HOME MORTGAGES IN BANKRUPTCY

The effects of the home foreclosure crisis have been severe and far reaching. In 2010 alone, homes were expected to lose $1.7 trillion in value.[1] Undoubtedly bankruptcy filings have increased as a result, but whether the worst is over is still up for debate.[2] In light of these considerations, this paper will address the HAMP Modification Program, the status of Fannie Mae and Freddie Mac, the Countrywide settlements, NACA, programs that attempt to assist debtors, the status of case law in the area and procedures affecting HAMP and other mortgages.

I. HAMP – What It Can Do and How You Get One

One in seven borrowers is delinquent on his/her mortgage or already is in foreclosure.[3] Nearly one in four mortgages is under water. The "Home Affordable Modification Program" (HAMP) was introduced in February 2009 as part of the Troubled Asset Relief Program. The program was funded with $50 billion. It was designed to give eligible homeowners the opportunity to modify their mortgages to make them more affordable, thus avoiding foreclosures. Widespread foreclosure prevention is intended to help stabilize the housing market.

The HAMP program has been widely criticized for several reasons. As of the Treasury's September 2010 report, less than 500,000 permanent loan modifications had been made.[4] This number is significantly less than the *3 to 4 million* modifications that were initially estimated by

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[1] Thomson Reuters, *US Home Values Down by $1.7 Trillion in 2010: Zillow* (December 9, 2010), http://www.cnbc.com/id/40590488.
[2] Diana Olick, *Negative Equity is Worse Than You Think*, quoting Mark Hanson (December 15, 2010), http://www.cnbc.com/id/40682173 ("In order to sell and re-buy [sell one's current home and buy a new one], a homeowner must receive enough proceeds from the sale to 1) pay off the mortgage(s), 2) pay a Realtor 5-6 percent and 3) put a 3.5-20 percent down payment on a new vintage loan." Also indicating that 22.5% of all home mortgages now have negative equity).
[3] Christian E. Weller, Center for American Progress, *Economic Snapshot for July 2010* (July 23, 2010), http://www.americanprogress.org/issues/2010/07/econsnap0710.html (last visited 12/21/2010).
[4] U.S. Treasury, *Making Home Affordable Program Inside: Report Highlights* (Sept. 2010), http://www.financial stability.gov/docs/Sept%20MHA%20Public%20**2010**.pdf (last visited 12/21/2010).

the Treasury. Recent Treasury reports indicate that the number of modifications is actually declining with a mere 27,840 permanent modifications being made in September of 2010.[5] The high level of selectivity does, however, have the benefit of a lower estimated redefault rate of an estimated 25%.[6] However, "if past trends continue, starting . . . [in December 2010], there will be more HAMP redefaults each month than new permanent modifications. That means that the total number of active permanent modifications will peak at around 500,000 and *decline.*" (italics in original).[7]

According to the Center for Responsible Lending, hundreds of thousands of people who received trial modifications ended up in a worse financial situation as a result of their participation because, despite complying with the trial period requirements, they were denied permanent modifications.[8] Therefore, the homeowners paid on loans that ultimately were foreclosed and wasted their money. This sentiment is also reflected frequently in editorials across the country.[9]

Overall, the HAMP program has not decreased foreclosures nationwide. A majority of modifications, approximately 3.2 million, have been done outside of HAMP. There have been several suggestions for improving HAMP including creating an independent appeals process for homeowners, increasing the mandatory forbearance period, transferring servicing duties to

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[5] *Id.*
[6] *Id.*
[7] Adam Levitin, *21% HAMP First Year Redefault Rate* (December 2010), www.creditslips.org/creditslips/2010/12/hamp-21-redefault-rate-in-1st-year.html (predicting 60-80% redefaults on permanent loan modifications over the next 5 years).
[8] *HAMP, Servicer Abuses, and Foreclosure Prevention Strategies: Testimony Before the Congressional Oversight Panel* (October 27, 2010) (statement of Julia Gordon), available at: http://www.responsiblelending.org/...lending/...testimony-julia-gordon-10-26-2010.pdf (last visited 12/21/2010).
[9] *See, e.g.*, Andy Faria, *HAMP Modification Denied-Whats Next?* (June 14, 2010), http://EzineArticles.com/?expert=Andy_Faria (last visited 12/21/2010); Greg Kaufmann, *If Big Banks Won't Play by the Rules, Where Does That Leave Homeowners in Distress?* (May 13, 2010), http://www.cbsnews.com/stories/2010/05/13/opinion/main6478450.shtml (last visited 12/21/2010); Corbett B. Daly, *UPDATE 1-Lawmakers Slam Top Mortgage Firms On Loan Mods* (June 24, 2010), http://www.reuters.com/article/idUSN2419665720100624 (last visited 12/21/2010).

companies without conflicts of interest, clarifying existing guidelines, and enforcing HAMP guidelines with serious penalties for noncompliance.

A. Eligibility

In order to be eligible for a HAMP modification, a borrower must meet several criteria. The applicant must:

> (i) Be an owner-occupant in a one-to-four unit property;
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> (ii) Have an unpaid principal balance on his/her loan that is equal to or less than $729,750 for one unit properties (higher for two-to-four unit properties);
>
> (iii) Have a loan that originated on or before January 1, 2009;
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> (iv) Have a mortgage payment (including taxes, insurance, and home owners association dues) that is more than 31% of gross (pre-tax) monthly income; and
>
> (v) Have a mortgage payment that is not affordable, perhaps because of a change in income or expenses.

