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May 11, 2012

The Honorable Noreen Evans
Co-Chair, Conference Committee on Assembly Bill 278 and Senate Bill 900
State Capitol, Room 4032
Sacramento, California 95814

The Honorable Mike Eng
Co-Chair, Conference Committee on Assembly Bill 278 and Senate Bill 900
State Capitol, Room 4016
Sacramento, California 95814

The Honorable Sam Blakeslee
Member, Conference Committee on Assembly Bill 278 and Senate Bill 900
State Capitol, Room 4066
Sacramento, California 95814

The Honorable Donald P. Wagner
Member, Conference Committee on Assembly Bill 278 and Senate Bill 900
State Capitol, Room 4153
Sacramento, California 95814

The Honorable Ronald S. Calderon
Member, Conference Committee on Assembly Bill 278 and Senate Bill 900
State Capitol, Room 5066
Sacramento, California 95814

RE: Conference Committee on Financial Services Legislation

Senator Evans, Assemblyman Eng, Senator Blakeslee, Assemblyman Wagner and Senator Calderon:

On behalf of the Federal Housing Finance Agency (FHFA), I wish to provide FHFA's views regarding legislation pending before your Conference Committee. FHFA is the regulator for the Federal Home Loan Banks, including the Federal Home Loan Bank of San Francisco, Fannie Mae and Freddie Mac and all have operations in California. Fannie Mae and Freddie Mac are currently operating in conservatorships with the support of taxpayers to maintain a positive net worth. Since the legislation under consideration affects mortgage markets and, in particular, addresses the default and foreclosure processes as well as provisions relating to homeowners and tenants, I hope that FHFA's views would benefit your deliberations.

While there are several bills before you, I will address two. The absence of comments on other measures does not constitute any endorsement of the other legislation, but rather a focus on the items of greatest consequence.

Assembly Bill 2425/Senate Bill 1471

AB 2425/SB 1471 contains provisions that would require servicers to establish a single point of contact and impose significant civil penalties for "robosigned" documents. FHFA is concerned that the "robosigning" provisions of SB 1471 are disconnected from the issues first giving rise to this practice in judicial states, go well beyond anything in the National Mortgage Settlement and pose significant risks for the housing market. The "robosigning" provisions of SB 1471 are overly broad and disproportionate to the perceived problem. As reported in the press, "robosigning" resulted from the high-volume generation of affidavits by persons who lacked the requisite "personal" knowledge to sign the affidavits; this contrasts dramatically with the legislative provisions in the bill that purport to address robosigning.

While the National Mortgage Settlement refers to "robosigning" as the "repeated false attestation of information in affidavits," it nowhere contains an actual definition of "robosigning." By contrast, Section 2924.17(a) of SB 1471 would define a "robosigned" document broadly to include "any document" that contains factual assertions that are "not accurate" or are "incomplete." The proposed bill would allow the Attorney General or a district attorney to punish any entity that records or files a "robosigned" document by imposing a $10,000 "civil penalty" per such document. No exception is made under this civil penalty for any technical or minor error in a foreclosure document, even in cases where the borrower's default and the lender's right to foreclose is uncontested. The vague reference to an "incomplete" document raises serious questions about compliance with a most uncertain legal requirement. Further, this creates a standard for any erroneous component of a foreclosure process, a process that under California law may include hundreds of pages of materials, many not central to the rights of a homeowner, and ties this broad and vague language to a strict liability standard. Such a strict liability approach is punitive, will have a chilling effect on the processing of lawful foreclosures and will result in lenders and investors re-evaluating the risks attendant to market operations in the state and may lead to reduced credit availability or higher interest rates.

The private remedies section that SB 1471 separately creates for borrowers compounds the challenges for lenders. Based on no more than an averment of a borrower's "reasonable belief" that a foreclosure document has been "robosigned," Section 2924.18 makes the courts available for a borrower to seek an injunction, attorney's fees, costs and $10,000 or more in damages. While a borrower may not recover for a violation that is "technical or *de minimis* in nature," the proposed bill leaves that defense to the vagaries of litigation and to a required defense by a lender that could entail tens of thousands of dollars in litigation costs. The potential recovery for a defaulted borrower and plaintiff's counsel will merely encourage litigation as part of a strategy to forestall a lawful foreclosure or extract a settlement. In the end, California's non-judicial foreclosure process, that has served the State well and allowed a faster recovery of its housing market, will suffer.

Assembly Bill 2610/Senate Bill 1473

AB 2610/SB 1473 is intended to provide greater protections to tenants by incorporating portions of the federal "Protecting Tenants at Foreclosure Act" ("ProTAFA") into California law. FHFA is concerned that this bill could encourage fraud and abuse of the foreclosure process. Federal law contains a definition of a "bona fide" tenancy. Under ProTAFA, a lease or tenancy is "bona fide" if the tenant is not the mortgagor or the parent, spouse or child of the mortgagor; the lease or tenancy is the result of an arms-length transaction; and, the lease or tenancy requires rent that is not substantially lower than fair market rent or is reduced or subsidized due to a federal, state, or local subsidy. This lack of a "bona fide" lease requirement under AB 2610/SB 1473 fails to account for the possibility that property owners could "game the system" by leasing property at below market rates or preventing the new owner from taking possession for 90-days or the duration of the lease with the "renter." This type of event has been seen in practice under the current federal law and the availability of the "bona fide" lease requirement has helped avoid fundamentally fraudulent practices.

