Center for American Progress

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It's Time We Talked

Mandatory mediation in the foreclosure process

Andrew Jakabovics and Alon Cohen June 2009

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Introduction and summary

It is estimated that as many as 9 million homeowners may lose their homes to foreclosure over the next four years, with nearly one in eight mortgages currently delinquent or in the process of foreclosure. And the foreclosure crisis is not limited to borrowers who were offered subprime loans, either. The most recent data available from the Mortgage Bankers Association shows that prime loans account for most new foreclosures.[1]

State courts in the United States already are facing a deluge of home foreclosures. The number of foreclosure filings have doubled in those states hardest hit by the housing crisis, with some counties in Florida and California registering 10-fold increases over levels at the beginning of the crisis two years ago. National headlines capture the crisis, highlighting case files shuttled around overworked courtrooms on hand trucks and embattled homeowners receiving sometimes as short as 15-second hearings before losing their homes.[2]

Behind the headlines, however, lurks even worse news—most judges discover that the vast majority of foreclosure proceedings in their courts are the first time homeowners and their mortgage lenders and mortgage servicing companies have discussed these financial crises writ small across our country.[3] The judges' experiences bear out estimates that more than 80 percent of homeowners at risk of losing their homes had not engaged in any efforts to mitigate foreclosures with their lenders or servicers as of the end of last year.[4]

In addition, jurisdictions in nine U.S. states now employ so-called "alternative dispute resolution" methods, and in particular mediation, to help at-risk homeowners deal with looming foreclosures by mortgage lenders or servicers. These states now realize that mediation helps reduce the impact of the housing crisis on neighborhoods, unclog courts, and achieve faster, cheaper, and better resolutions for homeowners, mortgage lenders and servicers, and the community at large.[5] These mediation programs are still young, but the best ones are showing impressive results, resolving in nearly three-quarters of all participating foreclosure cases without the need for formal foreclosure proceedings.

The federal response to this burgeoning foreclosure crisis has also ramped up significantly since the Obama administration took office. The administration created the Making Home Affordable Program, or MHP, in late February 2009 to help at-risk homeowners keep their homes by refinancing or modifying their loans through two related programs: the Home Affordable Refinance Program, or HARP, which offers refinancing at attractive rates to

Two approaches to foreclosure mediation

Bringing borrowers and servicers face to face at least once prior to the sheriff or trustees' sale is the goal of mandatory mediation, and early indications are that it works. Both Connecticut and Philadelphia represent two emerging approaches to foreclosure mediation, the differences between them stemming largely from the availability (or lack) of funding for the program.

Both Pennsylvania and Connecticut are judicial foreclosure states (where foreclosure is a court proceeding), but recent developments in states like Nevada demonstrate that the principles gleaned can be applied equally in nonjudicial foreclosure states, such as California, where foreclosure occurs without the court's involvement.

Philadelphia—one of the earliest mediation programs—receives no funding. It involves a two-step mediation process. First, the homeowner and lender's counsel meet informally in the courtroom during a "cattle call," with a housing counselor and, if necessary, a pro bono attorney present for the homeowner. The few cases that are not resolved informally are assigned to a mediator—a pro bono senior attorney or judge—who conducts a private session with the parties.

The program relies on departments within the court to make staff available and on volunteer attorneys to make it work. The success of the program is due in part to the fact that Philadelphia is a dense urban setting with a large legal community and robust community organizations able to provide counseling and outreach.

Connecticut represents the second approach. Covering an entire state, the program received $2 million to date and is scheduled to receive $6 million in the coming two years. The large geographic area involved makes a coordinated in-person housing counseling effort impractical as well as any statewide nonprofit outreach effort. The program relies instead on a full-time staff of approximately 30 people, a mediator and case flow coordinator in each of the state's 12 districts, several clerks, and a full-time administrator. These employees also engage in outreach, attending homeowner and industry events to raise awareness and participation.

To understand and help states and local governments set up such programs, we interviewed administrators of existing programs to learn how they set up their programs, how the programs functioned, what they planned to change, and what data they had regarding results. We've spoken to program participants, including homeowners, housing counselors, lender's counsel, community organization, and other policy experts. What has emerged is a better understanding of the need for mandatory mediation in foreclosure proceedings, the interplay between such mediation programs and the federal government's recent Making Home Affordable Program as well as best practices for creating, promoting, and running such programs (see main sections of the report)

homeowners with loans owned or guaranteed by Fannie Mae or Freddie Mac, including those who may owe slightly more on their house than it is currently worth; and the Home Affordable Modification Program, or HAMP, which seeks to help at-risk homeowners by providing incentives to their mortgage servicers to modify loans by reducing the interest rate, extending the length of the mortgage, or forbearing interest on the loan to reduce a homeowner's payments to a sustainable 31 percent of her gross income.

Each of these programs has already reached over 50,000 homeowners in the first few months, but it is far from certain that all eligible homeowners are receiving MHP-compliant modification or refinancing offers. MHP's compliance audit will not begin for another quarter and its efficacy is unknown, a concern already being voiced by members of Congress.[6] Adopting mandatory mediation in the foreclosure process provides homeowners who do not receive assistance under MHP, irrespective of the reason, an opportunity for sustainable modifications and refinancings. Among these are not only those deemed ineligible under MHP, but also the nearly 25 percent of homeowners whose servicers are not participating in the program.

In this paper we will argue that the federal government has an important role to play in expanding the implementation of mandatory mediation programs at the state and local level, as described below. Given the magnitude of the crisis and the degree to which the federal government is already invested in mortgages, we believe the federal government should take a more direct role in providing opportunities for mediation, as follows:

Best practices

The best practices detailed in the paper are focused on maximizing benefits for all parties. Here is a map to our best practices guidelines, which are detailed in the appendix on page 40:

Best practices for running a mandatory mediation program
- Maximize eligibility, maximize participation
- Involve housing counselors wherever possible
- Implement outreach programs
- Servicer or its counsel must have the authority to make a deal
- Require parties to meet in person where possible

Best practices for administering a mandatory mediation program
- Find a champion within the system
- Get buy-in from stakeholders
- Obtain funding, but do not wait for it
- Put in place a case management system
- Continually evaluate your program
- Require ongoing training for participating professionals

Open questions
- Should programs require a pre-mediation meeting with a counselor?
- Should there be a mediation time limit?
- Who should have the power to declare an impasse or lack of good-faith dealing?
- Should mediation stay foreclosure proceedings?

- Congress should fund state and local mandatory mediation programs just as it provides neighborhood stabilization funds to alleviate the housing crisis.

- In the interim the Department of Housing and Urban Development should issue guidance that explicitly permits community development block grants to be used to fund mandatory mediation programs.

- The government should require mediation for all federally insured home mortgages. This would be an extension of HUD's existing requirement that all servicers of Federal Housing Administration loans engage in loss-mitigation efforts prior to foreclosure and would minimize losses to the already stressed FHA insurance fund.

- By extension the Federal Housing Finance Agency, acting as the conservator of Fannie Mae and Freddie Mac, should require all servicers acting on behalf of those entities to participate in mediation prior to foreclosure.

- Likewise, the federal government should require all servicers participating in HAMP to participate in mandatory mediation prior to foreclosure in cases where a modification is not possible under program rules as a way of ensuring a level playing field and speedy resolution of offers for short sales and deeds in lieu of foreclosure.

For state and local governments, we present a set of recommendations for best practices gleaned from our analysis of existing programs in Philadelphia, Pennsylvania; Connecticut; Florida; and California. Philadelphia and Connecticut are examples of successful, established programs. Florida and California are examples of as yet ineffective responses. In addition, we analyze the forthcoming program in Nevada.

In Philadelphia, the Supreme Court of Pennsylvania established a pilot program that uses a two-step mediation system. The court runs an open session once a week during which servicers' counsel, homeowners, housing counselors, and pro bono attorneys engage in informal negotiations. Those cases that reach impasse are referred to formal mediation. The program receives no funding and relies on volunteers and housing counselors.

Connecticut runs a successful statewide program with 30 full-time staff including a dedicated mediator and clerk in each of the state's 12 counties. The program is funded by the state, but its geographic scope makes the inclusion of local housing counselors at the mediations impractical.

Unlike Pennsylvania and Connecticut, California, is a nonjudicial foreclosure state, which means that servicers need not involve the court to foreclose on a property. It has foregone true mediation and requires only that the parties conduct an informal telephone conference prior to foreclosure. Notably, it does not require the servicer to include its loss mitigation staff on that call.

In contrast to California, Nevada—also a non-judicial foreclosure state hit hard by the crisis—will deploy a full-blown mediation program on July 1, 2009. The program shares many characteristics with those in Philadelphia and Connecticut, including enhanced notice, referral to a housing counselor, and the requirement that servicer make available a representative with the authority to settle. If homeowners request mediation, any further action by the servicer is stayed until mediation concludes; the parties split the cost of mediation, capped at $400.

Defining terms in foreclosure mediation

Mediation: A process by which a neutral mediator assists parties in trying to reach a voluntary negotiated settlement to resolve their dispute

Foreclosure mediation: Mediation conducted in the course of foreclosure proceedings. The mediation can be a condition to initiating foreclosure or occur any time up to the sale of the property. The timing depends on the rules of the particular program. We also include "two-tier" mediation programs in this term. Two-tier programs, such as the one in Philadelphia, require the parties to hold an informal conciliation conference first without a mediator. If the parties reach an impasse, the case is referred to formal mediation.

Voluntary versus mandatory mediation: In voluntary mediation, a homeowner must request—or "opt in"—"for mediation. In mandatory mediation, a session is automatically scheduled for both parties. A homeowner may or may not be able to "opt out" depending on the particular program.

Judicial foreclosure versus nonjudicial foreclosure: Foreclosure mediation can take place in one of two contexts: judicial foreclosure, in which the servicer has to file a complaint in court to initiate foreclosure; and nonjudicial foreclosure, in which a servicer simply provides public notice of the default and sale without court intervention. While many states permit both types of foreclosure, most focus on one.

Mediation in a judicial foreclosure: This generally begins simultaneously with the foreclosure proceedings. To initiate a foreclosure, the servicer files a complaint and then sends the homeowner notice of that filing. Included within that notice is an additional document about mediation. If the mediation program is voluntary, then the notice informs the homeowner that mediation is available and explains how the homeowner can request it. If the program is mandatory, the notice includes the date and time of the first mediation session. Under most current programs, mediation occurs alongside the court proceedings—it does not stay them—so a homeowner must file an answer and provide discovery responses while also attending mediation sessions. Where mediation offers some protection on the back end, mediation is a condition for completing the foreclosure so the court will not enter judgment (which then leads to the sale of the property) until the mediation is complete. In cases where mediation is successful, the case generally settles and foreclosure proceedings are discontinued as unnecessary.

Mediation in nonjudicial foreclosure. This type of mediation takes place *before* the foreclosure proceedings, because nonjudicial proceedings are much faster and require far less process than judicial foreclosure proceedings. A servicer need only post a notice of sale and then sell the property after a set time period. Some states require one additional notice prior to the notice of sale telling the homeowner she has defaulted on the mortgage. For mediation to be effective, it must occur before the notice of sale is posted to give the parties sufficient time for adequate negotiations. If at all possible, it should occur before the notice of default. As above, if mediation is successful, the foreclosure proceedings generally become moot.

And in Florida so far it has been each judicial circuit for itself, with responses running the gamut: mandatory mediation, voluntary mediation, informal negotiations, and even a paper-based modification request resembling HAMP. The state's Supreme Court has a task force working to coordinate efforts with a report expected in August.

Our analysis of these programs leads us to propose a list of best practices for mandatory mediation—best practices that maximize benefits for all parties facing the prospect of foreclosing on a home. (See the "best practices" sidebar on page 3 for a list of these recommendations.) These best practices in mandatory mediation will help homeowners keep their homes or arrange for a "graceful exit." They will help servicers shortcut the foreclosure process, saving them and their investors time and expense and resulting in an economically superior outcome. They will help courts save resources. And they will help communities reduce the tax and social costs of foreclosure.

We detail how the best practices work in existing state programs and how they could work across the nation in the appendix beginning on page 40. We believe the dissemination of data and the practical experience gained from these programs is important for other state governments grappling with their own foreclosure crises and for the federal government, which can and should plan a more expansive role in deploying foreclosure mediation programs.[7] As we will demonstrate, our analysis shows that mandatory mediation will help mitigate today's national housing crisis by reducing unnecessary foreclosures, minimizing losses to investors, and easing the burden on local governments and taxpayers, thereby helping our economy recover more quickly from the recession bequeathed to us by the Bush administration.

In the pages that follow, we will first outline how mandatory mediation would fit into ongoing federal efforts to stem the national foreclosure crisis. We will then explore state foreclosure mediation programs in Pennsylvania, Connecticut, Florida, California, and Nevada going into extensive detail so that other state policymakers understand how these programs could work in their states and so that federal policymakers grasp where federal policy and state mandatory mediation programs could and should overlap.

We will then address possible barriers to mandatory mediation, including a detailed look at the complex array of contracts that govern mortgage-backed securities, which of course are where most residential mortgages reside these days. This analysis will enable us to demonstrate that there are no barriers to the institution of mediation in the foreclosure process based on either the Constitution's Contracts Clause or on takings concerns. In addition to a discussion of the issues at the Federal level, we also detail possible issues that may arise at the state level between the legislative and judicial branches.

We conclude with a summary of our recommendations for Congress and the Obama administration as well as state and local governments. We're confident these recommendations represent the best way to bring today's housing crisis to a swifter conclusion.

How mandatory mediation fits in

Over the next four years, we can expect as many as 9 million homes to be foreclosed upon,[8] with many states already reporting foreclosure rates over double what they were several years ago.[9] With a total of approximately 55 million homeowners carrying a mortgage on their homes in the United States, this figure means that nearly one of every six mortgaged homeowners will be at risk of losing their home.

Requiring delinquent borrowers and servicers to come face to face at least once in the foreclosure process for mediation can significantly reduce foreclosures by creating an opportunity to both parties to negotiate an outcome superior to foreclosure. Jurisdictions that have implemented mandatory mediation report that more than seven in 10 cases are resolved short of foreclosure.

Not all resolutions, of course, lead to borrowers staying in their homes. But mediation also allows homeowners to arrange "graceful exits" in lieu of evictions. The upshot: mediation is beneficial for homeowners and mortgage servicers, as well as for the courts that are straining to keep up with the number of foreclosure filings in heavily impacted jurisdictions.

Existing mediation programs

	Predominant type of foreclosure	Type of negotiation	Date	Program initiator
California	Nonjudicial	Mandatory teleconference	9/6/08	Legislature
Connecticut	Judicial	Mediation (now mandatory)	7/1/08	Legislature
Florida (multiple local courts)	Judicial	Mediation (multiple types)	Early 2009	Local court
Jefferson County, Kentucky (Louisville)	Judicial	Voluntary mediation	3/30/09	Local court
Michigan	Nonjudicial	Voluntary negotiation (no mediator)	7/5/09	Legislature
Nevada	Nonjudicial	Voluntary mediation	7/1/09	Legislature
New Jersey	Judicial	Voluntary mediation	10/16/08	State court
New York	Judicial	Voluntary mediation	6/1/08	State court
Ohio (multiple local courts)	Judicial	Voluntary mediation	11/1/08	State court
Philadelphia, Pennsylvania	Judicial	Mandatory mediation	4/16/08	Local court
Wisconsin	Judicial	Voluntary mediation	7/1/09	Legislature

Mandatory mediation dovetails with the Making Home Affordable Program

Mandatory mediation dovetails nicely with recent efforts by the Obama administration to prevent foreclosures. This process ensures that eligible homeowners receive the modifications for which they qualify and, where modifications under the administration's program are not possible or where homeowners are not eligible, mandatory mediation provides the parties the opportunity to identify alternatives that benefit each side both more than foreclosure.

The Obama administration's Making Home Affordable Program, or MHP, seeks to reduce the number of foreclosures dramatically by allowing some borrowers to refinance into lower interest-rate mortgages, thereby reducing monthly costs, and providing others with an opportunity to have the terms on their existing mortgages modified to create sustainable payments. As of mid-May, 51,000 newly eligible borrowers refinanced through this program's Home Affordable Refinancing Program, or HARP, and another 55,000 have received offers to modify their mortgages under the Home Affordable Modification Program, or HAMP.[10]

These recent efforts stand in stark contrast to the weak actions by the Bush administration, which was largely content to let the mortgage servicing industry call its own shots on modifying mortgages. As a result, even though the public had known the magnitude of the crisis for a year, as of September 2008, 80 percent of seriously delinquent homeowners were not on track for any loss mitigation.[11]

Moreover, when modifications were offered, they rarely benefited homeowners over the long term. The Office of the Thrift Supervisor and The Office of the Comptroller of the Currency report that more than half of the loans modified in the first three-quarters of 2008 were delinquent by at least 30 days within just three months. Half of loan modifications implemented did not reduce the homeowners' payments, and 32 percent of modifications resulted in increased monthly payments for homeowners clearly unable to afford their payments at the previous level.[12]

By comparison, the Obama administration's initiative leverages the capacity of Fannie Mae and Freddie Mac to refinance borrowers (as we called for last September when the two firms entered government-controlled conservatorship)[13] and establishes clear guidance for participating servicers on how modifications are to proceed, explicitly requiring modifications to reduce monthly payments. Thirteen servicers, collectively responsible for servicing 75 percent of the existing mortgages in the country, have already signed contracts with Treasury to participate in the program. This broad industry participation is necessary because 50 percent of all seriously delinquent mortgages at the end of last year were held in private-label securities (as opposed to mortgage securities issued by Fannie Mae, Freddie Mac, or Ginnie Mae), despite accounting for only 15 percent of outstanding mortgages.[14]

HAMP seeks economically and, by extension, socially optimal results through modifications. Participating servicers are obligated to examine their entire portfolio to identify qualifying mortgages. Borrowers need not be delinquent; the program allows servicers to reach out prospectively to offer modifications. Eligible mortgages are modified to reach a monthly payment equal to 31 percent of a borrower's gross income, widely-regarded as a debt-to-income ratio that most borrowers can sustain. Modifications are also subject to a so called net-present-value, or NPV test aimed at ensuring that the expected return on the modification is greater than the expected return on foreclosure for that property. A borrower who passes the NPV test receives a modification; one who fails proceeds to foreclosure. By making modifications only when they provide greater value to investors than a foreclosure, the program honors servicers' fiduciary duties while still seeking socially optimal results.