Being in a chapter 7 or chapter 13 bankruptcy case does not make a borrower ineligible. The Treasury Department issued Supplemental Directive 10-02[10], effective June 1, 2010, which amended an earlier directive that provided that borrowers in bankruptcy were eligible for HAMP modifications "at the servicer's discretion." Under Supp. Dir. 10-02, servicers must consider debtors for HAMP relief if they submit a request for a modification. However, the servicers do not need to actively solicit debtors for HAMP modifications as they must do with nonbankrupt borrowers.

B. Application Process

The application process for a HAMP modification is fairly straightforward. The applicant must complete a "Request for Modification and Affidavit" (RMA), tax authorization

[10] Making Home Affordable, *Home Affordable Modification Program – Borrower Outreach and Communication Supplemental Directive 10-02* (March 24, 2010), available at: https://www.hmpadmin.com/portal/docs/hamp_servicer/sd1002.pdf.

form IRS-4506-T, and must submit proof of income to the mortgage servicer. For loans backed by Fannie Mae, unemployed borrowers cannot count jobless benefits as income in applying for mortgage modifications.

If a borrower is in chapter 7 or chapter 13, the servicer may accept copies of the bankruptcy schedules and tax returns filed with the Bankruptcy Court in lieu of the RMA and Form 4506T-EZ. If the debtor's schedules are more than 90 days old, the debtor must provide updated income information. A Hardship Affidavit must still be provided. (This form can be found as a separate form at the HAMP website. It is also part of the RMA form.)

C. Trial Period

While the HAMP program does not require a homeowner to become delinquent before support can be provided, each borrower must participate in a three to four month trial period. During the trial period, homeowners must submit trial payments and all required forms and documents demonstrating they will be able to make their reduced payments on time. At the conclusion of the trial period the mortgage servicer will make a final decision.

If the borrower is in bankruptcy, the servicers are required to work with the borrower and borrower's counsel to obtain court or trustee required approvals. The bankruptcy approvals are discussed below in Section VI. If the three month period does not provide enough time to obtain the bankruptcy court approvals needed, Supp. Dir. 10-02 states that the servicer "should" extend the trial period to deal with any delays caused by the bankruptcy process. The servicer is not required to extend the trial period beyond 5 months however. Therefore, debtors and debtors' counsel must proceed diligently and file whatever is required as soon as possible.

While a debtor is in a trial period when a bankruptcy case is filed, the servicer is to refrain from filing motions for relief from stay and/or plan objections or motions to dismiss the

debtor's case unless the debtor is in default under the trial modification. The directive does not say that it applies to debtors who obtain a trial modification during a case, but it seems to be common sense that a servicer would not seek to sabotage the trial modification in the bankruptcy case when the servicer knew of the bankruptcy at the time of the approval of the modification.

If a debtor is in a chapter 13 case, Supp. Dir. 10-02 allows the debtor to enter into a permanent modification without completing a trial modification if (1) the borrower makes all post-petition payments on the mortgage to be modified and at least three of the payments are greater than or equal to the modified payment; (2) the bankruptcy court approves the modification; and (3) the trial period plan waiver is permitted by the guidelines of the investors in the mortgage. These modifications are at the discretion of the servicer because not all servicers have computer systems that will be able to deal with this situation.

D. Possible Modifications

Mortgage servicers can modify mortgages by reducing interest rates to as low as 2%, can extend the term of the mortgage to up to 40 years, and can engage in principal forbearance or deferral, possibly with principal forgiveness. After modification, the interest rate is fixed for 5 years. During year 6 and thereafter under the modification the interest rate may increase one percentage point per year until it reaches the Freddie Mac Primary Mortgage Market Survey rate in effect at the time the permanent modification was prepared.

E. Foreclosure Issues

Supp. Dir. 10-02 provides that, as of June 1, 2010, a servicer may not refer a loan to foreclosure or conduct a foreclosure sale without either (1) determining that the borrower is ineligible for a HAMP modification or (2) making reasonable attempts to solicit a HAMP application from the borrower which are unsuccessful. In the past, servicers would put

borrowers in trial modifications, but continue foreclosure procedures “in case” the debtor defaulted or was determined to be ineligible. There are three exceptions to this “stay” of foreclosure activity. The servicer does not violate the Directive if (1) a court or public official refuses to stop a foreclosure after the servicer has asked the court to stop; (2) the servicer must take action to protect the interest of an investor; or (3) there is not sufficient time to stop the action or event.

A borrower has been “reasonably solicited” by a servicer about applying for a HAMP loan if the servicer has, over a 30 day period, made four telephone calls to the borrower at different times of day and sent two written notices to the borrower describing HAMP with at least one notice being sent by certified or express mail and another by regular mail. The servicer must send a written communication to the borrower about the forms the debtor must send in if the borrower expresses interest in the program. The letter does not need to be sent if the borrower’s loan is not eligible for a modification or the borrower’s monthly mortgage obligation is substantially less than 31% of the borrower’s gross monthly income.

F. Denial of a HAMP Modification

A servicer must send a written notification to a borrower if a modification is NOT approved. The servicer may not conduct foreclosure sales within 30 days of such a notice. The 30-day period does not apply if the non-approval of the HAMP modification was due to ineligibility or the borrower withdraws from the program or fails to make any payments that are due.

The lender must use a set of guidelines to determine whether to grant a loan modification or foreclose. The decision is based upon the Net Present Value Test. The HAMP program has

an NPV test and each servicer has its own customized version for non-HAMP loans. In general, the test requires the following:

(i) Determine the probability that the mortgage defaults.

(ii) Project the future cash flows of the mortgage if it defaults and the present value of these cash flows.

(iii) Project the future expected cash flows of the mortgage if it does not default and the present value of these cash flows.

