June 30, 2002

Uniform Law Commissioner

Re: Uniform Nonjudicial Foreclosure Act
NCCUSL 2002 Annual Meeting, Saturday, July 27

Dear Uniform Law Commissioner,

The National Consumer Law Center[1] on behalf of its low-income clients, and Consumers Union,[2] are writing to express our substantial concerns with the Uniform Nonjudicial Foreclosure Act. The basic premise of this Uniform Act – that it is generally appropriate to replace judicial foreclosures with non-judicial foreclosures – ignores the increasingly serious problem of predatory lending in this country and the escalating foreclosure rates in hundreds of low and middle income neighborhoods. We do understand that judicial foreclosures can be both more costly and more time-consuming than their non-judicial counterpart, and we understand that you have provided some creative proposals to dealing with a few of these differences. Nevertheless, there are still a number of very important improvements that must be made to this Uniform Act.

Given the significant difference in consumer rights between the two types of foreclosure, consumer advocates will vigorously oppose this Act when it is introduced in the states. Making the proposed changes outlined below will significantly reduce the degree of difference in protections between this Act and judicial foreclosure regimes.

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[1] **The National Consumer Law Center, Inc**. (NCLC) is a non-profit Massachusetts Corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of sixteen practice treatises and annual supplements on consumer credit laws, including Truth In Lending, (4th ed. 1999) and Cost of Credit (2nd ed. 2000) and Repossessions and Foreclosures (4th ed. 1999) as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers.

[2] **Consumers Union** is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide consumers with information, education and counsel about goods, services, health, and personal finance; and to initiate and cooperate with individual and group efforts to maintain and enhance the quality of life of consumers. Consumers Union's income is solely derived from the sale of *Consumer Reports*, its other publications and from noncommercial contributions, grants and fees. In addition to reports on Consumers Union's own product testing, *Consumer Reports* with approximately 4 million paid circulation, regularly carries articles on health, product safety, marketplace economics and legislative, judicial and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

We respectfully request that you postpone approval of the draft Uniform Nonjudicial Foreclosure Act at your Summer 2002 meeting so that the changes listed below can be made before taking any action to approve the Act. Additionally, we believe there are serious concerns still to be raised, for example by advocates for tenants and condo owners. Listed below are those we have identified to date.

1. Modify section 206 to provide for meaningful due process rights and a separate mechanism for handling requests from residential debtors for mortgage workouts and other loss mitigation options, and to ensure that debtors are able to have access to an impartial hearing officer without having to post exorbitant bonds.

2. Modify section 502 to include minimum standards for the preparation of the appraisal report used in foreclosure by appraisal.

3. Delete all references appearing in the notes to a usual absence of homeowner defenses to foreclosure and to nonjudicial foreclosure as preferable to judicial foreclosure.

4. Modify the Act to address the special protections needed in connection with foreclosure of loans defined by other law as predatory or high cost loans.

5. Modify the 80% rule in subsections 403(c) and 503(c) to ensure that the 80% rule is not used in situations where it would result in unjustified profits to the lender, and modify subsections 404(d) and 504(d) to clarify that the failure to object to the stated foreclosure amount does not preclude a later claim that the foreclosure amount did not meet the 80% rule stated in subsections 403(c) and 503(c) or to otherwise challenge the adequacy of the foreclosure amount.

6. Modify section 607 to delete subsections 607(c)(1) and 607(c)(5) relating to the good faith of the debtor in relation to liability for a deficiency, to correct potential drafting errors in section 604(a), and to impose a fair market value test for calculating deficiency amounts resulting from all three forms of foreclosure.

7. Eliminate the portion of section 110 excusing minor errors which are not seriously misleading in foreclosure-related notices and the rule in section 104(d) placing the burden on the non-drafting party to show that a redefinition of the standards for performance is manifestly unreasonable, at least for residential debtors.

8. Shorten the one year time for a notice of foreclosure to remain effective, and limit the period of time after which a new foreclosure can be pursued with only 30 days notice, or with no notice, following a prior notice of foreclosure under section 207 or a notice of discontinuance of foreclosure under section 601(c).

9. Require added detail in the notice of default and the notice of foreclosure.

10. Change the phase-in rule in section 704 so that the Act becomes effective for all loans, including preexisting loans, on a specified date if the enacting state already permits nonjudicial foreclosure.

11. Postpone approval until the Act is amended to address these issues as well as those to be raised by other anti-predatory lending advocates.

Reasons for Requesting These Changes:

1. Request to modify section 206 to provide for meaningful due process rights and a separate mechanism for handling requests from residential debtors for mortgage workouts and other loss mitigation options.

The Prefatory Note to the Act attempts to justify the replacement of judicial foreclosure procedures with non-judicial on the basis that the Act incorporates meaningful due process rights. While consumer advocates in judicial foreclosure states will likely question whether sufficient due process safeguards can ever be incorporated into a non-judicial process, the current version of the Act falls short in several important respects. In addition, despite the success of loss mitigation efforts in reducing foreclosure rates over the past years, the Act fails to incorporate any notice or opportunity for the debtor to pursue such remedies as an alternative to foreclosure.

