of “borrower.” Compliance
38 with notice requirements by the servicing agent, for example, will suffice as
39 notice by the owner of the mortgage.

1 4. In November, Commissioner Rubin noted the need to be clear regarding
2 the questions of who must give, and who must receive, the notices required by
3 this Act. We have attempted to address those questions in our revisions to these
4 and other sections and in the comments; see, for example, the new comment
5 immediately above this Note, in the amendments to Section 401 and in new
6 Section 205.

7
8 **SECTION 202. NOTICE OF DEFAULT, INTENT TO ACCELERATE AND**

9 **RIGHT TO CURE.** A creditor may not commence foreclosure until 30 days after it has sent to
10 each borrower [and obligor?] the notice of default, intent to accelerate and right to cure described
11 in Section 201. The notice shall state:

12 (a) the nature of the default including an itemization of all past due payments, fees and
13 other charges as of the date of the notice,

14 (b) the specific action(s) the borrower must take to cure the default, as described in
15 Section 204 (b), including the exact amounts that must be paid.

16 (c) the date by which the borrower must cure the default, which shall be no sooner than
17 one day prior to the first scheduled foreclosure sale,

18 (d) the fact that if the borrower does not cure, the creditor may demand payment of the
19 full amount due, not just past due payments, and may foreclose and sell the property,

20 (e) the effect of curing the default, including the right to have the terms of the note and
21 mortgage remain in effect,

22 (f) a statement of why the borrower is receiving the notice and what the borrower's rights
23 are, including the borrower's right to dispute the default or raise any other defenses to
24 foreclosure and how that right may be exercised,

25 (g) the specific basis for asserting that the foreclosing creditor has the right to foreclose
26 and, if the creditor is acting as agent for the owner of the obligation, the identity of the owner,

27 (h) the borrower's right to request a copy of the borrower's mortgage note and copies of

1 any assignments of mortgage or deed of trust required to demonstrate the right to foreclose on
2 the mortgage, and

3 (i) a reference to the fact that the borrower will receive separate notices of available
4 foreclosure alternatives and facilitation.

5 **Reporters' Drafting Notes**

6
7 1. The mortgage obligation may be accelerated by filing a complaint,
8 scheduling a sale, or by separate notice of acceleration – the notice of intent to
9 accelerate does not by itself accelerate the debt. The notice need not refer to
10 acceleration if the creditor does not intend to accelerate the obligation, for
11 example if it is fully matured. The phrase “other legal action” includes other legal
12 methods that may be used to terminate the borrower’s interest in the mortgaged
13 property, such as a quiet title or ejectment action in the case of an installment land
14 sale contract. Purchasers of foreclosed properties are protected from assertions
15 that the sale was invalid because the chain of loan ownership described in the pre-
16 foreclosure notice was incorrect; the borrower must raise challenges to the notice
17 and other defenses before the sale, pursuant to Section 4-107.
18

19 2. Items (a) through (f) are the elements of notice in the standard
20 Fannie/Freddie mortgage instrument. Item (c) adds a specific deadline to cure the
21 default. Items (g) and (h) are the ownership statement required by the national
22 servicing settlement, and call for the servicer to identify its basis for standing at
23 the outset of foreclosure proceedings, so that any disputes can be resolved
24 promptly. Including this information complements Section 4-107, providing
25 conclusive effect to a completed foreclosure sale. This notice would not displace
26 all state-specific aid program and counseling notices which necessarily will
27 depend on state funding – for example, Pennsylvania requires a separate 30-day
28 notice of how to apply for its Homeowner’s Emergency Mortgage Assistance
29 Program.
30

31 3. The mortgage obligation may be accelerated by filing a complaint,
32 scheduling a sale, or by separate notice of acceleration – the notice of intent to
33 accelerate does not by itself accelerate the debt. The notice need not refer to
34 acceleration if the creditor does not intend to accelerate the obligation, for
35 example if it is fully matured. Purchasers of foreclosed properties are protected
36 from assertions that the sale was invalid because the chain of loan ownership
37 described in the pre-foreclosure notice was incorrect; the borrower must raise
38 challenges to the notice and other defenses before the sale, pursuant to Section 4-
39 107.
40

41 4. In Subsection (a), the itemization of amounts owed should be as of the
42 date of the notice, and should not include amounts that have not yet come due.

1 The notice may refer to the fact that additional sums will come due after the date
2 of the notice. Fees and charges imposed by the creditor or the creditor's attorney
3 should be ascertained and included.
4

5 The Committee should determine whether a "good faith estimate"
6 approach would be sufficient in the case of fees and charges that are imposed by
7 third parties and that have been incurred, but the amount of which are not known,
8 at the time of the notice.
9

10 5. In subsection (b), the actions the borrower needs to take in order to cure
11 the default are governed by § 204.
12

13 6. In subsection (g), the basis on which a particular creditor may assert the
14 right to foreclose is specified in §401. The notice may, but is not required to,
15 explain that the agent has full authority on behalf of the owner to negotiate with
16 the borrower.
17

18 **SECTION 203. MANNER OF NOTICE DELIVERY.** Both notices required by
19 Section 201 must be sent by first class mail to each borrower's last known address, and to the
20 mortgaged property address. If a borrower or borrower's representative has requested to receive
21 notices by electronic mail and has provided an electronic mail address to the creditor, both
22 notices must also be sent by electronic mail to the borrower's electronic mail address. The
23 notices may be sent at the same time, [but may not be combined with each other, or with any
24 other notices, or with the [complaint, in a judicial state or] Notice of Sale.]

25 **Reporters' Drafting Notes**

26

27 1. We bracket the language concerning 'combined', in order to highlight
28 an issue requiring further refinement. The drafters agree that by 'combined', we
29 mean at least that each of the mandated notices must be on a separate piece of
30 paper, or in a separate paragraph of an emailed notice. We did not discuss whether
31 'combined' precluded the mailing of multiple notices in a single envelope, or in a
32 single email.

33 2. The Complaint in a judicial foreclosure state, or Notice of Sale in a
34 nonjudicial foreclosure state, must be delivered according to existing law, usually
35 by personal service. The requirement for additional electronic mail notice does
36 not displace the paper notices required by this act or other law. The creditor may,
37 but is not required to, send the notice by certified mail as well as by ordinary first
38 class mail.

1 **SECTION 204. RIGHT TO CURE DEFAULT.**

2 (a) A borrower may cure a default by tendering the amount or performance specified in
3 subsection (b) at any time until 24 hours before the [first] scheduled foreclosure sale. The right
4 to cure may not be exercised more than three times in a calendar year.

5 (b) To cure a default under this section, a borrower must:

6 (1) Tender in cash or immediately available funds all sums that would have been
7 due at the time of tender in the absence of default or acceleration;

8 (2) Perform or tender performance of any other duty under the obligation and
9 mortgage that would have been due in the absence of default or acceleration;

10 (3) Tender all reasonable costs and attorney fees of proceeding to foreclosure that
11 are (A) specified in writing by the creditor and (B) actually incurred prior to the date of tender.

12 (4) Tender any late fees, if provided for in the mortgage and permitted by [state
13 law].

14 (c) Cure of a default pursuant to this section restores the residential mortgage debtor to
15 the same position under the mortgage and the obligation it secures as if the default had not
16 occurred.

17 **Reporters' Drafting Notes**

18
19 1. The right of a residential mortgage borrower to cure a default has the
20 effect of de-accelerating the payments due after acceleration, but before a
21 completed foreclosure sale. Once a sale is completed, the interests of potential
22 purchasers militate against further extending the possibility of a borrower cure.
23 The borrower receives notice detailing the amounts needed to cure the default
24 pursuant to Section 202, and identifying any nonpayment defaults, such as failure
25 to maintain insurance. The right to cure is independent of any right to redeem.

26
27 2. This section does not alter contractual rights to cure that are stronger,
28 but the statutory right to cure may not be waived by contract. In the event of a
29 dispute between the creditor and a borrower concerning the amounts needed to
30 cure, or any nonmonetary performance that may be claimed as due, either party

1 may seek declaratory relief from an appropriate court, and if appropriate, a
2 temporary stay of any foreclosure sale to resolve the cure dispute.
3

4 3. This language is adapted from Pennsylvania's statute, 41 Pa. Stat. §404.
5 Using the sale date as the deadline for a cure provides an appropriate balance
6 between rights of creditors and borrowers.
7

8 4. In a subsequent draft, we should insert reference to any relevant state law
9 permitting or restricting late fees.
10

11 5. The comments should discuss what is meant by the 'first' scheduled
12 foreclosure date. Presumably, this means the date on which the court - or the foreclosing
13 creditor in a non-judicial foreclosure state - first notifies the borrower that title will pass,
14 or the date on which a foreclosure sale will occur or, under Connecticut's strict
15 foreclosure procedure, the borrower's law date, that being the date on which the borrower
16 will lose its equity of redemption. Postponement of any of those dates, for whatever
17 reason, should not extend the date by which the borrower may cure.
18

19 **SECTION 205. [NEW] UNKNOWN BORROWER OR OBLIGOR.** A creditor does
20 not owe a duty to notify a person under Sections 201 through 203 based on its status as creditor
21 to a person that is a borrower or obligor, unless the creditor knows all of the following:

- 22 (1) That the person is a borrower or obligor
23 (2) The identity of the person and
24 (3) How to communicate with the person.

25 **Reporters' Drafting Note**

26 New Section 205 is based on UCC § 9-605. Its purpose is to relieve the creditor
27 from duties owed to a borrower or debtor if the creditor does not know about that
28 person. This may be the case, for example, when an original borrower has sold the
29 property to a purchaser, or when the original borrower has died and that
30 borrower's interest has passed to an heir or devisee.

1 isn't any way around that the foreclosure dynamic is almost incapable of
2 thoughtful resolution. The mediations here are adversarial. The amount of money
3 at stake is tremendous. The business models of the foreclosure industry, including
4 the attorneys for the foreclosure mills, often preclude reasonable resolution. So
5 coming to a "fair" resolution by legislation is very, very difficult. I am not sure
6 we succeeded yet."

7
8 In discussions after the November meeting, Alfred Pollard, General Counsel of FHFA,
9 had suggested that it might be useful to convene a small group to consider an alternative
10 approach to the existing mediation draft; his proposal – that we try and identify a set of standards
11 for mediation that would work for both lenders and borrowers - was consistent with the
12 recommendations of Attorney Scheiwe Kulp and the panel of mediators, who had suggested a
13 'best practices' approach to mediation.
14

15 Pollard's suggestion tracked the June recommendations of the mediation panel; it also
16 offered a potential response to the concerns about the limitations of the Washington State statute,
17 and the enactment concerns posed by promulgation of a single substantive statute that might not
18 be widely accepted.
19

20 Accordingly, on December 17, 2012, a small group convened in Washington DC at the
21 offices of Commissioner Ring's law firm, Ober / Kaler. In the morning, the group included your
22 Committee Chair, our two Reporters, Attorney Heather Scheiwe Kulp, Professor Judith Fox from
23 Notre Dame Law School, and Attorney Jacqueline Hagerott, manager of the Dispute Resolution
24 program conducted by the Ohio Supreme Court. The group spent the morning developing a set
25 of principles that a state might employ in developing a facilitation program best suited to that
26 State.
27

28 In the afternoon we were joined by Vicky Vidal, a senior representative of the National
29 Mortgage Bankers' Association who had been present at the June meeting, and by Alfred Pollard
30 of FHFA. These eight rigorously discussed the principles developed in the morning and
31 significantly amended them.
32

33 What emerged was the following set of principles that might form the basis for further
34 discussion at the February 2013 meeting. The text presented below includes editing from
35 Professor Fox regarding what she recalled as comments from Attorney Pollard and Ms. Vidal; it
36 was further edited by Reporter White in his effort to more clearly frame the issues that persisted
37 at the end of our day long discussion and then finally edited by the Chair for inclusion in this
38 draft of the Act.
39

40 It would be a substantial overstatement to suggest that these principles enjoyed the
41 unanimous support of all eight participants on December 17. However, it is also fair to say that,
42 from the Chair's perspective, these principles enjoyed a far greater sense of support during our
43 meeting than the Chair has sensed in any of our discussions at prior committee meetings.
44

1 **FACILITATION OF ALTERNATIVES TO FORECLOSURE**
2 **PREAMBLE: FACILITATION – OBJECTIVES, STANDARDS, AND ISSUES FOR**
3 **RESOLUTION**
4

5 1. The consensus goal of facilitation is to create commercially reasonable alternatives to
6 foreclosure, which achieve sustainable outcomes, including "graceful exits."
7

8 2. ISSUE – lenders/servicers object to facilitation that is imposed uniformly without
9 regard to the fact that some or many homeowners have been fully evaluated for foreclosure
10 alternatives before any process begins.
11

12 3. The borrower should have access to a housing counselor (or a lawyer) to assist in the
13 facilitation process.
14

15 4. The process of bringing the parties together to achieve an alternative to foreclosure is
16 facilitation, not mediation, because some of the standards typically followed by mediators are not
17 appropriate. Facilitation is not merely a requirement that parties "meet and confer, " i.e. a
18 mandate merely for two-party settlement negotiations.
19

20 5. The neutral facilitator should disclose any conflicts of interest. A lawyer serving as a
21 facilitator must inform unrepresented borrowers that the lawyer is not representing them.
22

23 6. ISSUE: The initial draft provides for an opt-out process, i.e. automatic scheduling of a
24 facilitation meeting, with a process that goes forward unless the homeowner does not participate.
25 The other alternative is an 'opt-in' approach, which requires the homeowner to respond to a
26 notice by requesting a meeting; in the absence of a request, there is no facilitation process
27 scheduled.
28

29 7. ISSUES: TIMING – In an opt-in system, the borrower would have [30] days to
30 respond to the opportunity for facilitation (either by opting in or failing to opt out) after the
31 notice of right to facilitation is sent to the borrower, unless this time period conflicts with local
32 rules of procedure, in which case they need to be reconciled. The [30] day period begins when
33 notice is sent (either by service of process in judicial foreclosure or in a notice sent by the
34 facilitation agency in non-judicial foreclosure). The lender or servicer should receive notice that
35 a request is made in an opt-in facilitation system.
36

37 8. If the borrower makes a timely request for facilitation, the relevant agency must
38 initiate the facilitation process within 14 days [for example, by a referral order or other local
39 protocol.]
40

41 9. ISSUE: Dual Track: Lenders would prefer to be able to proceed with facilitation
42 voluntarily, before or during foreclosure, without delaying the foreclosure. Homeowner
43 advocates call for facilitation to proceed to conclusion before any steps can be taken to move
44 foreclosure forward.
45

46 10. Documentation information exchange.