(iv) Take the probability weighted average of the two present values.

(v) Then, compute the net present value of the mortgage assuming it is modified, incorporating the effects on cash flows and performance of the modification terms and subsidies provided by the Home Affordable Modification Program.

(vi) Compare the two present values to determine if the HAMP modification is NPV positive.[11]

G. Rights and Remedies Under HAMP for Borrowers

One of the biggest problems with the HAMP program is the fact that borrowers were/are not sure of where their HAMP applications stand at any point in time. There are stories of borrowers being asked to submit the same information numerous times or being denied a modification because the servicer says the borrower never provided the necessary paperwork at all (when it had been timely submitted).[12]

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[11] Loan Fraud Investigations, *Net Present Value Test*, available at: http://www.loanfraudinvestigations.com/loan-modification/net-present-value-test (this site contains a list of factors used to determine cash flows and how other values in the formula are calculated).

[12] *See, e.g.*, Kathleen M. Howley, Dakin Campbell & Danielle Kucera, *Mortgage Modification Failures Push Borrowers into Foreclosure* (November 1, 2010), http://www.bloomberg.com/news/2010-11-02/mortgage-modifications-meant-to-save-u-s-homes-push-them-into-foreclosure.html (last visited 12/21/2010).

Supp. Dir. 09-98, which became effective January 1, 2010, requires notice to borrowers who do not qualify for a trial or permanent modification or who default on a trial modification. The notice must list the reason for non-approval of the loan. A borrower can request that the servicer provide at least some components of the Net Present Value test that the servicer used in denying approval if the denial was on that ground. If a debtor does not receive a written denial of the HAMP loan request, that failure might be a defense to a foreclosure action. A debtor has 30 days to request the NPV data after denial of a modification on that ground and the servicer has 10 days to respond to the request. A foreclosure cannot occur until at least 30 days after the NPV data has been provided. There is no process for appeal of a HAMP denial if the debtor believes that the servicer improperly calculated the borrower's eligibility or if the loan is denied for any other reason.

A borrower can seek more information about the status of a HAMP modification or the grounds for denial of one by sending a "qualified written request" pursuant to the Real Estate Settlement Procedures Act, 12 U.S.C. § 2605 and Regulation X. There are no reported cases dealing with such a request in a HAMP setting, but it should be allowed.[13]

Can failure to comply with HAMP guidelines be used as an affirmative defense in foreclosure proceedings? There is no reported case allowing HAMP requesters a private right of action to enforce HAMP rights in a law suit filed by the mortgagor. However, some cases have at least recognized a right to use HAMP guidelines as an affirmative defense in a foreclosure proceeding. *Lacy-McKinney v. Taylor, Bean & Whitaker Mortg. Corp.*, 937 N.E. 2d 853 (Ind. App. 2010). The case held that HUD guidelines were an appropriate defense. The HAMP guidelines are similar. The Court cited to 3 other cases that allowed HUD guidelines to be used

[13] *See* National Consumer Law Center, Inc., FORECLOSURES, § 8.2.2.3 (2d ed. 2007 and Supp.).

defensively. *Cross v. Fed. Nat'l Mortg. Ass'n*, 359 So. 2d 464 (Fla. Dist. Ct. App. 1978); *Wells Fargo Home Mortg. Inc. v. Neal*, 398 Md. 705, 922 A.2d 538, 447 (2007); and *Federal Nat'l Mortg. Ass'n v. Ricks*, 83 Misc. 2d 814, 372 N.Y.S. 2d 485, 497 (N.Y. Sup. Ct. 1975).

On equitable grounds, a New York Supreme Court stayed all proceedings in a case because U.S. Bank, N.A., the mortgagor, did not act in good faith in dealing with the debtors in regard to a HAMP loan modification request and proceeded with foreclosure even as the bank was allegedly trying to negotiate a new loan modification with the debtors. *U.S. Bank, N.A. v. Mathon*, 2010 NY Slip Op 62082(U) (N.Y. Sup. Ct. 2010). A U.S. Bank affidavit revealed that "[d]ue to a combination of factors, however, including missing documents, the submission of stale financial data and a significant influx of Trial Plan applications, the Mathons' Trial Plan was not reviewed by the underwriting department until on or about April 2, 2010." The Mathons had submitted the Trial Plan request on April 17, 2009 and made 13 payments pursuant to it! The Court held that the failure of U.S. Bank to proceed with the HAMP as required by the guidelines showed its conduct was "rife with bad faith."

Finally, in a foreclosure proceeding, the mortgagee made a "Motion to Enforce Home Affordable Modification Program Trial Period Plan." The lender, BAC Home Loans Servicing, did not oppose the motion. The mortgagors, the Bogars, had filed for a trial modification and fulfilled all of the terms, including making the three timely payments. Nonetheless, BAC had not provided a permanent loan modification and continued to prosecute its foreclosure action. The court ordered that the loan modification be given to the Bogars and ordered BAC to pay the

Bogars attorneys fees. *BAC Home Loans Servicing, LP, f/k/a Countrywide Home Loans Servicing, LP v. Bogar*, Docket No. 19-1-09 Oscv (October 6, 2010).[14]

II. Status of Fannie Mae and Freddie Mac

Two years ago the government rescued the Federal National Mortgage Association (Fannie Mae)[15] and the Federal Home Loan Mortgage Corporation (Freddie Mac), at an estimated cost to taxpayers of $259 billion, making it the most expensive bailout of the financial crisis. Following the close of the third quarter of 2010, Fannie Mae asked for $2.5 billion in additional federal aid. Both entities have been in conservatorship (under the complete control of the federal government) since September 8, 2008.

