Mortgage Modifications or Surrender:
Are They Getting Clients Relief?

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Recent Court Decisions Highlight Proper Party Issues in Non-Judicial Foreclosure States

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The requirement that a foreclosing party have the right to foreclose applies with equal force in non-judicial foreclosure states.[1] In fact, because mortgage creditors are permitted to avoid the judicial process, they are often held to a higher standard under state law with respect to strict compliance with pre-foreclosure procedural requirements.[2] Several recent court decisions confirm that standing and proper party issues can be successfully litigated in non-judicial foreclosure states.

U.S. Bank Nat. Ass'n v. Ibanez

In *U.S. Bank Nat. Ass'n v. Ibanez,*[3] two trustees acting on behalf of owners of mortgage-backed securities brought actions in the Massachusetts state land court seeking declaratory judgments that the foreclosure sales they had conducted on two properties were valid and that they held clear title. At the time of the sales, the foreclosing trustees held the borrowers' promissory notes indorsed in blank. However, when they sent out the foreclosure notices, advertised, and conducted the foreclosure sales, the trustees had not

[1] This article first appeared in the March/April 2011 edition of NCLC Reports. It is reprinted with the permission of NCLC and its authors, John Rao and Geoff Walsh.
[2] U.S. Bank Nat. Ass'n v. Ibanez, 941 N.E. 2d 40, 49-50 (Mass. 2011) ("Recognizing the substantial power that the statutory scheme affords to a mortgage holder to foreclose without immediate judicial oversight, we adhere to the familiar rule that 'one who sells under a power [of sale] must follow strictly its terms. If he fails to do so there is no valid execution of the power, and the sale is wholly void.'").
[3] 941 N.E. 2d 40 (Mass. 2011).

been assigned the mortgages. Instead, they took mortgage assignments months after the sales, as they prepared to convey the properties acquired at the sales to post-sale purchasers. Because the Massachusetts power of sale statute authorizes the "holder of the mortgage" to give notice, advertise, and conduct a foreclosure sale, the land court refused to grant the relief sought by the trustees and instead set aside the foreclosure sales on standing grounds.

In its decision affirming the lower court, the Massachusetts Supreme Judicial Court agreed that the controlling state foreclosure statute requires that the foreclosing party must be a "mortgagee" having a valid assignment of the mortgage.[4] At issue were the notices the trustees sent to borrowers and the advertisements of sale they published, all statutory requirements for a valid non-judicial sale. In both cases the foreclosing parties falsely identified themselves as mortgagees in all pre-foreclosure notices. According to the court, this defect rendered the notices themselves invalid. The borrowers had the right to know who was foreclosing and notices must accurately identify the mortgage holder. These notice defects in and of themselves constituted grounds for invalidating the sales.[5]

The court also rejected four arguments raised by the trustees in support of the validity of their sales: first, the trustees sought to establish valid written mortgage assignments through the securitization documents that established the foreclosing trusts; second, the trustees relied on the "mortgage follows the note" rule that is cherished by the industry; third, the trustees argued for the enforceability of mortgage assignments made

[4] Mass. Gen. Laws Ch. 244 § 14.
[5] *Ibanez*, 941 N.E. 2d at 50-51.

out in blank; and fourth, the trustees contended that post-sale "confirmatory" assignments corrected the absence of valid pre-sale assignments.

1. Securitization Documents Fall Short

Like many states, Massachusetts recognizes a mortgage as conveying an interest in land. State law requires that conveyances of any interest in land, including mortgage assignments, be in writing. The *Ibanez* court rejected attempts by the servicers to establish pre-foreclosure written transfers of the mortgages through reference to various documents prepared during the securitization of the loans. The court noted that as a basic principle, "[w]here a pool of mortgages is assigned to a securitized trust, the executed agreement that assigns the pool of mortgages, with a schedule of the pooled mortgages loans that clearly and specifically identifies the mortgage at issue as among those assigned, may suffice to establish the trustee as the mortgage holder."[6]

In *Ibanez*, the proffered securitization documents fell far short of meeting the court's standard for clear identification of the mortgage in a document transferring mortgage to a trust. In one case the servicer could not even produce a schedule showing the mortgages included in the bulk transfer to the trustee. In the other case the proffered schedule of mortgages failed to identify clearly that the mortgage in question was included in the transfer. In both cases the purported assignment documents failed to establish that the entity transferring loans into the trust (the "depositor") actually had an interest in the mortgages at the time of transfer. The court required appropriate documentation of a chain of mortgage assignments to the trust.[7] Finally, in the Ibanezes' case, the document

[6] *Id.* at 53.
[7] *Id*. at 53, *quoting In re* Parrish, 326 B.R. 708, 720 (Bankr. N.D. Ohio 2005) ("If the claimant acquired the note and mortgage from the original lender, or from another party who acquired it from the original lender,

offered to show a sale of mortgages to the trust was in conditional language, not a duly executed agreement providing for the unconditional final sale of mortgages and notes to the trust.[8]

2. No Help from "Mortgage Follows the Note" Doctrine

Both foreclosing parties in *Ibanez* had been in possession of properly indorsed negotiable instruments at the time of the sales. They had clearly been "holders" of the relevant notes while they foreclosed. In rejecting application of the "mortgage follows the note" rule, the *Ibanez* court held that mere possession of properly indorsed negotiable instruments did not give the foreclosing parties authority to conduct a valid non-judicial sale. In other words, one's status as a party entitled to enforce a note did not satisfy the requirement under state law to be a mortgagee. The court acknowledged that a transferee of a note might have an equitable right to obtain a court order that that the mortgage be transferred to it. However, the potential to assert such a claim did not make the noteholder a "mortgagee."[9] The Massachusetts statute required that the foreclosing party have an actual assignment of the mortgage when proceeding to sale.