Foreclosure Delays

Unfortunately, as noted here, some of the proposals under consideration in the Conference Committee present unnecessary and counterproductive approaches to addressing housing market issues and the needs of homeowners and tenants. FHFA is well aware of the challenges facing states and localities from the housing crisis— homeowners losing their homes, erosion of the tax base and resulting curtailment of local services and, in many areas, blighted neighborhoods. The enactment of local laws and ordinances that result in unintended consequences and fail, in many instances, to achieve their goals does not assist homeowners, neighborhoods or the localities. State laws that stretch out the period for legitimate foreclosures— after every effort is made to avoid foreclosure and to keep homeowners in their homes— result in no added benefit for the homeowner and produce harm to the housing finance system and to neighborhoods. Simply attaching the terminology of consumer protection to legislation does not mean it will benefit a consumer and adverse consequences need to be examined. Increasing legal risks for lenders and investors— where existing remedies exist and where new language creates incentives for litigation— ultimately creates harm for all homeowners.

Adding impediments to actions undertaken after default and layering restrictions on legitimate foreclosures, thereby permitting homeowners to stay in their homes for hundreds of days while not paying their mortgages, property taxes or homeowner's association dues, costs neighborhoods, costs lenders and, ultimately, costs local taxpayers and future borrowers.

Clearly, laws governing the default and foreclosure process must be followed. Where there are violations, they should be sanctioned. However, adding new laws, procedures and requirements where sanctions have been applied and remedial steps taken, may only add to delays and produce no different outcome for homeowners who have received appropriate efforts at loan modifications or foreclosure avoidance approaches. The preferred option of servicers and lenders is to keep the homeowner in the home. In the end, there must be some likelihood that the homeowner who has defaulted can renew meeting their obligations, if necessary with a loan modification, or can avoid foreclosure through a short sale or other device; if not, then foreclosure is appropriate. Despite discussion regarding mediation, procedural law discrepancies, "robosigning" and false affidavits—

all of which merit review and possible sanction and remediation where violations have occurred—few of these matters have affected a homeowner's ultimate situation regarding ownership where they have not met their financial obligations.[1]

At the present time, with the coming together of actions by federal regulators, federal law enforcement and state attorneys general, it is unclear why legislation would be undertaken that could produce contrary results to these remedial steps. Even if gaps are believed to exist in recent actions, such gaps may be filled or may prove non-existent in the implementation of new laws, consent orders and consent agreements.

As representatives of the people of California, you are well positioned to determine the critical balance that is needed. Protecting homeowners, assisting them to stay in their homes and providing vehicles to avoid foreclosure must be balanced with permitting foreclosures, when other alternatives fail, to proceed in an orderly fashion to the benefit of other taxpaying homeowners through more stable housing prices, avoiding neighborhood deterioration and preserving the tax base. Foreclosure delays simply add to the costs for neighborhoods and communities and losses to lenders and investors. State directed delays in such circumstances harm the very groups that are intended as beneficiaries as the cost of credit will increase if creditors and investors cannot act on their collateral. Once a bona fide and robust effort is made to avoid foreclosure and keep people in their homes, then creditors must be permitted to move forward with their contractual right to foreclose as provided by law and undertaken in an expeditious manner to the benefit of other homeowners.

Laws and ordinances that add to the overhang of properties simply depress values for other homeowners and increases losses for creditors and investors. State actions that increase costs, create new liabilities for mortgagees and delay foreclosures where most borrowers are unable to cure deficiencies do not benefit the majority of homeowners. At the same time, should a borrower be treated improperly, laws in all states have always provided protection for them from fraud or deceptive practices. Adding new charges before and during foreclosures, new procedures that fuel delays and otherwise encumber foreclosures in the long run will only increase costs for everyone.

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[1] In a recent study by the National Bureau of Economic Research, authors from the Federal Reserve Bank of Atlanta, the Federal Reserve Bank of Boston and the Massachusetts Institute of Technology Department of Urban Studies reviewed various foreclosure regimes and the outcomes for homeowners. For the most part, the study found that the result of many of the laws aimed to protect borrowers from foreclosure was delay in, but not prevention of, foreclosures. The delays contribute to an overhang in the market without borrowers finding relief during these excessive delay periods. Many borrowers neither cure their deficiency nor gain relief, but simply remain in delinquency for greater lengths of time. A key finding of the study was that most parties able to cure or benefit from loss mitigation do so in the first 60 to 90 days of delinquency; this approach has been the focus of FHFA and the Enterprises. Under the FHFA's Servicing Alignment Initiative, a GSE servicer does not refer a delinquent mortgage to foreclosure until the 120th day of delinquency in order to provide borrowers up to five (5) months from the due date of their last mortgage payment to engage in fruitful loss mitigation efforts with their servicers. This represents the early intervention approach being undertaken that is most likely to help homeowners.

FHFA provides these comments in the spirit of assisting in your deliberations on very significant legislation. I would add that FHFA stands ready to work with the State on positive steps that maintain homeowner protections while not adversely affecting housing finance. If FHFA can provide any assistance, do not hesitate to contact me at 202 649 3050.

With all best wishes, I am

Sincerely,

Alfred M. Pollard
General Counsel