The Prefatory Note is correct in stating that whether the due process requirements associated with a foreclosure by a governmental entity are also required in a foreclosure by a private creditor "is not settled." We also recognize that the level and type of due process protections that are required in a particular situation depend upon a balancing of the respective parties' interests as described in Mathews v. Eldridge, 424 U.S. 319 (1976). Nevertheless, we believe that residential debtors must at a minimum be afforded an appropriate notice of the right to a hearing to contest the foreclosure, and a sufficient opportunity to exercise their hearing rights and present their grievance to an impartial and disinterested hearing officer.

Section 206(b) provides that if a residential debtor objects to the foreclosure, the creditor will conduct an informal "meeting" to hear the debtor's objections. This section further provides that the representative conducting the meeting may be an "employee, agent, servicer, or attorney of the foreclosing creditor." It is not even clear that this representative will in fact be the decision-maker, since section 206(c) states that the decision following the meeting shall be given by the "creditor."

By the time a matter has reached foreclosure, a debtor having a dispute with the lender has no doubt had countless discussions to no avail with employees or agents of the creditor or servicer and will likely view the "meeting" as futile when informed that it will be before an employee or agent of the creditor or servicer. Section 206 does not even require that the creditor representative be someone other than those involved in the decision to foreclose. The integrity of any legitimate hearing procedure is dependent upon the parties having access to, as well as the perception of access to, an impartial decision-maker. A procedure that involves creditor employees will be viewed with a high degree of skepticism from consumers and will therefore have a chilling effect on the number of debtors who actually seek to invoke the dispute procedure.

The hearing procedure established by the Act also fails to recognize and treat separately debtors facing payment default who are seeking to negotiate a workout agreement with the lender or who wish to access other loss mitigation options. Virtually all national mortgage lenders and their servicers, as well as the FHA, FreddieMac and FannieMae, have all come to recognize the benefits of loss mitigation strategies such as loan modifications and forbearance plans in curing defaults, preventing foreclosures and retaining homeownership[3]. Even where the workout option involves the loss of homeownership, such as by third-party sale, this may still be less costly to the lender than the foreclosure methods provided under the Act and eliminate the possibility of a deficiency for the debtor.

The Act should require that lenders provide information about their loss mitigation programs in the Notice of Foreclosure (as well as in the earlier Notice of Default), and also provide information about the availability of local HUD-approved housing counselors. The Act should also designate a procedure separate from the dispute mechanism contained in section 206 for debtors who have applied for a workout arrangement. This procedure should ensure that the foreclosure process is stayed pending the resolution of a workout application, and that the time to object to the lender's right to foreclose is also stayed.

By creating a separate procedure for dealing with loss mitigation requests, the number of debtors objecting to foreclosure will be reduced. For the group of debtors that actually seeks to challenge the claim that they are in default or otherwise present a defense to the foreclosure, they should be afforded the opportunity to a trial-type hearing before an impartial hearing officer. *It is essential the debtors have access to this impartial hearing officer without having to post exorbitant bond amounts.* Since the number of these objections will be minimal, we propose that the simplest and most cost-efficient procedure in this situation would be for the creditor to use a judicial foreclosure process. This would still preserve the "fundamental premise" of the Act stated in the Prefatory Note (a premise which we refuse to embrace) that in the "great majority" of cases, judicial involvement is "unnecessary because there is no dispute between the debtor and creditor." Requiring judicial foreclosure only in those few cases where a residential debtor objects to the foreclosure would still permit the overwhelming majority of cases to be conducted by non-judicial foreclosure.

Irrespective of this request to modify section 206 to require a judicial hearing for foreclosure objections, other changes to the objection procedure should be considered. Section 206(a) provides that a request for a "meeting" to object to foreclosure must be received by the creditor within 30 days after the notice of foreclosure is given to the

[3] *See* "Lenders Trying an Alternative to Foreclosure," New York Times, May 4, 2002.

debtor. Section 204 should require that the exact date when the request must be received be specified in the notice. In addition, a drafting error in section 204(b)(10) and the sample Notice of Foreclosure should be corrected as it states that the request must be received within 15 days. We support the longer 30-day period provided in section 206(a) and request correction of the 15 day references.

Section 204 should also require that the notice indicate that the "meeting" can be requested orally or in writing and provide a toll-free number that the debtor can use to request a meeting. Section 204 should also require that the notice provide a description of the hearing procedure, and indicate that the debtor can request and obtain relevant documents and records from the creditor prior to the "meeting."

The Notice of Foreclosure should provide a detailed description of the process that the creditor intends to use that may result in the loss of the debtor's property interest. Section 204(b)(8) states that the Notice must include a "statement of the method or methods of foreclosure the foreclosing creditor intends to use." The sample Notice of Foreclosure attempts to satisfy this requirement in paragraph 8 by simply stating that the lender "elects to foreclose by auction or by appraisal." Creditors should be required to explain in detail the foreclosure process, particularly the new methods of foreclosure by negotiated sale and appraisal.