1 a. The servicer must specify whatever documents it requires from the borrower
2 within [5] days after initiation of the facilitation process.

3
4 b. The borrower must provide the income and other documents required by the
5 servicer listed in (a) above to the servicer and the facilitator not less than [30] days before the
6 scheduled first facilitation session. If the borrower fails to substantially provide the documents
7 specified by the servicer within the time frame required by this paragraph, the facilitation process
8 terminates.

9 c. The servicer must provide to the borrower and the facilitation agency: (i) the
10 borrower's payment history from the date of default; (ii) itemized amounts due on the loan,
11 including all fees.

12 d. The servicer should provide the facilitator its decision, including the inputs and results of any
13 net present value calculations it relies on in deciding not to offer any particular loss mitigation
14 alternative.

15
16 11. ISSUE – lenders/servicers would exclude fees accrued but not yet billed]; and (iii)
17 investor restrictions leading to denial of loss mitigation.

18
19 12. ISSUE: lenders prefer to limit this to “non-public” investor restrictions, presumably
20 because some investor restrictions are available in securities filings, or perhaps GSE handbooks].

21 13. The first facilitation session must take place within [XX] days after initiation of the
22 facilitation process.

23
24 14. ISSUE- [Lenders advocate a time limit to terminate the facilitation process.
25 Mediators experienced with existing programs point out that 90 days, for example, would in
26 most cases be inadequate to obtain complete documentation from a borrower and allow a
27 servicer to review and make a determination on appropriate loss mitigation options.] The
28 facilitation process terminates [XX] days after initiation of the facilitation process unless the
29 XX-day period is extended by the parties' agreement or for good cause.

30
31 15. ISSUE: Dual Track – lenders/servicers advocate that foreclosure be permitted to
32 move forward, with only a stay of the final foreclosure sale, while borrowers and mediators
33 advocate halting all steps in the foreclosure process while facilitation runs its course. Lenders
34 also wish to be able to request a termination of any stay for good cause at any point.

35
36 16. Participation – servicer must have lawyer and servicer representative present in
37 person or by telephone or teleconference, servicer must evaluate loss mitigation and make
38 decision as required by CFPB rule.

39
40 17. ISSUE – ELIGIBILITY Lenders/servicers advocate limiting facilitation to owner-
41 occupants, barring investors, and requiring owner to demonstrate occupancy for period of time
42 prior to foreclosure.

43
44 18. Standards of practice for facilitators: this issue needs development. There is
45 consensus that facilitator conflicts of interest should be avoided or disclosed. Traditional
46 mediator standards are problematic in some cases. For example, mediators traditionally do not

1 disclose anything that takes place during facilitation or report to a court on the parties' conduct,
2 whereas a facilitator may need to report on either party's conduct so that a court can decide
3 whether to permit foreclosure to proceed, or to impose sanctions.
4

5 19. Proceedings should be confidential, with appropriate exceptions to permit reporting
6 outcomes and/or noncompliance with rules to the court or supervising agency.
7

8 20. States should establish programs to provide appropriate training and continuing
9 education of facilitators.
10

11 21. All agreements for foreclosure alternatives should be memorialized in writing and
12 signed by both parties to minimize later disputes.
13

14 22. Facilitation agencies should collect enough data to determine the outcomes of
15 facilitation and whether it is achieving its objectives.
16

17 23. States should provide adequate funding to train and provide facilitators and for the
18 associated agency or court supervision.
19

20 24. Original copies of documents (as opposed to true copies) should not be needed during
21 facilitation. Issues about authenticity and possession should be resolved separately in litigation if
22 need be.
23

24 **Reporters' Drafting Notes**

25

26 1. A persistent issue raised by several commentators, including the ABA advisor, is the
27 absence in the current draft of any remedy for a servicer's failure to comply with the document
28 exchange requirements or other failure to participate in the facilitation process.
29

30 2. The current text of these principles in paragraphs 9 and 15 both address the issue of
31 dual tracking, but in different ways.
32

33 **The balance of the text in article 3 is much of the material as is appeared in the**
34 **November text, including all of sections 301 through 304.**
35

36 3. What policy choices are embedded in this particular version of the 'mediation'
37 process? What are some of the implications of this set of choices? Our basic set of choices here
38 involves these discrete elements:
39

40 First, by mandating 'mediation' before foreclosure may commence, we eliminate the so-
41 called 'dual tracking' problem, where borrowers find themselves simultaneously in a mortgage
42 modification discussion and a defendant in a foreclosure action.
43

44 Second, by creating an 'opt-out' rather than an 'opt-in' system, we are creating a system
45 that will surely serve more borrowers' interests, but will create potentially serious financial cost
46 issues in the states, for which we have no ready answer. Given our time constraints, we did not

1 draft alternatives.

2
3 Third, we were torn between the June discussion suggesting that the Act incorporate ‘best
4 practices’ for ‘mediation’ and the more substantive provisions for mediation found in the laws of
5 some states. For purposes of this draft, we chose to incorporate some of the new mandated
6 documentation of ‘net present value’ in the State of Washington, as detailed in the current text of
7 Section 303 (b).
8

9 The Chair’s memorandum accompanying this draft includes explanatory materials
10 describing the NPV process and the negotiation process by which both lender and borrower
11 representatives in that State apparently reached an agreement to support this process in
12 Washington.
13

14 To refresh the Committee’s recollection,¹ the fundamental concept here is that the lender,
15 using either the Treasury’s ‘Mod In a Box’ calculator or its own proprietary formula, is expected
16 to gather the borrower’s income and expense information, together with its own calculations of
17 the mortgaged property’s likely sales value in foreclosure plus the costs of foreclosure.
18 Simultaneously, the lender is expected, at least under federal HAMP standards, to determine

¹ 1 FHFA has published a document entitled ‘**Review of Options Available for Underwater Borrowers and Principal Forgiveness**, which was released on July 31, 2012. At page 8, the document describes the HAMP program in generally understandable ‘lay’ terms:

“1. For HAMP, an affordable payment is achieved by taking specified sequential steps (called the waterfall), as needed, in order to bring a troubled borrower’s monthly payment down to 31 percent of their gross monthly income. Specifically, servicers:

- ☐ Capitalize the arrearages, including accrued interest and escrow advances.
- ☐ Reduce the interest rate in increments of 1/8 to get as close as possible to 31 percent of the homeowners gross monthly income with the lowest possible interest rate set at 2 percent.
- ☐ If reducing the interest rate does not achieve an affordable monthly payment, servicers then extend the term and re-amortize the mortgage by up to 480 months (40 years).
- ☐ If reducing the interest rate *and* extending the term does not achieve an affordable monthly payment, servicers then provide principal forbearance down to 115 percent of the property’s current market value or as much as 30 percent of the unpaid principal, whichever is greater.

2 If a borrower does not qualify for HAMP, the Enterprises’ then look to employ a proprietary modification, sometimes referred to as a “standard modification.” The features of a proprietary modification are also applied sequentially to a loan’s mark-to-market LTV and include:

- ☐ Capitalizing the arrearage, including accrued interest and escrow advances.
- ☐ Providing principal forbearance down to 115 percent of the property’s current value or as much as 30 percent of the unpaid principal balance, whichever is less.
- ☐ Setting the interest rate to a fixed-rate mortgage, currently at 4.625 percent.
- ☐ Extending the term to 480 months (40 years).

After calculating the modified payment terms, the mortgage loan must result in at least a 10 percent reduction in the homeowner’s principal and interest payment.”

1 whether a loan modification that reduces the borrower's monthly payment to a sum which is no
2 greater than 31% of the borrower's net monthly income, has, on a Net Present Value basis, a
3 greater value to the investor than would the value the investor would receive after foreclosure of
4 the mortgaged property and its subsequent sale.

5
6 The detailed explanation offered by the United States Treasury Department, entitled *Home*
7 *Affordable Modification Program, Base Net Present Value (NPV) Model V5.0, Model*
8 *Documentation*, Effective: June 1, 2012, can be found at this link:
9 https://www.hmpadmin.com/portal/programs/docs/hamp_servicer/npvmodeldocumentationv50.pdf

10
11 The drafters acknowledge that most states' current statutes differ dramatically from the
12 approach taken by the State of Washington and broadly reflected in Section 303 of this Act. For
13 that reason, in the absence of a mandate imposed at the federal level, we acknowledge that it
14 would be difficult conceptually to mandate that each state engage the services of a third party
15 'mediator' intended to independently review the servicers' determination of net present value, as
16 they are now required to do under FHFA regulations, the law of states such as Washington and
17 the Attorney Generals' Servicer settlement.

18
19 At the same time, in the absence of some means of ensuring that the borrowers' interests
20 are being properly calculated by servicers who, by many accounts, have an economic interest in
21 preferring foreclosure to loan modification, it is not realistic to assume that borrowers will have
22 the independent capacity to consider the accuracy of that calculation.

23 24 **SECTION 301. NOTICE OF FACILITATION.**

25 (a) Before any creditor may commence foreclosure, the creditor must give the borrower
26 notice of facilitation.

27 (b) If the facilitation agency, by rule, establishes a procedure for the facilitation agency
28 to send notice of facilitation to borrowers, the creditor must request that a notice of facilitation be
29 sent by the facilitation agency to the creditor and the borrower. If the facilitation agency does
30 not send the notice, the creditor shall send the notice.

31 (c) The notice of facilitation must include the following:

32 (1) The names, addresses and telephone numbers of the housing counseling
33 agencies, lawyer referral services and legal aid agencies serving the borrower's geographic area
34 that are designated from time to time by the facilitation agency.

35 (2) The name, address, telephone number and e-mail address of the person

1 designated by the creditor as the borrower's single point of contact, if a person has been so
2 designated.

3 (3) The location, date and time at which the borrower may appear for an in-person
4 facilitation session with the creditor, under the supervision of the facilitation agency, together
5 with instructions on how to reschedule the in-person facilitation.

6 (4) A description of all documents the borrower should bring to the facilitation
7 session, in accordance with rules promulgated by the facilitation agency.

8 **Reporters' Drafting Notes**

9
10 Between 2007 and 2012 eighteen states adopted statewide foreclosure diversion or
11 mediation programs, and local jurisdictions in at least eight additional states have established
12 similar programs. The programs vary greatly in their timing and design, and exist in both
13 judicial and nonjudicial foreclosure states. Most programs in judicial foreclosure states call for
14 intervention after a foreclosure complaint is filed. While most stakeholders recognize that
15 starting mediation or facilitation earlier in the process would increase the chances of success and
16 reduce costs, most existing state laws do not provide a means to initiate facilitation before the
17 judicial process begins. Pre-foreclosure facilitation permits early sorting of foreclosure cases,
18 into those where the borrower wants to find a solution other than foreclosure, and those cases
19 that are uncontested or where there is no realistic alternative to foreclosure.

20
21 Automatic scheduling of facilitation meetings is the opt-out approach now used in
22 Connecticut, Philadelphia County and a number of counties in Indiana, among others. The opt-
23 in alternative used in other jurisdictions calls for the notice to inform the borrowers that they
24 have a right to request a facilitation conference within a designated period, and the specific
25 means for requesting the conference, by telephone, internet or other suitable means established
26 by the facilitation agency. Experience has shown that the opt-out approach, with automatic
27 scheduling of foreclosure facilitation, results in much higher rates of homeowner response, and
28 ultimately higher success rates in preventing foreclosure sales and maximizing creditor
29 recoveries.