But it is wrong to assume that because HAMP has been embraced by servicers, nothing more needs to (or can) be done to minimize foreclosures.

Mandatory mediation also closes some procedural gaps in the HAMP process. HAMP is servicer-driven. Participating servicers must analyze their portfolios to identify mortgages that would qualify for modification. Under current program rules, there is no opportunity for homeowners to negotiate with mortgage servicers during the initial determination of eligibility and no process for challenging a servicer's decision. Homeowners have no recourse if their circumstances have changed favorably since they submitted their applications or, worse, the servicer simply uses incorrect information in making the decision.[15]

Similarly, homeowners have no recourse if servicers deny the modification because servicers' assumptions were mistaken. Based on the elements of the NPV test that have been disclosed to the public,[16] the test may be highly sensitive to certain inputs, including, but not limited to, local housing market conditions. If a servicer were to proceed to foreclose based on an unrealistically high valuation of the property or the expectation of a quick sale post foreclosure, then both the homeowner and the investor are hurt. By providing an opportunity to challenge the servicer's valuation assumptions, mandatory mediation creates an opportunity to offer modifications to HAMP-eligible borrowers.

HAMP does have built-in compliance-checking, though it will likely involve a lag as Freddie Mac, which will act as program's compliance agent, obtains and reviews documentation on a sample of a servicer's mortgage pool with a 60- to 90-day delay.[17] It will likely come as little comfort to homeowners who improperly lose their homes if a mistake is discovered months after their home was sold in foreclosure. Mandatory mediation permits homeowners a last chance to ensure compliance prior to losing their homes.

In addition to using mandatory mediation as an opportunity to identify homeowners who might qualify for a modification but whose servicers failed to recognize it, mediation also provides the parties a chance to consider resolutions other than modification that may still provide homeowners, servicers, and investors greater value than foreclosure. In these resolutions, dubbed "graceful exits," the parties recognize that the homeowner cannot afford to stay and arrange for an exit that short-circuits the costly and lengthy foreclosure process and provides the homeowner greater control over her transition.

Graceful exits include short-sales, deeds-in-lieu, and consent judgments. In a short sale, the property is sold to a third party buyer for less than the principal due on the loan after the lender accepts the sale price in satisfaction of the mortgage. A deed-in-lieu of foreclosure occurs where a homeowner signs over the deed to the property to the servicer, but this is only an option where there are no other liens on the property. A consent judgment occurs where the homeowner short-circuits potentially lengthy foreclosure proceedings by consenting to the foreclosure judgment and agreeing to vacate by a certain date. The judgment allows the property to proceed to sale quickly, saving both sides time and expense. In return, homeowners get to dictate the terms of their vacancy and can often obtain "cash for keys."

Mandatory mediation repairs a communication breakdown

Finally, mandatory mediation helps address the communications breakdown between servicers and homeowners. Most homeowners have zero direct contact (by phone or in person) with their mortgage servicers prior to foreclosure, though, for many, it is not for lack of trying.[18] While it may seem that homeowners would have multiple opportunities to seek resolution prior to foreclosure, homeowners' actual experience is the opposite. Long wait times on hold are the norm, and even when progress towards a modification is made over the phone, following up is often difficult.

Servicers often will request additional information but borrowers' responses by fax and mail will often get misdirected.[19] In some cases, a delinquent borrower may be negotiating in good faith with one part of the servicing department only to find out the case has been reassigned for foreclosure only after learning claim has been filed or (worse) a notice for a sheriff or trustee's sale is posted to the homeowner's door.

There are multiple causes for these kinds of problems homeowner face with their mortgage servicers. The spike in defaults and staffing shortages at servicers is one reason. Other is homeowners' difficulty identifying servicers. But the result is that properties are entering foreclosure with no attempt to find what may be a faster, cheaper, and therefore better solution.

HAMP will likely address these communications concerns for some homeowners but may exacerbate them for others. Servicers have limited loss mitigation staff, and those participating are more likely commit that staff to HAMP, with its incentive payments on one hand and its threat of regulatory sanction for non-compliance on the other. Eligible homeowners will likely experience a proactive servicer that can earn $1,000 for modifying a loan and $1,000 in each of the next three years the loan continues to perform. Ineligible homeowners may find their previously swamped servicer completely unavailable. Then, of course, there are the 25 percent of homeowners whose servicers are not participating in HAMP and who continue to have difficulty communicating with each other.

Mandatory mediation benefits all stakeholders

All stakeholders stand to benefit from mandatory mediation. Foremost, there is the chance for a homeowner to reach a resolution that permits him or her to stay in the home. Barring that, the homeowner has the opportunity to negotiate a "graceful exit," avoiding the stress, cost, and time of a foreclosure and possibly receiving some support or compensation from the servicer to assist in the transition.

Experience in Connecticut and Philadelphia indicates that noteholders, be they the original lenders or investors in mortgages through mortgage-backed securities, get greater value in most cases when their mortgage services mediate than they would in foreclosure.[20] Given that an average of over 70 percent of mediations settle without the need for foreclosure, it stands to reason that servicers must do better for these mortgage noteholders in mediation than they do by foreclosing.

Servicers have a fiduciary duty to act in the best interest of the noteholders. As clarified by the recent amendments to the Truth in Lending Act, servicers only discharge that duty if the settlements they reach with homeowner have a higher expected value than the property would fetch at a foreclosure sale.[21] Mediation should be viewed as a mechanism for ensuring a more optimal outcome.

Servicers also benefit from the speedier process of mediation. Most servicers do not have a contractual right to charge for their work on loan modifications.[22] For loans that can be saved, faster resolutions mean that the servicer regains a performing loan more quickly, while in cases where the home will be lost, faster resolutions mean quickly taking title to a home through a "graceful exit" rather than working through the full foreclosure process.

Accelerating foreclosure cases through mediation is even more valuable in states that offer homeowners the right of redemption—a legal right to buy back the property within a statutorily defined period of time that can be up to two years after foreclosure.[23] Servicers want to sell the foreclosed property immediately and do not want to wait out the redemption period before obtaining clear title. Most states that offer the right of redemption do not permit homeowners to waive the right.[24]

Homeowners also want to eliminate the risk of claims following foreclosure—known as deficiency claims—brought where the servicer recovers less than the amount of the original mortgage. Forty states permit deficiency claims after foreclosure in some form.[25]

Mediation provides an opportunity for both parties to avoid such follow-on claims: The servicer can accept a deed in lieu of foreclosure in which it waives its right to pursue a deficiency judgment against the homeowner in exchange for the homeowner's waiver of the right of redemption. While homeowners cannot waive their right of redemption after foreclosure, courts do permit homeowners to waive that right as part of deed in lieu of foreclosure. Homeowners cannot waive the right of redemption as part of their mortgage, but the deed in lieu is a contract separate from the mortgage, so the prohibition does not apply.

The deed also avoids a foreclosure, which is the action that triggers the right of redemption. The caveat is that most courts scrutinize such transactions closely to ensure that the homeowner is receiving a real quid pro quo for the deed in lieu and is not simply permitting the servicer to achieve an end-around the prohibition. Homeowners who receive cash for keys or a waiver of a deficiency judgment worth four, five, or even six figures likely receive the sort of compensation that would survive this type of judicial scrutiny.[26] Providing servicers with clear title to the property in this way allows them to sell the home rapidly, potentially minimizing holding costs and stemming losses generated by further erosion of property values in declining markets.

Even neighboring taxpayers benefit. Mediations that result in homeowners keeping their homes prevent vacant properties and foreclosure sales that can drive down the values of surrounding properties. Property values decline an average of 0.9 percent for every foreclosure within an eighth of a mile of the property.[27] In low- and moderate-income neighborhoods, where the risk of foreclosure is higher because of the greater concentration of subprime mortgages, each foreclosed property is estimated to reduce house values by 1.4 percent.

This impact of foreclosures on local property values is long lasting. Depressed values can be observed up to five years after a foreclosure happens.[28] What's worse, vacant properties become magnets for vandalism, arson, and violent crimes, which further depresses local housing prices. More vacant and abandoned homes thus require a municipality to expend more resources keeping squatters, vandals, and thieves off the property and out of neighborhoods, the costs of which are placed on remaining residents.

Finally, courts clogged with foreclosures cost taxpayers more as they spend money on additional staff, overtime, and other resources. To put the scale of the problem in perspective, Florida courts have brought back retired judges to process foreclosures just to handle the volume of filings.[29]

Then there is very real—but much harder to tally—cost of delay in the justice system. Increased foreclosure filings are not just delaying other foreclosures. Unlike landlord-tenant disputes, which often have a dedicated court, foreclosures occupy the same docket as other civil proceedings. Courts with existing programs, however, report that mediation or informal negotiations are working, quickly reaching a resolution in the majority of cases and acting as a pressure release valve for clogged courts.

The federal role in establishing mandatory mediation

Implementing mandatory mediation can be done at the state and local level, but given the magnitude of the foreclosure crisis, it is appropriate for the federal government to take a more active role, just as it has with MHP. At a bare minimum, funds should be made available to jurisdictions that want to implement mandatory mediation. Congress can allocate funds as an emergency appropriation, similar to the way in which it created the Neighborhood Stabilization Program, which provides funds to local governments and non-profit organizations to acquire and rehabilitate foreclosed properties.[30] NSP was funded on an emergency basis rather than through the standard budgetary process. Adequate funds should cover not only direct program costs, but also make provision for additional housing counseling capacity that will improve outcomes.

In the interim, jurisdictions could use a small portion of their Community Development Block Grant allocations to fund these programs. Among the primary objectives of CDBG are:

> *…The conservation and expansion of the nation's housing stock in order to provide a decent home and a suitable living environment for all persons, but principally those of low and moderate income [as well as] the alleviation of physical and economic distress through the stimulation of private investment and community revitalization in areas with … [a] declining tax base.*[31]

The current crisis involves both. Given the demonstrated negative impact of foreclosed properties on the value and salability of neighboring homes and the consequent costs and diminished tax revenues to communities, it would seem reasonable that funds for the establishment of mediation programs to prevent foreclosures would be an eligible use.

While the CDBG program does not list mediation among its eligible uses, it resembles other permitted activities, such as housing counseling and certain loan subsidies.[32] More importantly, mediation is not listed among the ineligible activities, which revolve around paying a person's rent or mortgage. Note that CDBG funds cannot be used to "carry out the regular responsibilities of the unit of general local government."[33] The Housing and Community Development Act of 1974 is not clear as to whether courts are part of "general local government," or whether this includes just the executive arm. Foreclosure mediation, however, should not fall under the parameters of a "regular" responsibility of the local government, given that it is a practice developed to deal with this specific scenario.

To eliminate any ambiguity until such time as Congress provides funds to help offset the costs associated with mediation programs, the Secretary of Housing and Urban Development should issue a notice expressly permitting CDBG funds to be used in this manner.

As a valuable additional step, the federal government should require mediation prior to foreclosure for all federally-insured mortgages. HUD already requires servicers of FHA loans to seek loan modification prior to issuing a notice of foreclosure; this is simply an extension of that requirement.[34] Because mediation provides more valuable outcomes than foreclosure alone, mediation can reduce FHA's Mutual Mortgage Insurance fund payouts in the aggregate. By extension, therefore, requiring mediation for FHA mortgages reduces the fund's risk of not complying with its statutory capital ratio.

The Federal Housing Finance Agency, as conservator for Fannie Mae and Freddie Mac, should mandate that similar processes be adopted for all mortgages in their portfolios as well. And optimally, Treasury should also require servicers participating in HAMP to engage in mediation prior to foreclosure.

HAMP would retain its efficiency through a two-step process. Servicers would first process eligible mortgages internally and offer modifications without having to negotiate directly with the homeowner. Only in cases where a modification offer cannot be made would a servicer mediate with a homeowner. This type of negotiation is already implicit in Treasury's updated guidance issued May 14, 2009, to "simplify and streamline the process of pursuing short sales and deeds in lieu."[35] Both processes require negotiations between homeowner, servicer, and occasionally a third party. Mediation has the same requirements but provides more settlement options.

Moreover, existing mediation programs mandate that the servicer have someone—legal counsel or a representative—available in person, which reduces settlement times as compared to a process that requires parties to mail or fax documents back and forth, causing delay as documents are in transit or, worse, go missing. As is likely to be the case under Treasury's guidelines, the cost of mediation could be paid for out of the funds set aside for paying servicer incentives under the $700-billion Troubled Asset Relief Program.

Servicers with a federally imposed obligation to mediate should be allowed to discharge the obligation by participating in a qualifying mediation program established by the jurisdiction where the home is located. Absent a local program, servicers can enlist the help of a third-party mediation services provider, such as the American Arbitration Association, which provided mediation services to Mississippi and Louisiana for insurance claims following Hurricane Katrina.[36] HUD would establish standards, certify mediators, and negotiate a flat-fee for the service.

Just as in the best-run state and local programs, FHA—and FHFA and Treasury, which should implement mediation for Fannie and Freddie and as part of HAMP, respectively—should require servicers to refer homeowners to housing counselors prior to the mediation and make a representative available with the authority to enter into a settlement. Mediations should take place in person where feasible and include a homeowner, her representatives, and the servicer's counsel. The servicer's representative may appear electronically. If the parties are too far apart geographically, mediation by phone should be permitted. And if the property is located in a state, county, or city with an existing foreclosure mediation program, participation in that program would meet the requirement to mediate.

Finally, the federal government can fill the need for a working group of jurisdictions implementing foreclosure mediation programs so that they can learn from one another and pool their data. This would be an appropriate role for a revitalized Office of Policy Development and Research at HUD.

State and local roles for establishing mandatory mediation

State and local governments are the most appropriate places to set up and administer a mandatory mediation program. Property is a mainstay of state and local law, encompassing taxation, zoning, building codes, foreclosures and so on. Local courts and governments understand the social and economic nuances of their surrounding area and can mold programs to best address issues specific to their jurisdictions. Moreover, incorporating mediation into existing state and local processes is easier than developing an entirely new system and structure to handle foreclosures and mediation.

Alas, there is no single legal solution for setting up mandatory mediation programs in every state. But programs can be set up by a state legislature, a municipality, a state court, or a local one. Potential points of origin vary from state to state based on political will at the state level, the power of local governments, the power granted to courts by statute, and the type of foreclosure permitted—judicial, non-judicial, or both. We'll review most of these possibilities for mandatory mortgage mediation in the examples we will explore in the following section. Here we will describe a series of case studies demonstrating the range of mediation programs now in place. It is from these case studies that we have developed the list of best practices that are highlighted in our appendix on page 40.

Philadelphia

Philadelphia's history of mortgage foreclosure relief

Like most jurisdictions, Philadelphia experienced a large increase in foreclosure filings over the past two years. Unlike most jurisdictions, however, Philadelphia has experience dealing with a flood of mortgage defaults during an economic downturn and was quickly able to launch a pilot program in its Court of Common Pleas to begin to address the problem.

In 1983, Philadelphia experienced a serious contraction in its steel and manufacturing industries. The resulting unemployment led to foreclosures. To provide relief, state legislators enacted the Homeowners Emergency Mortgage Assistance Act of 1983, or HEMAP, under which the state would lend eligible homeowners funds on attractive terms to bring their loans current, securing the loan using a second lien on the property.[37]

Then, in 2004, subprime mortgages and an underfunded HEMAP caused foreclosures to balloon again, this time to levels several times those of 1983. Community groups filed a motion for injunctive relief before the Philadelphia Court of Common Pleas seeking a moratorium on foreclosures. Judge Annette Rizzo instead required the affected parties to meet and negotiate with the help of Legal Aid attorneys and housing counselors.

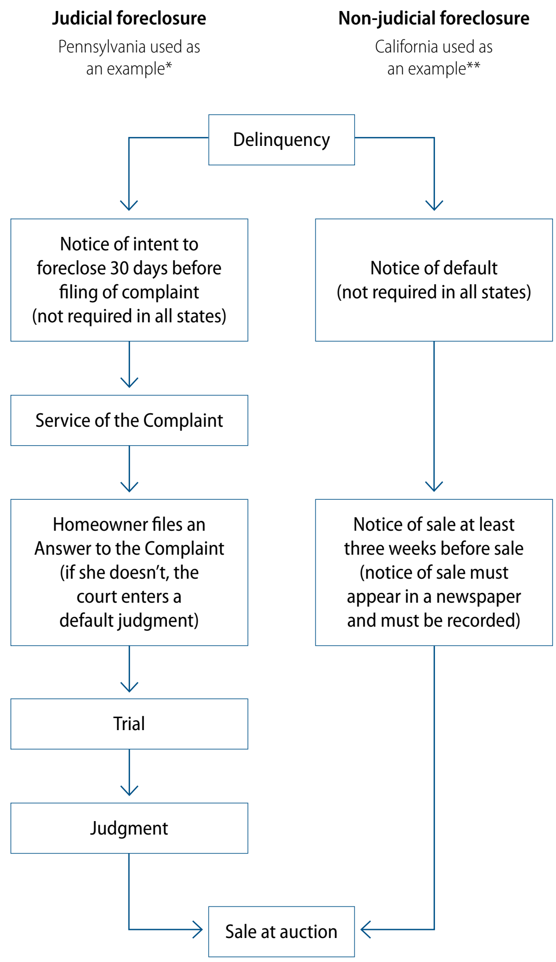
Going forward, the Court formed a Mortgage Foreclosure Steering Committee consisting of representatives from the mayor's office, lenders, industry groups, lenders' counsel, Legal Aid, the Philadelphia Bar Association, and housing counselors. The Committee's efforts led to a reduction in foreclosures until 2006. Two years later, the city had to launch a new program to cope with the current housing crisis.