Finally, the consequences of failing to provide adequate notice of foreclosure to interested parties are too severely restricted under the Act. Section 205(c) provides that a creditor who fails to provide a timely notice of foreclosure to a party who has recorded a proper request for such notice is liable to the party only for damages in the amount of $500, and no other remedy against the foreclosing creditor is available. It is hard to conceive that this provision would survive a due process challenge based on the holding in Mennonite Board of Missions v. Adams, 462 U.S. 791 (1983). The Proposed Comments to section 203 also state that "the only effect of a foreclosing creditor's failure to give notice to a person entitled to notice … is to preserve that person's interest." Though the comment does not seem consistent with language in section 203(a), we believe that Act should clearly state that compliance with the statutory notice requirements is a prerequisite to foreclosure and that noncompliance with the mandatory requirements can be grounds for invalidating the foreclosure. Strict compliance with the notice requirements is necessary to ensure that the foreclosure procedures are fairly conducted and that they will have the potential for producing an adequate sale price.

2. Request to remove statements that nonjudicial foreclosure is preferable to judicial foreclosure and that homeowner defenses are rare or unusual.

The Prefatory Note to the Uniform Nonjudicial Foreclosure Act states: "This Act is offered in the belief that nonjudicial foreclosure can be both fair to borrowers and efficient from the viewpoint of lenders, and hence a superior form of foreclosure for all of the affected parties." Judicial foreclosure, in the approximately 20 states that have it, is an important part of the fight against predatory lending. NCCUSL should not adopt a position favoring nonjudicial foreclosure over judicial foreclosure unless and until other strong protections are in place to address predatory lending, an issue outside the apparent scope of your Act. Removing the statements favoring nonjudicial over judicial foreclosure from the Prefatory Note would at least avoid taking a position on this sensitive issue.

The Prefatory Note reveals that the statements favoring nonjudicial over judicial foreclosure are based on a premise which is incorrect with respect to predatory loans. The Prefatory Note states: "The fundamental premise of this Act is that there is ordinarily no dispute between the debtor and creditor." It characterizes the existence of a defense to foreclosure as "exceptional" and occurring in "a small fraction" of foreclosures. Our experience in more than a decade of fighting predatory loan practices shows that these statements, at least for predatory loans, are untrue. We have seen and heard of many predatory loans where there is a defense to payment, including situations where a homeowner was induced to sign a blank loan application, tricked by a contractor into signing for home secured credit, or promised one set of terms and conditions and induced to sign for different terms[4].

After exhaustive community testimony, the U.S. Departments of Treasury and Housing and Urban Development documented predatory lender's tactics and the consequences for borrowers:

> In a predatory lending situation, the party that initiates the loan often provides misinformation, manipulates the borrower through aggressive sales tactics, and/or takes unfair advantage of the borrower's lack of information about the loan terms and their consequences. The results are loans with onerous terms and conditions that the borrower often cannot repay, leading to foreclosure or bankruptcy.[5]

The states of North Carolina, Georgia, and California, as well as the District of Columbia, have all enacted anti-predatory lending legislation. Anti-predatory lending bills have been considered or are currently pending in Hawaii, Minnesota, Colorado, Ohio, Florida, New York, New Jersey, to name just a few. The City of Oakland has passed an ordinance, now subject to litigation, and an ordinance is pending in the City of New York.

AARP has pointed out that elderly borrowers are particularly vulnerable to predatory practices. In a study of subprime lending and older borrowers, AARP found that borrowers over age 65 were three times as likely to have a subprime loan as borrowers

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[4] Norma Paz Garcia, *Dirty Deeds: Abuses and Fraud in California's Home Equity Market*, published by Consumers Union (1995), posted at: http://www.consumersunion.org/finance/home-ca1.htm

[5] Joint U.S. Department of Housing and Urban Development-U.S. Department of the Treasury Task Force on Predatory Lending, *Curbing Predatory Home Mortgage Lending,* at 16 (June 2000), at http://www.hud.gov/library/bookshelf18/pressrel/treasrpt.pdf.

under 35.[6] Justification for those more expensive loans was lacking: at least 11% of those borrowers over age 65 had FICO credit scores qualifying them for prime loans.[7]

Removing the statements in the Note suggesting a preference for nonjudicial over judicial foreclosure, and the statements suggesting that homeowner defenses are rare, would avoid taking a side in the highly charged debate over predatory lending, and would eliminate statements about the frequency of defenses that are not accurate for this type of lending.

3. Request to modify section 502 to include minimum standards for the preparation of the appraisal report used in foreclosure by appraisal.

The Act provides that a foreclosure may be accomplished without an actual sale of the property. Similar to strict foreclosure at common law, title to the property may pass to the creditor without any judicial action and without the property being offered for sale to third parties. (The two states that currently permit strict foreclosure, Connecticut and Vermont, both require that the creditor obtain an order from a court declaring the debtor to be in default, and also provide a right for post-foreclosure redemption.) The Act simply requires that the creditor obtain an appraisal and provide notice to the debtor that unless an objection is received, title to the collateral will be transferred to the creditor, and that a "foreclosure amount" designated by the creditor will be credited to the debtor's account.