30 **SECTION 302. DUTY TO PARTICIPATE IN FACILITATION AND**

31
32 **NEGOTIATE IN GOOD FAITH.** Both parties must negotiate in good faith to seek a
33 resolution other than a foreclosure sale. The creditor shall inform the borrower of the loss
34 mitigation options that are available to the borrower. The borrower shall provide reasonably
35 available financial and other information to permit the creditor to evaluate any loss mitigation

option. The creditor shall notify the borrower and the mediator, facilitator or facilitation agency of its willingness or refusal to offer any loss mitigation option requested by the borrower, and of the reasons for any refusal and the information on which the refusal is based. The creditor may not charge the borrower any fees for the facilitation process. The parties shall comply with any scheduling order established by the facilitation agency.

Reporters' Drafting Notes

As provided in Section 303, the facilitation agency may impose additional requirements on the parties, for example requiring the creditor or its agent to appear in person or to have a person with authority to approve loss mitigation alternatives available by telephone at the time of the facilitation session, to perform a net present value analysis, to disclose the assumptions on which the analysis is based, or requiring borrowers to meet with a housing counselor to qualify for facilitation. The agency will also regulate procedural matters, such as time limits for exchanging documents, scheduling and concluding facilitation meetings, reports by mediators or facilitators, and the like. States should continue to have flexibility in the design and implementation of facilitation programs.

SECTION 303. STANDARDS FOR CONDUCT OF FACILITATION.

(a) The facilitation agency shall adopt regulations pursuant to [insert reference to State Administrative Procedures Act or, if the facilitation agency is the judicial system, to the rules of court] describing the facilitation process.

(b) In addition to other regulations that the agency may adopt, in order to assist the parties in addressing issues of foreclosure, the facilitator must require the participants to consider the following:

(1) The borrower's current and future economic circumstances, including the borrower's current and future income, debts, and obligations for the previous sixty days or greater time period as determined by the mediator;

(2) The net present value of receiving payments pursuant to a modified mortgage loan as compared to the anticipated net recovery following foreclosure;

(3) Any affordable loan modification calculation and net present value calculation when required under any federal mortgage relief program, including the home affordable modification program (HAMP) as applicable to government-sponsored enterprise and nongovernment-sponsored enterprise loans and any HAMP-related modification program applicable to loans insured by the federal housing administration, the veterans administration, and the rural housing service. If such a calculation is not required, then the creditor must use the current calculations, assumptions, and forms that are established by the federal deposit insurance corporation and published in the federal deposit insurance corporation loan modification program guide.

Chair's Note: Sub-section (b) is excerpted from a statute enacted earlier this year in the State of Washington; See RCW 61.24.163(7). As reported by Attorney Bruce Neas, who was involved in the ultimate legislative negotiations:

“In the negotiations leading up to the compromise bill, an operating premise was that in order to make mediation effective for borrowers, there would have to be a series of specific requirements and some standards to apply at the mediation. Merely having an opportunity to discuss the issues leading up to a foreclosure would be meaningless. That had already been proven by the Legislature’s adoption of a “meet and confer” requirement as a condition precedent to a foreclosure. I should add that Washington being a non-judicial foreclosure state makes the necessity for a third party intervention acute. Primarily, the NPV test is a disclosure mechanism for the facilitation of a productive mediation. Under RCW 61.24.163(7), ‘The participants in mediation must address the issues of foreclosure that may enable the borrower and the beneficiary to reach a resolution, including but not limited to reinstatement, modification of the loan, restructuring of the debt, or some other workout plan. To assist the parties in addressing issues of foreclosure, the mediator must require the participants to consider’ the information described in the statute.”

Attorney Neas further informed the Chair that the lending community signed off on the compromise language; I have no knowledge of the political environment in which such cooperation was offered.

SECTION 304. NO FORECLOSURE DURING FACILITATION.

(a) After the facilitation process has begun, the creditor may not commence foreclosure

1 [or other legal action] to enforce the obligation unless:

2 (1) the borrower does not respond to the facilitation notice, by either appearing at
3 the scheduled facilitation session or by sending a written request for loss mitigation to the
4 creditor within 60 days of the facilitation notice; or

5 (2) The facilitation agency provides the creditor with a notice that the parties have
6 negotiated in good faith and reached an impasse, or that the borrower has failed to participate or
7 provide required information after a reasonable opportunity.

8 (b) Notwithstanding the limitations in subsection (a), the creditor may proceed to enforce
9 its mortgage 90 days] after the notice required by Section 301 is sent, unless the parties agree to
10 continue the facilitation process or the [facilitation agency][Court] directs the parties to continue
11 the facilitation process for good cause shown.

12 **Reporters' Drafting Notes**

13
14 1. Numerous states have recently enacted mandatory facilitation or loss
15 mitigation laws whose object is to delay or prevent foreclosure until the borrower
16 has had the opportunity to request loss mitigation or facilitation: Arkansas Act
17 885 (2011) Sec 3, Ark Code 18-50-104 (beneficiary must certify to selling
18 attorney or trustee that it has notified borrower of ineligibility for loss mitigation
19 options before nonjudicial sale); California Assembly Bill 278 (enacted July 11,
20 2012, prohibits foreclosure when loan modification request is pending); Idaho
21 Code 45-1506, HB 331 Idaho now requires notice of right to apply for loan
22 modification and bars nonjudicial sale until creditor responds to borrower's
23 request); Indiana Act 170 of 2011 (same; also prohibits servicer or attorney fees
24 for facilitation or loss mitigation); Massachusetts Chapter 194 of Acts of 2012 (
25 creditor must offer mortgage modification prior to foreclosing, if modification
26 would maximize value for mortgagee); Michigan Compiled Laws §3205a
27 (amended Act 302 of 2011); Nevada Rev. Stat. §107.086; Washington Chapter 58
28 Laws of 2011, amending RCW 61.24 (delays foreclosure 90 days if borrower
29 requests meeting with creditor to request loss mitigation, and for cases referred by
30 housing counselor to facilitation, until the parties comply with duty to mediate in
31 good faith). Requiring a complete facilitation process prior to initiation of
32 foreclosure allows necessary foreclosures to go forward promptly and efficiently
33 after cases suitable for other resolutions are identified and resolved.

34
35 2. The Committee should consider the bracketed text in subsection (a)

1 concerning the ability of the lender to take ‘other action’ during the facilitation
2 process.

3 4 **ARTICLE 4**

5 **RIGHT TO FORECLOSE, EFFECTS OF FORECLOSURE**

6 **SECTION 401. [Alternative #1] RIGHT TO FORECLOSE.** [This alternative
7 designates the person with the right to enforce the instrument under UCC Article 3 as the person
8 with the right to foreclose the mortgage when the obligation is set forth in a negotiable
9 instrument.]

10 (a) Only a creditor who has the right to foreclose may commence a foreclosure.

11 (b) A creditor has a right to foreclose its mortgage after default in the obligation if all
12 conditions required by the mortgage agreement as prerequisites to foreclosure are satisfied and
13 one of the following conditions is met:

14 (1) If the obligation is evidenced by an instrument, the person is

15 (A) the holder,

16 (B) a nonholder in possession of the instrument who has the rights of a
17 holder, or

18 (C) a person not in possession of the instrument who establishes the right
19 to enforce that instrument due to its loss or destruction by meeting the requirements of Section 4-
20 104.

21 (2) If the obligation is not evidenced by an instrument, the person is the owner of
22 the obligation.

23 (c) In a judicial foreclosure proceeding, the plaintiff must allege and prove facts
24 demonstrating that it has the right to foreclose under subsection (b). If the plaintiff relies upon
25 an instrument, the complaint must include a copy or image of the instrument and an allegation

1 that the original is either: (i) in the possession of the plaintiff; (ii) in the possession of the
2 plaintiff's principal; or (iii) lost [or destroyed], in which case the complaint must also include a
3 lost instrument affidavit that complies with [insert UCC reference].

4 (d) In a nonjudicial foreclosing proceeding, the creditor must prepare an affidavit
5 attesting to facts demonstrating that it has the right to foreclose under subsection (b), which
6 affidavit shall be included with the notice of foreclosure required by section 202.

7 (e) In a judicial or nonjudicial foreclosing proceeding, a person who has the right to
8 foreclose may exercise that right by authorizing an agent to foreclose in an authenticated record.
9 In that event, the complaint or affidavit described in subsection (c) or (d) shall name the principal
10 and the agent.

11 **Reporters' Drafting Notes**

12
13 1. Section 4-101(b)(1) follows the language of UCC § 3-301, which
14 defines who is "person entitled to enforce" an instrument. When the payee of the
15 negotiable instrument has retained possession of the instrument, that person has
16 the right to foreclose. When the payee has transferred possession of the
17 negotiable instrument to another person, the facts must be examined to determine
18 who has the right to enforce the note. The subsequent possessor may become a
19 holder under UCC Article 3 by obtaining a special endorsement or blank
20 endorsement, but this section does not require that a subsequent possessor become
21 a holder in order to acquire the right to foreclose. Such a subsequent possessor
22 may be entitled to enforce the note, but will have to allege and prove facts that are
23 sufficient to establish the right to enforce.
24

25 2. Subsection (b)(2) includes situations in which the secured obligation is
26 evidenced by an instrument that is not negotiable and situations in which the
27 obligation is not evidenced by any type of instrument authenticated by the debtor.
28 As an example of the former, an owner may sign a promissory note that has terms
29 that makes the note nonnegotiable. As an example of the latter, under the law of
30 some states an installment land contract creates a mortgage relationship between
31 the parties, in which the vendee's obligation to pay the price usually is not
32 reflected in an instrument. In all such cases, the owner of the obligation who has
33 the right to foreclose will be either the original obligee or an assignee.
34

35 3. In judicial foreclosure, under existing law the creditor generally must
36 confirm possession or account for possession of the original note at the time of

1 filing or prior to the foreclosure sale. In some nonjudicial foreclosure states, the
2 law appears not to require confirmation of possession of the original note prior to
3 commencement of foreclosure proceedings or the sale. This section requires that
4 the foreclosing person have possession of the instrument prior to the
5 commencement of foreclosure, whether the proceeding is judicial or nonjudicial,
6 unless that person prepares a lost note affidavit meeting the requirements of
7 Section 4-103.
8

9 4. This section does not state a separate rule for determining when a
10 creditor who holds a security interest in a note has the right to foreclose. UCC
11 Article 9 covers both sales of instruments and assignments of instruments that
12 secure an obligation of the assignor. A creditor who takes possession of a
13 negotiable instrument will acquire the right to foreclose. A creditor who takes
14 possession of an instrument that is not negotiable ordinarily will not acquire the
15 right to foreclose; the issue turns on whether the rights granted to the creditor are
16 sufficient to make the creditor the “owner” of the obligation (in other words, a
17 “buyer” of the payment rights).
18

19 5. Multiple persons may hold the right to foreclose a mortgage. Other law,
20 including UCC Article 3 and the law of agency, determines whether the right to
21 foreclose may be exercised by fewer than all such persons.
22

23 6. If it is unclear whether the secured obligation is evidenced by a
24 negotiable instrument or by an instrument that is not negotiable, the creditor may
25 choose to proceed by complying with both subsections (b)(1) and (b)(2). The
26 creditor should state whether it is relying on subsection (b)(1), (b)(2), or both in
27 the alternative.
28

29 7. Under subsection (c) the creditor’s production of the original negotiable
30 instrument is not necessary at the time of the filing of a complaint in a judicial
31 foreclosure. Production of the original would later become appropriate if, during
32 the course of the proceedings, the borrower seeks further demonstration of the
33 copy’s authenticity or the whereabouts of the original. Similarly, in a nonjudicial
34 foreclosure, if there are subsequent judicial proceedings, a court may decide to
35 order production of the original instrument if necessary to resolve a particular
36 issue.
37

38 8. Subsection (e) authorizes the person who has the right to foreclose to
39 exercise that right through an agent. By requiring a description of the agency it
40 does not permit the principal to remain undisclosed. An agent authorized to
41 foreclose may be a loan servicer who has a pre-existing contractual relationship
42 with the creditor, or any other person appointed at any time. If the secured
43 obligation is evidenced by a negotiable instrument, the agent or the principal (the
44 person entitled to enforce the note) may hold and retain possession of the note.
45 Subsection (e) is not intended to change existing laws that authorize a third
46 person, such as a trustee under a deed of trust, to foreclose in nonjudicial

1 proceedings. In such circumstances, subsection (e) allows the beneficiary to
2 appoint an agent, but does not speak to the procedure for appointing a substitute
3 trustee.
4

5 9. Section 401 as drafted, allowing an agent to foreclose, is consistent
6 with the standing decision in *Sprint Communications Co. v. APCC Services,*
7 *Inc.*, 554 U.S. 269 (2008). There, payphone operators had assigned claims for
8 compensation from long-distance carriers to collection firms. In *Sprint* the Court
9 permitted an assignee of a legal claim for money to pursue that claim in federal
10 court, even when the assignee had promised to remit the proceeds of the litigation
11 to the assignor.
12

13 **SECTION 401. [New Alternative #2] RIGHT TO FORECLOSE.** [This alternative
14 provides that only the person who owns the obligation secured by the mortgage has the right to
15 foreclose that mortgage.]