Mechanics of the 2008 pilot program

Between 2006 and 2008, the pace of foreclosures once again increased, prompting the Philadelphia City Council on March 27, 2008 to request a moratorium on foreclosures.[38] The Council did not enact the moratorium because the Sheriff's office responded and unilaterally postponed the April and May sheriff sales to July. On April 16, 2008, the Philadelphia Court of Common Pleas, with the assistance of the Mortgage Foreclosure Steering Committee, instituted the Residential Mortgage Foreclosure Diversion Pilot Program, which is set to run from spring 2008 through December 31, 2009.[39]

The Pilot Program was implemented with an eye to foreclosures already under way as well as for future foreclosure filings. For cases filed before September 8, 2008, borrowers were served with a form explaining that they could request mediation.[40] For cases filed on or after September 8, 2008, all owner-occupied residences containing up to four residential units are automatically scheduled for a "conciliation conference," explained below, within 30-45 days after the servicer files a complaint.[41]

The foreclosure process, explained



* 41 P.S. 101, Sec. §§ 401, 403; Housing Finance Agency Law, 35 P.S. § 1680.103.
** CA Civ. Code § 2924-2924l.

The time and date of the conference appear on a Case Management Order the Court provides to the servicer to include in the service of process. If a servicer certifies that a property is unoccupied or otherwise ineligible for mediation, that information is included in service of process along with a form permitting a borrower to object and request mediation.

Defendants receiving notice that mediation has been scheduled are directed to call the Save Your Home Philly Hotline and speak with a housing counselor. The hotline helps connect borrowers with counselors, avoiding the need for borrowers to locate suitable counselors. Borrowers are also provided information request forms from the HOPE NOW alliance—the mortgage servicing industry's non-profit partnership organized by the Bush administration—and instructed to fill them out with assistance of a counselor prior to mediation.

Conciliation conferences (the Court's term for its mediations) are held at the Court of Common Pleas every Thursday. Currently, the Court conducts approximately 200 such conferences every week, half in a morning session and half in an afternoon session. To handle this volume of cases, the Court does not assign a mediator, known as a judge pro tem, to each conference. Instead, informal conferences are held in small clusters arrayed around the president judge's courtroom.

These conferences include servicer's counsel, the borrower, counsel for the borrower (usually pro bono counsel), and a housing counselor. A servicer's representative with actual authority to enter into loan modifications must be present either in person or by telephone; failure to meet this requirement can result in a postponement.[42]

While Philadelphia has not released statistical data on the results of these informal conferences, it reports that very few participants ever require full foreclosure proceedings before the court. The vast majority of cases reach resolution during the informal conferences, either permitting a homeowner to remain in the home or arranging for a "graceful exit."

Where the parties cannot resolve matters informally, they are assigned to one of the judges pro tem, who usually wait in the jury box to be called. These formal conciliation conferences are true mediations. They are conducted privately in a separate room, and, again, the majority of these cases reach resolution. Cases that remain unresolved after the formal mediations continue to standard foreclosure proceedings before the Court. The Court hears these few "unresolvable" as well as the approximately 25 percent of cases where the borrower fails to appear, thereby foregoing his or her right to mediation.

Approximately one-third of resolved cases since September 2008 have involved payment plans, interest forbearance, and interest rate and term modifications. Of the rest, most result in "graceful exit" by the homeowner by methods such as a deed in lieu of foreclosure or "cash-for-keys." Administrators report that they have not seen many modifications of loan principal.[43]

Participation in the pilot program

Mediation is mandatory for both servicers and homeowners in cases filed on or after September 8, 2008. Homeowner participation is roughly 75 percent. It is not known why some homeowners do not participate. Indeed, the fact that they are not participating makes them impossible to track.

What is known is that Philadelphia's participation rate is higher than that of other current programs. While the reasons for this have not been studied, Philadelphia's participation rate is likely that high in part due to the outreach efforts of community organizations such as the Association of Community Organizers for Reform Now, or ACORN, which has mobilized a corps of volunteers to go door-to-door to homeowners that have received notice of foreclosure, but have not called the Save Your Home Philly Hotline. Carrying cellular telephones, these volunteers explain the program to homeowners in person and encourage them to call the hotline then and there.[44] ACORN has very high participation among those homeowners it has contacted.

Administering the pilot program

The Court has not received additional funding for this program. Instead, it relies on assets from different departments contributing their time one day a week to the process. In addition, the Court relies heavily on pro bono attorneys. Participation has gone from 58 pro bono attorneys and 23 judges pro tem in June 2008 to approximately 300 attorneys and 50 judges pro tem today.[45] The program has been designed to be a component within the case management system rather than as a free-standing program requiring its own funding and overhead.

Connecticut

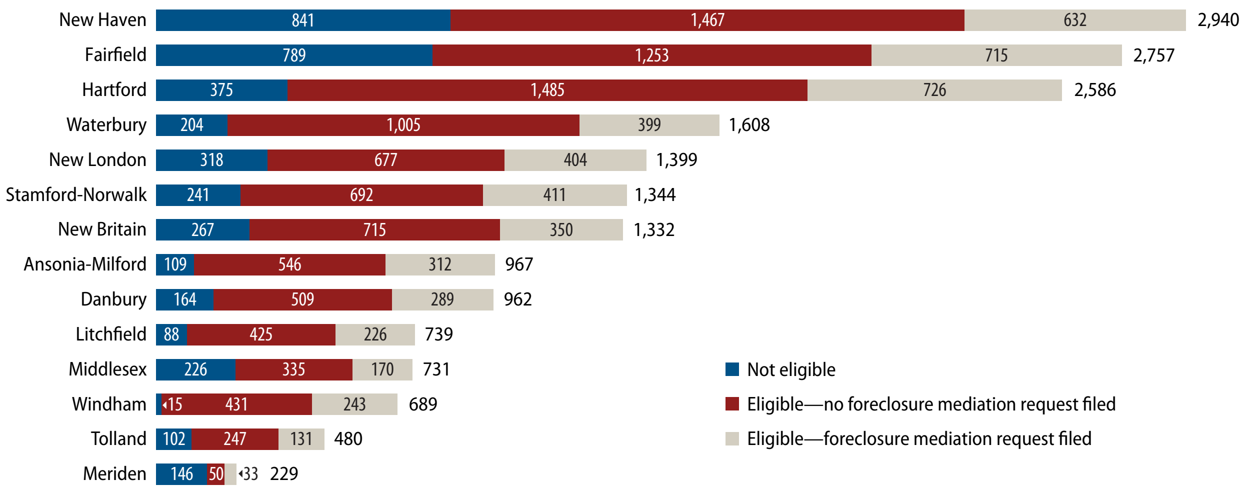
Mortgage filings in Connecticut have more than doubled since the 2004-2005 judicial calendar—or the court year that begins every September—with more than half of that increase occurring in the past year.[46] Connecticut's response represents a different approach to establishing a foreclosure mediation program from that of Philadelphia. Whereas the court in Philadelphia initiated a pilot program in one county without funding and relied on pro bono assistance, Connecticut established a funded program through legislation on a state-wide level without a pilot phase.

Connecticut's legislature created the foreclosure mediation program by passing PA 08-176 on May 7, 2008, later signed into law by Governor Rell on June 12, 2008. The program received $2 million in funding for 2009 from the State Banking Fund.

The Connecticut court system is divided into 12 judicial districts, with a dedicated mediator and office clerk in each district. In addition, there are seven full-time case flow coordinators.[47] It is overseen by Roberta Palmer, the full-time program manager and 20-year veteran mediator in Connecticut's landlord-tenant courts.

Foreclosure mediation program statistics

As of March 31, 2009



Notes: Statewide, there were 18,763 foreclosure cases filed between July 1 and March 31, 2009.. Foreclosure mediation requests (5,041) have been filed in 34% of the 14,878 eligible cases.

The Connecticut Senate is expected to pass bill number 619 shortly, amending the statute authorizing the program to improve procedures and raise the programs funding going forward to $4.8 million in 2010 and $1.6 million in 2011.[48] The additional funding would permit Connecticut to hire additional mediators and case flow coordinators, doubling or tripling its caseload capacity.

Mechanics of the program

Mediation in Connecticut is available for any qualifying mortgage, which includes both first and second liens on any one-to-four family owner-occupied property.[49] Eligible defaulted mortgages are not limited to mortgages taken out for the purchase of the property and can be loans for "personal, family or household purposes,"[50] such as refinancings, second mortgages, and home equity lines of credit.

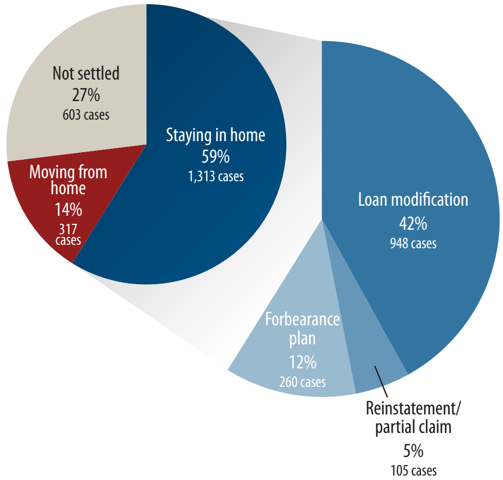
Connecticut is a judicial foreclosure state, so homeowners receive notice with service of the complaint on a form titled, "Notice to Homeowner: Availability of Foreclosure Mediation." The form lists the eligibility criteria and explains that "Mediation is a process by which a neutral mediator assists parties in trying to reach a voluntary negotiated settlement to resolve their dispute." The form also notes that a homeowner must fill out to participate. The notice ends with a statement in bold that there is no fee for applying to the program.

Unlike Philadelphia, where mediation is mandatory for both parties, Connecticut currently requires homeowners to opt-in by filing a form within 15 days of receiving service of process. Bill number 619 would make mediation mandatory for both parties, requiring the court to schedule a session automatically once a homeowner returned the writ of foreclosure (required by rule).[51] Scheduling mediation only after the homeowner responds conserves the court's resources by mediating only those cases in which the homeowner shows that she plans to participate.

The court must schedule mediation within 10 business days of the homeowner's response. Mediation must conclude within 60 days, though parties or the mediator can apply for a 10-day extension upon a showing of good cause.[52] Bill number 619 would give the court 15 days to schedule mediation and provide for an extension of 30 days. The homeowner and servicer's counsel must appear in person; servicer's counsel must have authority to enter into a settlement, and the servicer's representative must be available by telephone or electronic means. Within two days after the first mediation, the mediator must decide whether a further mediation would be fruitful and send the court and parties a report to that effect; otherwise the mediator may cancel any subsequent sessions and permit foreclosure to proceed.

Foreclosure mediation program results

Cases terminated as of 3/31/2009



Notes: Statewide, 2,233 cases have completed mediation as of March 31, 2009. This chart illustrates the outcome of these cases. The category "moving from home" includes agreements for a short sale, a deed in lieu, or an extension of the law day or sale date. The categories "moving from home" and "staying in home" when added together result in a settlement rate of 73%.

The foreclosure proceedings are not stayed during mediation, so a homeowner must file an answer and participate in the litigation as needed. However, no judgment can be entered until the mediation period has ended.[53]

Participation in the program

Between July 1, 2008 and March 31, 2009, 14,878 of the 18,763 foreclosure claims filed in Connecticut were considered eligible for mediation. Eligibility in this context simply means a foreclosure filing on a residential, as opposed to commercial, property. In practice, the court estimates that a large percentage of the so-called "eligible" cases did not involve the one-to-four family owner-occupied residential properties that actually qualify for mediation.

But because homeowners in only 5,041 of the 14,878 cases (33 percent) requested mediation, the court has not learned any more about the remaining 9,837 cases. Connecticut has engaged in more limited outreach efforts than those undertaken in Philadelphia, in part due to the large geographic area covered by the program.

Of the 5,041 homeowners who requested mediation, 2,233 (44 percent) have been completed, constituting about 200 cases per month. Despite the number of outstanding cases, Connecticut does not have a backlog. The remaining 2,808 cases are ongoing, having conducted least the initial meeting with a mediator. The courts have utilized their equitable powers to permit parties to continue mediations beyond the 90-day statutory limit with mutual consent. Parties in the vast majority of cases have requested this dispensation, often because servicers are overwhelmed and require additional time to assess a homeowner's financial submission and modification proposal.

Connecticut's results are more encouraging with 2,233 completed cases. 1,630 have reached a resolution, preventing the need for foreclosure proceedings in nearly three-quarters. 1,313 cases resulted in homeowners keeping their homes, indicating that, if a homeowner can resolve her case, she has an 80 percent chance of keeping her home through loan modification (used in the vast majority of cases), reinstatement, or forbearance.[54] Most of the loan modifications involve modifying the interest rate or the terms, but not the principal. The remaining 20 percent of settled cases involved "graceful exits," including short sales (38 percent), deeds-in-lieu of foreclosure (12 percent), or consent judgments (50 percent).

Florida

Of all the places that have moved toward implementing mandatory mediation, Florida is the most heavily affected by foreclosures. Three of the 10 metropolitan areas with the highest rates of foreclosure in April 2009 are in Florida, but the response to this clear crisis so far has been disjointed.[55] The majority of Florida's judicial circuits have made no response, while the five circuits that have recently instituted mediation programs vary widely in their policies. [56] One circuit requires informal conciliation conferences without the presence of a mediator, and yet another permits homeowners to file a paper application for loss mitigation similar to HAMP, with no mention of in-person negotiations.[57] Below, we examine the responses of several of these circuits in detail.

The Florida Supreme Court launched a Task Force on March 27, 2009 to provide statewide guidance on the problem.[58] Issued on May 8, 2009, The Task Force's Interim Report set out the Task Force's principles and information collected to date, but did not disclose any details of the final proposal, due in August 2009.

Going without—Lee County, Florida's 4th Judicial Circuit

Lee County is home to the Fort Myers-Cape Coral metropolitan area, which had the second-highest foreclosure rate in the nation in April 2009. The volume of foreclosures has increased more than 12-fold (from 1,900 to 24,000) in the past two years,[59] and the court made the covers of national newspapers in early 2009 when it instituted a "rocket docket" to deal with the flood of cases.[60]

Since the spring of 2008, the court had streamlined foreclosure filings through the clerk's office, brought back retired judges to hear uncontested cases, and otherwise attempted to speed up cases.[61] Even with hearings of less than a minute in some cases, Lee County, in Florida's 20th Judicial Circuit, remains inundated, as evidenced by lawyers swapping out the morning's cases with the afternoon's on a steady stream of hand trucks.

Providing mediation—Florida's 1st, 9th, 11th, 18th, and 19th Judicial Circuits

Florida's 1st, 9th, 11th, 18th, and 19th Judicial Circuits (Covering Escambia, Santa Rosa, Okaloosa, Walton, Orange, Miami-Dade, Seminole, Indian River, Martin, Okeechobee, and St. Lucie Counties) have established mediation programs, all since January 2009. Four of these make mediation mandatory; the last does not.

In the four Florida judicial circuits that have implemented mandatory mediation programs, data is not yet available on their success rates. Three circuits implemented mediation programs that tap vendors outside the court system to provide mediation services. All three circuits—the first, which covers the western half of Florida's panhandle; the 11th, which covers Miami-Dade, home to the 10th-highest foreclosure rate in the country; and the 19th, responsible for four counties on Florida's east coast, north of Palm Beach and southeast of Orlando—rely on the Collins Center for Public Policy to administer mediation services.[62]

For simplicity, we will focus on the terms of Miami's Circuit Homestead Access to Mediation Program, or CHAMP. There, any case filed on or after May 1, 2009 is referred to the Collins Center for Public Policy for mediation scheduling unless one of the parties objects within five days of the initial foreclosure filing.[63]

The Collins Center will attempt to contact the homeowner for 30 days and refer him or her to a housing counselor who, in turn, has 21 days to contact the homeowner and prepare the financial documentation necessary for mediation. All procedures under the order must be completed within 120 days. The Collins Center will only schedule mediation once the financial documentation is complete; given the newness of the program, it is not yet clear what happens if 21 days pass and the file remains incomplete. At the mediation, the homeowner and servicer's counsel must appear in person. Counsel must have authority to enter into a settlement and have telephonic or electronic access to the servicer's representative.

The administrative order contemplates that the case may proceed to summary judgment of foreclosure should the homeowner fail to appear or should the parties reach an impasse. The order does not define an impasse, does not state whether the parties, the mediator, or both can declare an impasse, and does not require the parties to negotiate in good faith. The mediator must report the results to the court within10 days of the session. Mediation does not stay foreclosure proceedings, but the court will not enter judgment until mediation procedures have concluded.

The servicer must pay the Collins Center $750 upfront for this service, $350 of which the Center will forward to the appointed mediator. Failure to pay can lead to dismissal without prejudice or other sanctions. If mediation does not occur under certain circumstances, then the Collins Center will refund $350 to the servicer. There is no provision for the servicer to add the costs of mediation to that of foreclosure.