3. Assignment in Blank Assigns Nothing

The *Ibanez* court noted the trustees' concession "that the assignments in blank did not constitute a lawful assignment of the mortgages."[10] State law had long considered conveyances of real property that omitted the name of the assignee or transferee as failing to convey any interest and therefore void. One purpose of the statue of frauds is to establish reliable evidence of conveyance of interests in real property. Written

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the claimant can meets its burden through evidence that traces the loan from the original lender to the claimant.").

[8] *Ibanez*, 941 N.E. 2d at 52-53.

[9] *Id*. at 53-54.

[10] *Id*. at 53.

acknowledgements of such conveyances that omit the names of the parties run afoul of the spirit of this basic evidentiary rule. The *Ibanez* court did not reach issues related to the validity of the terms of MERS' mortgage and assignments. However, the court's brief discussion certainly raises the question of whether naming MERS as mortgagee or assignee is substantially different from making out an assignment in blank.

4. Retroactive Assignments Not Effective Even if Industry-Wide Practice

The *Ibanez* court flatly rejected the trustees' attempts to correct the assignment defects retroactively by means of post-sale mortgage assignments labeled "effective" as of a date before the sale proceedings began. Although state law does not require pre-sale recording of assignments, the foreclosing party must hold a valid assignment of the mortgage when it takes the initial steps to foreclose. The court refused to give any weight to claims that retroactive dating of assignments was a common industry practice. Making its point emphatically, the court rejected the servicers' plea to give retroactive effect to its decision, a ruling that calls into question the validity of numerous past foreclosure sales completed in a similar fashion by lenders and servicers under the state's non-judicial procedures.[11]

Other Courts Strictly Apply State Non-Judicial Foreclosure Laws

The *Ibanez* decision represented a straightforward application of basic state law governing foreclosures. In other jurisdictions, state statutes and established state property law should create a basis for similar scrutiny of the rights of a party to exercise state law

[11] *Id*. at 54-55. The Massachusetts Supreme Judicial Court has heard argument on an expedited appeal of a case involving some of the "fallout" from the Ibanez ruling. Bevilacqua v. Rodriguez, 2010 WL 3351481 (Mass. Land Ct. Aug. 26, 2010), direct appellate review allowed Docket No. SJC 10889 (Mass. Dec. 20, 2010). The appellant in this case purchased one of the properties involved in the *Ibanez* appeals from U.S. Bank before any court had invalidated U.S. Bank's foreclosure sale. The lower court rebuffed the purchaser's attempt to obtain a declaration that the mortgagor's rights had been terminated. According to the trial court, because the sale was invalid the purchaser acquired no title to the property. The ruling leaves purchasers from invalidated sales with a remedy against the foreclosing entity.

foreclosure remedies. For example, in two recent decisions, bankruptcy courts in California considered whether a valid non- judicial sale could take place if the foreclosing entity failed to record its beneficial interest in the obligation prior the sale, as required by a California statute.[12] The courts rejected the argument that the common lender practice of using the MERS private recording system complied with the state's recording requirement. The court in *Doble* went further, expressly holding that MERS had no authority under the deed of trust or state law to assign a mortgage.[13] Thus, a party claiming authority to foreclose based on a MERS assignment could not conduct a valid sale. Addressing the recording requirement, the *Rodriguez* court rejected the creditor's "invitation to overlook the statutory foreclosure mandates of California law, and rely upon MERS as an extra-judicial commercial alternative."[14] According to both courts, sales conducted without the required recording in place before sale would be invalid.

A Michigan appellate court invalidated a non-judicial sale conducted under that state's foreclosure by advertisement statute because the foreclosing party lacked authority to proceed under the law.[15] The pertinent section of the Michigan statute requires that the foreclosing entity to be "either the owner of the indebtedness or of an interest in the indebtedness secured by the mortgage."[16] The appellate court concluded that MERS never has an ownership in interest in the debt secured by a mortgage. Therefore it could not conduct a valid sale under Michigan's foreclosure by advertisement statute. The court appropriately noted that the requirement that the sale be conducted by a party with

[12] *In re* Doble, 2011 WL 1465559 (Bankr. S.D. Cal. April 14, 2011); *In re* Salazar, 2011 WL 1398478 (Bankr. S.D. Cal. April 12, 2011).
[13] *In re* Doble, *supra*, 2011 WL 1465559 * 6-8.
[14] Salazar, 2011 WL 1398478, at *7.
[15] Residential Funding Co., LLC v. Saurman, 2011 WL 1516819 (Mich. App. April 21, 2011).
[16] Mich. Cons. Laws § 600.3204(1)(d).