16 (a) Only a creditor who has the right to foreclose may commence a foreclosure.

17 (b) A creditor has a right to foreclose its mortgage after default in the obligation if:

18 (1) the creditor is the owner of the obligation;

19 (2) all the conditions required by the mortgage agreement as prerequisites to
20 foreclosure are satisfied; and

21 (3) if the obligation is evidenced by an instrument, the creditor has possession of
22 the instrument or establishes the right to enforce that instrument due to its loss or destruction by
23 meeting the requirements of Section 4-104.

24 (c) In a judicial foreclosure proceeding, the plaintiff must allege and prove facts
25 demonstrating that it has the right to foreclose under subsection (b). If the plaintiff relies upon
26 an instrument, the complaint must include a copy or image of the instrument and an allegation
27 that the original is either (i) in the possession of the plaintiff or (ii) lost [or destroyed], in which
28 case the complaint must also include a lost instrument affidavit that complies with [insert UCC
29 reference].

1 (d) In a nonjudicial foreclosing proceeding, the creditor must prepare an affidavit
2 attesting to facts demonstrating that it has the right to foreclose under subsection (b), which
3 affidavit shall be included with the notice of foreclosure required by section 202.

4 **Reporters' Drafting Notes**

5
6 1. Section 4-101(b) requires that the person foreclosing the mortgage own
7 the obligation secured by that mortgage. When the original mortgagee has
8 assigned beneficial ownership of the obligation to another person, the assignee is
9 the only person who has the right to foreclose.

10
11 2. This Section does not allow an agent of the owner to foreclose in the
12 name of the agent. This Section, however, is not intended to change the current
13 practice in some nonjudicial foreclosure states, in which a third party such a
14 trustee initiates foreclosure proceedings for the benefit of the creditor. In such
15 states the record prepared by the trustee or other third party must disclose the
16 owner of the obligation.

17 **SECTION 402. TRANSFER OF MORTGAGE.**

18
19 (a) A transfer of an obligation secured by a mortgage also operates to transfer the
20 mortgage.

21 **DRAFTER'S NOTE**

22
23 Sections 401 and 402 must both be consulted to determine whether a particular
24 transferee is a person who is entitled to foreclose. After the Drafting Committee
25 makes choices as to the alternatives stated in both sections, as a matter of style it
26 may be expeditious to consolidate the two sections.

27
28 (b) [**Alternative #1**] If the transfer is accomplished by assignment, the assignment may
29 be recorded in the office in which mortgages are recorded, but recordation is not required for the
30 new creditor to foreclose the mortgage pursuant to Section 401.

31 (b) [**Alternative #2**] If the transfer is accomplished by assignment, the assignment may
32 be recorded in the office in which mortgages are recorded. After the transfer of an obligation to a
33 new owner, the new creditor may foreclose the mortgage only after recordation of the
34 assignment or other appropriate document in the office in which mortgages are recorded.

Reporters' Drafting Notes

1. Subsection (a) adopts the principle stated in UCC § 9-203(g), which provides that an Article 9 transfer of a instrument also transfers the mortgage (more formally, § 9-203(g) provides that attachment of a security interest in a right to payment or performance secured by personal or real property automatically transfers the security interest to the secured party). Section 9-203(g) covers sales of negotiable instruments, other instruments, and payment intangibles, as well as lending transactions in which those rights serve as collateral to secure an obligation of the transferor.

Subsection (a) is broader than § 9-203(g); it applies regardless of whether the transferee obtains an attached Article 9 security interest. It also encompasses involuntary transfers such as inheritance and judicial sales. Restatement (Third) of Property (Mortgages) § 5.4(a) (1997) proposes a similar rule: "A transfer of an obligation secured by a mortgage also transfers the mortgage unless the parties to the transfer agree otherwise." Under the Restatement rule, parties to the transfer may agree otherwise, but this section does not permit severance of the obligation from the mortgage, following UCC § 9-203(g) and common-law authorities in a number of states.

2. When the foreclosing party is not the originating creditor there is conflicting state law, both in judicial foreclosure and nonjudicial foreclosure states, as to (1) whether the foreclosing party must have an express assignment of the mortgage, or a chain of assignments running back to the original mortgagee, and (2) whether that assignment or the chain of assignments must be recorded in the county land records.

In some states, a statute explicitly requires a recorded assignment. E.g., Ga. Code § 44-14-162: "The security instrument or assignment thereof vesting the secured creditor with title to the security instrument shall be filed prior to the time of sale in the [county land records]." In many states, judicial decisions going in both directions interpret statutes that do not on their face provide immediately obvious answers to these questions. E.g, *In re Vasquez*, 266 P.3d 1053 (Ariz. 2011) (recording assignments of deeds of trust is not required, although trustee must record notice of trustee's sale); *U.S. Bank Nat. Ass'n v. Ibanez*, 941 N.E.2d 40 (Mass. 2011) (requiring written chain of assignments).

3. The two alternatives in subsection (b) provide different answers to the fundamental question of whether a creditor may foreclose a mortgage in the absence of a recorded chain of title in the land records demonstrating that the creditor owns the mortgage.

The first alternative in this subsection adopts the position that an express assignment is unnecessary; note that subsection (a) implies an assignment upon a transfer of the obligation. In addition, this alternative for subsection (b) adopts

1 the position that recordation of an assignment (or notice of an implied
2 assignment) is not a prerequisite for foreclosure.
3

4 4. In contrast, Alternative # 2 in subsection (b) confirms the rule in many
5 states – a rule which is intended to protect the interests of borrowers and
6 subsequent purchasers – that a written assignment in favor of the foreclosing
7 creditor is a necessary pre-condition to instituting a foreclosure. Because note
8 transfers are not generally recorded, advocates for mandating this outcome
9 believe that recording of mortgage assignments is necessary to provide a complete
10 public record of land title transfers, to protect borrowers from double liability, and
11 to prevent post-sale title challenges.
12

13 Under Alternative #2, a transfer of the note without an accompanying
14 express assignment of the note does not deprive the assignee of the ability to
15 foreclose. The principle that “the mortgage follows the note”, e.g., Restatement of
16 Property §5.4(a), means that the current holder or owner of the mortgage
17 obligation has an equitable right to obtain and record an assignment of the
18 mortgage or deed of trust from any prior record mortgagee, mortgage assignee or
19 beneficial owner, unless the parties intended otherwise.
20

21 Under the second alternative, the complaint or affidavit required by
22 Section 401 must identify and describe all necessary assignments and
23 substitutions. Recordation of a separate assignment, or endorsement on the
24 mortgage itself, provides record notice of the chain of mortgage ownership, and
25 insulates the foreclosure sale purchaser from attacks on title based on transfer
26 defects. The mortgage transfer should be described in the complaint in a judicial
27 proceeding or the affidavit in a nonjudicial proceeding and appear of record prior
28 to the recording of the foreclosure sale deed. It is sufficient to record an
29 assignment to the foreclosing person’s agent, so long as the agency is described in
30 the complaint or affidavit. When the mortgage is in the form of a deed of trust,
31 transfer is generally effected by recording a substitution of trustee. The recorded
32 substitution of trustee must describe any transfers of beneficial ownership.
33

34 **SECTION 403. LOST INSTRUMENT; AFFIDAVIT.**

35 (a) [**Alternative #1**] If an instrument secured by a mortgage has been lost [or
36 destroyed], the creditor may foreclose the mortgage only if the creditor makes an affidavit
37 attesting to the facts stated in [UCC § 3-309(a)(1) through (a)(3)].

38 (a) [**Alternative #2**] If an instrument secured by a mortgage has been lost [or
39 destroyed], the creditor may foreclose the mortgage only if the creditor was entitled to enforce
40 the instrument when loss of possession occurred and makes an affidavit attesting to the facts

1 stated in [UCC § 3-309(a)].

2 (b) If the creditor makes an affidavit pursuant to subsection (a), the obligor is entitled to
3 adequate protection against loss that might occur by reason of a claim by another person to
4 enforce the instrument, and the affidavit shall include a written indemnity from the creditor
5 against loss by the obligor. Whether adequate protection requires more than the indemnity is
6 determined by the facts of each case. Upon motion by the obligor, the court may also require that
7 additional adequate protection be provided by any reasonable means.. (c) In a judicial
8 foreclosure proceeding, the affidavit described in subsection (a) shall be filed with the complaint.

9 (d) In a nonjudicial foreclosing proceeding, the creditor shall include the affidavit
10 described in subsection (a) with the notice of foreclosure required by Section 2-103 together with
11 a statement that the borrower has the right to petition the [name of appropriate court] where the
12 property is located for an order requiring the creditor to provide adequate protection against a
13 claim by another person.

14 **Reporters' Drafting Notes**

15
16 1. The policy choice facing the Drafting Committee, of course, is the
17 extent to which this Act should give license to foreclosing creditors who sign
18 "lost" or "destroyed" note affidavits without ever having possessed either the
19 original or a certified copy of the note, and without any evidence of a written
20 assignment of the underlying mortgage to that creditor. For comparison purposes,
21 even under the "business records" exception to conventional hearsay rules, it is
22 not clear that unsigned contracts would be admissible evidence that the parties
23 named in the contract would be entitled to enforce it. Further, if one is to speak of
24 "moral hazard," there is little doubt that a liberal "lost note" affidavit policy offers
25 a powerful incentive to the first note holder intentionally to discard the original
26 note and thereby avoid the cost and uncertainty of maintaining thousands of
27 original paper notes. It would be useful for the Drafting Committee to discuss
28 this subject, in light of the potential for fraud against a borrower.

29
30 2. Subsection (a) offers two alternatives to deal with the problem of lost or
31 destroyed promissory notes, both of which interface with the UCC Article 3
32 treatment of lost or destroyed negotiable instruments. The first alternative is
33 compatible with the 2002 amendments to Article 3. In specifying when a creditor

1 is entitled to enforce a negotiable instrument secured by mortgage
2 notwithstanding its inability to confirm possession of the instrument, subsection
3 (a) tracks the requirements of UCC § 3-309 (2002). In states that have adopted
4 the 2002 amendments to Article 3, Section 3-309 makes it clear that the person
5 who lost possession may be a predecessor of the creditor who seeks to enforce the
6 instrument.
7

8 3. Alternative #2 to subsection (a) is consistent with the text of UCC § 3-
9 309 prior to the 2002 amendments. Most states have not yet adopted the 2002
10 amendments. Most of these states follow the 1990 Official Text of Article 3. In
11 these states there are a few cases holding that the affidavit must be signed by the
12 person who lost the note. See, e.g., *Atlantic Nat. Trust, LLC v. McNamee*, 984
13 So. 2d 375 (Ala. 2007) (examining prior cases; holding that assignee of
14 promissory note that was not in possession when lost may enforce the note).
15 Alternative #2 requires the creditor who forecloses be the person who lost or
16 destroyed the note and who executes the affidavit.
17

18 4. In some states, the circumstances in which a creditor is allowed to
19 enforce an unavailable instrument are broader than under either the 2002 version
20 or the earlier version of UCC § 3-309. E.g., Va. Code § 55-59.1(B) (“[i]f a note or
21 other evidence of indebtedness secured by a deed of trust is lost or for any reason
22 cannot be produced”). In some states, the circumstances are more restricted
23 because the creditor’s affidavit must attest to additional facts. E.g., Md. Code §
24 7-105.1 (affidavit not sufficient unless it “(1) Identifies the owner of the debt
25 instrument and states from whom and the date on which the owner acquired
26 ownership; (2) States why a copy of the debt instrument cannot be produced; and
27 (3) Describes the good faith efforts made to produce a copy of the debt
28 instrument.”).
29

30 5. When the loan documents executed by the parties did not include a
31 negotiable instrument, the creditor seeking to foreclose may or may not possess
32 an original writing or record (including a counterpart) that evidences the
33 obligation. This section does not require an affidavit for a creditor who lacks
34 possession of such an original record. Some states require “lost note affidavits”
35 under these circumstances. E.g., Va. Code § 8.01-32 (“any past-due lost bond,
36 note, contract, open account agreement, or other written evidence of debt”); Va.
37 Code § 55-59.1(B) (“note or other evidence of indebtedness”).
38

39 6. This section does not discuss the evidentiary effect of the affidavit in
40 judicial proceedings. Some states have statutory law on point. For example, an
41 Alabama statute provides that a lost note affidavit “must be received as
42 presumptive evidence both of the contents and loss or destruction of such
43 instrument, unless the defendant by answer, verified by affidavit, denies the
44 execution of such bond, note or bill or the endorsement, acceptance, or the
45 contents thereof, in which case proof of such execution, endorsement, acceptance,
46 or contents must be made by the plaintiff.” Ala. Code § 6-5-284.