Florida judicial circuit mediation programs

Judicial Circuit No.	1st	4th	9th	11th
Counties	Escambia, Santa Rosa, Okaloosa, Walton	Clay, Duval, Nassau	Orange	Miami-Dade
Largest Cities	Pensacola	Jacksonville	Orlando, Pine Hills	Miami
Percent Increase in Foreclosure Filings 2006–2008	230%	148%	444%	474%
# of 2008 Filings	7,736	13,979	36,939	56,100
Percentage of total state filings	2.10%	3.79%	10.02%	15.22%
Notice of Loss Mitigation	Collins Center will contact parties and notify them of mediation as soon as it is scheduled.	Notice that legal assistance is available is sent with service of process.	Included with service of process; if the servicer has its own loss mitigation program, that, too, must be included in the notice.	Collins Center will contact parties and notify them of mediation as soon as it is notified that a complaint has been filed.
Mediation	Mandatory	None	Opt In (Voluntary)	Mandatory
Housing Counseling/Pro Bono Representation	Both are noted in the notice of mediation, but neither are required.	Notice includes the contact number for legal representation, but not housing counseling.	Notice includes the contact number for legal representation, but not housing counseling.	Collins Center automatically refers homeowners to counselors. Notice is provided that pro bono representation is available.
Time Limit	No time limit.	n/a	Servicer's counsel must schedule mediation within 45 days of the request. There is no time limit for mediation once begun.	All procedures must be complete within 120 days. Collins Center will schedule mediation within the first 30 days.
Administrator	Collins Center for Public Policy	n/a	Court qualifies mediators, but parties conduct mediation privately.	Collins Center for Public Policy
Costs	Servicer pays $750 up front, but can receive up to $350 refund if mediation does not take place.	n/a	Servicer pays $275 for the first two hours and $100 for each additional hour; it can recoup 1/2 the costs in a foreclosure sale.	Servicer pays $750 up front, but can receive up to $350 refund if mediation does not take place.

Source: Foreclosure filing data taken from the Florida Supreme Court's Task Force on Residential Mortgage Foreclosures Interim Report (Dated May 8, 2009). Information on individual programs taken from each circuit's relevant administrative orders.

Mediation in Seminole County—the 18th Judicial Circuit—is automatic for both parties, but is handled within the court itself.[64] The 18th Judicial Circuit, however, only refers cases to mediation where the homeowner has filed a responsive pleading or other filing, in order to avoid expending resources on unresponsive homeowners.

The servicer must schedule the mediation and notify the mediator, homeowner, and subordinate lienholders of the date and time. Notice to the homeowner includes a financial questionnaire which the homeowner is encouraged, but not required, to complete prior to mediation. Neither the Administrative Order nor the court's forms make any mention of pro bono representation or the availability of housing counselors to assist the homeowner.

Mediation does not stay the proceedings. Indeed, the servicer may file a motion for summary judgment and schedule a hearing, provided the hearing falls after the scheduled mediation date.

The $250 cost for one-and-a-half hours of mediation is paid by the servicer, but may be taxed by the court as a cost of litigation in the foreclosure judgment. The servicer must make available a representative with full authority to enter a settlement. The representative must attend continuously through the mediation, whether in person of by phone. A servicer's failure to appear leads to dismissal without prejudice.

Florida judicial circuit mediation programs (continued)

Judicial Circuit No.	12th	15th	18th	19th	20th
Counties	Sarasota, Manatee, and DeSoto	Palm Beach	Brevard, Seminole	Indian River, Martin, Okechobee, St. Lucie	Lee (one of five counties in the circuit)
Largest Cities	Sarasota, Arcadia	Palm Beach, West Palm Beach, Boca Raton	Cape Canaveral	Vero Beach, Fort Pierce	Fort Meyers
Percent Increase in Foreclosure Filings 2006–2008	631%	496%	387%	550%	788%
# of 2008 Filings	14,530	29,411	15,699	13,984	41,626
Percentage of total state filings	3.94%	7.98%	4.26%	3.79%	11.29%
Notice of Loss Mitigation	Servicer contacts the homeowner directly.	Included with service of Process. Includes loan modification request forms.	If the homeowner files a responsive pleading, the matter is referred to mediation and the servicer provides the homeowner notice.	Collins Center will notify parties of scheduled mediation within 10 days of the filing of the complaint.	n/a
Mediation	None. Instead a conference call between homeowner and servicer.	None. This is a paper loan modification request like HAMP, though the parties can request mediation.	Mandatory	Mandatory	None
Housing Counseling/Pro Bono Representation	Availability is mentioned in the notice; a meeting is not required.	Neither are required; contact numbers for both are provided with notice.	No mention of either in notice documents.	Both are noted in the notice of mediation, but neither are required.	n/a
Time Limit	Servicer must contact homeowner within 45 days of service of process to schedule conference call. The parties must complete any action agreed to within 45 days after the conference call.	n/a	No time limit.	No time limit.	n/a
Administrator	None. The servicer files a certificate of compliance with the court.	n/a	Court qualifies mediators, but parties conduct mediation privately.	Collins Center for Public Policy	n/a
Costs	n/a	n/a	Servicer pays $250 for 1.5 hour session, which may be taxed as a cost of foreclosure.	Servicer pays $750 up front, but can receive up to $350 refund if mediation does not take place.	n/a

Source: Foreclosure filing data taken from the Florida Supreme Court's Task Force on Residential Mortgage Foreclosures Interim Report (Dated May 8, 2009). Information on individual programs taken from each circuit's relevant administrative orders.

Voluntary foreclosure mediation—Orange County, Florida's 9th Judicial Circuit

As of February 25, 2009, in the 9th Judicial Circuit serving Orange County, which includes Orlando—home to the ninth-highest foreclosure rate nationally—a servicer must notify the homeowner that mediation is available as part of service of process.[65] Unlike the programs above, mediation in Orange County is "opt-in." If the servicer has a loss mitigation program in place, information on accessing that program, such as a 1-800 number, must also be included with the notice. A servicer that cannot contact a homeowner after 30 days of diligent attempts may so certify, and the court will forego mediation and enter judgment. As in Miami, mediation does not stay the foreclosure proceedings, but judgment may not be entered until mediation procedures are complete.

Where a homeowner requests mediation, servicer's counsel must schedule it within 45 days with a participating mediator at reduced rates set for this program. Rates are $275 for the first two hours and $100 for each subsequent hour. The servicer must pay this fee within 20 days of the mediation, but may recoup half as costs included within the final judgment.

The homeowner, servicer, and servicer's counsel must all appear in person at the mediation unless the servicer's representative is located more than 25 miles from the place of the mediation. In that case, servicer's counsel must attend in person and the representative must be available by phone for the duration of the conference—something that, in practice, we have yet to see elsewhere. Either party's failure to appear can result in dismissal or judgment.

Unlike Miami, Orange County requires only that the homeowner make a good-faith effort to collect and provide financial information prior to the mediation session, noting that doing so will assist the servicer and help identify "programs or other means of assistance and potential workouts."[66]

Falling short—Florida's 12th and 15th Judicial Circuits

As of December 1, 2008, Sarasota, Manatee, and DeSoto Counties representing the 12th Judicial Circuit, instituted the Homestead Foreclosure Conciliation Program, or HFCP.[67] Within 45 days of service of process on the homeowner, the servicer must contact the homeowner and schedule a telephone conference "to have an open and frank discussion about the alleged default and to consider realistic alternatives to foreclosure."[68]

Anything the parties agree to during the conference must be complete 45 days after the date of the conference, at which point the servicer must file a certificate of compliance with the court. The notice to the homeowner must include mention that pro bono legal assistance is available. The administrative order makes no mention of housing counselors. The order explicitly states that it does not limit the authority of the court to order mediation.[69]

In Palm Beach County representing the 15th Judicial District, the Court put in place a loan modification request program resembling HAMP.[70] The homeowner is notified that he or she can request loss mitigation from the servicer and that legal assistance and housing counseling are available. The notice includes forms resembling those published by the HOPE NOW alliance. A homeowner submits the forms to the servicer, which reviews the application and cannot obtain judgment until it provides a response.

The administrative order notes that either party may request mediation at any time, though the option is not mentioned on the notice sent to homeowners.[71] Interestingly, the only requirement in the order regarding mediation is that servicer's representative certify prior to any mediation session that it has the authority to enter into a settlement. Mediation has been granted at the court's discretion in several recent cases.[72] The Court has developed a standard order which divides the cost of mediation, capped at $500, evenly between the servicer and homeowner.

California

California, consistently one of the top foreclosure states, is a predominantly non-judicial foreclosure state. While there appears to be no bar to mandating mediation in such a legal regime, California has opted to mandate private telephone conferences instead of mediation.

Under California law, a servicer cannot file a notice of default—the notice which begins a non-judicial foreclosure in California—until 30 days after contacting the homeowner to schedule a telephone call. The call must occur within 14 days of initial contact to "assess the borrower's financial situation and explore options for the borrower to avoid foreclosure."[73]

During the initial contact, the servicer must provide the homeowner with a 1-800 number supplied by HUD to locate a housing counselor. The homeowner is not required to contact a counselor, but is permitted to designate a housing counselor, attorney, or other advisor to negotiate with the servicer on her behalf. Most importantly, the servicer may (but is not required to) involve loss mitigation personnel in the call. Once the call has occurred, the servicer files a declaration to that effect and can proceed with the foreclosure.

The California statute does not contemplate any data tracking mechanism, so there is no way to determine what effect it has had.

In February 2009, California further amended its statutes to delay foreclosures an additional 90 days unless the mortgage servicer obtains an exemption by showing that has put in place a "comprehensive loan modification."[74] It has been styled a moratorium by some and, if so, would be the first in the country when it takes effect June 15, 2009.[75]

In practice, it appears that the statute will have little effect because most servicers will be able to obtain an exemption. Any servicer with a loan modification program consistent with HAMP would be eligible for an exemption under the language of the statute. To qualify, a program must permit loan modifications of first mortgage on owner-occupied residential properties where the NPV test to the servicer and its noteholders is positive, the resulting debt-to-income ratio of the homeowner is 38 percent or less, and the modifications include those allowed under HAMP or the reduction of principal. The statute explicitly states that servicers having a program in "[c]ompliance with a federally mandated loan modification program" could be deemed exempt.[76]

Nevada

Nevada, also one of the top foreclosure states, demonstrates that there is no bar to foreclosure mediation in non-judicial foreclosure states. The state has approved a new statute, effective July 1, 2009, creating a system of voluntary foreclosure mediation.

Under existing Nevada law, a servicer must provide a homeowner with "notice of breach and election to sell" (for example, default), wait three months, and provide notice of sale 21 days prior to selling the property. The new statute will require servicers to include in the notice of breach a form for requesting mediation as well as contact telephone numbers for the servicer, housing and credit counselors, and pro bono legal services.[77] The homeowner will have 30 days to request mediation, at which point the court must appoint a judge, senior judge, hearing master, or other agent of the court as a mediator – charging no more than $85 per hour for a total of not more than $400.[78]

As in other jurisdictions, the servicer must negotiate in good faith and either appear in person or appoint a representative with authority to finalize a settlement who will be accessible at all times during the mediation.[79] Unlike in other jurisdictions, the servicer must bring to the mediation the original or certified copy of the deed of trust, the mortgage trust, and each assignment of such documents. If a servicer fails to do any of these things—including supplying the documentation—the mediator is required to submit to the program administrator a petition recommending sanctions. The mediation program administrator will provide that petition to the court, which has discretion to impose sanctions up to and including a forced loan modification on the court's terms.

Another difference between Nevada and other jurisdictions is that the mediator has the exclusive power to determine when the parties have reached an impasse and can terminate the mediation.[80] In other jurisdictions, that power is also granted to the parties.

Finally, as in California, the Nevada statute does not contain any provision for tracking results.

Addressing potential barriers to mandatory mediation programs in mortgage-backed securities contracts

The biggest barrier to foreclosure mediation are the pooling and servicing agreements, or PSAs, which govern the rights and duties of servicers who oversee pools of securitized mortgages. The vast majority of home mortgages reside in such pools, known as Residential Mortgage-Backed Securities or RMBS. The PSAs address the servicer's power to modify loans, rather than mediation directly, but the effect is the same.[81] The power to modify a loan is a precondition to mediation or settlement; if the servicer cannot modify the loan, then there is nothing for the parties to negotiate.

PSAs have two problems. They either contain vague language about the servicer's ability to modify mortgages or they cap the frequency, amount, or type of modifications permitted. Congress has addressed both with recent legislation.

Congress and the industry have remedied vague PSA language

The vast majority of PSAs permit the servicer to modify mortgages in a pool if it determines, consistent with industry practice, that the loan is in default or default is imminent—or reasonably foreseeable or similar language.[82] When these PSAs were written, so-called distressed modifications were so rare that there was no industry standard for handling them. Now, servicers raise concerns that investors may sue them because modifications will require investors to recognize a loss based on the drop in their investment's value. Until modifications began, investors could cite the uncertainty about the actual performance of their mortgage-backed securities and argue that the assets were worth what they originally paid for them.

In 2007, after extensive consultation with its members, the American Securitization Forum issued a Statement of Principles, Recommendations, and Guidelines containing the "general servicing practice standard" for loan modification. The principles required servicers to act in the best interest of investors *in the aggregate*; that is, to maximize value for the pool as a whole and to modify loans where the net present value of a modification was greater than the anticipated recovery in foreclosure.[83] By so defining the term, the American Securitization Forum attempted to thwart lawsuits from investors who may have been disproportionately affected by the modification.

The disproportionate effect is a consequence of the structure of most mortgage-backed securities, which split pools of mortgages into groups or "tranches" having a range of credit qualities. Investors in the highest-rated tranches are paid first as homeowners pay their mortgages; the lowest-rated tranches are paid last. A modification that lowers a homeowner's payments will first affect the lowest-rated tranches in the pool, leaving those with higher ratings untouched.[84]

Providing further cover, Congress enacted similar language in the Housing and Economic Recovery Act of 2008.[85] The statute amended the Truth In Lending Act provisions to state that a servicer acts in the best interest of investors where it modifies a loan for an owner-occupied property in default or imminent default and the NPV of the modified loan exceeds the expected recovery in foreclosure.[86] Further, the statute provided that servicers having a fiduciary duty to maximize the NPV of pooled mortgages discharged that duty by maximizing the value to investors as a group, not to any individual.[87]

A significant portion of PSAs explicitly restrict modifications

While Congress's 2008 Truth In Lending Act amendment may have clarified the language in vague PSAs, it carved out—and thus did not affect—any PSA containing explicit terms limiting or prohibiting modification.[88] A recent Berkley Law School study on subprime securitizations from 2006 found that nearly a quarter of PSAs contain such terms.[89] Among them are Morgan Stanley's, which prohibit any modification and represent over nine percent of the deals reviewed.[90] The other 15 percent belonged to Countrywide, the country's largest servicer and now part of Bank of America.[91] A significant portion of Countrywide's PSAs contain two express limitations:

- Any modification requires the servicer to purchase the modified loan from the pool at the original purchase price.
- The servicer may not modify loans representing more than 5 percent of the aggregate principal balance of the pool.[92]

The language is at the center of a lawsuit by investors against Countrywide—a lawsuit in its earliest stages.[93]

In the fall of 2008, however, Countrywide settled cases with 11 state attorneys general regarding its servicing practices. As part of the settlement, Countrywide agreed to modify at least 50,000 mortgages by March 31, 2009.[94] On December 1, 2008 Greenwich Financial, a hedge fund investor in a mortgage pool serviced by Countrywide, sued the company, claiming that Countrywide had to purchase the modified mortgages pursuant to the PSAs.

Countrywide maintains that the purchase provision applies only to "retention modifications," or modifications in which servicers would refinance loans at a lower rate or under more favorable terms to retain a customer. Investors wanted to limit such modifications, which generated fees for the servicer but yielded less for investors due to the improved terms.[95] Countrywide maintains that the parties never intended to apply the provision to "distressed modifications" seen now. The PSAs don't include separate language for such modifications. Greenwich Financial claims that the language of the PSAs is clear and applies to all loan modifications.

To remedy this, Congress passed the Servicer Safe-Harbor, Section 201 of the Helping Families Save Their Homes Act of 2009, signed into law May 20, 2009.[96] The provisions revise the same section of the Truth In Lending Act previously amended, 15 U.S.C. § 1693a, this time adding a provision preventing servicers from being held liable or made subject to an injunction, stay, or other equitable relief as the result of engaging in loan modifications.

The law should permit servicers to modify mortgages even where explicitly limited or prohibited in their PSAs. The 2009 act as passed removes the contract carve-out contained in the 2008 act, leaving the 2009 act silent regarding PSAs. Language explicitly applying the safe harbor to contracts ("notwithstanding any investment contract between a servicer and a securitization vehicle or investor") was present in the House bill, but did not survive to the final version; the plain language of the 2009 act renders it unnecessary. It protects *any* servicer engaging in qualified loss mitigation efforts.

If Congress simply wanted to eliminate the specter of vague PSA language with this new bill, it could have stopped at defining servicers' fiduciary duties as applying to the mortgage pool as a whole instead of to a particular investor or group of investors. That would have protected servicers who had the power to modify loans under their PSAs, but were afraid of claims for violations of their fiduciary duties. The addition of the safe harbor indicates that Congress intended to go further and eliminate liability also for those servicers whose PSAs prohibited or limited modification.

There are no constitutional barriers to state or local mandatory mediation

A state or local mandatory mediation program should not run afoul of the Constitution. The relevant sections are Contracts Clause of Article I and the Due Process and Takings Clauses of the 14th Amendment.[97]

The Contracts Clause prohibits states from "passing any … law impairing the obligation of contracts."[98] The Court has held that emergency statutes limiting a creditor's rights in foreclosure do not violate the Contracts Clause. Further, the U.S. Supreme Court has noted that parties enter contracts knowing that the state law governing their remedies may change, so changes to available remedies cannot be said to impair a contract.

The most commonly cited case considering the Contracts Clause is *Home Building & Loan Association v. Blaisdell*.[99] The Court held that a Minnesota statute that temporarily permitted borrowers to apply in court for a stay of foreclosure for up to two years—enacted in response to the Great Depression—did not violate the Contracts Clause because it was a valid use of the state's police power, "appropriate to the emergency and granted only upon reasonable conditions."[100] Under the law, the court had discretion to grant the stay and to require the borrowers either to forward income from the property to the lender or pay the fair rental value. The Blaisdell family applied for and received a two-year stay and were required to pay $40 a month in rent.