an ownership interest in the indebtedness must be read consistently with the U.C.C. terminology defining who is entitled to enforce a negotiable instrument.[17]

Courts in other non-judicial foreclosure states have similarly rejected arguments by foreclosing parties who have attempted to evade the strict requirements of state non-judicial foreclosure statutes.[18]

[17] Residential Funding Co., LLC v. Saurman, *supra* (referring to MCL § 440.3602 (U.C.C. § 3-602)), which requires that payment due on a negotiable instrument be made to a "a person entitled to enforce the instrument" and noting that MERS does not meet the requirements to be any of the entities defined in U.C.C. § 3-301 as entitled to enforce a negotiable instrument).

[18] Burgett v. Mortg. Elec. Registration Systems, Inc., 2010 WL 4282105 (D. Or. Oct. 20, 2010) (foreclosing party failed to establish compliance with state power of sale statute which required recording of all assignments of deeds of trust, including all transfers of beneficial interest, prior to non-judicial sale); *In re* Adams, 693 S.E.2d 705, 708 (N.C. Ct. App. 2010) (applicable power of sale statute, N.C. Gen. Stat. 45-21.16(d), required showing of "valid debt of which the party seeking to foreclose is the holder," and this standard required showing that note was indorsed, transferred or otherwise made payable to foreclosing party); *In re* Bailey, 437 B.R. 721 (Bankr. D. Mass. 2010) (foreclosing party must be actual holder of mortgage at time of sale).

Steps Taken By Bankruptcy Courts to Facilitate Loan Modifications Short of Formal Loss Mitigation Programs

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The bankruptcy court for the Southern District of New York established the first formal Loss Mitigation Program in 2009,[1] followed soon after by a similar program in Rhode Island.[2] A more limited program designed in coordination with the state court foreclosure mediation program has been adopted by the bankruptcy court in Vermont,[3] as well as a program in the Orlando Division of the Middle District of Florida.[4] The stated purpose of the LMPs is to "bring debtors and secured lenders together, to encourage them to discuss mutually beneficial financial resolution of their home mortgage difficulties..."[5] and "to facilitate resolution by opening the lines of communication between the debtors' and lenders' decision-makers."[6]

A number of bankruptcy courts have taken steps to facilitate loan modifications short of formal loss mitigation programs. These have generally taken the form of local

[1] *See In re* Adoption of Loss Mitigation Program Procedures, General Order M-364 (Dec. 18, 2008), amended by General Order M - 413 (Dec. 30, 2010). Several of the judges in the E.D. of New York have also adopted the program.
[2] *See* General Order Adopting Fourth Amended Loss Mitigation Program and Procedures (February 4, 2011), amending General Orders 10-002, 09-003 and 10-001.
[3] Vermont Standing Order 10-01, July 1, 2010, available at: http://www.vtb.uscourts.gov/orders/ord10-01.pdf.
[4] See Mortgage Modification Mediation for Chapter 13 Debtors, available at: http://www.flmb.uscourts.gov/procedures/.
[5] *In re* Simarra, 2010 WL 2144150, * 1 (Bankr. D.R.I. April 14, 2010).
[6] New York General Order M-413, p. 1.

rules, standing orders or local forms. The following describes the categories of actions taken.

1. Creditor Communications with Debtor not Stay Violation

Some bankruptcy courts have issued local rules or orders which provide that a mortgage creditor's contact with the debtor's counsel or debtor to negotiate a loan modification is not deemed to be a violation of the automatic stay. For example, Local Rule 4008-2 for the District of Oregon provides:

> Chapter 13 Cases. A mortgage creditor may negotiate a modification of its secured claim with the debtor and the debtor's attorney at any time during the pendency of a Chapter 13 case. A modification is voluntary on the part of the secured creditor and the debtor. The court will not consider a mortgage creditor's contact with the debtor and the debtor's attorney and any negotiation to effect a modification, by themselves, to violate the automatic stay of 11 U.S.C. §362.

The District of New Jersey entered a General Order on May 13, 2009 which additionally provides that any communications will not be used in litigation:

> ORDERED, that communications and/or negotiations between debtors and mortgagees/mortgage servicers about loan modification shall not be deemed as a violation of the automatic stay;
>
> IT IS FURTHER ORDERED, that any such communication or negotiation shall not be used by either party against the other in any subsequent litigation;

2. Loss Mitigation Requirement before Plan Confirmation/Stay Relief

Some courts have issued procedural orders related to loss mitigation or mediation requirements that are not part of a formal program, and which may be imposed in relation to Chapter 13 plan confirmation or relief from the automatic stay proceedings. For example, the Northern District of California (San Francisco and San Jose Divisions) released "Guidelines re: Residential Loan Modifications on Relief From

Stay Motions and in Chapter 11 and Chapter 13 Plans" which provides in part for chapter 13 cases:

> 1. Creditors must state on the cover sheet accompanying their motion whether or not debtor(s) have requested a loan modification prior to bankruptcy and/or prior to the date the motion is filed.
> 2. If debtor(s) have made such a request, the creditor must also indicate on the cover sheet the status of the request (e.g. request pending, no decision yet; modification in trial period; denied in writing (attaching a copy of the denial),etc.).
> 3. If debtor(s) have not made a request for a loan modification prior to the date of filing the motion for relief from stay, but intend to do so, or have done so after that date and the creditor has not so indicated in its motion for relief from stay, then they should advise the court accordingly at the hearing on the motion for relief from stay. As one form of adequate protection, the court may set a deadline for the debtor(s) to file and serve on the creditor (and in Chapter 13, on the trustee) a declaration stating under penalty of perjury:(1) the date of such a request and to whom it was sent (attaching a true copy of any transmittal letter or cover sheet, without exhibits); (2) if known, the status of the request (e.g., request pending but no decision yet; modification in trial period; denied in writing, etc.); and (3) the amount that is 31% of the debtor(s)' monthly gross income as shown on Schedule I.
> 4. As additional adequate protection of the creditor's interest in the debtor(s)' principal residence pending consideration of the loan modification request by the creditor, the court will set an appropriate monthly payment amount, and in doing so may consider as adequate a monthly amount that is 31% of the debtor(s)' monthly gross income, with payments beginning in the month that follows the first hearing on the motion for relief from stay or at the end of the contractual grace period in the month that follows after the motion was filed.
> 5. The court's adequate protection order will normally provide that if the creditor in its sole discretion denies the loan modification request in writing provided to debtor(s) and counsel, if any, either (1) the adequate protection payments will revert to the amount provided in the loan documents in the next calendar month after the denial or (2) the creditor will be permitted to restore the matter to calendar on ten (10) days notice.

3. Loan Modification Approval

Some bankruptcy courts have issued local rules or orders requiring court or trustee approval of loan modification and forbearance agreements. For example, Local Rule 4008-2 for the District of Oregon provides:

> No modification can become effective until the trustee consents in writing or the court approves the modification.

The District of New Jersey General Order entered on May 13, 2009 provides:

> IT IS FURTHER ORDERED, that prior to consummation of a loan modification agreement, the agreement must be presented for approval to the Court by motion, on fourteen days notice to the Standing Chapter 13 Trustee and to all creditors whose claims are secured by liens against the underlying real estate. A copy of the proposed loan modification agreement must accompany the motion. Unless an objection to the loan modification is served and filed with the Court, an order may be entered approving the proposed loan modification, which will be effective as of the date on which the motion was filed. If a timely objection is filed, the Court will schedule a hearing at the earliest opportunity.

The Southern District of Georgia General Order Number 2010 -2 provides:

> The Court recognizes that after the filing of a petition under chapter 13 of the bankruptcy code it may be necessary for a debtor to enter into agreements with creditors to modify security interests in real property of the debtor or to incur consumer debt to obtain goods or services necessary to the debtor's performance under a chapter 13 plan. As set forth in II U. S. C. § 1305(c), where prior approval of the trustee is practicable to obtain,
>
> IT IS HEREBY ORDERED that the case trustee is authorized, without further order of this Court, to grant permission to the debtor to enter into agreements to modify a security interest in the debtor's real property or to incur debt as set forth in 11 U. S. C. § 1305 . Nothing in this General Order is to prevent the trustee from denying a request from the debtor to so modify or to incur debt, or prevent the debtor from filing a motion seeking Court approval of a debtor's request to so modify or to incur debt. Applications depicting the approval of the chapter 13 trustee to so modify or to incur debt may be filed with the Clerk 's office in accordance with the Court's filing procedures.

The District of Nevada Administrative Order 2010-03 details the procedure for motions seeking approval of loan modifications. In addition to specifying the notice

requirements and required attachments for the motion, the Order requires that the motion provide detailed information about the new loan terms.

4. Filing of Amended Plan and/or Schedules I and J

If the loan modification of other loss mitigation action will have an impact on the debtor's proposed or confirmed plan, some courts require that an amended plan or schedules be filed. For example, the District of New Jersey General Order entered on May 13, 2009 provides:

> IT IS FURTHER ORDERED, that if a loan modification approved by the Court impacts on the provisions of a Chapter 13 plan, a modified plan must be filed.

5. Debtor Not Required to Dismiss Case or Waive Rights

Consistent with the Dept. of Treasury HAMP guidelines, which provide that a debtor in a pending bankruptcy case must be considered for HAMP if a request is made and may not be terminated from a trial plan if the borrower files a bankruptcy, some courts have issued orders stating that the debtor need not dismiss a bankruptcy case if a loan modification agreement is being negotiated or has been reached. For example, the District of New Jersey General Order entered on May 13, 2009 provides:

> IT IS FURTHER ORDERED, that a debtor need not dismiss a pending case in order to enter into negotiations with a mortgagee/mortgage servicer, or to achieve a loan modification

The District of Massachusetts entered Emergency Standing Order 10-02, which provides that default clauses in loan modification agreements which waive the benefits of the automatic stay are not enforceable and are void unless they are conspicuously disclosed and specifically approved by the court.