As with strict foreclosure at common law, this process can be grossly unfair to borrowers, who stand to lose substantial equity in their property, and can provide a windfall to lenders. Any process that allows such a forfeiture of a debtor's property interest must be strictly regulated. While we believe that the sections dealing with foreclosure by appraisal should be substantially revised, at a minimum section 502 should be modified to include some basic standards for the appraisal report. In its current form, the section does not require that the appraisal be based on an inspection of the interior of the home or that the conclusion of value should be based on a comparable value method or some other widely-accepted valuation approach. Though section 502 states that the debtor is to provide reasonable access to the property to the appraiser, the section does not address what may happen if the appraiser does not gain such access. The section should provide that a "drive-by" appraisal cannot be used for a foreclosure by appraisal. We would look forward to working with the drafting committee in developing other appraisal standards.

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[6] Sharon Hermanson and Neal Walters, "Subprime Mortgage Lending and Older Borrowers." AARP Research, March, 2001, citing unpublished study by H. Lax, et. al. http://research.aarp.org/consume/dd57_lending.html

[7]Ibid.

4. Request that Act be modified to address special protections needed in connection with foreclosure of loans defined by other law as predatory or high cost loans.

The interplay between predatory lending and foreclosure does not appear to have been considered in the preparation of the Uniform Nonjudicial Foreclosure Act, although foreclosure is a key issue in predatory lending. Subprime lenders, some of whom engage in predatory practices, are overrepresented in foreclosure. At the end of 1999, the loans of just 16 large subprime lenders accounted for possibly more than 72,000 families being in or near foreclosure.[8] The cost of predatory lending, even before the costs of foreclosures, emotional distress, and the cost of destabilized communities, is roughly $9.1 billion a year.[9] The astounding growth of the rate of foreclosure on homeowners over the past two decades compared to the growth of homeownership, leads to questions of the quality of lending.[10]

AARP has developed an extensive model law to restrain predatory practices in home-secured lending.[11] That model law contains specific proposed changes both for states with judicial foreclosure and for states with nonjudicial foreclosure, essentially requiring a court hearing and declaration of absence of defenses for covered high cost loans prior to initiation of a nonjudicial foreclosure. The AARP model bill, written by the National Consumer Law Center and the N.C. Self Help Credit Union, has been endorsed by the American Congress of Consumer Organizations (ACCO), whose membership includes ACORN, Consumer Federation of America, Consumers Union, Essential Information, the National Association of Consumer Advocates, Public Citizen, U.S. PIRG and 53 state and local consumer organizations.

It would be irresponsible for the NCCUSL to endorse a new Nonjudicial Foreclosure Act unless that Act is structured to address predatory lending, and that adoption of this Act by a state does not eliminate any need for additional safeguards and preconditions in predatory lending generally, or in connection with foreclosure of predatory loans.

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[8] Kurt Eggert, *Held Up in Due Course: Predatory Lending, Securitization and the Holder in Due Course Doctrine*, 35 Creighton Law Review 503, at 513, citing Allen Fishbein and Harold L. Bunce, *Subprime Market Growth and Predatory Lending*, at http://www.huduser.org/publications/pdf/brd/13Fishbein.pdf.

[9] Eggert, *Held Up*, 35 Creighton Law Review at 513, citing *Predatory Mortgage Lending: The Problem, Impact and Responses: Hearing Before the Senate Commission on Banking, Housing, and Urban Affairs*, 107th Congress (2001) (testimony of the Honorable Thomas J. Miller, Attorney General, State of Iowa, July 26, 2001). The cost analysis was first performed and reported by the Coalition for Responsible Lending. Eric Stein, *Quantifying the Economic Cost of Predatory Lending, A Report from the Coalition for Responsible Lending 2*, at http://www.responsiblelending.org.

[10] *See* Margot Saunders, *The Increase in Predatory Lending and Appropriate Remedial Actions*. 6 North Carolina Banking Institute (April, 2002) 112. From 1980 – 1999, the rate of foreclosure on home-owned units in the United States increased 227% while the rate of homeownership increased 2%.

[11] To view the Model Act, go to http://research.aarp.org/consume/d17346_loan.html.

5. Request to modify the 80% rule in subsections 403(c) and 503(c), and to modify subsections 404(d) and 504(d) to clarify that these subsections do not preclude a claim against the creditor or its agent for the failure of the foreclosure amount to meet the 80% rule stated in subsections 403(c) and 503(c) or to otherwise challenge the adequacy of the foreclosure amount.

Sections 403 and 503 permit a foreclosing creditor to retain all of the proceeds of a negotiated sale, and all of the appraised value, which exceeds the creditor-selected "foreclosure amount." Under Sections 608 and 604(a), the "foreclosure amount" is also used to determine a debtor's liability for a deficiency. Despite this significance, the concept of a "foreclosure amount" under the Act is virtually without precedent in the law; it is an amount that bears no relationship to a creditor's actual expenses but rather is determined solely in the creditor's "discretion." (See Proposed Comments to Sections 403 and 503).

Given the strong potential for abuse in the exercise of this unbridled discretion, the Act offers some substantive protection in subsections 403(c) and 503(c) by requiring that the foreclosure amount be at least 80% of the sale price under section 403, or the appraised value under section 503. A homeowner, guarantor, or another interested party also may stop the use of one of these two methods by objecting.