1 7. Some statutes dealing with lost note affidavits appear to require an
2 affidavit only if the creditor is unable to produce the original *or a copy* of the
3 instrument.
4

5 8. Subsection (b) follows UCC § 3-309(b), which requires adequate
6 protection for the obligor from the risk that at some point in the future the
7 instrument will surface and its possessor will assert the right to be paid. (UCC §
8 3-309(b) was not affected by the 2002 amendments to Article 3.) Subsection (b)
9 requires that the affidavit include a written indemnity, binding the creditor, to
10 protect all obligors against the risk that a person other than the creditor will seek
11 to enforce the instrument. This indemnity serves to reinforce the rights that the
12 obligor already has under principles of restitution and unjust enrichment. See,
13 e.g., Restatement (Third) of Restitution and Unjust Enrichment § 6 (2011):
14 “*Payment Of Money Not Due*. Payment by mistake gives the payor a claim in
15 restitution against the recipient to the extent payment was not due.” In appropriate
16 cases, a court may require a bond in addition to a written indemnity.
17

18 **SECTION 404 . PUBLIC ADVERTISEMENT OF FORECLOSURE SALE.**

19 (a) Mortgaged property may be sold at a public sale only after giving a commercially
20 reasonable public advertisement of the sale. If the sale is postponed, a commercially reasonable
21 notice of postponement must be given.

22 (b) A public advertisement of the sale must indicate:

23 (1) the name of the borrower and, if not the same, the name of the person who
24 signed the mortgage agreement;

25 (2) the name of the creditor or other person who will conduct the sale;

26 (3) the date, time, and place of the sale;

27 (4) the street address or, if there is no street address, other information identifying
28 where the mortgaged property is located;

29 (5) any improvements and personal property that are included in the sale, if that
30 information is readily discernable by the creditor;

31 (6) the amount of the debt, including costs, to be satisfied by proceeds of the sale;

32 (7) whether the mortgaged property is to be sold subject to senior indebtedness;

1 (8) the material terms of the sale, including payment terms to be required for the
2 successful bidder at the completion of the auction;

3 (9) whether access to the mortgaged property for the purpose of inspection is
4 available to prospective bidders before the sale; and

5 (10) a telephone number and email address from which a person may obtain
6 additional information concerning the mortgaged property and the sale.

7 (c) The public advertisement does not have to contain a legal description of the
8 mortgaged property or recording information for the mortgage or other instruments of record.

9 (d) The public advertisement, or other information pertaining to the sale, may be posted
10 at the location of the mortgaged property.

11 (e) Except as otherwise provided in subsections (e)(1), (e)(2), (e)(3), and (e)(4), whether
12 the method and timing of publication of the public advertisement is commercially reasonable is a
13 question of fact.

14 (1) The method of publication is commercially reasonable if published both in a
15 newspaper having general circulation in the [county] where the mortgaged property is located
16 and in an Internet website that is reasonably expected to be viewed by persons having an interest
17 in purchasing the mortgaged property.

18 (2) For a newspaper advertisement, the timing of publication is commercially
19 reasonable if published once per week for three consecutive weeks before the sale, with the first
20 publication not more than 30 days before the sale.

21 (3) For an Internet website, the timing of publication is commercially reasonable
22 if published at least 21 days before the sale and the Internet posting remains regularly available
23 between the time of posting and the time of sale.

(4) Notice of postponement is commercially reasonable if published in the same outlets as the original notice for at least 7 days before the postponed sale.

(f) A copy of the public advertisement shall be sent to the borrower and to any obligor. The notice of public advertisement may be sent with the notice of commencement of foreclosure or may be sent separately.

Reporters' Drafting Notes

1. This section allows a public sale of the mortgaged property only if the creditor first gives a commercially reasonable public advertisement. The purpose is to ensure that the public has a meaningful opportunity to learn of the proposed sale in order to appear and engage in competitive bidding. This section supersedes existing state laws covering advertisements for public sales for all foreclosures that are within the scope of this [act].

2. This section does not specify the person who is obligated to give the advertisement of sale. In many states, that person will be the creditor, but in other states, another person such as a trustee or sheriff performs that function. This [act] does not mandate a change in who is responsible for advertising the sale.

3. This [act] does not require the accomplishment of foreclosure by a public auction sale. If other state law allows alternative methods of foreclosure, such methods remain permissible. For example, Connecticut law allows strict foreclosure without a sale of the property.

4. Subsection (b) states minimum requirements for the public advertisement. An advertisement that lacks any of the information set forth in subsection (b) is insufficient as a matter of law. An advertisement may contain additional information about the mortgaged property or the sale.

5. Traditionally the law required the advertisement of foreclosure sales in local newspapers. This section allows the creditor to continue that practice, but no longer specifies newspaper advertisement as required or sufficient in all cases. Whether a newspaper advertisement alone is sufficient depends upon whether it is commercially reasonable under the facts, which must be determined based upon the nature of the property, the newspaper, and other local circumstances. Similarly, whether it is commercially reasonable for a creditor *not* to publish a newspaper advertisement, relying instead on other outlets, depends upon the facts. 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

1 the creditor and the borrower by saving the expense.

2 6. Subsection (c) adopts a bright-line rule with respect to legal descriptions
3 of the real property and recording information. The failure to include such
4 information does not make the public advertisement insufficient. This
5 information is seldom of importance to a person who reads a foreclosure
6 advertisement for the purpose of deciding whether the person has potential
7 interest. Anyone who develops a potential interest is highly likely to investigate
8 further before appearing at the sale to bid. That investigation may include title
9 information, which will disclose the legal description and recording references for
10 the mortgage and other recorded instruments in the chain of title, and typically
11 will include other information as well bearing on the property.
12

13 7. Subsection (d) authorizes the creditor to post the public advertisement
14 or a sign on the property, regardless of whether that right is reserved in the
15 mortgage. [Note: Is this appropriate? Do foreclosure signs including “bank sale”
16 signs have negative consequences for the neighborhoods? What about zoning and
17 HOA covenants that may restrict or limit signs?]
18

19 8. Subsection (e) creates four safe harbors. First, the method of
20 publication is commercially reasonable if the creditor publishes the public
21 advertisement both in a local newspaper and with an appropriate Internet website.
22 The Internet site may be one operated by the newspaper or by any other person,
23 whether or not located in the jurisdiction where the mortgaged property is located.
24 The Internet site, however, must be one that has characteristics suggesting that
25 interested members of the public are likely to find and to read the posting. There
26 are two safe harbors with respect to timing for newspaper advertisements and
27 Internet advertisements, which seek to ensure public access to the advertisement
28 for approximately one month preceding the date of sale. Last, a safe harbor for
29 postponed sales allows a shorter length of time than required for the safe harbor
30 for the original notice because members of the public with potential interest in the
31 property had the opportunity to read the original notice.
32

33 **SECTION 405. NOTICE OF SALE.** The creditor shall give the borrower

34 written notice of the date, time and place of the scheduled foreclosure sale. If the sale is
35 postponed, the creditor shall give the borrower a new written notice of the date, time and
36 place of the sale. Notice of sale, including postponed sales, shall be delivered by first
37 class mail to the borrower’s last known address, and by personal delivery to the property
38 address. Notice of sale shall be delivered at least 30 days prior to the sale date, or the
39 postponed sale date.

1 **Drafter's Notes to the alternatives presented in Sections 406 and 407**

2 These alternatives comprise what the drafters believe to be a rational range of options on
3 the question of whether confirmation of a foreclosure sale is appropriate.

4 **Alternative 1**, set forth in sections 406 below, requires confirmation of the sale at
5 the conclusion of a judicial foreclosure action. This conforms to present law in
6 most judicial foreclosure states. As drafted, it requires a court to confirm the sale
7 absent evidence of procedural irregularity or unconscionability; ample case law in
8 several states supports both exceptions to judicial confirmation.

9
10 **Alternative 1** is continued in Section 407 of this draft, and addresses the need for
11 a confirmation hearing in a non-judicial foreclosure state. It requires judicial
12 confirmation of the sale after a nonjudicial sale if the creditor desires to obtain a
13 deficiency judgment against an obligor.

14
15 The Reporters are not aware of any nonjudicial foreclosure state that requires
16 judicial confirmation of a foreclosure sale as a general matter. North Carolina
17 requires a lender who sells property pursuant to a power of sale to file with the
18 clerk of the superior court "a final report and account of his receipts and
19 disbursements within 30 days after the receipt of the proceeds of such sale." N.C.
20 Gen. Stat. § 45-21.33. The lender also must file copies of notices, and the clerk is
21 required to audit and record the account of sale. The North Carolina statute,
22 however, does not require confirmation of the sale.

23
24 A number of nonjudicial foreclosure states require confirmation of the foreclosure
25 sale if the creditor wishes to obtain a deficiency judgment. Two examples are
26 Georgia and Texas. See Ga. Code § 44-14-161; Tex. Property Code § 51.003.
27 Georgia requires a report of the sale to the superior court within 30 days of the
28 sale, followed by a confirmation hearing and the issuance of a confirmation order
29 if the court finds the property sold for "its true market value." Under a Texas
30 statute adopted in 1991, an action to recover a deficiency must be brought within
31 two years of the sale. If requested by the borrower, the court determines the fair
32 market value. If the fair market value exceeds the foreclosure sale price, that
33 value is used instead of the sale price to calculate the deficiency.

34
35 **Alternative 2**, set forth below, is presented in a newly drafted provision granting
36 the lender an optional right to seek judicial confirmation in order to establish the
37 conclusive effect of a sale and thereby promote the certainty of title which
38 subsequent purchasers may require. This alternative does not mandate judicial
39 confirmation of the sale for either judicial or nonjudicial foreclosures
40 Further, the drafters are aware of the proposal from Commissioner Walters that
41 Section 406 should track the requirement in Section 408 for a final and non-
42 appealable order, and have addressed that issue in revised Section 406(e) in
43 bracketed text. The Reporters and Chair are uncertain when this outcome - which
44 would substantially delay passage of title following an auction – is a desirable

1 result or tracks the intention of the proposer.

2
3 **SECTION 406. [Alternative #1] CONFIRMATION OF SALE PURSUANT TO**
4 **JUDGMENT.**

5 (a) After an auction sale of the mortgaged property pursuant to an order or judgment of a
6 court, the person conducting the sale shall file a report of sale with the court, which must name
7 the purchaser and describe the property, the amount bid, the amount paid to date, the expenses of
8 the sale, and any other material terms.

9 (b) After notice and a hearing, the court shall grant an order confirming the sale unless it
10 finds:

11 (1) there was a material procedural irregularity such as the failure to give required
12 notices to parties,

13 (2) the terms of sale were unconscionable,

14 (3) the sale was conducted fraudulently, or

15 (4) justice was otherwise not done.

16 (c) If the court fails to confirm the sale, it may order a resale of the property on such
17 terms as are just.

18 (d) An order confirming the sale shall also confirm the expenses of the sale [and shall
19 indicate whether the borrower or an obligor who is party to the action has any remaining liability
20 on the obligation secured by the mortgaged property.]

21 (e) Upon confirmation of the sale [and when the confirmation has become final and non-
22 appealable] title to the property shall pass to the purchaser named in the order without the
23 necessity of any further proceedings or instruments. A certificate of sale shall be recorded within
24 _____ days after the later of the order of confirmation or payment in full of the price.

Reporters' Drafting Notes

1. In many states the court has substantial discretion with respect to confirmation of auction sales, consistent with traditional doctrine that foreclosure is an action in equity. Case law often provides guidance and sets parameters on the court's exercise of equitable discretion. The standard for confirmation set forth in subsection (b) is modeled upon 735 Ill. Comp. Stat. 5/15-1508. In some states, the statutory standard is briefer. Minnesota, for example, requires the entry of a confirmation order unless "it appears upon due examination that justice has not been done." Minn. St. § 581.08.

2. Subsection (b) does not require the court to make an express finding with respect to the value of the property in all cases. When a party, however, has made an objection to the report of the sale based on the amount of the bid, evidence of value is relevant. It is well established that a low price by itself is not grounds for rejecting the sale. A number of states express the rule as calling for rejection when the bid is "grossly inadequate" or "shocks the conscience." *E.g.*, *Intervest Nat. Bank v. Ashburton 70, LLC*, 928 N.Y.S.2d 475 (App. Div. 2011) (price "was not so low as to shock the conscience of the court"); *Irwin Union Nat. Bank and Trust Co. v. Famous*, 4 A.3d 1099 (Pa. Super. Ct. 2010) (to set aside sale the price must be "grossly inadequate"). Subsection (b) does not adopt either of those formulations, but allows the court to refuse confirmation when the price is "unconscionable."