Rhode Island's Experiment with Loss Mitigation – A Creditor's Quagmire

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In October, 2009, the Bankruptcy Court for the District of Rhode Island adopted its Loss Mitigation Program and Procedures (General Order 09-003), a program modeled largely after a similar program in effect in the Southern District of New York. These are the only bankruptcy districts currently known to this author to have adopted formal loss mitigation procedures. Notwithstanding, a stubbornly slow economic recovery and persistent problems with the implementation of the Home Affordable Mortgage Program may encourage other bankruptcy districts to consider the adoption of similar programs. A critical analysis of the Rhode Island program is thus warranted with the goal of advancing suggestions as to the how the program might be amended to at once make it more effective and less susceptible to substantive or procedural challenge.

A. In the Absence of a Contested Matter or Adversary Proceeding Is there a Case or Controversy conferring jurisdiction on the bankruptcy court to provide a forum for Loss Mitigation?

Under the Rhode Island Bankruptcy Court's Fourth Amended Loss Mitigation Program and Procedures (see General Order 10-001, 10-002 and 10-003)(hereinafter the "LMP"), an individual debtor in a case filed under chapter

7, 11, 12 or 13 may file a Request for Loss Mitigation with any "holder," "assignee" or "servicer" of a mortgage loan encumbering real estate in which such Debtor holds an ownership interest and used by such Debtor as his principal residence [LMP, Art. III, ¶¶ B, C and D]. The Debtor may file such request at any time during the pendency of the case including after entry of a discharge or after relief from stay has entered in favor of the secured creditor with whom the Debtor seeks Loss Mitigation ("LM") [LMP, Art. III, ¶ A]. Under the LMP, the fact that a Debtor's Request for LM is filed after relief from stay has entered in favor of the secured creditor does not prevent such creditor "from pursuing their state court rights during the LM period, if they so elect" [LMP, Art. III, ¶ A].

A threshold question arises as to whether a bankruptcy court has jurisdiction to require a secured creditor to participate in the LMP or similar program in instances where there is no contested matter or adversary proceeding pending that involves the debtor and the secured creditor with whom mitigation is sought.

In the case of *In re Smith,* 409 B.R.1 (Bankr.D.N.H. 2009), the Court considered the debtors' motion to approve a proposed loan modification offered by the holder of the first mortgage on their principal residence. The mortgagee assented to the motion and in fact required, as a condition of its offer, that the debtors obtain court approval of the proposed modification failing which the offer would be deemed withdrawn. Although the mortgage holder had filed a

motion for relief from stay and such motion was still pending [the hearing on the motion had been continued several times for the express purposes of allowing the parties more time to negotiate a mortgage modification] at the time the motion to approve was filed, the motion to approve was not styled as or otherwise expressly filed for the purpose of resolving the pending motion for relief. Noting that an Article III court's judicial power is restricted to "cases" and "controversies" Judge Deasy concluded that a stand-alone motion to approve a loan modification did not present the court with any case or controversy and denied the motion.

Rhode Island's LMP proclaims that the program "is designed to function as a forum for debtors and lenders to reach consensual resolution when a debtor's residential property is at risk of foreclosure" [LMP, Art. I]. So then, in the absence of a pending contested matter or adversary proceeding involving the debtor and creditor "participants" in the LMP, what case or controversy bestows jurisdiction on the bankruptcy court to provide a "forum" for such parties to negotiate a modification of the mortgage obligation?

B. What identifiable Right found Elsewhere in the Bankruptcy Code Is a Bankruptcy Court Preserving in invoking its Section 105(a)Powers to Compel Creditors to participate in an LMP?

Addressing a secured creditor's challenge to the LMP wherein such creditor asserted that provisions of the LMP were inconsistent with the Bankruptcy Code in the matter of *In re. Alberto G. Sosa,* Case No. 10-11702 (Bankr.D.RI 2011) the court stated that the LMP was implemented (a) "in

response to the home mortgage and foreclosure crisis generally" and (b) for the purpose of "regulat[ing] the administration of cases pending before it" [citing repeated continuances of motion for relief hearings sought by creditors and debtors alike to allow contemporaneous loan modification negotiations between the parties to continue].

In the General Order No. 09-003 which initiated the LMP, the Court cited its general equity powers under 11 U.S.C. Section 105(a) as the source of the Court's authority to implement such a program. Our First Circuit Court of Appeals, however, has admonished that "Section 105(a) does not provide bankruptcy courts with a roving writ, much less a free hand" and that "the authority bestowed thereunder may be invoked only if, and to the extent, the equitable remedy dispensed by the court is necessary to preserve an identifiable right conferred elsewhere in the Bankruptcy Code." *In Re Jamo,* 283 F.3d 392, 403 (1st Cir. 2002).

In the absence of a pending contested matter or adversary proceeding it would seem that the Court has neither a case or controversy conferring jurisdiction upon it nor an identifiable right possessed by either debtor or secured creditor to preserve in convening a "forum" for the negotiation of a loan modification. The court in *Sosa* referred to the LMP as one of its many "case management tools" referring most notably to its power to convene status conferences pursuant to Fed. Rule of Bankruptcy Procedure 7016 (applicable to adversary proceedings) which the court may declare applicable to contested

matters pursuant to Fed. Rule of Bankruptcy Procedure 9014(c). Arguably in *Sosa,* however, the Court had no case or controversy before it, and thus no jurisdiction to compel the creditor to participate in court-supervised loss mitigation in the first instance since no motion for relief from stay or other contested matter or adversary proceeding was pending between the targeted participants at the time the Debtor filed his request for Loss Mitigation.