Economic emergencies, the Court noted, were no different from physical disasters with regard to the state's police power.[101] "Preservation of the reasonable exercise of the protective power of the state is read into all contracts," and the state government had to ensure that the Contracts Clause and emergency powers existed in harmony.[102] To this end, the Court determined that proper emergency legislation has to be "(a) temporary, (b) "addressed to a legitimate end [- the emergency]" and (c) "reasonable and appropriate to that end."[103]

The Court also has ruled that legislation which alters a contractual remedy—but does not go so far as to severely impair that remedy—does not violate the Contracts Clause. In *Richmond Corp. v. Wachovia Bank & Trust Co*., the Court upheld a North Carolina law limiting a lender's right to recover a deficiency if the property foreclosed on was later sold for less than the amount of the secured debt.[104] The Court found that:

> *The legislature may modify, limit, or alter the remedy for enforcement of a contract without impairing its obligation, but, in so doing, it may not deny all remedy or so circumscribe the existing remedy with conditions and restrictions as seriously to impair the value of the right. The particular remedy existing at the date of the contract may be altogether abrogated if another equally effective for the enforcement of the obligation remains or is substituted for the one taken away.*[105]

There, the Court determined that the statute limited the lender to its expected recovery under the contract—namely, the value of the property securing the debt.

State mediation should pass muster under both aspects of this analysis. Under *Blaisdell,* whether the severity of the current crisis compares to that of the Great Depression may be up for debate, but fact that the current situation constitutes an emergency is not. Mediation programs are intended to address a central aspect of this economic emergency—the housing crisis that lies at its heart. Most existing programs have an explicit termination date or are otherwise characterized as temporary in their statutes or rules.

And the mediation requirement is a limited and reasonable response. Most, if not all, state courts can already order mediation under their equitable powers, so that mandating mediation is less a change in state law than a shift from making it optional to making it mandatory.

Second, mediation does not alter or abrogate a servicer's remedy, but merely delays it. Mediation does not compel a servicer to accept settlement; it merely requires that it take time out in the early stages of foreclosure to negotiate in good faith. Mediation programs currently in place, as well as those being contemplated, take great pains to ensure the delay resulting from foreclosure mediation is as short as possible, the rapid reduction in case volume being one of these programs' major goals. If a two-year stay with compensation was reasonable in *Blaisdell*, then surely mediations lasting several months, even the minority that stay the foreclosure proceedings, are reasonable too.

Similarly, under *Richmond*, the parties to these housing contracts clearly understood that their mortgage contract was subject to an ever-changing federal and state legal regime. The requirement that a lender delay foreclosure for a short period to mediate does not so impair that remedy as to violate the Contracts Clause.[106]

Foreclosure mediation laws have a rational basis, so they satisfy the Due Process Clause of the 14th Amendment.

The fact that state foreclosure mediation programs are "addressed to a legitimate end" and are "reasonable and appropriate to that end" satisfies the Due Process Clause of the 14th Amendment as well. The Supreme Court has applied heightened scrutiny in cases involving fundamental rights, such as privacy, or discrimination based on gender. But foreclosures, being a matter of contract and property law, are reviewed under the "rational basis" standard.

This test merely requires that the government have a legitimate end and that the law in question be rationally related to that end—a test that the proposed foreclosure mediation programs clearly satisfy for the reasons cited above.

Foreclosure mediation is not a taking

Altering a servicer's rights under a PSA does not constitute a taking under the 14th Amendment for multiple reasons. There are two types of takings, direct appropriations and regulatory takings.[107] A direct appropriation occurs when the government takes property for its own use, which does not apply here where PSAs address contracts between servicers, noteholders, and homeowners. A regulatory taking occurs when government regulation has a significant impact on the value of a property right.

Here, the property right at issue would be the interest of noteholders or investors in pools of mortgage-backed securities. A noteholder or investor's right is contractual and not one of real property; indeed much of the value to investors in mortgage-back securities comes from the tax benefits in the REMIC statute. The Supreme Court has noted repeatedly that contractual or other administrative rights are subject to alteration or even extinguishment by subsequent regulation without a takings violation.[108] The exception would be when the government was taking the property for itself as a result of the regulation, but that is not the case here.[109]

When determining if a taking has occurred, the Court considers the entire property and not its discrete segments.[110] As noted above, reducing income to the investor pool would first affect those holding lower-rated tranches. Here, the possibility that reducing the income to the investor pool could hurt a single investor significantly is unimportant if the effect on the pool as a whole is minor.

Furthermore, as required by the servicer's fiduciary duty, loan modifications will serve to maximize the value of the mortgage pool, not diminish it. It is hard to see how maximizing value could be construed as its opposite—a taking.[111]

State law considerations of implementing foreclosure mediation programs

Some states permit foreclosure through the courts (known as judicial foreclosure), while others permit foreclosure without involving the courts (or nonjudicial foreclosure). Still other states permit both.[112] The differences have not yet affected state foreclosure mediation efforts, mostly because California is the only state with a predominantly nonjudicial foreclosure regime to require loss mitigation efforts, although Nevada will be deploying a program beginning July 1, 2009.[113] Governor Tim Pawlenty of Minnesota vetoed a similar bill in that state.[114]

Foreclosure in nonjudicial foreclosure states is granted by statute. Nothing prevents the legislature from amending the statute to require mediation before a party can initiate (or, for that matter, complete) a nonjudicial foreclosure. The legislature amended its foreclosure statute to alter the notice provisions and mandate a conciliation conference between the parties. It could just as easily go further as Nevada has done to require mediation. Requiring mediation might give the appearance of converting foreclosure in California or Nevada into a quasi-judicial process, and thus meet with greater resistance from servicers, but there is no legal bar to doing so.

At first blush it may appear that, counter-intuitively, requiring mediation by statute in nonjudicial foreclosure states may be easier than doing so in judicial foreclosure states. As Geoff Walsh of the National Consumer Law Center has pointed out, courts in most states already have the power to refer a foreclosure action to mediation as part of their equitable powers.[115] A legislative action mandating the use of the court's rule power could arguably violate states' own separation of powers principles. In fact, legislative action creating a foreclosure mediation program would likely leave courts' powers untouched, supplementing rather than supplanting those powers.

In practice, we have found that judiciaries and legislatures are strongly aligned in favor of foreclosure mediation, so this type of "turf war" is unlikely. As detailed below, we recommend reaching out to all government stakeholders when establishing such a program. Getting buy-in presents a simple, practical solution to this issue.

Finally, governments within a state must determine the appropriate level (city, county, or state) at which to implement and administer foreclosure mediation programs. Legally, this involves analysis of whether a particular state subscribes to Dillon's Rule (which defaults all power to the state) or Home Rule (which defaults power to municipalities) and what powers are granted each municipality.[116]

In practice, however, the issue is again moot. So far, Florida, Pennsylvania, and New York have implemented their programs in individual municipalities. In Pennsylvania and New York, this decision was made by the state supreme court, not the local governments, so Dillon's Rule was not an issue. In Florida, the courts used their existing equitable and clerical powers to establish the mediation programs, without the assistance of local government. Dillon's Rule does not prevent local courts from managing their dockets in this way.

Recommendations

Below is a recap of recommendations we have made throughout this paper for local, state, and federal governments. Foremost, we advocate for the widespread implementation of foreclosure mediation programs. For maximum effectiveness and impact on communities, participation in these programs should be mandatory for both homeowners and servicers.

The programs should be implemented at the state and local level because conceptually foreclosures are property claims that are classically a matter of state law and, practically, foreclosure processes vary widely from state to state. State and local governments are best suited to tailor mandatory mediation programs to the legal and practical realities in their communities. We have collected a list of best practices for establishing and running a mandatory mediation program in the appendix on page 40 and encourage state and local governments to use them.

To leverage these best practices, we recommend that the Department of Housing and Urban Development create a nationwide working group for government officials establishing and administering mandatory mediation programs. The working group would allow participants to share experiences on an ongoing basis and allow programs to learn from each other's mistakes. This way, programs will avoid repeating mistakes and learn strategies for improving their programs more quickly than they could alone.

A nationwide working group also would help raise awareness of these programs, drawing more government and community support and federal, state, and local levels. The working group may include other stakeholders, including industry and community groups, but HUD should balance this against the need to keep the size of the group small enough to allow productive discussions.

Beyond bringing stakeholders to the table, the federal government also has an active role to play in enabling and promoting mandatory mediation programs. Congress should fund state and local mandatory mediation programs just as it provided neighborhood stabilization funds to alleviate the housing crisis.

While Congress works to provide funding, the Department of Housing and Urban Development should issue interim guidance that explicitly permits Community Development Block Grants to be used to fund mandatory mediation programs.

Mandatory mediation serves one of the main purposes of the CDBG program to help alleviate economic distress in areas with a declining tax base caused by falling housing prices. Nothing in the grants' regulations prohibit mediation and, indeed, mediation occurs in concert with housing counseling and loan subsidies that are explicitly enumerated as proper recipients in the CDBG regulations.

Further, the federal government should institute mandatory mediation for loans over which it exerts direct control—primarily federally insured home mortgages. This would be an extension of HUD's existing requirement that all servicers of Federal Housing Administration loans engage in loss-mitigation efforts prior to foreclosure. The efficient outcomes would benefit taxpayers and minimize losses to the already-stressed FHA insurance fund.

By extension, the Federal Housing Finance Administration, as the conservator of government-controlled mortgage securitizers Fannie Mae and Freddie Mac, should require all servicers acting on behalf of those entities to participate in mediation prior to foreclosure. To avoid multiple mediations in a single case, federal regulations should permit servicers of FHA, Fannie Mae, or Freddie Mac loans to fulfill the mediation requirement by participating in a qualifying state or local foreclosure mediation program. A "qualifying" program would be defined by HUD and should adhere to, among other things, the best practices we enumerate in the appendix.

As a final step the federal government should require all servicers participating in HAMP to engage in mandatory mediation prior to foreclosure in cases where a modification is not possible under program rules. Mandatory mediation ensures that the servicer and homeowner have at least one opportunity to negotiate directly—in person or over the phone. This acts as a sort of appeal process where the HAMP modification application is denied and permits the parties to consider information not captured on the HAMP forms that may lead to an economically superior outcome short of foreclosure.

This requirement is not far from the Department of Treasury's current effort to add guidelines for short sales and deeds in lieu of foreclosure where modification is not possible. Short sale and deeds in lieu require the parties to negotiate directly (in person or by phone); if the parties are already negotiating, they should consider all possible workout options with the assistance of housing counselors and a mediator.

Conclusion

Foreclosure mediation is already working to help homeowners, servicers, and communities in a half dozen jurisdictions around the country. Some of those have already determined that their programs should be mandatory for all parties to achieve the best results. Using that knowledge, along with the best practices we present in the appendix that follows, all states (those already pursuing mediation as a solution as well as those waiting in the wings) can establish and run effective mandatory mediation programs to keep more homeowners in their homes, speed up the foreclosure process for those who cannot, provide maximum value to mortgage noteholders, and reduce the costs to courts and other public resources.

Requiring mediation prior to foreclosure for federally insured mortgages is a good way to reduce the costs of foreclosure to the FHA by creating the opportunity for minimizing foreclosure-related insurance losses. Of course, this is not enough. As programs continue and more come online, there will be an increasing need for coordination to permit program administrators and local government officials to learn from one another and achieve the optimal program for their demographic.

Even absent congressional action to fund these programs, HUD should create a national working group for these stakeholders to monitor programs' effectiveness, help new jurisdictions bring programs online, and identify and disseminate best practices.

Appendix: Best practices

The ultimate goal of a mandatory mediation program is to present homeowners and servicers with an opportunity to come together and resolve those cases which do not require formal foreclosure proceedings in a manner that offers both an economic benefit to the noteholders and a sustainable housing solution for borrowers. To achieve that goal, successful programs should cast a wide net for servicer and homeowner participation and provide the necessary infrastructure to get the program started and maintain it over time.

The benchmark for success should not simply be one foreclosure avoided, but the creation of greater long-term value to the investor and a stable housing situation for the homeowner, be it through a sustainable loan modification that keeps the owner in the home or a "graceful exit" that allows her time to transition to safe, decent rental housing. In speaking with participants and reviewing state and federal program materials we have determined the following best practices for establishing and running a mandatory mediation program.

Best practices for running a program

Maximize eligibility, maximize participation

Mediation programs should both make mediation available to a wide pool of participants and require them all to participate. To date, every foreclosure mediation program has made mediation mandatory for the servicer. Bringing the often hard-to-reach servicer to the table is the whole point.

But mediation should also be mandatory for homeowners. The value of foreclosure mediation extends well beyond the parties, benefiting the court and the taxpayer. Foreclosure mediation lowers the cost to the court and by extension the state as more settlements result in lighter dockets.

Second, mediation conserves judicial resources by minimizing the time the court spends determining whether a case qualifies for mediation. Offsetting that savings is the fact that foreclosure mediation programs entail costs of their own, yet many of those costs can be kept low by leveraging the court's existing resources. It is mediation's impact on the court and the taxpayer—as much or perhaps more than the impact on servicers and homeowners—that has pushed states and local governments to implement these programs.

Given the importance of foreclosure mediation to the community at large, the choice to mediate should not be left to each homeowner. It should be mandatory for them just as for servicers.

Mandatory mediation is best initiated by the court scheduling a mediation session automatically as part of the initial foreclosure filing and notice sent to the homeowner. Some jurisdictions wait until a homeowner responds to the service of process before scheduling a mediation session in order to focus judicial resources on those parties most likely to appear. We discourage this practice because we believe that mediation should be provided to the maximum number of litigants. Courts can achieve similar efficiencies by scheduling a mediation session for every homeowner, but permitting the servicer to continue to file for summary judgment if the homeowner fails to appear.

This has been the realization in Connecticut, where the legislature is working to move from the existing program where homeowners opt in to one where mediation is scheduled automatically, as in Philadelphia. Under Connecticut's opt-in model, the data indicates that as many as two-thirds of qualified borrowers do not seek mediation. Philadelphia, where mediation is automatically scheduled for both parties when the complaint is filed, reports a mirror-image result—over two-thirds of homeowners do participate.[117]

Both programs report that approximately 72 percent of homeowners who participate in mediation reach a resolution, either receiving a modification or arranging for a "graceful exit" through a deed in lieu or similar resolution. While the data is far from perfect given the small sample size and lack of normalization, Connecticut believes that if it could increase participation it would see its success scale accordingly.

Increasing participation starts with setting the appropriate eligibility requirements. The best eligibility requirements are those broad enough to encompass the vast majority of individual homeowners and clear enough that litigants themselves can determine if they are eligible. Certain Florida courts have relied on that state's constitution for their eligibility requirement. Those programs apply to "homesteads," which the Florida constitution defines as real estate that is the permanent residence of the owner or her dependant.[118] Others, such as New Jersey and Philadelphia, have a version of the following requirements for eligibility similar to those under HAMP:

- The property is owner occupied.
- It is one- to four-unit residential property.
- It is the borrower's primary residence.
- And the borrower is not in bankruptcy or the proceedings have been stayed.[119]

By setting a simple standard and setting the bar low for entry, the litigants, rather than the court, can determine whether the borrower meets the participation criteria.

Eligibility requirements require a balance. The bar should not be set so low as to be nonexistent. The Ohio Supreme Court's model for foreclosure mediation provides no eligibility criteria,[120] leaving it to the mediator to determine eligibility on a case-by-case basis and report findings to the court. The court then has discretion to require mediation. The court's increased participation saps judicial resources and runs counter to the program's goal of reducing the strain on courts.

By the same token, the bar for entry should not be set too high. For example, access to the program should not be limited to homeowners with a certain type of loan, as New York has done,[121] providing mandatory settlement conferences only for "high-cost," "subprime," and "nontraditional" home loans.[122]

The attempt to single out subprime mortgages for mediation has limited the usefulness of the program. The type of loan going into foreclosure is irrelevant from the perspective of both the court and public policy. Delinquencies among prime loans are also significantly rising, and the impact on communities of a vacant, foreclosed home is the same regardless of the form of the underlying financing.

Further, it has placed a serious and unnecessary burden on servicers. In New York, the notice requirements differ between loans that are eligible for the program and those that are not, and servicers must make this determination. Loans don't come with a "subprime" stamp. Servicers have to review both the terms (adjustable, interest only) and the interest rate for each loan and then compare the interest rate to the rate of treasuries at the time that particular loan was given.

On the back end, this requirement can lead to litigation if a servicer fails to provide adequate notice to a homeowner because a calculation error leads to the conclusion that a loan is subprime when it is not, and vice versa. It is far simpler to include all loans, regardless of terms, in the mediation program.

Foreclosure mediation programs should similarly avoid placing burdens on homeowners. New Jersey will only permit a borrower to participate in mediation after the homeowner has returned to the court a financial worksheet detailing his or her assets, income, and monthly expenses, along with taxes returns, pay stubs, and bank statements attached.[123] This requirement is likely the product of concerns that mediations would be lengthy and burdensome to servicers and the court, due in part to the fact that early sessions would be dedicated to having homeowners gather the required information.

That concern turns out to have been well founded, but the answer is not to withhold mediation until homeowners have assembled copious documentation, some of which an individual servicer may not even require. Rather, the first mediation session, which can be held informally on the assigned date, should be used for both sides to share (or verify) information necessary for modifying the mortgage.

Knowing this, courts can set their schedules more efficiently. Armed with the knowledge that most first mediation sessions end quickly after the homeowner receives her marching orders and a continuance, Connecticut's case flow coordinators schedule initial mediation sessions for shorter time slots, improving efficiency. Courts and legislators should also consider instituting an information session for homeowners in lieu of, or in connection with, their first mediation session.

Involve housing counselors wherever possible

We recommend that all programs provide homeowners the name and contact information of a HUD-approved housing counseling agency and strongly encourage (but not require) them to make contact prior to mediation. There is general consensus that early intervention produces better results.[124] Housing counselors intervene early, help provide outreach (as described in the next section), and act as "triage" for the mediation program by:

- **Educating the homeowner.** Housing counselors can educate homeowners about not only the mediation and foreclosure processes, but also about other resources available to help save their home. Today, these include MHP loan modifications and refinancing, as well as Hope for Homeowners, at the federal level, similar financing programs at the state level,[125] and other social services that may assist the homeowner and improve her financial condition, such as social security, unemployment, and food stamps. In addition, housing counselors will often develop a budget with homeowners, creating a comprehensive financial structure that is sustainable whether or not it is possible for the homeowner to save her home.