Fannie Mae and Freddie Mac own or guarantee over half of mortgages in the United States. That number continues to grow as Fannie and Freddie purchase about ninety-percent of home loans made today. Because these government-sponsored enterprises buy mortgages from lending institutions and then either hold them in investment portfolios or resell them as mortgage-backed securities, they play a vital role in financing the housing markets. Given how much taxpayer money has already gone towards Fannie Mae and Freddie Mac, Congress will likely put the organizations under closer scrutiny in the coming term.

In September of 2010, following the exposure of "robo-signing" and other wrongful practices, all Fannie Mae and Freddie Mac foreclosures were brought to a halt. As of November 29, 2010, real estate agents were allowed to resume selling foreclosed homes. (Note – however, that resuming sale of foreclosed properties does not necessarily mean that robo-signing problems

[14] For a list of cases on HAMP enforceability as a foreclosure defense, see http://www.nclc.org/issues/recent-trial-court-decisions-on-hamp-enforceability-as-foreclosure-defense.html

[15] Fannie Mae got its name from a creative pronunciation of its acronym, FNMA. It is unclear how anyone got Freddie Mac from FHLMC.

have been resolved). The halt in selling foreclosed homes has had a depressing effect on the housing market that is likely to continue more suits are filed.

In December 2010, U.S. Treasury Chief, Timothy Geithner, stated that Fannie and Freddie should participate in the loan writedown program instituted by FHA. The program provides government incentives to lenders who reduce principal for borrowers who are current on a mortgage whose balance exceeds the home's worth. The program, dubbed the "short refi" program, has not resulted in many actual write downs yet. Fannie and Freddie have not agreed to do such write downs, even with Secretary Geithner's urging, because it would increase their already enormous losses and require more taxpayer bailout money.

III. Countrywide Settlements

A. Settlement with States' Attorneys General

Countrywide Financial was a private residential mortgage banking company founded in 1969. It was purchased by Bank of America on July 1, 2008, after liquidity problems surfaced due to its loan portfolio defaults. In 2007, it held about 17% of all mortgages in the United States. After numerous irregularities were exposed (alleged to include deceiving borrowers by misrepresenting loan terms, loan payment increases, and borrowers' ability to afford loans), Countrywide entered settlements with the Attorneys General of numerous states under which the company will offer payments to borrowers who meet certain eligibility criteria. The settlement amount could be as much as $8.6 billion dollars. The criteria that a borrower must meet include: (1) the loan was made by Countrywide, (2) the loan was secured by an owner-occupied property that was collateral for the loan, (3) the first payment was due between January 1, 2004, and December 31, 2007, and (4) the property was lost through foreclosure, deed in lieu of foreclosure, or short sale. Owners of homes that went into foreclosure after March 31, 2009, are

not eligible. In addition to paying a settlement amount to eligible borrowers, Countrywide is required to offer other forms of assistance such as loan modification and relocation assistance. Information about the settlement process can be found at: http://www.countrywidesettlementinfo.com.

Checks will be mailed in early 2011 to eligible borrowers who submitted timely claims in Massachusetts and Vermont. Missouri borrowers will receive claim forms and releases in Missouri in early 2011. Georgia, Florida, Kentucky, Louisiana, Mississippi, North and South Carolina, West Virginia, Tennessee and Texas have also settled with Countrywide and the deadline for submitting claims has passed. Alabama is not in the list and has not settled its state's claims. For the states that have settled, there is a pool of money that will be available to pay claims and the amount of the payments will be determined based upon the amount of claims filed and the damage amounts alleged.

B. Settlement with the Federal Trade Commission

A $108,000,000 settlement with the Federal Trade Commission is also available to settle claim for parties who were "charged excessive fees for default-related services like property inspections [], [who paid] amounts [claimed by Countrywide] in bankruptcy that were false or could not be backed up; and [who were in bankruptcy and were not told] when new fees or charges were being added to their loans."[16] There is no claim form on the website. The FTC says that it will identify eligible borrowers and "you'll get a letter in the mail."[17] An update as of 12/06/2010 states that the FTC is still in the process of identifying eligible consumers and it might take some time. If a borrower thinks he or she may be eligible, the borrower may submit his/her address to the claims administrator whose address in on the website.

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[16] Federal Trade Commission, *FTC Settlement with Countrywide*, available at: http://www.ftc.gov/countrywide (last visited 12/18/2010).

[17] *Id*.

C. Criminal Settlements

In the United States District Court for the Central District of California the former chief executive officer of Countrywide, Angelo Mozilo, has agreed to pay $67.5 million to settle claims by the Securities and Exchange Commission that he misled shareholders about the risks associated with Countrywide loans. Of that amount, $45 million is “ill-gotten gains.” Mozilo is set to pay the largest penalty ever levied against a senior corporate executive in a SEC settlement.

SEC Enforcement Division director Robert Khuzami stated: “Mozilo’s record penalty is the fitting outcome for a corporate executive who deliberately disregarded his duties to investors by concealing what he saw from inside the executive suite.” What he kept to himself was “a looming disaster in which Countywide was buckling under the weight of increasing risky mortgage underwriting, mounting defaults and delinquencies, and a deteriorating business model.” Settling the SEC charges permitted Mozilo to avoid a trial that could have provided a basis for future criminal charges.

Former Countrywide president David Sambol settled for $5.5 million, and former CFO Eric Sieracki settled for $130,000. Bank of America, which acquired Countrywide in 2008, will pay the disgorgement amounts on Sambol’s behalf. Regarding the settlements, U.S. District Judge John Walter stated that they are “fair and adequate, reasonable and in the public interest….It’s my view that the SEC has aggressively investigated and prosecuted this action.”