C. Coercing Consensus

The LMP's emphasis on forging consensual resolution(s) notwithstanding, there is nothing voluntary about a creditor's participation in the LMP. As currently written, a creditor with relief from stay long-since in hand and on the verge of consummating a foreclosure sale can still find itself invited to a party it has no desire to attend. This is the case even in a chapter 7 proceeding where the debtor has his discharge in hand and wherein all assets have been fully administered. Indeed the debtor may have elected "surrender" on his previously filed Statement of Intention and had an 11th hour change of heart prompting the filing of a Request for loss mitigation.

The Creditor then has 14 days to object to the Request [LMP, Art. V., ¶ D]. "A party failing or refusing to participate in loss mitigation in good faith may be subject to sanctions" [LMP, Art. VII, ¶ A.]. The creditor must be prepared to articulate "specific reasons why loss mitigation would not be successful." The LMP does not provide any examples of what "reasons" might

be acceptable to the court or any criteria for determining same. Some presumably satisfactory "reasons" why LMP would not be successful are:

1. Creditor previously offered HAMP modification to the Debtor and the Debtor rejected the offer;
2. Creditor previously offered HAMP modification to the Debtor – Debtor accepted the offer but subsequently defaulted on his payment obligations on the modified payment schedule;
3. Debtor previously applied for HAMP, was determined ineligible but was offered conventional modification but rejected the offer or, accepted the offer but subsequently defaulted on the modified payment terms;
4. The Servicer is not a participant in the HAMP program.
5. The Investor has chosen not to participate in the HAMP program (be prepared to produce sufficient documentation evidencing such declination).
6. HAMP application not received in sufficiently timely manner to allow review of same prior to consummation of the foreclosure sale (Midnight of 7th business day before scheduled sale for Non-GSE HAMP – See *Making Home Affordable Program, Handbook for Servicers of Non-GSE Mortgages, Version 3.0 as of December 2, 2010,* §3.3, pg. 53; Guidelines for GSE Mortgages appear not to be as specific);

7. The Foreclosure has already occurred (will this be sufficient?).
8. A post-discharge modification will be non-recourse (will this be sufficient?).

D. Is "Loss Mitigation" a viable retention option under §521(a)(2)(A)?

It is axiomatic, even in the aftermath of BAPCPA, that as §521(a)(2)(A) is presently interpreted by our First Circuit Court of Appeals a Debtor has but three choices with respect to obligations secured by property of estate: surrender, redeem or reaffirm the debt. *In re Pratt,* 462 F.3d. 14, 17-18 (1st Cir. 2006). In *Sosa, supra,* the Debtor first elected to surrender the collateral; shortly thereafter he amended his Statement of Intention and elected "Other – Loss Mitigation". In the course of rejecting the creditor's contention the loss mitigation was not a viable retention option, the court in *Sosa* suggested without deciding that §521(j) enacted as part of BAPCPA was a tacit endorsement by Congress of the so-called "ride-through" option. The court emphasized that it was not finding that the debtor could retain collateral without the creditor's consent, rather the court was merely "extend[ing] the time necessary to perform the stated intention."

There are two fundamental flaws with this rationale. First, the rationale ignores the requirement in §521(a)(2)(B) that the Debtor perform his stated intention within "30 days after the first date set for the meeting of creditors under Section 341(a) or within such additional

time as the court, for cause, within such 30-day period fixes." No such finding within this prescribed time period was made in *Sosa.* Second, the court makes no attempt to reconcile the LMP's generous extension of time within which to perform a stated intention (even post-discharge) with the requirement that reaffirmation agreements must be made before entry of the discharge pursuant to §521(c)(1) in order to be enforceable under applicable non-bankruptcy law. Moreover, any modification agreement is, by definition, an agreement "the consideration for which, in whole or in part, is based on a debt that is dischargeable in a case under this title" [§521(c)].

The *Sosa* court emphasized that in creating the LMP it was neither creating new substantive rights nor infringing on existing Code provisions. Notwithstanding, the LMP in its current incarnation can effectively coerce a creditor into entering a post-discharge, non-recourse modification with the Debtor.