- **Gathering documents for mediation.** The most common complaint is that homeowners appear at the first mediation session without sufficient documentation to permit a productive negotiation. Housing counselors can identify these documents with homeowners before mediation begins, serve as a repository for these documents, and find replacement documents as needed. More importantly, housing counselors can build a robust financial profile of the homeowner, including nontraditional sources of income or other financial support such as extended family that can assist in negotiations.

- **Triage.** Housing counselors can reduce the court's workload by identifying cases in which the homeowner will not be able to stay in the home under any scenario. This foregoes modification proposals and focuses instead on negotiating a graceful exit of hastening foreclosure and the homeowner's transition to a more stable living situation.

- **Preparing loan modification proposals.** Housing counselors also work with homeowners outside the formal setting and time constraints of mediation to talk through multiple scenarios and determine which are most appropriate. Housing counselors, like those in Philadelphia, can transmit these offers to servicer's counsel before the first mediation session, likely reducing the number of required sessions. Housing counselors should be (and most are) trained to utilize scenario tools like the FDIC's "Mod in a Box" to assess loan modification options.[126] Given the servicing industry's shift to adopting HAMP as the *de facto* modification standard, access for counselors to the base NPV (net present value) model developed by Treasury and others for use by servicers, is increasingly important.

Housing counselors do have shortcomings. Foremost, they are human, so their quality of service varies. At the very worst, they can mislead a homeowner to believe that mediation is a scheme to have servicers foreclose more quickly—a sentiment we have encountered several times. The only solution to this is quality training.

Second, housing counselors lack the resources to assist every homeowner. Many counselors are based in dense urban areas and cannot meet with geographically dispersed homeowners. Further, due to the protracted housing crisis, most are operating at or above capacity. Still, even in these circumstances, housing counselors add value.

Connecticut does not require parties to contact housing counselors but refers over 90 percent of homeowners to them to get help assembling documents, assess options, and produce settlement/modification proposals. Connecticut's housing counselors are strapped for resources, so they rarely appear at mediations. Instead, they contact mediators between conferences for help in transmitting modification proposals to servicers who, in turn, are more likely to make time for a request from a mediator than a counselor.

Involving mediators in this capacity is not ideal as it can give the appearance that the mediator is advocating for the homeowner. Nonetheless, it is an effective adaptation by participants to the reality in that state.

In addition to local counseling agencies, another option for addressing the volume of foreclosures in places with scant capacity is the use of telephone-based, HUD-approved housing counseling agencies. Their staff is as well trained as local counselors and often has the ability to quickly share borrower information with a servicer, streamlining the entire process. Thus, where housing counselors are locally unavailable for reasons of geography or lack of resources, we highly recommend providing homeowners with information on reaching out to telephone-based counselors.

Implement outreach programs

While mediation programs that are mandatory for both parties capture more participants, it is not clear why homeowners do not participate *voluntarily* in greater numbers. Anecdotal evidence suggests that some do not understand the mediation process, while others are overwhelmed by the prospect of losing their home and attempt to forestall foreclosure by ignoring it. Still others do manage to contact their servicers and believe that workout will be achieved, making mediation unnecessary, only to have their plans fall through at the last moment after the opportunity for mediation has passed.

With this in mind, achieving significant participation rates requires outreach. Outreach can take many forms, and given the scope of the current crisis, governments and courts should use every outreach resource at their disposal.

In Philadelphia, outreach started with the court, which required that service of process to the homeowner include a separate sheet clearly explaining the mediation program.[127] The executive branch has also done its part: Mayor Michael Nutter has released several public statements and made several speeches promoting the Save Your Home Philly Hotline. After each mention, the hotline reported a jump in calls.

Taking it one step further was ACORN, which obtained lists of homeowners eligible or scheduled for mediation who had not responded to the court's notice.[128] ACORN volunteers went to each person's house with their cell phones, knocked on the door, and encouraged the homeowner to call a housing counselor on the spot.[129] In the first month of the project, ACORN got over 60 percent of these previously unresponsive homeowners to participate.[130] While we are not aware of any data that measures the effectiveness of that outreach against a control, those involved in the Philadelphia program credit it with much of their success.

Connecticut is too large a geographic area to permit door-to-door outreach, so it provides effective outreach through its full-time mediation program staff. The program administrator, the mediators, and other staff have attended an average of one event per week to talk up the program and encourage participation. Events include foreclosure fairs held by Connecticut legal services, meetings of pro bono legal services organizations, banking and mortgage lending industry associations, and more. Program staff members receive comp time for their outreach efforts.

The role of clergy should also not be overlooked. Many people turn to clergy in times of stress and share with them personal troubles they do not feel comfortable sharing with even close friends.[131] Working with clergy to inform them of the mediation program and counseling options can leverage local faith communities to help improve participation.

Outreach is critical to increasing participation. Any outreach should be seen as valuable, including phone campaigns, mailers, or advertisements on outdoor media, television, and radio.

Servicer or its counsel must have the authority to make a deal

Another prevalent aspect of existing mandatory mediation programs is the requirement that the servicer make someone available with authority to finalize a settlement. Foreclosure mediation is a waste of everyone's time if the servicer cannot agree to a deal. The raison d'etre of the program is to enable homeowners to have meaningful contact with the servicer. If a servicer's attorney must endure the same lengthy wait times and lack of substantive responses that borrowers have endured, there is little benefit to the program.

Courts currently permit servicers' representatives with authority to finalize a settlement to be available by phone or email rather than present in the courtroom. The system is not ideal, as administrators report that servicers' counsel will occasionally get a simple "no," sometimes on a group of loans, without a reason. The indirect, impersonal nature of telephone and email makes such opacity possible. On the other hand, permitting servicers to participate remotely allows them to leverage a smaller number of centralized decision makers that rely on local counsel to do the lion's share of the work. This may be necessary given servicers' staffing difficulties and the impracticality of having an employee located in every jurisdiction.

In judicial foreclosure states, courts administering these statutes or rules have the power, either explicit or in equity, to impose sanctions on any party committing a violation. Failure by the servicer to make a decision maker available has usually resulted in a continuation of proceedings. Until now, this has been an adequate response, as servicers sought to complete foreclosures with as little time and money as possible. Continuances may lose their sting as servicer inventories grow and they become willing to wait rather than take on additional properties. At that point, courts may—and should—resort to other sanctions, including fines or dismissal if necessary, to guarantee compliance.

In nonjudicial foreclosure states, legislatures should permit homeowners or mediators to file papers with the court stating that the servicer has acted in bad faith if, for example, it fails to make an authorized representative available. Such is the case in Nevada's program, set to debut in July 2009.[132] In Nevada, the filing permits the court to issue sanctions, up to and including loan modification, at its discretion. We believe such a filing should carry more weight, either automatically extending a statutory stay of proceedings or establishing grounds for a homeowner's action to enjoin foreclosure.

Require the parties to meet in person where possible

Program administrators report that conducting the mediation in person at a neutral location—often the courthouse—under the auspices of the court puts the parties in a mindset to seriously discuss settlement. Being there lets both sides know that foreclosure, with its costs and schedule, is imminent. Holding the conciliation conference by telephone as done in Florida's 12th judicial district and California is not recommended.[133]

In-person meetings permit additional players, such as pro bono counsel or housing counselors, to participate more effectively. These additional players have limited time. Pro bono counsel or a housing counselor can handle multiple cases in the same room or building at the same time, checking in on each as needed. Attempting the mediation process by phone would require a counselor or attorney to dedicate as much as a whole morning to just one borrower. In addition, sharing documents and other pertinent information in such remote proceedings is more difficult.

The experience in Philadelphia shows that being in the courthouse also provides access to judges and mediators who can immediately resolve issues that crop up in the course of negotiation. An impasse in a conciliation conference can lead to mediation the very same day, conserving judicial resources and saving the parties time and expense.[134]

Best practices for establishing a mandatory mediation program

Find a champion within the system

Every successful mandatory mediation program to date has a point -person who is the operational and—just as often—emotional center of the program. In Philadelphia, every single person with whom we spoke credited the program's success and continued existence to Judge Annette Rizzo's enthusiasm and hard work. She reached out to stakeholders, she lobbied city government for funding, she recruited senior attorneys to volunteer as mediators, and she continues to be the public face of the program, doing outreach, raising awareness, and assisting other jurisdictions. In Connecticut, that person is Roberta Palmer, the court administrator. While she did not establish the program, she is just as committed as Judge Rizzo to its success.

Having a champion is a best practice for the same reason that homeownership is not merely houseownership—there is an emotional aspect which requires an emotional response during a crisis. A champion combines the emotional desire to resolve the crisis and keep people in their homes with the logistical acumen to make it happen. The result is a magnetism that draws people in to assist.

Legislators, executives, and judges see the political benefit of helping such a champion. Attorneys, having a standing tradition of public service, contribute their time. Administrative staffs work hard to arrange workloads to accommodate the program. And, finally, participants see the seriousness of the endeavor and bring that seriousness in turn to their own negotiations.

Get buy-in from stakeholders

Foreclosures extend well beyond servicers and homeowners to the greater community, particularly during an economic downturn. A successful program must engage these stakeholders early and continue to do so consistently. The Supreme Court of Ohio recommends:

> *Schedule a meeting with stakeholders such as: judges; magistrates; lenders; attorneys for borrowers and lenders; community organizations; mediators; legal aid organization; clerk of court; county auditor, treasurer, and/or commissioners; local social service agencies; community organizations such as churches, homeowner's and bank associations, etc.*[135]

To establish and operate a program, perform outreach, educate homeowners, process loan modifications or agreements for graceful exit, and to actually execute those agreements, requires these stakeholders to cooperate and to commit resources. Any one of the stakeholders, if unhappy, can stymie the process to the point of breaking the whole system.

On the political front, regardless of which branch of state government establishes the program, it will require the assistance of the other two to make it a success. The executive branch can raise awareness and marshal state housing and finance agencies to provide counseling and, to the extent available, streamline mortgage relief efforts for homeowners in mediation. The judiciary, in states that use judicial foreclosures, must administer the program and cannot do so quickly and efficiently if it does so reluctantly. The legislature holds the purse strings and so it must be invested in the success of the program to continue funding. In nonjudicial foreclosure states, the legislature is also central to passing necessary laws establishing the program. Any branch considering the program should involve the other two so that at the outset it is seen as a joint effort and a political boon for all.

In the private sector, servicers, their industry associations, and their counsel are perhaps the most important stakeholders. Servicers are predisposed to dislike modifications because they represent additional time and costs in foreclosure. Connecticut and Philadelphia engaged these stakeholders early, listened to their concerns, and tailored the programs to address some of those concerns. Having been heard, these groups took ownership of the program and became advocates for it.

Particularly important are servicers' counsel, which serve as a bridge to the servicers. Real estate is a highly localized practice, and servicers' counsel is usually a small group of local attorneys and firms hired by regional or national servicers to handle foreclosures. Unlike servicers, these attorneys have a personal stake in their local community and the local court. They want to make sure the court in which they regularly appear stays happy. In addition, as counsel, they have both access and clout with their servicer clients often necessary to reach someone with sufficient authority to approve a modification.

The remaining interest groups, homeowners, counsel, housing counselors, and other community groups need little encouragement to participate in such meetings. They are necessary to balance the viewpoints represented in meetings, contributing both the layman's perspective as well as their knowledge of community needs that extend beyond the courtroom.

Obtain funding, but do not wait for it

A successful foreclosure mediation program requires resources, but the Philadelphia Pilot Program demonstrates that it is unnecessary to wait for funding. That program has operated for a year with no additional funding. Every Thursday the court borrows administrative personnel from the prothonotary (the clerk) and the office of complex litigation to run the mediation session and process orders. Managers in those offices are committed to the success of the program and have arranged schedules and workloads to permit their personnel to participate.

Both judges pro tem (mediators) and homeowners' counsel provide their services pro bono. The president judge of the Court of Common Pleas provides the use of his large courtroom. And the housing counselors are independently funded. All of this permits the program to hear 200 cases every week without additional cost to the court. It serves as proof that any committed organization can field a foreclosure mediation program.

Funding, of course, is not a bad thing. Philadelphia is only a pilot program in one city. With funding, Connecticut was able to launch a full-fledged successful state-wide program in the same time period, relying on paid staff around the state to administer it.

To the extent possible we recommend against shifting the cost of foreclosure mediation to the litigants. This practice is in place in Florida, New Jersey, and New York, among others.

Foremost, imposing the costs on the homeowner is unfair. The court is requiring the homeowner to shoulder the cost of someone else's lawsuit against her. This runs contrary to standard civil practice, where for reasons of fairness the plaintiff pays the court fees because it initiated the claim, even though the parties bear the cost of their own legal representation.

Further, splitting the charges is untenable. A homeowner is in foreclosure and likely to appear pro se because she can't afford to pay. Imposing additional costs on a person in such circumstances is inappropriate.

Requiring the servicer to bear the cost of mediation is also problematic because it creates a disincentive for servicers to see mediation through to resolution. Few mediations conclude within the roughly two-hour window contemplated by most existing fee structures. For example, Orange County, Florida charges servicers $275 for the first two hours and $100 for each additional hour. If mediation has to be continued, eventually, the servicer will balk not just at the delay, but also at the additional cost of pursuing mediation.[136] Consequences could include abandoned mediations, lower settlement offers, or more contentious or unresponsive servicers.

Put in place a case management system

Foreclosure mediation is unlike other court processes. It is a rapid, high-volume, alternative dispute resolution-based program where housing counselors are often more important than a homeowner's pro bono counsel, or even the homeowner herself. Just like other highly specialized areas of law—such as family and landlord-tenant disputes—it requires a separate case management system.

These programs are too large and move too fast to be managed along with all the other cases through the clerk's office. Connecticut, Philadelphia, and several counties in Florida have realized this and arranged for dedicated staff to schedule mediations and manage case files. The staff is trained on the filing, case management, and scheduling requirements of the program, permitting them to perform their duties quickly and efficiently.

Require ongoing training for participating professionals

Training is the one area that most existing programs have properly addressed. A proper training program should require mediators, housing counselors, and pro bono counsel to receive training prior to taking their first foreclosure mediation case. For many this will be the first time they have dealt with residential foreclosures. Case in point: Philadelphia's mediators are often senior attorneys with significant negotiating experience, some even in the commercial real estate area, but the economics and legalities of residential property are sufficiently different that they require training.

The same goes for housing counselors. Counselors often specialize in different phases of the ownership cycle, including pre-purchase, purchase, and ownership. Given how critical they are to the program, all housing counselors must receive training on residential foreclosures, the resolution options, and the mechanics of the mediation program. Pro bono counsel require even more training as most practice in subject areas completely unrelated to real estate, let alone residential real estate.

In particular, housing counselors and pro bono counsel (as well as mediators) should be trained on the importance of achieving a sustainable debt-to-income ratio on a modified loan. The target modification under HAMP achieves a 31-percent debt-to-income ratio, so they should be prepared to perform additional due diligence about a homeowner's payment history and financial situation when accepting an offer that deviates from this guideline.[137]

Housing counselors, pro bono counselors, and (barring these) mediators should explain the debt-to-income guideline and its import to the homeowner, often the least sophisticated party in the negotiation. Homeowners should understand that higher ratios can lead to re-default, at which point they will lose their homes anyway after having made several months of additional payments at what was clearly an unsustainable rate.

The Office of Thrift Supervision and the Office of the Comptroller of the Currency report that more than half of the loans modified in the first three quarters of 2008 were delinquent by at least 30 days within just three months.[138] This is not surprising given that over half of loan modifications implemented prior to HAMP did not reduce payments for homeowners clearly unable to afford the payments at that level.[139] It is expected that adherence to HAMP guidelines will eliminate this problem by standardizing modifications, but counselors should be wary in the event that a servicer reports that a borrower is ineligible for HAMP but that an alternative modification is being offered.

This training can have a spill-over effect in another scenario: direct negotiations between the servicer and homeowner. Participants have told us that servicers many times begin parallel negotiations directly with homeowners once mediation has been scheduled. While mediators, housing counselors, and pro bono counsel are not involved in these informal settlements, homeowners often keep them informed and consult them. A well-trained counselor, pro bono counsel, or mediator can help highlight red flags for homeowners in these situations and help them avoid entering an unsustainable deal.

Continually evaluate your program

Tracking data permits review and process improvement and should be done at both the local and national levels. Most state programs, as well as all federal programs, require it.[140]

Locally, existing programs have already used the data to improve their own processes and pass that knowledge on to others. For instance, Connecticut noticed that most homeowners did not use their full one-hour slot for initial mediation sessions. Digging further, the program coordinators determined the reason was that homeowners often arrived without necessary documentation or knowledge of the process, received a short explanation and task list, and scheduled a follow-on conference.

Connecticut's case flow coordinators adjusted their scheduling practices, allotting just 20 to 30 minutes for initial sessions and permitting mediators to hear a greater volume of cases. Philadelphia, having made similar findings, has taken steps to permit a housing counselor who sees that his or her client does not have sufficient documentation for mediation to reschedule the first mediation session without the parties having to appear in court.

Sharing this information nationally permits jurisdictions to learn without repeating others' mistakes. Further, tracking data on participation and resolutions at a national level can help unearth trends too difficult to see in the small sample size representing a local program. Program administrators can collect data through reports from the mediators or where a mediator is not involved in a filing, setting out the status of negotiations at the end of each session.

Here's a way that quantitative data could be tracked by mediation programs:

- Number of mediation sessions held.
- Was resolution reached?
  - If resolution was not reached, did the matter continued to foreclosure or was it settled privately?
- Type of resolution:
  - Homeowner staying in the home.
    - Loan modification, specifying whether the interest rate or the principal was modified and, if so, listing the original and resulting rates.
    - Changes to the term of the loan, specifying the original and modified terms.