We do not agree with the concept that a creditor should always be able to retain 20% of the sale or appraisal price, particularly in high cost markets. In June 2002, the median home price in Alameda County, California was reported at $530,000. A negotiated sale of this home at that sale price would allow the creditor to retain $106,000 of the homeowner's equity, far more than the creditor's expenses of foreclosure and sale. Sections 403(c) and 503(c) should be modified to provide that the foreclosure amount shall be at least 85% of the gross sale price or value of the collateral for homes where the sale price or value is less than $150,000, 90% of the gross sale price or value of the collateral for homes where the sale price or value is between $150,000 and less than $300,000, and 95% of the gross sale price or value of the collateral for homes where the sale price or value is $300,000 or higher.

The 80% rule contained in the draft, as modified above, can be a safeguard against a creditor setting a low foreclosure amount and then retaining very significant sale proceeds over that amount. It will not, however, prevent other abuses by creditors, such as a pair of creditors who buy property from one another in pairs of low-price negotiated sales. (This type of conduct has been seen in "courthouse steps" foreclosure auctions.) The 80% rule (or 85%-95% as proposed) provides an important check on an approach that otherwise could allow any foreclosure amount, however low, in the absence of objection.

However, subsections 404(d) and 504(d) undermine the protective effect of the 80% rule and provide a license to unscrupulous lenders to engage in collusive price-setting. These subsections state that a person who received notice and did not object "may not assert that the foreclosure amount was inadequate." A homeowner's failure to object to the notice should not waive the right of the homeowner or his or her guarantor to assert the basic safeguard built into these alternative methods - that the foreclosure amount be set to reflect at least 80% (or 85%-95% as proposed) of a sale price or an appraised value that is not obtained through improper or collusive price-setting between the foreclosing creditor, purchaser, or appraiser.

The Prefatory Note to the Act states that any potential concern about collusive price-setting or other fraudulent conduct is "eliminated" because a debtor can simply object to the negotiated sale or sale by appraisal if the foreclosure amount is unreasonable. There are many common situations in which a homeowner is unlikely to object to any notice received (assuming it is received), regardless of its contents. (The Act does not provide that the notice of proposed negotiated sale under section 403 and the notice of appraisal under section 503 are subject to the special notice requirements for residential debtors contained in section 108(b)). This can be due to failure to understand the notice, literacy levels, language difficulties, mental challenges for some older homeowners, or just a paralysis in decision-making stemming from the financial crisis that precipitated the foreclosure.

Legal services attorneys have often reported to us that people of all ages commonly fail to understand, or do not even read, foreclosure-related notices. Empirical research on consumer bankruptcy in eight federal judicial districts showed that a medical problem, including medical debt or interruption in employment income due to a medical condition, was associated with nearly half of all bankruptcies, and with an even higher percentage of bankruptcies for women-headed households and the elderly.[12] Consumers facing the deep financial difficulties which lead to foreclosure on a family home may also be experiencing medical bills or interruption in income, or that common financial stressor, divorce. This is a difficult time to make informed financial decisions about options presented in a written notice.

In addition, the debtor may not have sufficient information to evaluate the "foreclosure amount" and to detect potential abuse until after the "time of foreclosure." This is exacerbated by the limitations of the Act's notice requirements. For example, section 403 does not even require that the creditor identify in the notice of proposed negotiated sale the potential purchaser of the property, information that would clearly assist the debtor in determining whether the sale price is collusive. As a result, we believe that a debtor should be allowed to object to a negotiated sale, or sale by appraisal, at any time prior to the "time of foreclosure." The Act currently would preclude (in Section 404) any objection made after the date which is seven days or more prior to the *proposed* sale, even if the actual sale date is much later.

The 80% rule currently in the draft, or the alternatives proposed, will not provide any protection to a homeowner if the debtor is precluded from asserting that the foreclosure amount was grossly inadequate or the result of collusive price-setting. If the rule is waived by failure to object before the foreclosure by sale or appraisal, then sections

[12] Melissa A. Jacoby, Teresa A. Sullivan, and Elizabeth Warren, *Rethinking Debates Over Health Care Financing: Evidence from the Bankruptcy Courts*, 76 N.Y.U.Law Rev. 375, 377 (2001).

404(d) and 504(d) would give a lender who knows that its consumers are unlikely to read or to understand notices an opportunity to set a low foreclosure credit amount which is claim-proof even if it does not meet the statutory 80% requirement.

Far worse, since there is no requirement in the Act that the negotiated sale price or foreclosure amount be fair and reasonable, or bear any relationship to fair market value, sections 403(c) and 503(c) would insulate from liability an unscrupulous lender who has engaged in collusive price-fixing or other fraud. The lender could also use this fraudulently obtained foreclosure amount in seeking a deficiency under sections 607 and 608 against the debtor and the debtor's only defense (one with severe limitations as discussed below) is that he or she acted in "good faith." The potential for abuse of these new foreclosure procedures by predatory mortgage lenders is of great concern since predatory loans are often made with low loan-to-value ratios without consideration of a borrower's ability to repay the loan.

Our concern here is not limited to those instances where there is actual fraud or collusive behavior. The real problem is that there is no incentive in this Act for the lender to seek the highest sale price. For example, a lender with a mortgage balance of $100,000, secured by a home with $225,000, would suffer no consequences from accepting the first offer for the sale of the house at $125,000.