E. An Invitation to Default on Payments to Secured Creditors

Keeping in mind that an individual Debtor under chapter 7, 11, 12 and 13 of the Code may file a Request for Loss Mitigation at any time during the pendency of the case, the following provision of the LMP requires no embellishment being sufficiently troublesome to creditors in its own right:

> "The Court's LMP is intended to bring debtors and secured lenders together, hopefully, to reach

> consensual and mutually beneficial resolutions when residential property is at risk of foreclosure. **With this in mind, and consistent with the federal HAMP eligibility requirements – that homeowners must be in default or at imminent risk of default, the requirement that debtors make regular mortgage payments during the loss mitigation process will not be automatically imposed as a condition to participation in the LMP. To do so would likely be fatal to the viability of most of the federal, state and municipal programs that have been developed in response to the residential foreclosure crisis (emphasis added)."**

[LMP, Art. V, ¶D]. This provision is troublesome for a number of reasons. First, the provision is at best tacit acquiescence in, if not endorsement of, conduct that could achieve the exact opposite of what is intended [See *Attachment – Guidelines for the FHA-Home Affordable Modification Program* (supplementing requirement outlined in Mortgagee Letter 2009-23), page 1 of 6, "The mortgagor must not have intentionally defaulted on their existing mortgage. (Note: Intentionally defaulted means the mortgagor had available funds that could pay their mortgage and other debts without hardship, but failed to pay)."]. Second, how is such a statement reconciled with a chapter 13 debtor's obligation to abide by the terms of a confirmed plan? Third, if the court is going to effectively suspend a Debtor's obligation to make post-petition payments otherwise required under the terms of a confirmed plan should the Debtor not be required as condition of filing a post-confirmation Request for Loss Mitigation to demonstrate as a threshold matter and before an Order for

Loss Mitigation enters, sufficient documentary evidence of changed circumstances? Moreover, a request for a mortgage modification necessarily means that the Debtor continues to maintain a regular, albeit reduced source of income and an ability to continue to make a mortgage payment in some amount. Should not a Chapter 13 Debtor be further required, as a condition of the entry of an Order for Loss Mitigation, to pay at least that amount that the Debtor would reasonably expect to pay under the terms of the sought after modification?

F. No Relief in Sight

In the wake of the creditor's challenge in *Sosa* the court amended its Third Loss Mitigation Program and Procedures to allow creditors with whom Loss Mitigation had been requested by the Debtor to file motions for relief during the pendency of the Loss Mitigation period [General Order 11-001]. This is of little, if any, practical consequence since the LMP further provides that:

> "Any Lift-Stay Motion filed by such LM Party Creditor prior to or after the entry of the Loss Mitigation Order shall be postponed to a date after the last day of the loss mitigation period, and the stay shall be extended pursuant to Section 362(e) of the Code."

[LMP, Art. VI, ¶ B]. The LMP effectively alters a creditor's burden of proof with respect to a motion for relief filed before the Loss Mitigation period or during such period. The provisions of §§362(d) and 362(g) are for all practical purposes cast aside because a disposition of the motion

is deferred until the LM period is terminated. A secured creditor may request that the LM period be terminated early "for cause" [LMP, Art. IX, ¶ C]. Once again, "cause" is not defined in the LMP. Presumably, "cause" within the meaning of the LMP is something different than a demonstration of "cause" under §362(d)(1) of the Code and is more closely related to the showing required on an objection of the entry of a Loss Mitigation Order in the first instance [i.e., specific reasons why LM would not be successful].