    - Reinstatement/repayment plan, specifying the amounts being repaid and the terms and duration of the repayment plan.
    - Forbearance, specifying the terms and the amount forborne.
- Homeowner leaving the home.
    - Deed in lieu of foreclosure.
    - Short sale.
    - Consent judgment, specifying any delays in judgment or foreclosure.
    - For any of the above, did the homeowner receive a payment ("cash for keys")?

We recommend that to the extent possible programs also track the following data:

- The type of property (single vs. multifamily).
- The original loan principal.
- The basic terms of the first mortgage (fixed, adjustable, interest -only).
    - Was the mortgage for the purpose of purchasing the home or a later equity loan or line of credit?
- Was there a second mortgage? If so, in what amount and how was it dealt with in settlement?
- Was the servicer participating in MHP? If so, was it applied in this case and what was the result?

Several states, most notably Ohio, have set out forms soliciting qualitative feedback from all participants as well as the mediator. Participants including homeowners, servicers, counsel, and third parties provide feedback about their mediators, the timeliness of the process, and whether they thought the mediations were fair.[141] Ohio provides a form for program administrators to track and quantify responses from both qualitative and quantitative questionnaires.[142]

Mediator feedback is solicited at a more general level once a quarter and focuses on the challenges mediators faced, how they addressed them, and how they plan to address them going forward. Such documents would facilitate training as well as discussions at stakeholder meetings, discussed below.

Open questions

Our best practices outlined above do not answer all the questions raised by mandatory mediation or voluntary mediation. Below are what we feel are outstanding questions.

Should programs require a pre-mediation meeting with a housing counselor?

New Jersey, Cleveland, and Philadelphia all require homeowners to meet with a housing counselor prior to the first mediation session. New Jersey, for example, has a strict requirement that a homeowner must compile all financial documents and meet with a housing counselor before mediation is scheduled. The rule is well intentioned. The purpose is to avoid expending court resources on educating homeowners and gathering documents necessary for fruitful negotiations.

In contrast, Philadelphia has not enforced a similar rule because many homeowners simply don't contact housing counselors and the court does not want to exclude them from mediation on that basis. Instead, the court assigns them a housing counselor on the day of mediation and the process begins there, often requiring a continuation. It would appear, then, that pre-mediation meetings with housing counselors should be encouraged, but not required.

Should there be a mediation time limit?

Servicers generally advocate for time limits in order to minimize the delay to the foreclosure proceedings, but time limits have proven unrealistic. As they negotiate, parties frequently consent to extensions beyond the 60-, 90-, and 120-day limits. Many times servicers themselves will request extensions to work through the volume of modification requests.

With their growing backlogs, a time limit may just burden courts with the added task of granting extensions using their equitable powers. At worst, if the court enforced a time limit, it could prevent a homeowner from receiving a modification just because time runs out—something which servicers could utilize to game the system.

That said, servicers are still requesting time limits in states working to establish foreclosure mediation programs.[143] Given the experience so far, our current recommendation is to accept the provision, but make sure that the court retains the power to extend the limits upon mutual consent or upon a finding of good cause.

Who should have the power to declare an impasse or lack of good–faith dealing?

Most existing programs permit the foreclosure to proceed if mediation reaches an impasse, which includes situations in which one party fails to appear or will not negotiate in good faith. Other than Nevada, which will grant the mediator the exclusive power to declare an impasse, existing programs do not define what constitutes an impasse or who makes the determination.

The outstanding questions include: Must both parties consent to an impasse? Should the mediator, independent of the parties, have the power to declare an impasse? In judicial foreclosure, can one party petition the court to declare an impasse? In non-judicial foreclosure, how do we expedite the servicer's return to the foreclosure in an instance of bad faith, and what power do we give homeowners if the opposite is true?

Should mediation stay foreclosure proceedings?

Currently, most programs do not stay foreclosure proceedings during the mediation, opting instead to prevent any judgment or sale until the mediation is complete. This permits mediation to take as long as necessary without delaying foreclosure. On the other hand, requiring a homeowner, likely already overwhelmed by the process and appearing pro se, to participate in parallel proceedings may be too much. Moreover, without a stay, foreclosure mediation does little to free up the court's docket, which remains clogged with active cases.

Endnotes

1 Credit Suisse, "Foreclosure Update: Over 8 Million Foreclosures Expected," (2008), available at http://www.nhc.org/Credit%20Suisse%20Update%20Dec%202008.doc; "Delinquencies and Foreclosures Continue to Climb in Latest MBA National Delinquency Survey," available at http://www.mortgagebankers.org/NewsandMedia/PressCenter/69031.html.

2 Michael Corkery, "A Florida Court's 'Rocket Docket' Blasts Through Foreclosure Cases," February 18, 2009, available at http://www.wsj.com/article/SB123491755140004565.html.

3 Some mortgage lenders service their own loans; some service others' as well. Some companies are purely servicers. To avoid confusion, we will refer to the party that has the power to declare default and foreclose on a property as the "servicer" here, because it is almost always the servicer that has this power, whether it is the lender acting for its own portfolio or a third-party servicer acting on behalf of investors in mortgage-backed securities.

4 Conference of State Banking Supervisors, State Foreclosure Prevention Working Group, "Analysis Of Subprime Mortgage Servicing Performance" (Data Report No. 3, September 2008), p. 2, available at http://www.csbs.org/Content/NavigationMenu/Home/SFPWGReport3.pdf.

5 California, Connecticut, Florida, New Jersey, New York, Ohio, and Pennsylvania have programs. Milwaukee, Wisconsin and the states of Michigan and Nevada plan to bring programs online in early July 2009.

6 Lee Howard, "Dodd calls for more effective foreclosure-prevention program," The Day, June 4, 2009, available at http://www.theday.com/re.aspx?re=b09b5a7c-045c-4e6c-be21-9be9ccee627c

7 Localities considering mandatory mediation programs include Pima City, Arizona; Delaware; Atlanta, Georgia; Chicago, Illinois; Marion City, Indiana; Louisville and Jefferson Counties, Kentucky; Prince George's County, Maryland; Portland, Maine; Minnesota; Pittsburgh and Washington Counties, Pennsylvania; and Detroit, Michigan.

8 Credit Suisse, "Foreclosure Update: Over 8 Million Foreclosures Expected."

9 For example, Connecticut has seen a 102-percent increase in foreclosures in the past four years. See Roberta Palmer, "Foreclosure Mediation Program: Presentation to the Connecticut Legislature" (2008). A more extreme example is Lee County in Florida's 20th Judicial Circuit, which had 1,900 mortgage filings two years ago compared to 24,000 today. See Corkery, "A Florida Court's 'Rocket Docket' Blasts Through Foreclosure Cases."

10 Making Home Affordable, "Obama Administration Announces New Details on Making Home Affordable Program," May 14, 2009, available at http://makinghomeaffordable.gov/pr_051409.html.

11 Conference of State Banking Supervisors, "Analysis Of Subprime Mortgage Servicing Performance," p. 6.

12 OCC and OTS Mortgage Metrics, Fourth Quarter (April 2009), pp. 20-21, available at http://www.occ.treas.gov/ftp/release/2009-37a.pdf.

13 Andrew Jakabovics, "Crisis Averted But Unresolved," Center for American Progress, September 8, 2008, available at http://www.americanprogress.org/issues/2008/09/crisis_averted.html.

14 James Lockhart, III, "Stabilizing the Mortgage Market," Speech to the Urban Land Institute, Washington, D.C., May 7, 2009; based on data provided by Freddie Mac.

15 Laura Conaway, "Hear: and Three Baby Camels," National Public Radio Planet Money Blog, May 22, 2009, available at http://www.npr.org/blogs/money/2009/05/hear_and_three_baby_camels.html.

16 At this point in time, the details of the NPV model are only available to participating servicers.

17 Making Home Affordable, "Supplemental Directive 09-01: Introduction of the Program" (2009), available at https://www.hmpadmin.com/portal/docs/sd0901.pdf.

18 Courts implementing foreclosure mediation programs cite the lack of communication prior to foreclosure as a core impetus for the programs. See Fla. 9th Cir. Judicial Cir. Ct., Administrative Order 2009-02 (February 25, 2009), p. 1 ("WHEREAS, in many cases the first opportunity for the owner-occupant to discuss potential resolution short of judicial sale is at a hearing on the lender's motion for summary judgment."); Fla. 18th Judicial Cir. Ct., Administrative Order 0909-S (January 29, 2009), p. 1 ("WHEREAS: The Judges in Seminole County Circuit Civil Division are routinely advised by owner-occupant litigants that it is difficult, if not outright impossible, to negotiate settlements due to the inability to communicate with the appropriate representatives of the lender or the lenders' attorneys after the complaint of foreclosure has been filed. In many of these cases, the first opportunity the owner/occupant litigants have to discuss the issues and attempt to resolve their difference is at a hearing on the lender's motion for summary judgment, or later that the foreclosure sale. . .").

19 See, for example, "Wells Fargo Home Modification Program," Walker Pad, available at http://walkerpad.com/index.php/archives/621.

20 Results from these programs are discussed in detail on pages 16–22.

21 15 U.S.C. § 6193a. Amended by the *Housing and Economic Recovery Act of 2008*, Public Law 289, 110th Cong., 2d sess. (2008) § 1403, 122 Stat. 2809.

22 HAMP sought to address this by paying participating servicers $1,000 per loan for each modification as well as ongoing annual payments of $1,000 for up to three years if the loan continues to perform.

23 Tennessee allows a two-year redemption period, but in practice, many mortgage documents include a waiver of this right. See Clark and Washington, P.C., "Understanding Tennessee Foreclosure Law," available at http://www.knoxvillebankruptcyattorney.com/tennessee_foreclosure_law.html.

24 At common law, a lender's request that the homeowner waive the right of redemption (known as the "equity of redemption") was considered a "clog" on that right and was not permitted for public policy reasons. The policy was based on the unequal bargaining powers of the two parties. In the years since, most states have maintained that a homeowner cannot waive the right of redemption, though the rule has eroded some. Tennessee and Alaska are the two states that have gone so far as to permit waiver by statute. See John Rao and Geoff Walsh, "Foreclosing a Dream: State Laws Deprive Homeowners of Basic Protections" (National Consumer Law Center, February 2009), p. 38-41. (Proposing that states prohibit or at least restrict deficiency judgments).

25 John Rao and Geoff Walsh, "Foreclosing a Dream" (National Consumer Law Center, February 2009), available at http://www.consumerlaw.org/issues/foreclosure/content/FORE-Report0209.pdf.

26 See Scott Griswold, "A Redeeming Interest In Religious Freedom," 13 Fordham J. Corp. & Fin. L. 419 (Oh. Ct. App. Dec. 1, 2008), available at http://www.judicialview.com/Law-Review/Finance-Banking/A-Redeeming-Interest-In-Religious-Freedom/Are-Islamic-Mortgage-Alternatives-Clogs-on-the-Equitable-Right-of-Redemption/27/4826-1. For a sample decision, see *Hendrickson v. JGR Properties, Inc.*, 2008-Ohio-6192.

27 Dan Immergluck and Geoff Smith, "The External Costs of Foreclosure: The Impact of Single-family Mortgage Foreclosures on Property Values," *Housing Policy Debate*, 17 (1) (2006).

28 Zhenguo Lin , Eric Rosenblatt, and Vincent W. Yao,. "Spillover Effects of Foreclosures on Neighborhood Property Values," *The Journal of Real Estate Finance and Economics* 38 (4) (2009): 387

29 Valli Finney, "Lee County Sets Foreclosure Record in February," *Naples Daily News,* March 3, 2008, available at http://www.naplesnews.com/news/2008/mar/03/lee-county-sets-foreclosure-record-february/.

30 See U.S. Department of Housing and Urban Development, "Neighborhood Stabilization Program Grants," available at http://www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/

31 Housing and Community Development Act of 1974, Sec. 101, 42 U.S.C. § 5301(c)(8).

32 U.S. Department of Housing and Urban Development, "Basically CDBG Course Training Manual," Chapter 4 (2009), available at http://www.nls.gov/offices/cpd/communitydevelopment/training/basicallycdbgmanual/chapter4.pdf.

33 Ibid Chapter 4.6. 24 C.F.R. § 570.207(a)(2).

34 This clarified the FHA Loss Mitigation Program requirements. See Department of Housing and Urban Development, "Mortgagee Letter 00-05, Loss Mitigation Program - Comprehensive Clarification of Policy And Notice Of Procedural Changes," January 19, 2000. (clarifying the FHA Loss Mitigation Program requirements). For additional information, see the FHA's Servicing and Loss Mitigation Frequently Asked Questions page at http://www.hud.gov/offices/hsg/sfh/nsc/faqnsctc.cfm.

35 Making Home Affordable, "Obama Administration Announces New Details on Making Home Affordable Program."

36 For more information, see the American Arbitration Association's website at http://www.adr.org/sp.asp?id=29629.

37 Homeowner's Emergency Mortgage Assistance Program, Act of 1983, 35 Pa. Stat. Ann. § 1680.401c *et seq*. For more, see, NCLC National Consumer Law Center, "Local Foreclosure Moratoriums: the Philadelphia Story," 27 (July/August 2008).

38 Pennsylvania law permits the presidents of the Courts of Common Pleas to "supervise the judicial business of the court" and "promulgate all administrative rules and procedures." See 42 Pa. Cons. Stat. Ann. § 325(e). Here, President Judge Darnell Jones implemented the program by issuing Joint General Court Regulation No. 2008-01. See Philadelphia Court of Common Pleas, "President Judge C. Darnell Jones announces adoption of Resident Mortgage Foreclosure Diversion Pilot Program," April 16, 2008. The program materials ("Pilot Program Materials"), including the order are available at http://fjd.phila.gov/pdf/forms/civil/Residential-Mortgage-Foreclosure-Diversion-Pilot-Program-Materials.pdf

39 Philadelphia Court of Common Pleas, "President Judge C. Darnell Jones announces adoption of Resident Mortgage Foreclosure Diversion Pilot Program."

40 "In Re: Joint General Court Regulation No. 2008-01" Order, Item C (April 16, 2008), available at http://fjd.phila.gov/pdf/regs/2008/2008-01-Order-Certification-Objection.pdf..

41 Ibid, Item B (amending Sec. 3(c) of the regulation).

42 Ibid, Item 6.

43 Interview with Judge Annette Rizzo and Rachel Gallegos, Philadelphia Court of Common Pleas, April. 23, 2009.

44 Outreach is discussed in greater detail in the Best Practices section below.

45 Pilot Program Materials, pp. 74-75, 78. (Orders appointing pro bono counsel and judges pro tem on June 11, 2008).

46 Conn. Public Act No. 08-176 (May 17, 2008), available at http://www.cga.ct.gov/2008/ACT/PA/2008PA-00176-R00HB-05577-PA.htm.

47 Roberta Palmer, "Foreclosure Mediation Program: Presentation to the Connecticut Legislature," December 2008.

48 Conn. Senate Bill No. 619, January Session, 2009, available at http://www.cga.ct.gov/asp/cgabillstatus/cgabillstatus.asp?selBillType=Bill&bill_num=619&which_year=2009#.

49 Ibid. Sec. 17.

50 Ibid. Sec. 2(2).

51 Conn. Senate Bill No. 619.

52 Ibid. Sec. 18.

53 Ibid. Sec. 16.

54 Connecticut Foreclosure Mediation Results for Cases Terminated Through February 28, 2009 (obtained from Connecticut).

55 RealtyTrac, "Foreclosure Activity Remains at Record Levels In April" (May 13, 2009), available at http://www.realtytrac.com//ContentManagement/PressRelease.aspx?channelid=9&ItemID=6379.

56 Unlike most states whose courts have jurisdiction over a municipality, Florida's courts are separated into judicial circuits which may cover more than one county.

57 For additional developments in Florida, see the Collins Center for Public Policy webpage on current programs at http://www.collinscenter.org/publications/publications_show.htm?doc_id=818538.

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60 See Corkery, "A Florida Court's 'Rocket Docket' Blasts Through Foreclosure Cases."

61 Finney, "Lee County Sets Foreclosure Record in February."

62 "In Re: Establishment Of 11th Circuit Homestead Access To Mediation Program ("Champ") For Case Management Of Residential Foreclosure Cases In The Eleventh Judicial Circuit Of Florida," Case No. 09-1, Administrative Order No. 09-08 (Fla. 11th Jud. Cir. Apr. 9, 2009), available at http://reports.jud11.flcourts.org/Administrative_Orders/1-09-08-Establishment%20of%20HOME%20Mediation%20Program.pdf, and "In Re: Administrative Order For Case Management of Residential Foreclosure Cases and Mandatory Referral of Mortgage Foreclosure Cases Involving Owner-Occupied Residences to Mediation," Administrative Order No. 2009-01 (Fla. 19th Jud. Cir. Feb. 20, 2009), available at http://www.circuit19.org/documents/AO/2009-01%20Foreclosure%20Mediation.pdf.

63 Mediation is being made available for cases filed before May 1, 2009, subject to the availability of mediators.

64 "In Re: Mediation - Mandatory Mediation Circuit Court Seminole County Owner-Occupied Residential Mortgage Foreclosures," Administrative Order No. 09-09-S (Fla. 18th Jud. Cir. Jan. 29, 2009).

65 Administrative Order 2009-02, "Administrative Order Governing Mandatory Circuit Court Mediation for Owner-Occupied Residential Mortgage Foreclosures," 9th Jud. Cir. (February. 25, 2009).

66 Ibid. at Item 7, p. 4.

67 Administrative Order 2008-15.1, "Administrative Order Establishing Circuit-Wide Homestead Foreclosure Conciliation Program," 11th Jud. Cir. (November 25, 2008), available at http://reports.jud11.flcourts.org/Administrative_Orders/1-09-08-Establishment%20of%20HOME%20Mediation%20Program.pdf.

68 Ibid.

69 Ibid.

70 "In Re: Homestead Foreclosure Actions By Institutional Lenders," Administrative Order No. 3.305-1/09 (Fla. 15th Jud. Cir. January 30, 2009), available at http://15thcircuit.co.palm-beach.fl.us/c/document_library/get_file?folderId=139&name=DLFE-1676.pdf.