Although Countrywide has entered these settlements, the full extent of problems related to foreclosure irregularities is unknown and the problems go beyond Countrywide’s involvement. In fall 2010, GMAC, Bank of America, JP Morgan Chase, and PNC suspended their foreclosure proceedings. According to Professor Katherine Porter (visiting professor at

Harvard Law School), in addition to robo-signing there are other serious irregularities including imposition and collection of improper fees, mortgage origination fraud, and the pursuit of foreclosure without rights.

IV. Neighborhood Assistance Corporation of America

The Neighborhood Assistance Corporation of America (NACA), founded in 1988, is a homeowner's advocacy group that seeks to persuade lenders to modify existing home mortgages. Its stated goal is "to build strong, healthy neighborhoods in urban and rural areas nationwide through affordable homeownership." NACA's "Save the Dream" tour, as well as its protest methods against executives of lending companies, received much media attention in 2009. This community action group has over 30 offices in the East, Southeast and West. There are offices in Atlanta and Augusta Georgia, Jacksonville and Tampa Florida, Birmingham, Alabama, Charleston and Columbia South Carolina, Charlotte and Raleigh, North Carolina, Nashville and Memphis, Tennessee, and Jackson, Mississippi to name some locations.

NACA has a mortgage program with $10 billion in funding commitments. It provides home loans to qualified members with very favorable terms. The mortgage loans have no down payment, no closing costs, no fees, and a below market interest rate. A borrower need not have perfect credit either.

NACA counselors provide free services, but require homeowners to become members of the group, attend workshops, and participate in advocacy on behalf of NACA. Services include: one-on-one counseling, financial counseling, credit resolution, house hunting assistance, property evaluation, mortgage application assistance, mortgage process assistance, and closing assistance. For existing homeowners, the goal is to lower interest rates, principal, or both. These mortgages are restructured rather than refinanced. NACA earns $500 for each successful

mortgage modification. For new homeowners, NACA makes its own low-interest loans that meet certain criteria and provides for no down-payment or closing costs.

In order to participate in NACA a person must fulfill "Ten Steps." Members must: remain in good standing (paying dues, attending workshops, paying neighborhood stabilization fees); may not have an ownership interest in any other property; must occupy the home purchased for as long as the mortgage is through NACA (secured by a NACA lien on the property); and must participate in at least five "actions and activities" each year on behalf of NACA such as participating in protests, demonstrations, or litigation against certain companies, volunteering in the NACA office, participating in peer lending committees, or assisting other members in the home buying process. Membership in NACA costs $20/year and a credit report fee of $10 is charged as well.

A mortgage from NACA can be obtained on a one-to-four family home, condominium or cooperative. The maximum purchase price is determined by the region in which the borrower lives. For Atlanta Georgia, the maximum purchase price is $253,000 for a single family home and up to $399,300 for a four family home. In Miami Florida, the maximum purchase price for a single family home is $362,790 and for a four family home is $697,696. For Birmingham, Alabama, a single family home may be purchased for up to $200,160 and a four family home for $384,936.

NACA has a mortgage modification program as well for those in existing mortgages that their incomes do not support. It is not clear if the program is exactly like the HAMP program, but it appears to be. NACA states that it has "legally binding agreements with all the major lenders/servicers and investors (i.e. Fannie Mae and Freddie Mac) covering approximately 90%

of homeowners."[18] The program offers modified mortgage payments based upon the borrower's income.

Finally, NACA also offers financial help in rehabilitating properties that are purchased. There is no payment on the mortgage on a property during the rehabilitation to allow a borrower to pay rent and live during the repair. The repair costs will be added to the mortgage balance.

V. Programs to assist Debtors

Two options for debtors in some jurisdictions are mediation or loss mitigation. These programs are available at the state and federal court levels. The Bankruptcy Court for the District of Rhode Island instituted its Loss Mitigation Program in November of 2009 with the purpose of bringing together debtors and secured lenders to encourage them to discuss mutually beneficial resolution of mortgage difficulties. Based on a similar program in the Southern District of New York, the program is intended to "avoid or reduce unnecessary bankruptcy litigation and cost to debtors and secured creditors." Several state supreme courts have implemented similar programs. Florida, for example, requires automatic mediation in all foreclosure cases. The Orlando Division of the Middle District of Florida Bankruptcy Court adopted a rule in 2010 that compels a bank representative with full authority to modify mortgages to meet with a debtor and a mediator to engage in good faith negotiations toward a loan modification. This rule is in addition to the Florida state court program adopted by the Florida Supreme Court that requires mediation in foreclosure cases.[19] The Bankruptcy Court rule is designed to correct mortgage problems before they result in foreclosure actions. New

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[18] NACA, *Home Save Program – Overview*, available at: http://www.naca.com/program/homesaveProgram.jsp?language=null (last visited 1/27/2011).

[19] Susan Taylor Martin, *Mortgage Mediation Cases On Hold as Fraud Allegations Unravel David J. Stern Law Firm* (November 30, 2010), available at: http://www.tampabay.com/news/mortgage-mediation-cases-on-hold-as-fraud-allegations-unravel-david-j/1137077. David Stern is accused of sloppy and fraudulent documentation of the right to foreclose. Over 400 of his cases have been put on hold in the mediation program.

