State News

With CFPB Reguluations Looming, California Looks to Jump the Gun and Implement Its Own Regulations For Working With Successors To A Deceased Borrower

By T. Robert Finlay, Esq., Wright, Finlay & Zak, LLP

Despite the Consummer Finance Protection Bureau's (CFPB) promise to issue guidelines this summer, directing loan servicers on how to work with successors to a deceased borrower, the California Legislature moves forward with its effort to duplicate and undoubtedly confuse servicer's efforts to work with these affected individuals. Last year, a similar effort to give non-borrowing successors the same rights as a borrower, failed in the face of strong opposition and obvious conflicts with federal privacy laws. This year, SB 1150 is gaining momentum having just passed the Senate. To date, the hearings have been reportedly long and contentious, with Senior Citizen groups, consummer groups and the State Attorney General sending representatives to argue in favor of the bill. Consummers also testified as to the problems they experienced with servicers purportedly not working with widows and widowers to assume and modify mortgage loans. At the same time, the California Mortgage Bankers Association, California Bankers Association, Credit Union League and others testified to the many problematic provisions and the harm the bill will cause for borrowers, lenders and the housing market. Despite the strong opposition, the bill passed the Senate and is under review by the House.

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Some of the key provisions and the corresponding potential issues are set forth below:

a. Proposed 2920.7(a) provides that the servicer cannot record a NOD until it does both of the following: (1) provides the claimant a reasonable period of time, not less than 30 days, to provide proof of the BR's death; and (2) provides the claimant with a reasonable period of time, not less than 90 days, to provide proof of that person's interest in the real property. In addition to adding at least 90 days to the pre-foreclosure process, the proposed language leaves the servicer exposed to several potential problems. For example: (i) although the legislature attempts to define "reasonable documentation", it is still left for interpretation, which welcomes litigation; or (ii) what if the loan is in probate and the reasonable documentation could take years.

b. 2920.7(b)(1) and (2) provide that, once the claimant provides the above required proof, he or she is defined as a "successor in interest" ("SIT"). The statute specifically states that there can be more than one SIT. How is a servicer supposed to handle multiply SITs – can it require all that all the SITs assume the loan? What if one SIT want to assume the loan and another does not? What if one wants a loan mod and one does not? The statute provides no guidance.

c. 2920.7(c) provides that, within 10 days of the claimant becoming a SIT, the servicer must provide the SIT with key information on the loan. The statute does not address the fact that providing some of that information would violate applicable Federal Law. In addition, 10 days is a very short period of time to provide the necessary information.

d. 2920.7(d) provides that the servicer "shall" allow a SIT to either: (1) assume the loan, unless assumption is prohibited by the terms of the loan, state or federal law; or (2) where the

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SIT of an assumable loan also wants a foreclosure prevention alternative, simultaneously apply for both. As drafted, there is no requirement that the SIT qualify to assume the loan. In addition, the statute is unclear on whether the servicer can require that the SIT assume personal responsibility for the loan and what happens if the SIT refuses or delays in signing the assumption documents. SB 1150 does not provide any guidance on how long the servicer must give the SIT to assume the loan or apply for loss mitigation.

e. 2920.7(e)(1) gives the SIT all the same rights as a borrower under HOBR. But, what happens if the servicer had already complied with the provisions of HOBR as to the borrower and then the borrower passes on the eve of recording the NOD? The statute is unclear whether the servicer must re-comply with all same provisions as to the SIT or, can it pick up mid-stream?

f. 2920.7(e)(2) thru (4) give the SIT the same private right of action afforded to BRs, including the right to an injunction (pre-sale), damages (post-recording of the TDUS) and attorneys' fees.

g. 2920.7(f)(4) defines who can be a SIT. But, those definitions include a "personal representative" under Probate Code 58 or a trustee of the deceased BR's trust. That begs the question – who is entitled to assume the loan or qualify for a loan mod – the representative, the trustee?

Opponents do not generally oppose the concept of the Bill. After all, it would be hard to oppose something labeled as the Widows and Orphans Bill. Instead, opponents object to several conflicting and troubling provisions in the Bill. For starters, the Bill requires disclosure to third parties of key loan information protected by federal privacy rights. Since federal privacy law is likely to trump state law, it puts servicers in a tough position and exposes them to unnecessary litigation. The Bill also requires that the servicer allow the deceased borrower's successor (or successors) to assume the loan WITHOUT qualifying. While the Bill's drafters tried to address this concern by adding an amendment stating that the successor(s) can assume the loan "to the extent permitted under state and federal law and the terms of the loan", it does not remedy the concern because neither state or federal law, nor the language of most deeds of trust, prohibit the assumption of the loan. In other words, assumption is likely to be mandatory regardless of the successor's ability to repay the loan. Lastly, the Bill makes a feeble attempt to address the CFPB's anticipated guidelines in the same arena. "It is the intent of the Legislature that this act work in conjunction with federal [CFPB] servicing guidelines." This language does not concretely resolve potential inconsistencies with the anticipate CFPB servicing guidelines amendments. The Bill needs to say that compliance with the CFPB guidelines, will be deemed compliance with SB 1150.

As anyone can see, the Bill has several problems. Fortunately, there is still time to address these issues. Industry lobbyists continue to work with members of the House to remedy these and other issues. But, servicers should expect some version of this Bill passing later this summer and being signed into law by September.

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