71 Ibid.

72 A sample mediation order is available at http://15thcircuit.co.palm-beach.fl.us/c/document_library/get_file?folderId=155&name=DLFE-2045.pdf.

73 Ca. Civ. Code § 2923.5(a)(2) (West 2008), effective September 6, 2008.

74 California Foreclosure Prevention Act of 2009, CA ABX2 7 (February. 20, 2009), amending Ca. Civ. Code §§ 2923.52, et. al. and 2924. In California, a servicer files a notice of default to initiate a foreclosure, waits three months, files a notice of sales, waits another 21 days, and then sells the property. The 2008 amendment requiring the parties to negotiate inserted a 30-day waiting period at the start of the process, before filing the notice of default. The 2009 amendment inserted a 90-day waiting period near the end, between the notice of default and the notice of sale.

75 California Dept. of Corp., Financial Services Division, "California Foreclosure Prevention Act" (May 27, 2009), available at http://www.corp.ca.gov/FSD/CFP/default.asp.

76 Ibid.

77 Nev. Rev. Stat. § 107.080 *et. al.* revised by Nev. Assembly Bill No. 149, § 1 (May 22, 2009), available at http://www.leg.state.nv.us/75th2009/Reports/history.cfm?ID=313.

78 Ibid.

79 Ibid.

80 Ibid.

81 The term "modify" is used loosely here to encompass any change to the terms of the loan and includes deeds in lieu and short sales.

82 A recent study by the University of Berkley indicates that over 90 percent of PSAs permitted material modification (i.e. changes to the principal, interest, or length). The researchers reviewed terms for the 614 subprime loan securitizations from 2006. See John P. Hunt, "What Do Subprime Securitization Contracts Actually Say About Loan Modification" (Berkley:U.C. Berkley Center for Law, Business and the Economy,,March 25, 2009), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1369286. For an example of such a provision, see ACE Securities Corp. Home Equity Loan Trust, Series 2006-ASAP3, Current Report Filing (Form 8-K), at Sec. 3.06 (Filed June 16, 2006):

> "Notwithstanding the foregoing, in the event that any Mortgage Loan is in default or, in the judgment of the of the Servicer, such default is reasonably foreseeable, the Servicer, consistent with Accepted Servicing Practices may waive, modify or vary any term of such Mortgage Loan (including, but not limited to, modifications that change the Mortgage Rate, forgive the payment of principal or interest or extend the final maturity date of the such Mortgage Loan)."

83 American Securitization Forum, "Statement of Principles, Recommendations and Guidelines for the Modification of Securitized Subprime Residential Mortgage Loans" (June 2007), available at http://www.americansecuritization.com/uploadedFiles/ASF%20Subprime%20Loan%20Modification%20Principles_060107.pdf.

84 To compensate for this risk, investors in lower-rated tranches receive a higher interest rate on their investment, just like investors in "junk" bonds. Similarly, there are mortgage-backed securities that have tranches separated out by interest and principal payments. In those cases, modifications that lower the interest rate would reduce returns (relative to the original loan) for investors in the interest-only tranche while actually increasing returns for the principal-only tranche.

85 *Housing and Economic Recovery Act of 2008,* Pubic Law 289, 110th Cong., 2d sess. (2008) § 1403, 122 Stat. 2809.

86 Ibid 15 U.S.C. § 1693a.

87 Ibid. It is not clear that Congress has the ability to determine the standard for a fiduciary duty under state law or that a state court would pay heed to Congress's declaration when determining the general servicing practice standard. On the other hand, the principles in the statute mimic those being produced in the industry, such as those set by the American Securitization Forum, so it is unlikely that the language will need to be challenged directly.

88 Ibid.

89 John P. Hunt, "What Do Subprime Securitization Contracts Actually Say About Loan Modification" (U.C. Berkley Center for Law, Business, and the Economy (March. 25, 2009), p. 6, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1369286.

90 Ibid.

91 Ibid.

92 The relevant language:

> (a) The Master Servicer may agree to a modification of any Mortgage Loan … if (i) CHL [Countrywide] purchase the Loan from the Trust Fund immediately following the modification as described below and (ii) the Stated Principal Balance of just Mortgage Loan, when taken together with the aggregate of the State Principal Balances of all other Mortgage Loans in the same Loan Group that have been modified since the Closing Date at the time of those modifications, does not exceed an amount equal to 5% of the aggregate Certificate Principal Balance of the related Certificates.

CWABS, Inc., Depositor, Countrywide Home Loans, Inc., Seller, PARK MONACO INC., Seller PARK SIENNA LLC, Seller, COUNTRYWIDE HOME LOANS SERVICING LP, Master Servicer, The Bank of New York, Trustee Pooling and Servicing Agreement, Dated as of June 1, 2006, § 3.12, *which appears at* Greenwich Financial Services Distressed Mortgage Fund 3, LLC v. Countrywide Financial Corp., No. 650474/2008, Complaint Ex. 4.1 (Filed Dec. 1, 2008).

93 Ibid.

94 For an example, see, *People v. Countrywide Financial Corp., et. al.*, Case No. LC083076, Stipulated Judgment Sec. 6.3.12 (Entered October 20, 2008), available at http://ag.ca.gov/cms_attachments/press/pdfs/n1618_cw_judgment.pdf.

95 Ibid.

96 *Helping Families Save Their Homes Act of 2009,* Public Law 22, 111th Cong., 1st sess. (May 20, 2009).

97 United States Const. art. I, § 10, Cl. 1.

98 Ibid. The Contracts Clause is limited by its terms to the states and does not apply to the federal government.

99 *Home Building & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934).

100 Ibid.445.

101 Ibid.439-40.

102 Ibid.

103 Ibid. The Court clarified this standard in Energy *Reserves Group v. Kansas Power & Light* 459 U.S. 400 (1983): The state regulation must substantially impair a contractual relationship; the state "must have a significant and legitimate purpose behind the regulation, such as the remedying of a broad and general social or economic problem;" and the law must be reasonable and appropriate for its intended purpose. Ibid. 411-413.

104 300 U.S. 124 (1937). Specifically, it granted the borrower an affirmative defense to a deficiency judgment if the borrower could demonstrate that the property securing the debt had a value equal to the debt at the time of foreclosure, but nonetheless sold for substantially less at auction due to a low-ball bid.

105 Ibid. 129.

106 During the farm crisis of the 1980's, Minnesota and Iowa enacted mandatory mediation provisions. Courts in both states upheld those acts, which were temporary and applied to mortgages already in place. See *First Nat'l Bank in Lenox v. Haimke,* 407 N.W. 2d 344 (Iowa 1987), *Laue v. Production Credit Association Of Blooming Prairie*, 390 N.W. 2d 823 (Minn. App. 1986)

107 Michael S. Barr and James A. Feldman, "Issue Brief: Overcoming Legal Barriers to the Bulk Sale of At-Risk Mortgages," Center for American Progress, April 2008, available at http://www.americanprogress.org/issues/2008/04/pdf/reimc_brief.pdf.

108 Ibid. See also Christopher Mayer, Edward Morrison, and Tomasz Piskorski, "A New Proposal for Loan Modification" (2009), p. 27, available at http://www4.gsb.columbia.edu/null?&exclusive=filemgr.download&file_id=53861 (citing *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1027-1028 (1992) and *Connolly v. Pension Ben. Guar. Corp.,* 475 U.S. 211, 223-24 (1986)).

109 Ibid.

110 Ibid. (quoting *Penn Central Transportation Co. v. New York City*, 438 U.S. 104, 131 (1978): "'Taking' jurisprudence does not divide a single parcel into discrete segments and attempt to determine whether rights in a particular segment have been entirely abrogated. In deciding whether a particular governmental action has effected a taking, this Court focuses rather both on the character of the action and on the nature and extent of the interference with rights in the parcel as a whole… .")

111 Ibid., p. 26.

112 States which do not require court intervention in foreclosure include Alabama, Alaska, Arkansas, Arizona, California, the District of Columbia, Georgia, Hawaii, Idaho, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Mexico, Oklahoma, Oregon, Rhode Island, South Dakota, Tennessee, Texas, Utah, Virginia, Washington, West Virginia, and Wyoming. See Rao and Walsh, "Foreclosing a Dream."

113 Nev. Rev. Stat. § 107.080 et. al. revised by Nev. Assembly Bill No. 149 (May 22, 2009), available at http://www.leg.state.nv.us/75th2009/Reports/history.cfm?ID=313.

114 Minnesota Governor Tim Pawlenty vetoed Minn. State Legislature, H.F. No. 354, 4th Engrossment - 86th Legislative Session (2009-2010), available at https://www.revisor.leg.state.mn.us/revisor/pages/search_status/status_detail.php?b=House&f=HF0354&ssn=0&y=2009. He cited as grounds the fact that the statute granted the mediator power to decide when and whether mediation should continue. See Betsy Sundquist, "Finance and Commerce, Legislative efforts to hold back foreclosure tide died in committee, vetoed," *Finance and Commerce,* May 27, 2009, available at http://www.finance-commerce.com/article.cfm/2009/05/28/Legislative-efforts-to-hold-back-foreclosure-tide-died-in-committee-vetoed.

115 Rao and Walsh, "Foreclosing a Dream," p. 4.

116 Just as the Constitution helps define the division of authority between the federal government and the several states, Dillon's Rule and Home Rule are approaches to the division of power between the state government and that of municipalities. Dillon's Rule states favor state-level power, granting to municipalities only those powers that are (a) expressly granted, (b) fairly implied by the express powers, or (c) essential to the purposes of the local government. Home Rule states are the opposite, favoring self-governance by municipalities. Roughly 40 states follow Dillon's Rule and 10 follow Home Rule. For more detail and breakdown of states applying each rule , see Water Systems Council, Information about Dillon's Rule (January 2007), available at http://www.watersystemscouncil.org/VAiWebDocs/WSCDocs/7108424Dillon_Rule_FINAL.pdf.

117 This may also be due to the extensive outreach efforts undertaken by the government and community groups in Philadelphia, as discussed in the next section.

118 Fla. 12th Judicial Cir. Ct., Administrative Order 2008-15.1 (November. 25, 2008) (affecting Desoto, Manatee, and Sarasota Counties); Fla. 18th Judicial Cir. Ct., Administrative Order No. 09-09-S (January. 29, 2009) (affecting Seminole County and superseding Administrative Order 08-20-S). Homestead is defined at Fla. Const., Art. 7, § 6.

119 Administrative Office of the Courts, "New Jersey Foreclosure Mediation," p. 2-3 (January 2009). (New Jersey's program covers one- to -three- unit properties.) See also the Department of the Treasury's guidelines of the Home Affordability Mortgage Program (March 4, 2009), p. 2, available at http://treas.gov/press/releases/reports/modification_program_guidelines.pdf.:

- The home must be an owner occupied, single-family, one- to four-unit property (including condominium, cooperative, and manufactured home affixed to a foundation and treated as real property under state law).
- The home must be a primary residence (verified with tax return, credit report, and other documentation such as a utility bill).
- The home may not be investor owned.
- The home may not be vacant or condemned.
- Borrowers in bankruptcy are not automatically eliminated from consideration for a modification.
- Borrowers in active litigation regarding the mortgage loan can qualify for a modification without waiving their legal rights.
- First lien loans must have an unpaid principal balance (prior to capitalization of arrearages) equal to or less than: One Unit: $729,750; Two Units: $934,200; Three Units: $1,129,250; Four Units: $1,403,400.

120 Supreme Court of Ohio, "Foreclosure Mediation Program Model" (Updated April. 14, 2008), p. 17-18.

121 New York's legislature added Rule 2408 to New York's Civil Practice Rules ("CPLR") on September 1, 2008 establishing mediation for certain categories of loans.

122 "Non-traditional" loans are defined as interest-only or option payment adjustable- rate mortgages under New York's Real Property Actions and Proceedings Law ("RPAPL") § 1304 (5)(e). "Subprime" home loans are defined RPAPL § 1304 (5)(c) as those with a first mortgage with an interest rate of 3 percent or more over treasuries with a similar maturity as of the month the loan was consummated. "High-cost" loans are defined in New York's Banking Law § 6-l (1)(d) in a similar manner, but with an interest rate 8 percent higher than comparable treasuries.

123 Administrative Office of the Courts, New Jersey Foreclosure Mediation (January 2009), p. 4.

124 See Office of the Comptroller of the Currency and Office of Thrift Supervision Mortgage Metrics, Fourth Quarter (April 2009), pp. 20-21, available at http://www.occ.treas.gov/ftp/release/2009-37a.pdf; Testimony of Roberto G. Quercia before the U.S. House Subcommittee on Housing and Community Opportunity, March 19, 2009.

125 As an example, Pennsylvania offers three programs, HEMAP, described above, REAL, or Refinance to an Affordable Loan Program, and HERO, or Homeowners' Equity Recovery Opportunity Loan Program. HEMAP provides low interest state loans to help bring homeowners current; REAL permits qualifying homeowners to refinance to a low, fixed-interest, state-administered home loan; and HERO involves the state purchasing qualifying loans from existing holders and modifying the terms to make them more affordable.

126 For more see "require ongoing training for participating professionals" in the best practices section of this report.

127 In nonjudicial foreclosure states such as California and Minnesota, the legislature rather than the court has amended the notice provisions in a similar manner.

128 ACORN, "Road to Rescue: How the Philadelphia Model Can Reduce Foreclosures Across the Country" (April 28, 2009), p. 1, available at http://www.acorn.org/fileadmin/ACORN_Reports/2009/Road_to_Rescue_Report.pdf.

129 Ibid., p. 9.

130 Ibid. pp. 9, 12. ACORN determined that 117 of the 164 homes it was assigned were owner occupied. The organization communicated with someone in 94 of these homes and 73 of them participated in the conciliatory conferences.

131 One example is the HARP program in New Jersey started by the Rev. DeForest "Buster" Soaries of the First Baptist Church, which offers counseling and buys distressed homes and rents them back to homeowners as a last resort. See David Keoppel, "Personal Tales: Saved from Foreclosure," MSNMoney, April 17, 2009, available at http://articles.moneycentral.msn.com/Investing/StockInvestingTrading/personal-tales-saved-from-foreclosure.aspx.

132 Nev. Rev. Stat. § 107.80 et. al. as amended by Nev. Assembly Bill 149 (May 22, 2009), available at http://www.finance-commerce.com/article.cfm/2009/05/28/Legislative-efforts-to-hold-back-foreclosure-tide-died-in-committee-vetoed.

133 For an example, see Administrative Order 2008-15.1, "Administrative Order Establishing Circuit-Wide Homestead Foreclosure Conciliation Program," p. 2 (Fla. 12th Jud. Cir. Nov. 25, 2008), available at http://12circuit.state.fl.us/LinkClick.aspx?fileticket=yaRGUDW%2bsWg%3d&tabid=279&mid=822.

134 There is a bigger picture point to be made here as well. These parties arguably should have had the chance to speak before, whether through a lender/servicer hotline, the Hope for Homeowners hotline, the MHP programs, etc. Those communications likely happened through electronic means. Mandatory mediation is intended to be the last line of defense before foreclosure and merit the more serious tone of a face-to-face meeting after those other attempts did not succeed.

135 Supreme Court of Ohio, Foreclosure Mediation Program, February 27, 2009, available at http://supremecourtofohio.gov/foreclosure.

136 Additionally, cynics note that charging the servicer would simply result in a corresponding reduction in the offer to the homeowner. Certain counties in Florida, such as Miami-Dade, require the servicer to bear the $750 cost up front and permit the court to add the mediation fee as a cost or apply it as a set -off in the subsequent foreclosure action does not settle. If a case settles in mediation, servicers may seek to recoup these costs indirectly, by adjusting settlement amounts or refusing to provide cash for keys. At the end of the day, however, servicers get reimbursed for their costs, which would include mediation. In the case of a HAMP-compliant modification, Fannie Mae will provide the reimbursement, and if the property is taken by the servicer either via settlement or foreclosure, the servicer is entitled to recoup all foreclosure-related costs from the proceeds of the sale of the home.

137 In conversations with Philadelphia program participants, housing counselors and legal aid representatives expressed concerns that these ratios were unrealistic for those most in need of modification, the poor. Those living at 200 percent to 250 percent of the poverty line often have DTIs closer to 50 percent, but were and are able to make a mortgage payment at a reasonably fixed rate. Indeed, most only fell behind because their teaser rate, what to most middle-class Americans would resemble a higher-than-average interest rate, rose sharply as markets declined. Philadelphia participants argued that it is these homes in at-risk neighborhoods that we most need to save and that the DTI goals may disproportionately serve to remove lower-income families from their homes.

138 Office of the Comptroller of the Currency and Office of Thrift Supervision Mortgage Metrics, Fourth Quarter.

139 Ibid., p. 6.

140 Data tracking is required both of servicers participating in MHP and those engaging in "qualified loss mitigation" activities under the newly-enacted safe-harbor provisions of TILA. Pub. Law 111-022 (May 20, 2009).

141 Supreme Court of Ohio, "Foreclosure Mediation Program Model" (April 14, 2008), pp. 143-151, available at http://supremecourtofohio.gov/JCS/disputeResolution/foreclosure/foreclosureMediation.pdf.

142 Ibid., p. 151.

143 Even though servicers have found time limits to be unworkable in existing programs, they continue to push for limits in proposed programs, such as that in Minnesota. Minn. State Legislature, H.F. No. 354, 4th Engrossment - 86th Legislative Session (2009-2010), available at https://www.revisor.leg.state.mn.us/revisor/pages/search_status/status_detail.php?b=House&f=HF0354&ssn=0&y=2009.

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Acknowledgements

The authors would like to acknowledge the assistance of the following people:

David Abromowitz
Michael Ettlinger
Rachel Gallegos
Arthur Greenspan
Zachary Meisel
Roberta Palmer
Judge Annette Rizzo
Geoff Walsh
Sarah Rosen Wartell

This research was made possible in part through the generous support of Living Cities.

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