Jersey Bankruptcy Court has a mediation program for debtors with mortgage problems.[20] Connecticut has a state court program of mediation.[21] The Vermont Bankruptcy Court has instituted a Judiciary Foreclosure Mediation Program as of May 29, 2010.[22]

Loss mitigation programs are designed to open communication between loan servicers and homeowners. These programs streamline production of documents under court supervision, which means the process often moves more quickly. The National Consumer Law Center argues that bankruptcy courts are best situated to facilitate modifications because the courts have authority to break through bureaucratic barriers, ensure good faith negotiations, provide basic due process, provide protection from foreclosure, avoid "robo-signers" and other abuses, are equipped to deal with second mortgages and a homeowner's entire debt load. The NCLC recommends the Executive Office of the U.S. Trustees actively review and publicize bankruptcy courts' use of loss mitigation and mediation.

VI. Legal Issues Involving HAMPs and Other Modifications in Bankruptcy Cases[23]

A. *Automatic Stay*

Do you need to seek relief from the stay to obtain a loan modification? Section 362 stays Aany act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate.@ ' 362(a)(3). Section 362 stays any act to create, perfect, or enforce any lien against property of the estate.@ ' 362(a)(4). Section 362(a)(5) stays Aany act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case." These sections could

[20] New Jersey Bankruptcy Court, http://www.njb.uscourts.gov/dw/mediation.

[21] John Hoctor, *Connecticut's Mandatory Mediation Process Slows The State's Foreclosure Rate—Is That Too Good To Be True?*, The Hartford Advocate (December 10, 2010), available at: http://www.hartfordadvocate.com /featured-news/connecticuts-mandatory-mediation-process-slows-the-states-foreclosure-rate-is-that-too-good-to-be-true-052138-2 (last visited 12/20/2010).

[22] *See* http://www.vtb.uscourts.gov/orders/ord10-01.pdf (last visited 12/20/2010).

[23] Part of this section was prepared for a seminar for the National Association of Chapter 13 Trustees presented in July 2010.

be read to require relief from the stay, especially if the homestead is not a fully exempt asset. If the home is exempt under section 522, then once exempted, the property is no longer property of the estate. *See, e.g.*, *In re Scrivener*, 535 F.3d 1258 (10th Cir. 2008). However, even the fact that the homestead is exempt will not alter the applicability of section 362(a)(5) since it applies to property of the debtor.

In districts in which property of the estate is revested in the debtor after confirmation, under the default rule under section 1327(b), the only section of section 362 that might apply postconfirmation is section 362(a)(5). Some lenders are requiring relief from stay orders before the lenders will begin negotiation of a loan modification. When in doubt, seek relief from the stay to prevent possible sanctions. A movant can term the motion AMotion to Determine that Relief From the Stay is Unnecessary@ or AMotion to Determine the Applicability of the Stay.@ In *In re Roderick*, 425 B.R. 556 (Bankr. E.D. Cal. 2010), in a chapter 7 case, the court deferred expiration of the automatic stay by deferring discharge until a mortgagee decided whether to allow a loan modification. Rule 4004(c).

B. Proposing a Plan with a HAMP Mod Preconfirmation

Since all property of the debtor is still property of the estate preconfirmation, the debtor may propose a plan with a HAMP modification in it. The modification will have been negotiated with the creditor and placed in the plan. Does the plan need language that notifies the trustee and creditors of the modification? Including language in the plan that indicates the mortgage holder=s treatment is a modification would be helpful to the court, trustee and creditors even if not required. The Court has an independent duty to review chapter 13 plans and insure that they comply with the Bankruptcy Code. *See, e.g. Flynn v. Bankowski (In re Flynn)*, 402 B.R. 437 (B.A.P. 1st Cir. 2009). Since a plan modification would appear to be a modification of a

residential mortgage a court might not approve it, even if there is no objection, simply because it is a violation of section 1322(b)(2) unless there is an explanation. Therefore, language that makes clear that a HAMP modification is being incorporated in the plan is appropriate. Should payments under a HAMP mortgage be made directly or through the plan? There is no statutory requirement as to either alternative. Some districts have local rules that deal with this issue.

C. Proposing a HAMP Mod Postconfirmation

Is the homestead property of the estate? Pursuant to section 1327(b), upon confirmation, unless the confirmation order provides otherwise, Aall of the property of the estate [vests] in the debtor.@ In districts in which the property revests in the debtor, the bankruptcy court may not have jurisdiction over the homestead property and no order from the Court will be necessary. If there has already been relief from stay given to the lender, depending on the wording of the order, the lender may not need any further relief from the Court. Some Courts have local rules that deal with this issue. If the payment of the modified loan is to be made through the plan, the plan may need to be amended to reflect the modification terms. Loan modifications may require the filing of a reaffirmation agreement. Without a reaffirmation agreement, the modified loan may be a nonrecourse loan. *In re Roderick*, 425 B.R. 556 (Bankr. E.D. Cal. 2010). As stated in 11 U.S.C. ' 524(c), the loan modification is Aan agreement. . . the consideration for which, in whole or in part, is based on a debt that is dischargeable. . .@ A loan modification done postdischarge will not preserve the recourse nature of the loan. AA mortgage modified after the discharge is entered can only modify the terms under which the lien will be released.@ *Id.* at 565.

D. Is a Plan Modification Required?

Section 1329 of the Code deals with postconfirmation modifications of plans. It allows a modification to be proposed by the debtor, the trustee or an unsecured creditor. There are 4 grounds for modification: (1) Increase or reduction in the amount of payments to a particular class, (2) Extension or reduction of the time of payments, (3) Alteration of the amount of the distribution to a creditor whose claim is provided for by the plan to the extent necessary to take account of any payment of such claim other than under the plan, and (4) Reduction of amount to be paid under the plan to allow a debtor to obtain health insurance coverage. Since a HAMP modification usually reduces payments to the lender, such a modification clearly fits the criteria for a section 1329 modification.