3. When the court finds there is a reason not to confirm the sale, ordinarily a resale of the property is appropriate. Subsection (c), however, makes a resale permissive rather than mandatory. Depending upon the nature of the flaw, it may be appropriate for the court to approve the sale if the purchaser agrees to a modification of the terms of the sale.

4. The report of the sale filed with the court should include a list of all expenses incurred in connection with the sale. Subsection (d) provides that if the court confirms the sale, the confirmation order should state the expenses approved by the court.

5. There is substantial variation among the states as to whether the creditor may obtain a deficiency judgment after a judicial foreclosure sale, and if so, what procedures are necessary to obtain a deficiency judgment. Subsection (d) accommodates existing state law on deficiency judgments, but provides, in the bracketed language, that the confirmation order should indicate the amount of any deficiency judgment liability in a case in which the judgment has made one or more persons personally liable on the obligation. This raises a separate policy issue which the Committee should discuss, namely, whether a separate hearing should be held regarding the deficiency in order to expedite confirmation of the sale.

1 6. This section does not set forth details with respect to the procedures for
2 confirmation or contractual obligations. Notice and opportunity to be heard are
3 fundamental and are expressly required by subsection (b), but specific parameters
4 are not stated. If no objections are made to the report of sale, the hearing does not
5 necessarily have to consist of an in-court proceeding with counsel present. *See*
6 *U.S. Bank Nat. Ass'n v. Bjeljac*, 43 So. 3d 851 (Fla. Dist. Ct. App. 2010) (hearing
7 is required when creditor timely files objection based upon low price and
8 creditor's failure to attend sale was due to mistake).
9

10 7. Ordinarily a confirmation of sale is a final judgment, having the legal
11 effect of final judgments in general, including immunity from collateral attack.
12 The purchaser does not have enforceable contract rights prior to confirmation of
13 the sale by the court. Whether the purchaser is allowed to rescind his offer to
14 purchase prior to confirmation depends upon other law.
15

16 **SECTION 407. [Continuation of Alternative #1] CONFIRMATION OF SALE**

17 **PURSUANT TO [POWER OF SALE]; DEFICIENCY JUDGMENT.**

18 (a) If the price at which the mortgaged property is sold at an auction sale, without legal
19 process, pursuant to a power contained in a mortgage agreement, is less than the obligation,
20 resulting in a deficiency, any action to recover the deficiency must be brought within [60 days]
21 after the sale.

22 (b) No deficiency judgment shall be granted unless the court, after notice and a hearing,
23 grants an order confirming the sale. The court shall grant a confirmation order unless it finds:

24 (1) there was a material procedural irregularity such as the failure to give required
25 notices to parties,

26 (2) the sale was conducted fraudulently, or

27 (3) the property sold at a price less than its fair market value as of the date of the
28 foreclosure sale.

29 (c) The fair market value referred to in subsection (b)(3) shall be determined by the
30 finder of fact based upon competent evidence of value, which may include,
31 but is not limited to, the following:

- (1) expert opinion testimony;
- (2) comparable sales;
- (3) anticipated marketing time and holding costs; and
- (4) cost of sale.

Reporters' Drafting Notes

1. This Section conforms to existing law by not requiring that a court confirm the sale conducted in a nonjudicial foreclosure as a general matter. However, confirmation is required if the creditor wishes to obtain a deficiency judgment. A number of states follow this approach. See, e.g., Ga. Code § 44-14-161; Tex. Property Code § 51.003.

SECTION 406-407. [Alternative #2] OPTIONAL CONFIRMATION OF SALE.

(a) The foreclosing creditor may file a motion in the [specify court] for confirmation of a foreclosure sale within 60 days of the auction sale of the mortgaged property. The motion shall be served on the person conducting the sale, who shall file a report of the sale with the court. The report must name the purchaser and describe the property, the amount bid, the amount paid to date, and any other material terms.

(b) The court shall grant an order confirming the sale unless it finds:

- (1) there was a material procedural irregularity such as the failure to give required notices to parties;
- (2) the terms of sale were unconscionable;
- (3) the sale was conducted fraudulently; or
- (4) justice was otherwise not done.

(c) If the court fails to confirm the sale, it may order a resale of the property on such terms as are just.

(d) If the court confirms the sale, the purchaser may record the confirmation order.

1 **Reporters' Drafting Notes**

2
3 1. Comments at the November 2012 meeting highlighted the conflict between
4 mandating judicial confirmation of sales in nonjudicial foreclosure states where it is not
5 presently required, on one hand, and the need for a mechanism to establish the conclusive
6 effect of a sale on the other. This draft attempts to resolve the conflict by providing for
7 an optional, rather than mandatory, sale confirmation process. Confirmation is a
8 prerequisite for the conclusive effect of the sale for the benefit of bona fide purchasers. In
9 a nonjudicial foreclosure state, the creditor (or title insurer) seeking to prevent possible
10 claims of a defective foreclosure process can opt for judicial confirmation, or can choose
11 not to obtain confirmation if it is confident that there were no defects in the foreclosure
12 process. The addition of an optional confirmation process in states without one should
13 prove less controversial than mandating judicial confirmation. For judicial foreclosure
14 states, while the foreclosure judgment is conclusive as to the basic prerequisites to
15 foreclosure, such as the existence of a default, an optional sale confirmation can add
16 some protection against challenges to defects in post-judgment procedures, such as the
17 notice of sale.

18
19 **SECTION 408. CONCLUSIVE EFFECT OF FORECLOSURE SALE.** A final and
20 non-appealable court order confirming the sale pursuant to Section 406 conclusively establishes
21 compliance with this Act in favor of purchasers of the mortgaged property in good faith for
22 value. [For purposes of this section, the foreclosing creditor is not a good faith purchaser for
23 value.]

24 **Reporters' Drafting Notes**

25
26 1. At the November 2012 meeting there was disagreement regarding
27 whether the foreclosing creditor should benefit from the conclusive effect of the
28 confirmation of a foreclosure sale. The language remains bracketed for further
29 discussion.

30 **ARTICLE 5**

31 **OTHER PROVISIONS**

32 **SECTION 501. NEGOTIATED TRANSFER OF MORTGAGED PROPERTY IN**
33 **SATISFACTION OF OBLIGATION.**

34 (a) A borrower may transfer mortgaged property to a creditor in full satisfaction of the
35 borrower's obligation to that creditor secured by that property if:

1 (1) The borrower and the creditor agree to the transfer in a record authenticated by
2 both parties after the borrower's default; and

3 (2) An authenticated notification of objection to the proposed transfer is not
4 received from any person entitled to notice under section 502 within 20 days after notification
5 was sent to that person.

6 (b) If the borrower or a person claiming under the borrower is in possession of the
7 mortgaged property, the agreement must specify the date and time when the borrower is to
8 surrender possession to the creditor. If there is any person entitled to notice under section 502,
9 the borrower is not obligated to surrender possession before the 20-day period described in
10 subsection (a)(2) has elapsed.

11 **Reporters' Drafting Notes**

12
13 1. The Section authorizes a transfer from the borrower to the creditor in
14 full satisfaction of the debt or other obligation. In so doing, it provides a
15 framework for existing workout arrangements such as cash-for-keys agreements
16 and deed-in-lieu of foreclosure transactions. This Section and the following two
17 sections provide for a safe harbor by specifying the effect of a transfer that meets
18 the requirements of this Section. This Section is based in part on UCC § 9-620,
19 which provides for the acceptance of personal property mortgaged property by a
20 secured party in full or partial satisfaction of a secured obligation. The important
21 innovation here is to discharge junior liens on the property without the need for a
22 foreclosure sale.

23
24 2. This Section does not specify a minimum consideration to be received
25 by the borrower in exchange for the borrower's agreement to transfer the
26 mortgaged property in satisfaction of the obligation. The sole exception is that if
27 the borrower is in possession and there are third parties entitled to notification of
28 the proposed transfer, the agreement may not require the borrower to vacate
29 possession prior to the expiration of the period for notified persons to submit an
30 objection.

31
32 3. As suggested in the prior paragraph, the Reporters, Chair and ABA
33 advisor note that the consensus of the discussion at the November meeting
34 appeared to be that there was no apparent justification for mandating that a
35 'negotiated transfer' under this section include any statutory minimum
36 consideration to be paid to the borrower; this draft accordingly deletes reference

1 to that original requirement in this section.

2
3 As a consequence, this section as it is now drafted confers a substantial
4 benefit on mortgage creditors - in the form of a new mechanism for converting
5 every 'deed in lieu' transaction into an accelerated means of clearing title of
6 junior encumbrancers without the need for a more traditional judicial foreclosure
7 – but does not confer any minimum benefit on borrowers (other than the general
8 statement of effects of such an agreement contained in Section 504 and the rights
9 of possession noted in paragraph 2 above,)

10
11 **SECTION 502. NOTICE OF NEGOTIATED TRANSFER.**

12 (a) If a negotiated transfer pursuant to Section 501 is proposed at a time when a judicial
13 foreclosure proceeding is pending with respect to the mortgaged property, the court must send
14 notice of the proposed negotiated transfer to all parties, except for the borrower and the creditor
15 that is foreclosing.

16 (b) If a negotiated transfer pursuant to Section 501 is proposed at a time when a judicial
17 foreclosure proceeding is not pending with respect to the mortgaged property, the creditor must
18 send notice of the proposed negotiated transfer to:

19 (1) any person from which the creditor has received, before the borrower and the
20 creditor agreed to the proposed transfer, an authenticated notification of a claim of an interest in
21 the mortgaged property; and

22 (2) any person that, 10 days before the borrower and the creditor agreed to the
23 proposed transfer, held an interest in the mortgaged property, perfected by a filing in the public
24 records, that is subordinate to the mortgage that is the subject of the proposed transfer.

25 **Reporters' Drafting Notes**

26
27 1. This section is based on UCC § 9-621, which provides for a notification
28 procedure for an acceptance of personal property by a secured party in full or
29 partial satisfaction of a secured obligation.

30
31 2. Subsection (a) provides for the court to notify parties to the foreclosure
32 proceeding of an agreement proposed by the borrower and creditor for a transfer

1 in full satisfaction of the debt or other obligation. If there are no parties to the
2 action, other than the borrower and the creditor, then there is no one to notify.
3 Holders of subordinate interests in the mortgaged property should have been
4 joined as necessary parties to the foreclosure action.
5

6 3. Subsection (b) provides for the creditor to notify persons who have
7 subordinate interests in the mortgaged property of an agreement proposed by the
8 borrower and creditor for a transfer in full satisfaction of the obligation. Such
9 subordinate interest holders may have their rights terminated by the negotiated
10 transfer, and therefore they have the right to request protection pursuant to
11 Section 503.
12

13 **SECTION 503. HEARING ON OBJECTIONS TO NEGOTIATED TRANSFER.**
14

15 (a) If the court receives an effective notification of objection from any person holding an
16 interest in the mortgaged property that would be affected by the negotiated transfer, the court
17 shall promptly schedule a hearing regarding that objection.

18 (b) If, at the hearing, the creditor who is a party to the proposed transfer demonstrates by
19 appraisal or otherwise that there is no equity in the mortgaged property available to satisfy
20 the interests of the objecting interest holder, the court shall overrule the objection and approve
21 the negotiated transfer.

22 (c) If, at the hearing, the objecting party demonstrates by appraisal or otherwise that
23 there is equity in the mortgaged property available to satisfy the interests of the objecting interest
24 holder, the court shall set a date not later than [30] days after the date of the hearing by which the
25 objecting party shall be entitled to tender to the creditor who is a party to the proposed transfer a
26 sum equal to the obligation owed to the proposing creditor, including interest and court costs. If
27 the objecting party tenders that sum to the creditor within the time set by the court, the objecting
28 party shall be entitled to the benefit of the proposed negotiated transfer. Otherwise, the rights of
29 the objecting party under this section shall be extinguished.

30 (d) If a creditor who has sent a notice under Section 502(b) receives an effective

notification of objection from any person holding an interest in the mortgaged property that would be affected by the negotiated transfer, the negotiated transfer shall not proceed unless the creditor initiates a judicial proceeding for the purpose of holding a hearing pursuant to the rules set forth in subsections (b) and (c).

SECTION 504. EFFECT OF NEGOTIATED TRANSFER.

(a) A borrower's transfer of the mortgaged property pursuant to Section 501 to a creditor in full satisfaction of the obligation to that creditor it secures:

(1) discharges the obligation in full;

(2) transfers to the creditor all of the borrower's rights in the mortgaged property , except for any right of the borrower to continue to occupy the mortgaged property pursuant to an agreement between the borrower and the creditor which is incorporated into the negotiated transfer agreement;

(3) discharges the mortgage held by the creditor and any subordinate mortgage or other subordinate lien; and

(4) terminates any other subordinate interest.

(b) A subordinate interest is discharged or terminated under subsection (a), even in the event of noncompliance with the requirements of this Act; provided, that a creditor who fails to comply with the requirements of this Act is liable for damages in the amount of any loss caused by its failure to comply.