For these reasons, subsections 404(d) and 504(d) should be modified to provide that any waiver or bar for failure to object does not apply to noncompliance with the 80% rule (or 85%-95% as proposed) of subsections 403(c) and 503(c), or otherwise preclude a challenge to the adequacy of the foreclosure amount. Protection of consumers from collusive price-fixing and other predatory foreclosure practices must not hinge on the consumer's requirement to file a timely objection.

6. Request to modify section 607 to delete subsections 607(c)(1) and 607(c)(5) relating to the good faith of the debtor in relation to liability for a deficiency, to correct potential drafting errors in section 604(a), and to impose a fair market value test for calculating deficiency amounts resulting from all three forms of foreclosure.

For consumers in many states, the Act's imposition of a potential deficiency judgment is a significant erosion of existing consumer rights. In approximately 28 states, there is currently either an absolute bar to recovery of a deficiency or substantial consumer protections that limit its availability. For example, many states that permit deficiencies require that the sale price be confirmed by a court as representing the fair market value of the collateral or otherwise limit the deficiency to some form of a fair market value test. Many of these states also require that a suit seeking a deficiency be brought within a short limitation period of 1 year or less. Still other states permit deficiencies only where the debtor has been afforded the substantial right of post-foreclosure redemption.

Unlike these existing laws, the Act's limitation on deficiencies is inadequate because creditors should have little problem establishing that the debtor acted without the requisite "good faith." In addition, once an entitlement to a deficiency has been established, there is no fair market value limitation where the foreclosure is by negotiated sale or appraisal.

Section 607(c)(1) provides that a debtor has not acted in good faith where the debtor does not vacate the collateral in a "reasonable time" after the "time of foreclosure." While a provision in an earlier draft of this section defining reasonable time as 10 days has been deleted, it has effectively been retained by the Proposed Comment which states that "a period of one to two weeks would ordinarily be a reasonable time for the debtor to vacate the property. "

In many instances, one to two weeks is simply not a reasonable time to vacate following a foreclosure. The impact of foreclosure can be devastating, particularly for elderly homeowners, families with young children, and those who have owned their homes for many years. It is unreasonable to expect that families can secure new housing and complete moving arrangements in one to two weeks, a period that may even be shorter that that provided to tenants in many states under landlord/tenant law.

In addition, the notices required by the Act do not provide the debtor with sufficient information for a debtor to determine whether a creditor will in fact seek a deficiency or how the debtor can satisfy the good faith requirement. Although the sample Notice of Foreclosure provides some explanation of the Act's characterization of "good faith," it does clearly specify that the failure to vacate within one to two weeks may be deemed bad faith. (Since the explanation to be provided under section 204(9) is not mandatory and may be included "if applicable," section 204 should be modified to state that the failure to provide an explanation of the debtor's right to avoid a deficiency in the Notice will bar the creditor from later seeking a deficiency).

There is also no requirement in the Act that the creditor notify the debtor as to the exact date of the "time of foreclosure" in the case of a foreclosure by negotiated sale or appraisal, leaving the debtor without specific reference to gauge a "reasonable time." While the "reasonable time" under section 607(c)(1) apparently also runs from the time a notice demanding possession is sent to debtors, this notice would not be sent by the creditor if there has been a purchase and it may likely provide for a period to vacate based on state eviction law, which may be longer than one to two weeks.

Also, since the Act does not require that the debtor be provided with a copy of the Affidavit prepared under section 602, or any notice of the outcome of the auction sale or the application of the foreclosure proceeds under section 604, the debtor may not immediately be aware that a creditor is likely to pursue a deficiency.

Section 607(c)(5) permits the recovery of a deficiency where the debtor has failed to provide "reasonable access to the collateral for inspection by the foreclosing creditor and prospective purchasers." While the granting of such access theoretically may be advantageous to the debtor by potentially producing a higher foreclosure sale price, the reality is that most homeowners are not likely to permit pre-foreclosure access to the property. Most are embarrassed by foreclosure and would seek to avoid any public display of their financial problems in front of their children, other family members, and friends and neighbors. Particularly where the homeowners are working desperately to save their home from foreclosure, permitting access to potential purchasers may be viewed as a sign that their efforts to solve the problem have failed. Other homeowners may be legitimately resistant to having unknown individuals entering their home based on safety and security reasons. Still others may question the creditor's right to seek such access for itself and others where no clear legal right may exist under state law or the mortgage documents.

If the Act is to permit creditors an opportunity to obtain a deficiency judgment, then it should be limited to cases involving fraud or waste caused by the debtor. Thus, subsections 607(c)(1) and 607(c)(5) should be stricken.

The Act also fails to include adequate protections for consumers in the method of calculation of the deficiency amount. Section 604(a) provides the order in which the "foreclosure amount" is to be applied by the creditor after a foreclosure. Although the section apparently applies to all three forms of foreclosure and is dependent upon the existence of a "foreclosure amount," a foreclosure by auction sale does not involve the designation of a "foreclosure amount." The "foreclosure amount" is a term of art that is not defined in the general definition of the Act, section 102, and is therefore defined by its use in sections 403 and 503. In the case of foreclosure by auction sale, it would appear that the amount to be applied under the formula set out in section 604 should be the sale price.