Courts are divided over the instances in which a modification is allowed. Some courts require a substantial change in circumstances. *See, e.g.*, *In re Murphy*, 474 F.3d 143 (4th Cir. 2007); *In re Hoggle*, 12 F.3d 1008 (11th Cir. 1994). Other courts hold that any change is sufficient. *See, e.g.*, *In re Meza*, 467 F.3d 874 (5th Cir. 2006); *Barbosa v. Solomon (In re Barbosa)*, 235 F.3d 31 (1st Cir. 2000); *In re Witkowski*, 16 F.3d 739 (7th Cir. 1994).

Are modification payments (Trial Period or Permanent) made directly or through the trustee? There is no Code or Rule requirement that dictates payments must be inside or outside of the plan. There will be much better record keeping if the trustee makes the payments, and a trustee=s commission is charged on the payments. Another consideration is that the payment dates of the trustee may differ from the mortgage payment due dates. Local plan forms, rules, or culture determine which way the plan should be structured.

E. What Happens to Mortgage Claims at the End of a Case?

How do you ensure mortgage claims are current at discharge? Notice is the key requirement of any attempt to have a mortgage declared current at the time of discharge. Some districts use a Motion to Deem the Mortgage Current at discharge. Some districts use a plan provision to have the mortgage debt deemed current at discharge. These provisions are in many ways similar to the issue raised in *USAF, Inc. v. Espinosa*, 530 F.3d 895 (9th Cir. 2008), *aff=d*, 130 S.Ct. 1367, 176 L.Ed.2d 158 (2010). In *Espinosa*, the debtor placed a provision in his plan which declared that his student loan debt was paid off at discharge, even though the entire debt was not paid and no adversary case determining the dischargeability of the debt had been filed. As to mortgages, an adversary to determine the extent of a lien must be filed pursuant to Federal Rule of Bankruptcy Procedure 7001. The *Roderick* case cited above indicates that a modified loan will be nonrecourse post discharge without a reaffirmation. The new Rule 3002.1 going into effect on December 1, 2011 and the forms associated with it may obviate many of these problems.

F. Is It Possible to Modify a HAMP Modified Mortgage?

Section 1329(b)(1) of the Bankruptcy Code incorporates into it section 1322(b). Section 1322(b) is the section which prohibits modifications of residential mortgages. Therefore, unless the mortgage holder consents, it would appear that a HAMP modification through a plan would not be permitted. Why would a lender ever agree to an initial modification of the loan if it only served to establish a baseline for further modification? The HAMP rules do not discuss further modifications of the mortgage. If possible, or the lender consents, do you use the same procedure as used to do the initial modification? Using whatever procedure a debtor=s district uses for modification of plans would be the best route.

G. Litigation Over Denial of Mortgage Modification

A class action has been commenced in the state of Washington that claims Bank of America has intentionally withheld government funds intended to save mortgagors= homes from foreclosure. The homeowners claim Bank of America has intentionally thwarted the homeowners= access to TARP funds by denial of their requests for reasonable loan modifications. The class action says Bank of America accepted $25 billion in TARP funds but has only qualified 12,761 mortgages for permanent modifications out of more than 1 million loans that qualify for the relief.

In *In re Simarra*, Order of April 14, 2010, Case No. 09-14245, Judge Votolato ruled that a creditor could not object to a loan being dealt with in the court=s loan modification program without Aspecific reasons why loss mitigation would not be successful.@ The court held that failure of the debtor to make postpetition mortgage payments was not a sufficient reason. The fact that the creditor alleged that the debtor had not proposed a feasible plan was not sufficient. The creditor failed to show that either of these facts meant loss mitigation would not be successful.

VII. New Cases

A. U.S. Bank National Association v. Ibanez, Massachusetts Supreme Judicial Court, Case No. SJC-10694.

On January 7, 2011, the Massachusetts Supreme Judicial Court issued a decision that laid out problems mortgage lenders may have when bringing foreclosure actions in Massachusetts. Essentially, the Court reaffirmed what all real estate and bankruptcy lawyers know—in order to foreclose on a mortgage, the mortgage holder must hold title to the mortgage at the time it files the foreclosure action. An assignment of a mortgage need not be recorded, or even be in recordable form, but the chain of title must be established. In the *Ibanez* case, the mortgage

holder of record was Option One but U.S. Bank brought the quiet title action to establish a proper foreclosure after the foreclosure had already occurred. Option One had executed an assignment of the mortgage in blank prior to the foreclosure. U.S. Bank stated that this assignment was to Lehman Brothers Bank which then assigned the mortgage to Lehman Brothers Holdings Inc. which then assigned it to the Structured Asset Securities Corporation. It then assigned the loan, along with about 1220 others to U.S. Bank, as trustee of the Structured Assets Securities Corporation Mortgage Pass-Through Certificates, Series 2006-Z. This pool was then securitized and sold to investors. U.S. Bank stated that the assignment of the mortgage to U.S. Bank occurred pursuant to a trust agreement that was not offered in evidence. The Bank only provided a copy of a private placement memorandum ("PPM") that described the trust and that was unsigned. The PPM stated that the mortgages "will be" assigned to the trust and each assignment "will be intended to be a sale." The PPM also stated that each mortgage to be placed in the trust would be identified in a schedule attached to the trust agreement. No schedule was offered into evidence.

The Court held that U.S. Bank did not establish a proper chain of title. In Massachusetts, a securitization trust will need to produce 3 things to establish title to allow a foreclosure. (1) Executed copies of documents that show the chain of title from origination of the loan to securitization (2) an executed PSA and (3) a PSA loan schedule that clearly identifies the loan in question as one of the pooled loans.[24] If a pooled loan has proper documentation, there should be no issue with a foreclosure. However, some commentators doubt the ability of trustees to produce the proper documents in many cases.[25]

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[24] Adam Levitin, *Ibanez and Securitization Fail* (January 2011) available at: www.creditslips.org.creditslips /2011/01/ibanez.html.
[25] *Id*.