(c) If the borrower and creditor have agreed that the borrower has the right to continue to occupy the mortgaged property for a fixed period of time, that agreement creates a license unless the parties have expressly agreed to enter into a landlord-tenant relationship.

(d) A transfer of the mortgaged property waives all rights of the creditor to obtain a

1 personal judgment for the obligation, including costs and expenses, against the borrower or any
2 other person liable for the obligation secured by the mortgaged property.

3 (e) A transfer of the mortgaged property waives all rights of the borrower to redeem the
4 mortgaged property.

5 (f) [Nothing in Sections 501 through 504 prevents a borrower and creditor from entering
6 into any other form of agreement on mutually agreeable terms, but the effects of a negotiated
7 transfer described in these sections do not apply to an agreement that fails to state that the
8 agreement is made pursuant to section 501.] (g) Nothing in this article affects the rights of any
9 creditor holding an interest in the mortgaged property which is senior to the interests of the
10 creditor that takes title to the mortgaged property pursuant to this section.

11 **Reporters' Drafting Notes**

12
13 1. This section is based upon UCC § 9-622, which specifies the effect of
14 acceptance of personal property mortgaged property by a secured party in full or
15 partial satisfaction of a secured obligation. Subsection (a) specifies the effect of a
16 transfer of the mortgaged property in full satisfaction of the secured obligation.
17 The transfer to which it refers is one that results from performance of the
18 agreement made by the borrower and the creditor. If a timely objection is
19 received by the court or by the creditor from a person entitled to notification, then
20 neither this subsection nor subsection (b) applies. Paragraph (1) expresses the
21 fundamental consequence of accepting the mortgaged property in full satisfaction
22 of the secured obligation—the obligation is discharged.

23
24 2. Paragraphs (2) through (4) indicate the effects of a transfer on various
25 property rights and interests. Under paragraph (2), the creditor acquires “all of the
26 borrower’s rights in the mortgaged property.” Under paragraph (3), all junior
27 encumbrances are discharged. Paragraph (4) provides for the termination of other
28 subordinate interests. Under existing law, a deed-in-lieu of foreclosure accepted
29 by a creditor does not terminate subordinate mortgages, subordinate liens, or other
30 subordinate property rights. This Act changes by result by authorizing a transfer
31 in full satisfaction of the obligation, which terminates junior interests.

32
33 3. Subsection (c) specifies that the status of the borrower who continues to
34 occupy the property after entering into an agreement to transfer the property to the
35 creditor in full satisfaction of the obligation is that of a licensee. The parties’
36 agreement and other state law determine the rights and obligations of the parties

1 as licensor and licensee.

2
3 4. The last sentence of subsection (f) is bracketed to reflect at least one
4 policy choice that the Reporters, Chair and the ABA Advisor believe should be
5 made by the Committee.

6
7 As drafted, the sentence authorizes borrowers and creditors to enter into
8 any other type of agreement that they might desire, but no such agreement –
9 presumably including a traditional ‘deed in lieu’ arrangement – would confer the
10 benefits of Section 504 unless the agreement expressly provided that it was made
11 pursuant to Section 501.

12
13 The converse of the policy is reflected in this observation from Reporter
14 Smith:

15
16 “I believe the better policy is to displace existing state laws on “deed in
17 lieu” transactions within the scope of this act. Among other problems, if
18 we keep both, there will be transactions in which the lender has not clearly
19 documented whether the intent to proceed under this act or under other
20 law.”

21
22 **SECTION 505. ABANDONED PROPERTY.**

23 (a) A government agency’s determination, finding, or order that mortgaged property is
24 abandoned or vacant, or the presence of not less than [three] of the following conditions,
25 constitutes prima facie evidence that the mortgaged property is abandoned property:

26 (1) Windows or entrances to the mortgaged property are boarded up or closed off.

27 (2) Multiple window panes on the mortgaged property are broken and unrepaired.

28 (3) One or more doors to the mortgaged property are smashed through, broken
29 off, unhinged, or continuously unlocked.

30 (4) Gas service, electric service, water service, or other utility service to the
31 mortgaged property has been terminated; or utility consumption is extremely low so as to
32 indicate that the property is not regularly occupied.

33 (5) Rubbish, trash, or debris has accumulated on the mortgaged property.

34 (6) The mortgaged property is deteriorating and is either below or in imminent

1 danger of falling below minimum community standards for public safety and sanitation.

2 (7) The creditor has changed the locks on the mortgaged property and for at least
3 30 days after the changing of the locks the borrower has not requested entrance to the mortgaged
4 property.

5 (8) There exist one or more written statements, including documents of
6 conveyance, signed by the borrower that indicate a clear intent to abandon the mortgaged
7 property.

8 (9) The police or sheriff's office has received at least two reports of trespassers on
9 the mortgaged property or of vandalism or other illegal acts being committed on the mortgaged
10 property.

11 (10) The borrower has died and there is no evidence that a survivor of the
12 borrower is in actual possession of the mortgaged property.

13 (b) In a judicial foreclosure proceeding, the plaintiff may petition the court for a
14 determination that the mortgaged property is abandoned property. The city or other
15 governmental entity in which the mortgaged property is located shall have the right to intervene
16 in the proceeding. After notice and a hearing, the court may issue an order finding that the
17 mortgaged property is abandoned property.

18 (c) In a nonjudicial foreclosure proceeding, the creditor may seek a determination that
19 the mortgaged property is abandoned property by submitting a request accompanied by an
20 affidavit to [name of official]. The creditor must send a copy of the request and affidavit to the
21 borrower and other persons entitled to notice under Section 201. After personal inspection of the
22 mortgaged property, which shall include entry into the dwelling unit, the [name of official] may
23 issue a written determination finding that the mortgaged property is abandoned property. The

1 [name of official] shall send the written determination to the creditor, the borrower, and other
2 persons entitled to notice under Section 201. The written determination, or the refusal of the
3 [name of official] to issue a written determination, shall be subject to judicial review de novo in
4 an appropriate court.

5 **Reporters' Drafting Notes**

6
7 1. This Act authorizes an expedited foreclosure procedure for abandoned
8 properties for both judicial foreclosure and for nonjudicial foreclosures.² An
9 expedited procedure is appropriate for two reasons. First, the borrower is no
10 longer making a valuable economic use of the property to provide shelter for the
11 borrower or the borrower's family or someone claiming under the borrower, such
12 as a tenant. A foreclosure sale will not result in a possessor being forced to
13 relocate to other housing. Second, properties that are facing foreclosure and that
14 are vacant have significant negative impacts on neighborhoods and the
15 surrounding communities. Vacancies reduce the market values of neighboring
16 properties. Neighborhood crime increases. The vacant properties tend to suffer
17 from lack of repair and maintenance, creating public health risks, including
18 infestations by vermin, mosquitoes, and other insects. There are fiscal impacts on
19 local governments, who find property taxes on vacant properties often become
20 delinquent; yet the governments are faced with added expenses to provide
21 essential services to blighted neighborhoods, such as police and fire protection.
22 By providing for an expedited foreclosure procedure, this Act seeks to return
23 abandoned properties to the stock of occupied, well-maintained housing as soon
24 as reasonably possible.

25
26 2. The conditions giving rise to prima facie evidence of abandonment set
27 forth in Subsection (a)(1) through (a)(9) closely track the criteria set forth in Ind.
28 Code § 32-30-10.6-5(a)(1) through (9) (effective March 16, 2012). The presence
29 of one or more of the statutory conditions is prima facie evidence, giving rise to a
30 presumption of abandonment. Such conditions are not conclusive on the issue of
31 abandonment. If the borrower or another person holding under the borrower is in
32 actual possession of the mortgage property, the property is not abandoned
33 notwithstanding the existence of such conditions. Likewise, mortgaged property
34 may be abandoned under this Section notwithstanding the absence of any of the
35 statutory conditions.

36
37 3. Mortgaged property often becomes vacant, both under standard
38 mortgage and reverse mortgage transactions, when the borrower dies. Under
39 Subsection (a)(11) proof of death of the borrower constitutes prima facie evidence
40 that the mortgaged property is abandoned, provided that there is no evidence that

² Defer for later discussion by the Committee maintenance and repair obligations of borrowers and creditors with respect to abandoned property.

1 an heir or other beneficiary of the borrower's estate is in actual possession. Of
2 course if there are multiple borrowers, this condition is met only if all the
3 borrowers have died.
4

5 4. In a nonjudicial foreclosure proceeding, the creditor may treat the
6 mortgaged property as abandoned only by submitting evidence of abandonment to
7 an independent third party. Subsection (c) provides for the submission of evidence
8 to a person, who as part of the decision making process must personally visit the
9 property and enter the dwelling unit. Normally jurisdictions enacting this Act will
10 designate an employee of local government, such as a building inspector, who is
11 responsible for evaluating the physical condition of dwelling units.
12

13 Judicial review of the decision is available to any interested person.
14 Subsection (c) does not specify the nature of that actions, which in many
15 jurisdictions will be a mandamus action.
16

17 **SECTION 506. FORECLOSURE OF ABANDONED PROPERTY.**

18 (a) If the court issues an order finding that the mortgaged property is abandoned property
19 pursuant to Section 505(b), at the same time the court shall order an expedited sale of the
20 property. The order shall call for public sale of the property no sooner than [30] days and no
21 later than [60] days after entry of the order.

22 (b) In a nonjudicial foreclosure proceeding, upon the issuance of a written determination
23 that the mortgaged property is abandoned property pursuant to Section 505(c), the creditor may
24 conduct an expedited sale of the property. A public sale of the property may take place no sooner
25 than [30] days and no later than 60 days after the issuance of the written determination, unless
26 judicial review of the determination is commenced. The creditor shall comply with the notice
27 requirements of Section 405, except that [15] days advance notice of the sale is sufficient.

28 (c) After a judicial order or a written determination finding that the mortgaged property
29 is abandoned property, the creditor shall take necessary and appropriate action to cause the
30 foreclosure sale to be completed within a reasonable time unless the creditor releases its
31 mortgage and files that release on the land records. The creditor shall not have the right to

1 dismiss, terminate, or suspend foreclosure proceedings, and thereby end its obligations to
2 maintain the abandoned property under Section 507.

3 [(d) The completion of a foreclosure sale pursuant to subsection (a) or (b) shall have the
4 effect of terminating the rights of the borrower or any other person to redeem the property after
5 the sale under Code Section ____.]

6 **Reporters' Drafting Notes**

7
8 1. This Section provides for an expedited public sale of the mortgaged
9 property after a determination that the mortgaged property is abandoned. In a
10 judicial foreclosure, the court must order the sale to take place no longer than ____
11 days after the court enters its order finding the property to be abandoned, unless
12 the creditor agrees to a later sale date. In a nonjudicial foreclosure, the creditor
13 may select the date, provided it is no sooner than ____ days after the written
14 determination of abandonment.

15
16 2. This Section does not authorize a disposition of abandoned property
17 other than public sale, but other dispositions are available under other sections of
18 this Act. For example, the borrower and creditor may agree to a negotiated
19 transfer to the creditor in lieu of foreclosure pursuant to Sections 501 to 504 [cash
20 for keys agreement].

21
22 3. Once a creditor decides to take advantage of the expedited foreclosure
23 procedure allowed by this Section, there is a public interest in ensuring that the
24 property becomes occupied as soon as reasonably possible. For this reason
25 subsection (c) does not allow the creditor to suspend indefinitely its efforts to
26 consummate the foreclosure. There may be exceptional circumstances in which it
27 is not feasible to hold the foreclosure sale within 60 days of the judicial order or
28 written determination finding the property to be abandoned, as required by
29 subsection (a) and (b). In that event, subsection (c) provides an outside limit of
30 [four months] to complete the sale.

31
32 Subsection (c) poses the substantial question of what consequences should
33 flow from the failure of the creditor to comply with its requirements. On the one
34 hand, in the view of the Reporters, the Chair and the ABA Advisor, it would
35 clearly be inappropriate to impose an obligation on a creditor to repair the
36 property subject to the mortgage before the creditor has taken possession or an
37 official determination is made that the property is abandoned. Indeed, we
38 anticipate that the lending community will resist a statutory duty to maintain
39 property on which it holds a mortgage in those instances where the lender would
40 prefer to release its mortgage and forego any interest in that property.

1 On the other hand, the consequences of a creditor's failure to either
2 commence and complete a foreclosure action or to release its mortgage, on other
3 stakeholders in the abandoned property – including the fee owner, the
4 municipality and neighbors in which the abandoned property is located, and
5 where appropriate, a homeowners association - are very real. We believe this is a
6 subject deserving of substantial discussion during the February meeting.

7 4. In states that afford the borrower and other persons a statutory right of
8 redemption after completion of a foreclosure sale, subsection (d) serves to
9 terminate those redemption rights.

10
11 **SECTION 507. MAINTENANCE OF ABANDONED PROPERTY.**

12 (a) In a judicial foreclosure proceeding, a creditor shall maintain abandoned property
13 from the time the court issues an order finding that the mortgaged property is abandoned
14 property pursuant to Section 505(b).

