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Lending a Hand

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On July 8, 2008, the California Legislature adopted, and the governor signed Senate Bill 1137 finding that California was facing an unprecedented threat to the state economy and local economies because of skyrocketing residential property foreclosures. Between 2006 and 2007, residential real property foreclosures increased seven-fold. In 2007, more than 84,375 properties were lost to foreclosure in California and 254,824 loans went into default, the first step in the foreclosure process. Based on these statistics, the Legislature enacted a series of changes to California's foreclosure laws designed to deal with the mortgage meltdown.

Specifically, the new law requires lenders who made loans between Jan. 1, 2003, and Dec. 31, 2007, to provide loan counseling to their defaulting borrowers before commencing a nonjudicial foreclosure; requires lenders to provide notice to a non-owner occupant of real property where there is a pending foreclosure sale and then provide that party with an extended time to comply with a notice of termination of tenancy; and lenders and/or third-party purchasers at a foreclosure sale to maintain the properties and protect them from vandalism, decay and infestation.

Because the law was enacted as an urgency measure, some parts of the law became effective immediately; the remaining provisions take effect on Sept. 6, 2008. Because of the 30-plus day lead time on some of the provisions, foreclosure trustees and lenders should consider immediately changing their procedures in order to avoid any delays in foreclosures.

Pre-Foreclosure Contact

Prior to the enactment of SB 1137, lenders were not required to contact a borrower and provide the borrower with options for foreclosure avoidance. California Civil Code Section 2923.5 now requires lenders or their loan servicers to contact their borrowers or at least exercise due diligence in attempting to discuss with borrowers their financial situation and the possible alternatives to foreclosure. This requirement must be completed at least 30 days before a lender may begin a non-judicial foreclosure (record a notice of default).

Also prior to the bill's enactment, a lender was required to serve and record a Notice of Default on borrowers and junior lienholders permitting the borrower an opportunity to cure a default within three months. Thereafter, the lender was required to post and record a Notice of Sale on the borrower giving the borrower at least 20 days' notice of the sale date.

The newly enacted Civil Code provision now requires a lender, loan broker, agent or related party to contact by telephone and counsel a debtor regarding the delinquent debt and "to explore options" to avoid foreclosure as a prerequisite to being able to file and record a Notice of Default. The newly enacted statute applies to all residential real estate loans made between Jan. 1, 2003, and Dec. 31, 2007.

Alternative Counseling

A lender must now contact by telephone a borrower at least 30 days prior to the recording of a Notice of Default to discuss the borrower's alternatives. During that initial conversation, a borrower may request and a lender must arrange for a subsequent meeting that must occur within 14 days. The subsequent meeting may also be conducted by telephone.

The new statute contains no guidance as to what alternatives the lenders or its agents are required to offer, if any. Possible alternatives include, but are not limited to: loan restructuring from the existing lender (i.e., interest reduction or term extension); obtaining a new loan from the same or another lender; placing delinquent payments at the end of a note; and filing a consumer bankruptcy petition in bankruptcy court.

In addition to providing foreclosure avoidance alternatives, a lender must provide the borrower with a toll-free telephone number with which to contact Department of Housing and Urban Development-certified counseling agencies.

Due Diligence Alternative

If the lender is unable to contact the debtor, it may assert that it complied with the new Civil Code section's due diligence alternative. California Civil Code Section 2923.5 provides a four-step alternative to the counseling described above:

The lender must first attempt to contact the debtor by first-class U.S. mail requesting that the borrower contact the lender and also referring the borrowers to a certified housing counseling agency.

Assuming the debtor does not respond to the lender's correspondence, the lender must attempt to contact the borrower by telephone on at least three occasions on three different days and at different hours. The call must be made to the borrower's primary telephone number on file with the lender.

A better practice might include attempts to reach the borrower by contacting him or her at their alternative telephone number. A lender may also make the calls by auto-dialer so long as the call is referred to a live person if the borrower answers.

A lender may satisfy the telephonic communication requirement if both the primary and secondary contact numbers provided to the bank are disconnected.

If the borrower does not respond to the telephone calls and correspondence within two weeks after the telephone requirements are satisfied, a second letter must be mailed to the borrower by certified mail, return receipt requested, notifying the borrower of the attempt to reach him or her and providing information as to how he or she may contact the lender. A lender's loss mitigation personnel may participate by telephone in the conversations with the borrower.

In addition to the due diligence efforts described above, California Civil Code Section 2923.5 (g)(5) requires that a lender/agent post a prominent link on its homepage to the following information: Options available to borrowers who cannot afford their mortgage payments and who wish to avoid foreclosure and instructions to borrowers advising them on the steps; a list of financial documents borrowers should collect and be prepared to discuss; a toll-free number for the borrower to discuss the borrower's options with the lender and the toll-free number from the Department of Housing to find a certified housing counseling agency.

Although the new pre-foreclosure counseling provisions do not go into effect until Sept. 6, 2008, a lender is not precluded from conducting the counseling now so that it may send out Notices of Default on Sept. 6. Since Civil Code Section 2923.5(a)(1) will not permit a lender to record the Notice of Default until 30 days after contact is made or 30 days after satisfying all of the due diligence requirements, the new loan counseling procedures should begin immediately

to avoid any delays in September.

Notices

While it did not exist under the prior foreclosure laws, lenders must now notify the non-owner/borrower occupier of residential real property in writing by U.S. mail at the property address at the time the notice of sale is posted on the property.

The envelope should be addressed to "Resident of Property Subject to Foreclosure Sale." The notice must advise the non-owner occupier that a foreclosure sale is pending, which will affect the occupier's right to reside on the subject property. Also, that the property could be sold at a foreclosure sale within 20 days after the Notice of Sale, and if the non-owner occupier is a renter, the new property owner may enter into a new lease or give the occupant a 60-day notice to vacate the property.

The notice must be translated into Spanish, Chinese, Tagalog, Vietnamese and Korean. The translation of the notice is supposed to be provided by the State of California prior to Sept. 6. The Notice of Sale and the notice of non-owner occupier must be posted on the subject property and mailed to the resident of the property at the time of the service of the Notice of Sale. In addition to the new notice provisions, the California Legislature enacted Code of Civil Procedure Section 1161(b), which increases the amount of notice (from 30 days to 60 days) given to a non-owner occupier of foreclosed property to vacate the premises prior to the commencement of an unlawful detainer action.

The new provision clarifies that if any borrower occupies the premises at the time of the foreclosure, only a three-day notice is required. It also appears that the amount of notice required to be given to a non-owner occupier of a foreclosed mobile home has also been increased from 30 to 60 days.

The statutes governing non-owner occupied evictions also go into effect on Sept. 6.

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