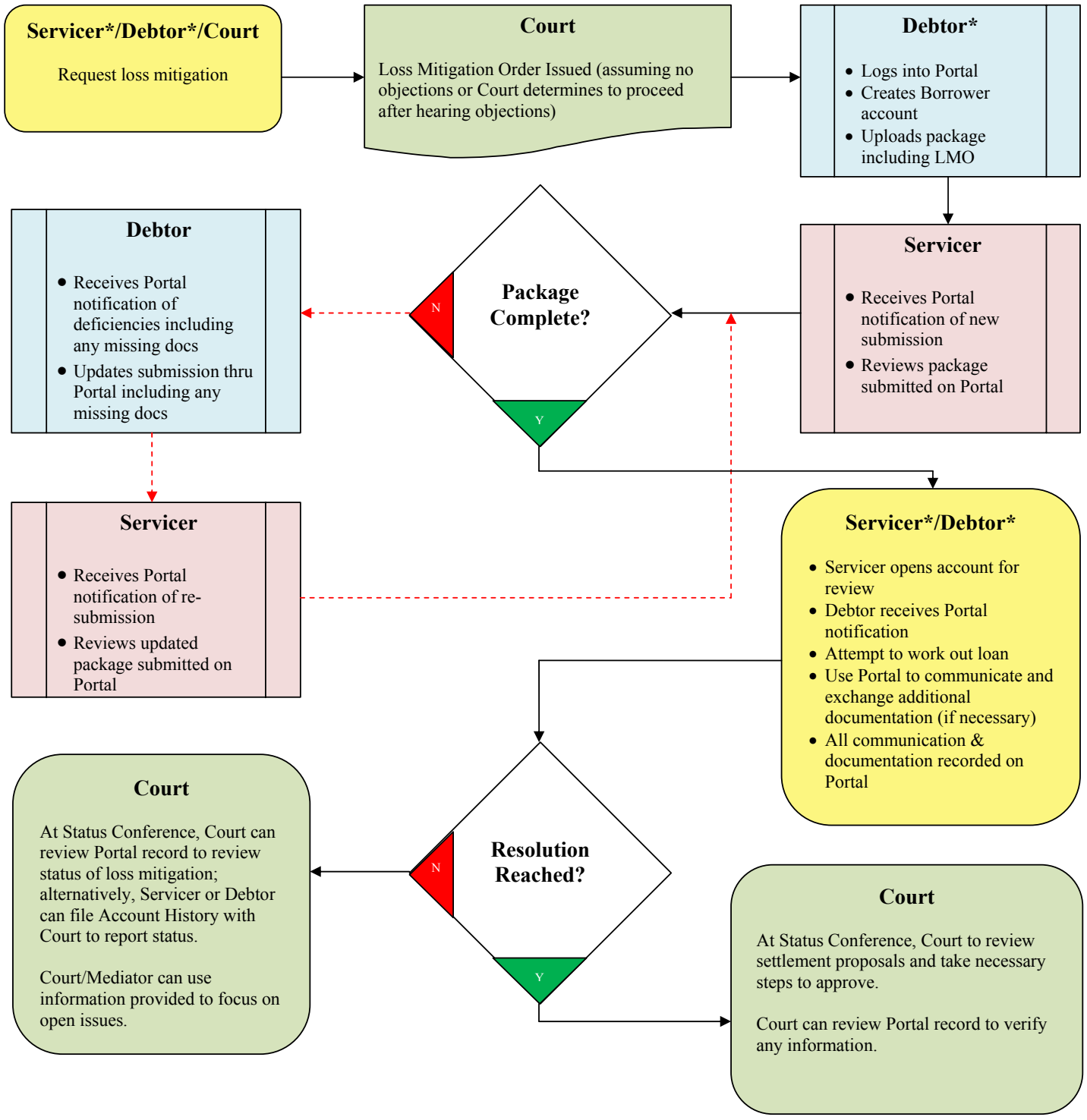
Conclusion

It may be possible to fashion a loss mitigation program that is more palatable to secured creditors particularly in a chapter 13 case and provided that the program is tailored to prompt a determination of eligibility for HAMP and conventional programs as early on in the case as possible. Application of Rhode Island's LMP is particularly troublesome in and perhaps in many ways inherently inconsistent with the orderly prosecution and administration of chapter 7 cases. One could even argue that in the wake of BAPCPA and means-testing, it would not be manifestly unfair to limit application of similar loss mitigation programs to debtors in chapter 11, 12 and 13 cases.

With the advent of case law which has emerged since the inception of Rhode Island's LMP, some of the concerns that motivated the program's adoption in the first instance may best be pursued in other

venues or through other means (such as an adversary proceeding). There is a formidable consensus amongst the courts which have confronted the issue that find that a borrower does not have a private cause of action under HAMP for alleged failures of a loan servicer or mortgage holder to abide by applicable HAMP guidelines. There is also, however, a growing number of cases finding that the borrower may have a cognizable cause of action under Chapter 93A of the Massachusetts General Laws (presumably other consumer protection statutes in other states will be susceptible to the same or similar interpretation) for a loan servicer's failure to abide by HAMP guidelines to the extent that such failure rises upon the level of mere clerical error or negligence to actions or omissions constituting unfair or deceptive conduct. *Emmanuel Ording, et al v. BAC Home Loans Servicing, L.P.*, Memorandum and Order RE. Defendant BAC Home Loans' Motion to Dismiss, C.A. No. 10-10670-MBB (D.Mass. January 10, 2010).

BK COURT LOSS MITIGATION PROGRAM – DMM PORTAL



Submit. Track. Resolve.

* Servicer/Borrower can act directly or through counsel.

LOSS MITIGATION PROGRAM
PORTAL ADVANTAGES

LMP Objective	Without Portal	With Portal
"The Loss Mitigation Program aims to facilitate such resolution by opening lines of communication between the debtors' and lenders' decision-makers."	Loss Mitigation Program (LMP) provides procedural hurdles to ensure parties eventually communicate with one another but traditional methods of contact – phones, faxes, and mail – have and continue to be only marginally effective in bringing about meaningful communications.	Communications take place over a secure electronic platform that **directly** connects the debtors' and lenders' decision-makers. Documents and communications can readily be exchanged so parties can focus on resolutions. No lost faxes or messages. All communications are 100% transparent.
Loss Mitigation Order establishes deadlines by which both parties must complete certain tasks.	Difficult and time consuming to verify compliance.	All activity is time/date stamped so independent verification is quick and easy.
The Loss Mitigation Program requires documents to be exchanged.	Traditional methods for delivering documents – faxes, email and mail – do not work. Communications are not coordinated which lead to lost documents, mis-communications and delays.	Servicers automatically deliver required information requests. All communications are consolidated in one place so parties know exactly what to submit and where to submit it. All parties can independently verify document delivery/receipt.
"Loss Mitigation Parties shall negotiate in good faith"	Very difficult to verify.	Court has access to all communications which are time/date stamped and logged in the history of each account. This transparency creates greater incentive to meet this standard.
Parties must provide the Court with a Status Report	Parties must provide written or verbal report to Court. Subject to "interpretation".	Court can easily review an account to independently verify and determine objective status of review. Alternatively, debtor or creditor can simply print out history log of account.

* Because all information is captured and processed electronically, the Portal can report on key program indicators such as:

- Time to complete intake
- Time to decision
- Time to close
- Percentage of files rejected
- Reasons for file rejections
- Percentage of files approved