In addition, the Act includes a protection for consumers in section 608 that permits a court to substitute the sale price obtained at auction sale with an amount representing 90% of the fair market value of the collateral. Consistent with many similar provisions under existing state law, we propose that this section be modified to adopt the full fair market value of the collateral rather than 90%. Also, the fair market value test set out in section 608 should not be limited to auction sales. For the reasons noted above concerning the lack of adequate protections in the Act against collusive price-setting and other fraudulent behavior, the fair market value limitation on deficiencies should apply equally to foreclosures by negotiated sale and appraisal.

Finally, since the Act represents such a significant departure from existing law in states that currently prohibit deficiency judgments, section 607 should be modified to include two additional consumer protections. First, a creditor seeking a deficiency should be required to bring the action within a short period after the foreclosure, ideally within 6 months but not more than one year after the foreclosure. As consumers attempt to rebuild their lives after the disastrous consequences of a foreclosure, they should not have to endlessly fear that they may be subject to a large deficiency judgment. (Note that in some states the statute of limitations for general contract claims can be as long as 10 years). Second, if the creditor does seek a deficiency, the Act should require that the debtor be provided with a right to redemption, at least until such time as the court rules on the entitlement to a deficiency and the collateral has not been sold to a bona fide purchaser.

7. Request to eliminate two "escape hatches" borrowed from the UCC, at least for residential foreclosure.

Section 110 excuses minor errors not seriously misleading in foreclosure-related notices. This language appears to be borrowed from UCC section 9-616(d), where it applies only to the one entirely new notice which was added by revised Article 9. That notice is a simple post-disposition disclosure, not a notice upon which the consumer may have to act very promptly. A nonjudicial foreclosure notice is substantively different from an Article 9 post-disposition notice. First, the consumer's home is at stake, not merely a car or a couch. Second, the concept of requiring foreclosure-related notices is not new, as the 9-616 notice was new. Third, the consumer's precarious financial position at the time of foreclosure may well make harmful even minor errors which are not objectively "seriously misleading." A small misstatement in the amount of daily interest accruing, or in any other aspect of the amount that the consumer must repay to cure a default, could affect whether the consumer is able to prevent the foreclosure. Particularly for residential debtors, the "minor errors not seriously misleading" standard for sufficiency of notices in section 110 should be deleted.

Section 104(d) contains another rule borrowed from the UCC which is not appropriate for residential debtors in foreclosure. Section 104(d) places the burden on the challenging party to show that a definition of the standards for performance of an obligation is manifestly unreasonable. This is a standard UCC, "freedom of contract" based approach, developed for commercial law contracts. However, freedom of contract is largely meaningless for residential home loan borrowers. Lenders, not borrowers, draft the contracts; or lenders use standard contract language that will be acceptable to secondary market buyers. Home loan borrowers commonly have no say in the contract language. The "manifestly unreasonable" standard shifts the burden to the homeowner to prove that a standard is unreasonable, and manifestly so, instead of leaving any obligation to show reasonableness on the drafter or offerer of the contract. Section 104(d) should be eliminated or restricted to non-residential debtors.

8. Request to resolve timing problems with the notice of foreclosure: shorten the one-year time for initial effect, eliminate the tolling period, and eliminate or restrict provisions excusing the full 90 day period after re-noticing.

Section 207 allows the foreclosure to be conducted up to one year after an original notice of foreclosure is recorded and provided to the debtor. This would permit a lender to effectively take no action on a foreclosure notice for almost 8 months and then suddenly advise the debtor of an auction date, or give notice for a negotiated sale or foreclosure by appraisal (and the notices of auction, negotiated sale, or appraisal are not covered by the protections of section 108(b)). This period of inaction could seriously undermine the impact of the initial foreclosure notice and potentially lull the debtor into believing that the lender will not proceed with foreclosure. This may be exacerbated in the situation where the debtor and lender have been attempting to negotiate a workout agreement during the period of inaction, especially if the homeowner has resumed payments. The validity period for the notice of foreclosure should be shortened to not more than six months.

Section 207 also tolls the limitation period on the duration of the notice of foreclosure while a foreclosure has been enjoined by a court and for 45 days after the lifting of the automatic stay in bankruptcy. In a Chapter 13 bankruptcy, this part of section 207 would allow a lender to rely upon an original foreclosure notice that was sent several *years* before a subsequent dismissal of the Chapter 13. The tolling provision of section 207 should be eliminated or at a minimum subject to some reasonable limitation on the total duration of the effective time for the notice.

Section 207 permits a new foreclosure to be pursued with only 30 days notice after a prior notice has expired. Section 601(c) permits foreclosure to be reinitiated with no notice after a notice of discontinuance. The fact of a prior notice of foreclosure should not shorten the basic 90 day notice period. The fact that a notice of foreclosure was given several years ago, or even last year, but no foreclosure was completed, should not trigger an expedited period for a subsequent foreclosure process. The homeowner who receives a notice of foreclosure needs time to understand the issues, get legal advice if possible, attempt workout, or plan to sell and move. *We request that the "shorter second time" concept be removed from sections 207 and 601(c).* If you choose not to make this change, you should still add a cap on the time during which a full no notice period would not be required. Home mortgages can be for 30 years. If a prior notice is to eliminate the need for later notice, or to shorten a later notice period, this should occur only when the two foreclosure proceedings are close in time, perhaps within six months or at most, one year.