The result of the case is that U.S. Bank did not properly foreclose and thus there is a cloud on the title to the property. The property was sold to a purchaser who may or may not be a bona fide purchaser in light of these issues. A purchaser arguably should have had notice of the chain of title problems in looking at the land records. Title insurers may have liability in cases like this and it may be difficult, in light of this case, to obtain title insurance on foreclosed property sales in the future.

B. *Harp v. JPM Chase,* Maine Supreme Judicial Court, Case No 2001 ME 5, Han-10-252 (January 11,2011).

JPM Chase commenced a foreclosure proceeding upon Harp's mortgage before the loan was assigned to it. In the foreclosure action, JPM filed a summary judgment motion after the assignment and prevailed. The Supreme Court ruled that as long as JPM Chase had title to the mortgage at the time of the summary judgment motion, Harp had the ability to litigate against the real party in interest before foreclosure was granted. In all cases it is clear that the Court does not condone post-foreclosure assignments to cure title defects.

C. *Wells Fargo Bank, N.A. v. Eng*, New York State Supreme Court, Index No. 329792/2007 (Novmeber 15, 2010).

The Court granted summary judgment to Eng in the foreclosure case brought by Wells Fargo because Wells Fargo could not prove it had standing to maintain the action. Mr. Eng provided an affidavit of the Chief Executive Officer of HTFC that held the mortgage of record of Mr. Eng. The CEO stated that he did not know the person who signed a purported mortgage assignment to Wells Fargo, that the person had never been an employee of HTFC and never given authority to sign mortgage assignments as a "Limited Signing Officer."

D. *Federal Home Loan Mtge. Corp. v. Raia*, 2010 NY Slip Op 52003(U), 29 Misc. 3d 1226(A) (November 23, 2010)

A New York State attorney was sanctioned $5000 and ordered to pay the Volunteer Lawyers Project attorney's fees of $14532.50 in a case in which the attorney brought the action asserting that Federal Home Loan Mortgage Corporation was the owner and landlord of the premises to be foreclosed upon. The mortgage had been held in the name of Wells Fargo. The attorney stated that Wells Fargo assigned its bid to FHLMC. However, the Assignment was signed by the attorney himself. The assignment did not indicate which party he was signing for. He had authority to sign the document for FHLMC but gave no evidence of authority to sign for Wells Fargo. The court sanctioned the attorney for the false statements. "False allegations cannot be so cavalierly dealt with by claiming they were mere errors, when, in point of fact, these allegations served, until challenged, as a means to disguise petitioner's lack of standing." (quoting the homeowner's brief). The court said that the attorney had "been professionally irresponsible which has impeded the proper administration of justice." The Court referenced New York Rule of Professional Conduct 3.3 which states that an attorney is guilty of professional misconduct if he/she asserts "a false statement of fact or law to a tribunal or fail[s] to correct a false statement of material fact or law previously made." Rule 8.4 states that a lawyer shall not "engage in conduct that is prejudicial to the administration of justice" and the attorney had violated that rule as well.

Due in part to this case and other situations in which paperwork presented to courts was false or unclear, the New York Supreme Court is, as of October 20, 2010 and after, requiring all attorneys to submit an affirmation in every foreclosure case that states that the attorney communicated with a person at the mortgage firm and that person informed the attorney "that he/she (a) has personally reviewed plaintiff's documents and records relating to this case; (b) has

reviewed the Summons and Complaint, and all other papers filed in this matter in support of foreclosure; and (c) has confirmed both the factual accuracy of these court filings and the accuracy of the notarizations contained therein." The attorney then certifies that he/she "based upon my communication with . . . [the person at the mortgage firm] as well as upon my own inspection of the papers filed with the Court and other diligent inquiry . . . that, to the best of my knowledge, information and belief, the Summons and Complaint and all other documents filed in support of this action for foreclosure are complete and accurate in all respects." The attorney also understands that there is a duty to supplement this affirmation if new facts are found. The intent of the Supreme Court is to hold the attorneys liable for sanctions and other possible relief if the information is not true. "This new filing requirement will play a vital role in ensuring that the documents judges rely on will be thoroughly examined, accurate, and error-free before any judge is asked to take the drastic step of foreclosure."[26] In part this was prompted due to the number of foreclosures that are brought against unrepresented homeowners.

A new 2010 Rule 1.110(b) of the Supreme Court of Florida, effective February 11, 2010, provides:

> When filing an action for foreclosure of a mortgage on residential real property the complaint shall be verified. When verification of a document is required, the document filed shall include an oath, affirmation or the following statement: 'Under penalty of perjury, I declare that I have read the foregoing, and the facts alleged therein are true and correct to the best of my knowledge and belief.

Hopefully this rule will prevent future problems of this nature.

[26] Judge Ann Pfau, *New York Courts First in Country to Institute Filing Requirement to Preserve Integrity of Foreclosure Process* (October 20, 2010), available at: http://www.courts.state.ny.us/press/pr2010_12.shtml (*quoting* Chief Judge Jonathan Lippman).

VIII. CONCLUSION

HAMP mortgages are conceptually a good idea. However, the implementation of the program has been fraught with problems and delays that have minimized HAMP's practical value. The ongoing issues with mortgage lenders about title and allegations of fraud have only complicated the picture. It will be interesting to see how the program fares over the next few years.