15 (b) In a nonjudicial foreclosure proceeding, a creditor shall maintain abandoned property
16 from the time of issuance of a written determination that the mortgaged property is abandoned
17 property pursuant to Section 505(c).

18 (c) In the absence of a judicial order under subsection (a) or a written determination
19 under subsection (b), a creditor who has commenced foreclosure proceedings shall maintain the
20 mortgaged property if a governmental entity issues a citation finding that the mortgaged property
21 is abandoned property in a condition that poses a threat to public safety or health.

22 (d) The creditor's obligation to maintain abandoned property shall continue until the
23 conveyance of the property through foreclosure to a purchaser other than the creditor.

24 (e) For purposes of this section, "failure to maintain" means (i) failure to care for the
25 exterior of the property, including, but not limited to, permitting excessive foliage growth that
26 diminishes the value of surrounding properties; (ii) failing to take action to prevent trespassers or
27 squatters from remaining on the property; (iii) failing to take action to prevent mosquito larvae
28 from growing in standing water; or (iv) other conditions that create a public or private nuisance.

1 (f) A creditor who has the obligation to maintain abandoned property shall have the right
2 peaceably to enter the property, or to cause others peaceably to enter the property, for the limited
3 purposes of inspection, repair, and maintenance as required by this section. All reasonable
4 expenses incurred by the creditor pursuant to this section shall be an obligation of the borrower
5 and shall be secured by the mortgage.

6 (g) No person who enters the abandoned property for the purposes described in
7 subsection (f) shall have any liability to the borrower for trespass or for damage to the property.

8 (h) The following persons shall have the right to enforce the obligations created by this
9 section in any appropriate action or proceeding:

10 (1) The city or other governmental entity in which the mortgaged property is
11 located.

12 (2) A homeowners association, condominium association, or cooperative
13 association if the mortgaged property is subject to the rules of that association.

14 (i) The obligations of the creditor to maintain abandoned property are limited to those
15 stated in the Section; provided, that if the creditor becomes the owner of the abandoned property,
16 its obligations with respect to the property shall be determined by other law. The creditor shall
17 not become a mortgagee in possession of the property by virtue of its performance of the
18 obligations stated in this Section.

19 **Reporters' Drafting Notes**

20
21 1. This Section requires creditors to maintain abandoned properties under
22 certain circumstances. The obligation may arise based upon action of the creditor
23 or action of the municipality or other governmental entity where the property is
24 located. The creditor does not become obligated to maintain merely by
25 commencing foreclosure proceedings at a time when the dwelling unit is vacant.
26 Rather, the obligation arises when the creditor seeks to use the expedited
27 foreclosure procedure authorized by Section 505 and obtains either a judicial
28 order or official determination that the property is abandoned. Under subsection

1 (c) the obligation may also arise any time after the creditor has commenced
2 foreclosure proceedings if the municipality or other local governmental entity
3 cites the property as both abandoned and presenting a threat to public safety or
4 health.

5
6 2. Subsection (e) defines the scope of the creditor's obligation to maintain
7 abandoned property. The focus is on the outward appearance of the property,
8 including yards and other exterior spaces, and other conditions that are likely to
9 have significant impacts on the neighborhood, such as interior spaces frequented
10 by squatters or persons engaged in criminal activities. This subsection is modeled
11 closely on Cal. Civ. § 2929.3(b), enacted in 2008.

12
13 3. Subsection (f) grants a license to the creditor and to its agents or
14 contractors to enter abandoned property for the purpose of inspection, repair, and
15 maintenance, regardless of whether that right is reserved in the mortgage.
16 Similarly, this subsection authorizes the addition of the creditor's reasonable
17 maintenance expenses under this section to the debt secured by the mortgage,
18 regardless of whether the mortgage contains a provision to that effect.

19
20 4. Subsection (h) provides for enforcement by the local government that
21 has jurisdiction over the abandoned property. When the property is located in a
22 common-interest community, it also provides standing for the association as a
23 means to protect neighboring property owners whose interests are likely to be
24 harmed by the creditor's failure to maintain the property. In conferring standing
25 both to the local government and to owners' associations, this subsection follows
26 the approach taken by N.Y. Real Prop. Acts. § 1307(3), enacted in 2009. This
27 subsection does not grant a direct enforcement right to neighbors. If negatively
28 impacted, such persons may have a remedy under other laws, such as public or
29 private nuisance.

30
31 5. At common law a creditor who takes possession of mortgaged property
32 prior to the completion of foreclosure becomes a "mortgagee in possession," who
33 by virtue thereof undertakes a number of obligations to the borrower with respect
34 to maintenance and care of the property. Subsection (i) expressly provides that a
35 creditor who enters the property for the purpose of complying with its obligations
36 under this Section does not assume the liabilities of a mortgagee in possession.

37
38 **SECTION 508. LIEN FOR SUMS DUE ASSOCIATION; ENFORCEMENT.**

39 **PREAMBLE TO REVISED SECTION 508.**

40 The Committee will recall that Section 3-116 of the Uniform Common Interest
41 Ownership Act provides the unit owners association a super priority – that is, priority over first
42 mortgages - for six months of regular common expense assessments, plus court costs and legal
43 fees, when those common charges are unpaid.

1 The November draft presented 4 alternatives to address the issues that home owner
2 associations for condominiums, cooperatives and planned communities face in collecting those
3 common charges. The problem is made considerably more complex by the extended delays in
4 finalizing foreclosures now being experienced in some states. The arguments favoring enhanced
5 priority for CIC assessment liens were presented at the November meeting by representatives of
6 the Community Association Institute.

7
8 Of those four original alternatives, the first provided super priority for all regular periodic
9 common charges plus interest – compared to the existing six months - , but did not give super
10 priority for any association’s legal fees, for special assessments or for other charges.

11
12 The second alternative proposed a limitation on the priority claim of the association’s
13 legal fees, but was otherwise identical to alternative 1.

14
15 Alternative # 3 proposed an automatic increase in the super priority lien for all delayed
16 foreclosures, while Alternative 4 provided the association a right to accelerate its own
17 foreclosure actions for non-payment of common charges, as well as to seek acceleration of a
18 foreclosure of the first mortgage, in order to minimize the association’s own lost common
19 charges which would be wiped out by the foreclosure.

20
21 Upon consideration, it may simplify consideration of this issue by the Drafting
22 Committee to consider only a single proposed section. In drafting that section, we sought
23 to take into account much of the discussion at the November meeting, as well as the
24 thoughts of association advocates and other views expressed by lenders.

25
26 Finally, and separate from consideration of this section, it may be appropriate for
27 the Drafting Committee to consider the utility of authorizing creditors who provide
28 mortgage financing to purchasers of dwelling units in common interest communities to,
29 first, require those purchasers to escrow funds for common charges as well as real estate
30 taxes and casualty insurance; and, second, to require that home owner associations accept
31 periodic payments of common charges from lenders –say, quarterly instead of monthly –
32 rather than directly from the unit owner, in order to minimize the lenders’ risk of failed
33 common charge payments.

34
35 **SECTION 508. [NEW] LIEN FOR SUMS DUE ASSOCIATION;**
36 **ENFORCEMENT.**

37 **Drafter’s Note**
38

39 Other than necessary style matters, this section incorporates all the
40 relevant language of Sec. 3-116 of the Uniform Common Interest Ownership Act,
41 with two exceptions:

42
43 First, the highlighted text in subsection (c) limits the association’s legal
44 fees in an uncontested matter to a sum equal to 3 months of the association’s

1 common charges;

2
3 Second, the highlighted text in subsection (d) provides that if a mortgage
4 foreclosure is not completed in 12 months, then, in addition to the existing 6
5 month priority granted to associations, the association would thereafter begin to
6 add a month's priority for every additional month, beginning in month 13.

7
8 (a) The association has a statutory lien on a dwelling unit for any assessment attributable
9 to that unit based on the periodic budget adopted by the association pursuant to the declaration
10 and the statutes of this state authorizing creation of the common interest community in which the
11 dwelling unit is located; and fines imposed against its unit owner. Unless the declaration
12 otherwise provides, reasonable attorneys' fees and costs, other fees, charges, late charges, fines
13 and interest charged pursuant to other law and any other sums due to the association under the
14 declaration or as a result of an administrative, arbitration, mediation or judicial decision, are
15 enforceable in the same manner as unpaid assessments under this section. If an assessment
16 described in this section is payable in installments, the lien is for the full amount of the
17 assessment from the time the first installment thereof becomes due.

18 (b) A lien under this section is prior to all other liens and encumbrances on a dwelling
19 unit in a common interest community except (1) liens and encumbrances recorded before the
20 recordation of the declaration, (2) a first mortgage on the dwelling unit recorded before the date
21 on which the assessment or other charge sought to be enforced became delinquent, and (3) liens
22 for real estate taxes and other governmental assessments or charges against the dwelling unit.

23 (c) A lien under this section is also prior to first mortgages described in subdivision (2)
24 of subsection (b) to the extent of (1) the "priority amount," that is, an amount equal to the
25 common expense assessments based on the periodic budget adopted by the association pursuant
26 the declaration and the statutes of this state authorizing creation of the common interest
27 community in which the unit is located which would have become due in the absence of

1 acceleration during the six months immediately preceding institution of an action to enforce
2 either the association's lien or a mortgage described in subdivision (2) of subsection (b); and (2)
3 the association's costs and attorney's fees in enforcing its lien. **However, if (i) an action to**
4 **enforce the association's lien is uncontested or (ii) no defense to the association's priority is**
5 **raised in a creditor's action to foreclose a first mortgage on a dwelling unit, the amount of**
6 **the association's attorney's fee for which this subsection grants a priority over a first**
7 **mortgage may not exceed a sum equal to [three] months of the common expense assessment**
8 **due from that dwelling unit based on the periodic budget adopted by the association.**

9 **(d) In addition to the priority amount over a first mortgage as described in**
10 **subsection (c), if a creditor commences a civil action to foreclose a first mortgage described**
11 **in subsection (b)(2) against a dwelling unit in a common interest community and if [twelve]**
12 **months passes after the date the action is commenced without judgment having entered in**
13 **that action and title to the dwelling unit having passed pursuant to that judgment, the**
14 **amount of the association's lien which has priority over the first mortgage shall thereafter**
15 **automatically increase by an additional month of common expense assessment based on the**
16 **periodic budget adopted by the association on that dwelling unit for each additional month**
17 **or part thereof that subsequently passes until judgment enters and title passes to the**
18 **creditor or the purchaser of that dwelling unit.**

19 (e) This section does not affect the priority of mechanics' or materialmen's liens or the
20 priority of liens for other assessments made by the association. A lien under this section is not
21 subject to [insert appropriate reference to state homestead, dower and curtesy, or other
22 exceptions].

23 (f) Unless the declaration otherwise provides, if two or more associations have liens for

1 assessments created at any time on the same property under this section, those liens have equal
2 priority.

3 (g) Recording of the declaration constitutes record notice and perfection of the lien. No
4 further recordation of any claim of lien for assessment under this section is required.

5 (h) A lien for unpaid assessments is extinguished unless proceedings to enforce the lien
6 are instituted within three years after the full amount of the assessments becomes due.

7 (i) This section does not prohibit actions against unit owners to recover sums for which
8 subsection (a) of this section creates a lien or prohibit an association from taking a deed in lieu of
9 foreclosure.

10 (j) Unless the declaration provides for a lesser interest rate, a statutory lien under this
11 section shall accrue interest at the rate of one percent per month.

12 **ARTICLE 6**

13 **REMEDIES**

14 **SECTION 601. BORROWER REMEDIES.**

15 (a) A borrower may assert any material violation of this statute as a defense in a judicial
16 foreclosure, or seek injunctive relief against any nonjudicial foreclosure sale based on any
17 material violation of this statute, prior to the confirmation of the sale pursuant to Section 406.

18 (b) A borrower injured by any violation of this statute may bring an action in [specify
19 court] for damages against the foreclosing creditor before or after confirmation of the foreclosure
20 sale. The court shall award reasonable attorney's fees and costs to a borrower who prevails in an
21 action under this Section.

22 [(b)(ALT) A violation of this statute that causes injury to a borrower is also a violation
23 of [state consumer protection or unfair and deceptive practices statute] and entitles the borrower

1 to all remedies provided for under [relevant section of CP or UDAP statute]].

2 **Reporters' Drafting Notes**

3
4 Prior to confirmation of the foreclosure sale, the borrower may raise a material violation
5 of the statute, for example a materially inaccurate notice of the amounts needed to cure a default,
6 to prevent the foreclosure sale (or confirmation), until the violation has been corrected and
7 remedied. After a foreclosure sale the borrower's remedy for violations of the statute is to seek
8 damages from the foreclosing creditor, and a bona fide sale purchaser is entitled to rely on the
9 conclusive effect under Section 407. If a violation by the creditor can be cured timely so that full
10 compliance is achieved, the foreclosure may proceed.