Finally, section 108(a) would apparently operate to allow a creditor, when providing a new notice to a party it has determined would not receive the original notice, to rely upon the time periods for the taking of actions under the Act as set out on the original notice. If we are reading this section correctly, a notice of default providing 30 days to cure a default, if returned as undeliverable, could then be resent to the debtor at a corrected address without adjusting the time period for curing the default, even if the letter is actually received by the debtor on the last day of the cure period or after the cure period has expired. Since it is critical that debtors have the full 30 days to cure a default on a notice of default, at least 90 days to redeem and at least 30 days to object to foreclosure on a notice of foreclosure, creditors should be required to issue a new notice with corrected time periods in this situation.

9. Request to require added detail in the notice of default and the notice of foreclosure.

Section 202(b)(2) requires that the notice of default provide "the amount to be paid" if the default is curable by payment of money. The comments give a useful example, which itemizes which payments are missing and identifies any amount owing for insurance coverage force-placed to protect the lender's interest. Unfortunately, the black letter of the draft Act does not require that the level of detail in the comments be met. Instead, a simple statement of the total amount necessary to cure, unlike the sample Notice, would satisfy the plain language of section 202(b)(2).

Section 204 is similar. It requires that the notice of foreclosure provide "the amount to be paid or other action necessary to redeem," including a daily amount to calculate the balance owed as of future dates. Section 204(b)(7). The sample form in the comments gives this example: "the entire balance of $137,455.34 is now due and payable." This is insufficient information.

The notice of default and the notice of foreclosure should be required to provide an itemization of the amount necessary to cure and to redeem, respectively, identifying which payments are missing, the total of principal and interest, late charges, and charges for items such as forced-placed property insurance or inspection and monitoring fees. Mere disclosure of the balance due will not help the homeowner to determine whether the amounts shown are consistent with the homeowner's own record of or recollection of payments made, whether the balance includes force-placed insurance, or whether there is a dispute related to the amount claimed by the lender. Itemization of the amounts necessary to cure and redeem should help some homeowners to understand that the amount claimed is owed, and assist other homeowners to prepare for and use the optional meeting with the creditor to explore any disagreements about the amount owed. *The black letter in sections 202(b)(2) and 204(b)(7) should be adjusted to require the kind of itemization included in the illustrative form in the comment to section 202.*

The illustrative notice of default in the comments contains the date when the right to cure expires. However, the language of section 202 does not clearly require these items. *Sections 202 and 204 should be amended to clarify that the Notice of Default must give the date when the right to cure expires, and the Notice of Foreclosure must give the date when the redemption period expires.*

10. Request to change the phase-in rule in section 704 so that the Act becomes effective for all loans, including preexisting loans, on a specified date if the enacting state already permits non-judicial foreclosure.

The rule of section 704 that the Act applies only to loans originated after the effective date of the Act is sensible for states which are converting from judicial to non-judicial foreclosure. Homeowners who had the protection of judicial foreclosure at the time a loan was originated should not later be deprived of that protection for an existing loan. The transition rule in section 704, with application to new loans only, makes less sense in a state which replaces an existing nonjudicial foreclosure statute with the uniform act. Two statutes could apply to a single home, since one property may have liens on it from loans originated both before and after passage of the Act. It would also be anomalous for a repealed non-judicial foreclosure statute to continue to apply to some loans for years or even decades even though it may not have been kept up to date after it was replaced by this Act.

11. **Request to postpone approval until the Act is amended to address these issues as well as those to be raised by other anti-predatory lending advocates.**

The authors of this letter speak only for our own organizations. The phone calls we made after first learning of this Act in late May 2002 indicate that the many consumer and community organizations nationwide working against predatory lending were unaware of this Act. The lead anti-predatory lending advocates for ACORN and NCLC were not aware of it, nor were those others whom we contacted. The Conference must consider and address further changes to prevent contributing to the substantial problems caused by predatory lending.

Process issues

We became aware of this Act in late May 2002. We expressed preliminary concerns about it by email of May 24th, and received a short response on the issue raised. We provided courtesy notice that Consumers Union would be expressing deep concerns about the Act to the Conference Executive Director on June 11th, to the Committee Chair on June 12th, and to the Reporter on June 12th. We did not receive a call back from the Committee Chair or the Reporter during the preparation of this letter. We stand ready to work with the drafting committee or others in the Conference to try to work out the issues raised before or during your Annual Meeting.

Conclusion

We ask you to:

1) postpone approval of the Act,

2) make the changes described in this letter,

3) consider additional requests from advocates representing consumers in predatory lending cases, and

4) decline to approve any Uniform Nonjudicial Foreclosure Act unless and until it substantially addresses these important issues.

If you would like to discuss these issues, please do not hesitate to call John Rao of the National Consumer Law Center (617 542-8010) or Gail Hillebrand at Consumers Union (415 431-6747).

Thank you very much for your attention to these important issues.

Very truly yours,

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