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Using Mediation

by Carla Dickstein, Coastal Enterprises Inc.

TO STEM FORECLOSURES IN MAINE

With foreclosure starts of about 1 percent (roughly equal to New England's average, if less than the nation's), the state of Maine passed a bill in June 2009 to help borrowers get loan modifications. The law required loan servicers to include information about a state mediation program whenever they sent borrowers complaint notices of default.¹

The Act to Preserve Home Ownership and Stabilize the Economy by Preventing Unnecessary Foreclosures enables court-supervised mediation for owner-occupied residential mortgages that meet certain requirements.² The property must be the owner's primary residence, be in Maine, and have four or fewer units. Already the program, which builds on work in Connecticut and Philadelphia, has gained recognition for its transparency and accountability.

The legislation creates the framework, with implementation left to the state's Supreme Judicial Court. While the legislation was being developed, the court set up a Foreclosure Diversion Commission to make recommendations on program design and rules. Today the program, operating statewide since May 2010, already offers useful insights.

Preventing Foreclosures

The program's underlying premise is that there will be fewer preventable foreclosures if homeowners can communicate directly with lenders who have loan-modification authority.³ Previously, housing counselors and lawyers struggled to ascertain who was in charge. Now there is a requirement that a decision maker participate in mediation in person, by phone, or by Internet. If a loan cannot be modified, the process can still result in outcomes that avoid foreclosure, such as *short sales* (the loan amount exceeds the sales price) or *deeds in lieu of foreclosure* (the property owner deeds the property to the lender and is released from all obligations under the mortgage).

When a lender delivers a notice of default, the borrower has 35 days to pay the full amount plus interest and fees. If the homeowner fails to pay or to contact the lender to work out a new plan, the lender may initiate a foreclosure lawsuit by serving a *summons and complaint* (including the form that enables the homeowner to choose mediation).⁴

Homeowners have 20 days to file a request for mediation. The form is short

and written in simple language. Court rules restrict a lender from filing a motion to proceed to foreclosure while mediation is pending. Homeowners use that time to prepare for mediation and potentially to work out a solution. They are permitted to change their minds and request a waiver of mediation, which is granted only if the court can verify that they understand the consequences. Mediation costs are covered by a fee charged to lenders who file for foreclosure actions in the state's courts.

Homeowner preparation for the mediation session is critical. When lenders first serve the summons and complaint, they must provide information not only on the homeowner's right to request mediation but also on where to get legal and counseling assistance. They also must notify the Maine Bureau of Consumer Credit Protection (BCCP), which sends homeowners similar information and provides a hotline to answer questions and to refer people for assistance. That gives homeowners an independent, trustworthy source of information beyond the lender alone.

The courts also set up informational sessions on the mediation process for

homeowners who have opted in. Each judicial region manages its process and may decide whether to require homeowners to attend sessions. Sessions also are attended by either a housing counselor or a legal aid attorney to provide information about what is expected of homeowners, the importance of completing financial forms that lenders send, and the availability of helpful resources. Typically, the mediation session is scheduled to occur six to seven weeks after the informational session. The statute provides additional funds to BCCP to cover outreach, education, and counselors, but the funding is not sufficient to ensure that all homeowners have attorneys or housing counselors present at mediation.⁵

According to court documents, the mediation session is a “flexible, informal process during which the parties agree to work together with the assistance of a neutral third party trained by the state, the mediator, to explore their interests and generate options for resolving their dispute.”⁶ The mediator facilitates communication, but the parties must voluntarily come to a resolution. The parties also must agree whether to extend the number of mediation sessions.

Lenders and homeowners do not always come to the first session with adequate financial information. Without a good-faith effort to provide information and participate in the process, homeowners may lose the option of continued mediation; lenders may lose the right to foreclose. Coastal Enterprises Inc. (CEI) has found that 30 percent to 40 percent of homeowners who attend the court’s information session request follow-up counseling services to prepare for mediation. Unfortunately, counseling resources are spread thin, and among agencies receiving new BCCP funding, some are substituting it for lost federal grants instead of adding counseling capacity.⁷ More work is needed.

According to the National Consumer Law Center, good mediation programs provide transparency, objectivity, and accountability. To achieve those standards, the Maine statute contains the following language.⁸

- To proceed to mediation, the lender must certify proof of ownership of the mortgage note.⁹
- Mediators must use the Federal Deposit Insurance Corporation’s Net Present Value Worksheet with the assumptions, calculations, and forms that the FDIC has established to review loan modification.¹⁰
- Mediation must address all issues of foreclosure, including but not limited to reinstatement of the mortgage,

modification of the loan, and restructuring of the mortgage debt.

- The parties must make a good faith effort to mediate all issues. Otherwise the court can impose appropriate sanctions.
- Mediators must complete a report for each mediation conducted, indicating that the parties completed in full the Net Present Value Worksheet, including the outcomes of such worksheet. Mediators may also notify the court if, in the mediator’s opinion, either party failed to negotiate in good faith.
- Data also must be submitted to the legislature for program evaluation. Reports include *process measures* of the number of people notified of mediation, participating in mediation, and receiving counseling, as

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well as *outcome measures* of loans restructured, number of principal write-downs, interest rate reductions, and number of homeowners who default on mortgages within a year after restructuring—to the extent the court has available information.

Results to Date

As of July 2010, mediators turned in about 300 report forms from the sessions. The reports represent more than one session per homeowner. The first program report to the legislature in February 2011 will provide data on outcomes of the mediation sessions.

Anecdotal reports from a CEI housing counselor, attorneys at Pine Tree Legal Assistance, and volunteers participating in an initiative called Maine Attorneys Saving Homes (MASH) indicate that the process of bringing the parties together has achieved modifications that lower payments by using reduced interest rates and establishing an extended amortization period. Homeowners who are unemployed have also been able to get modifications, sometimes for a trial period. Others have taken advantage of a short

sale or deed in lieu to avoid foreclosure. In time, empirical data will help us ascertain the number and quality of modifications, but so far anecdotal evidence seems promising.

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Endnotes

¹ The program applies to mortgages filed after December 31, 2009, but could include mortgages filed on or before then if a court so orders.

² Public Law, Chapter 402, An Act to Preserve Home Ownership and Stabilize the Economy by Preventing Unnecessary Foreclosures, <http://www.mainelegislature.org/ros/LOM/LOM124th/124R1/PUBLIC402.asp>.

³ In Paul Willen, “Why Few Lenders Are Modifying Loans,” *Communities & Banking* 21, no. 2 (spring 2010), the author challenges that premise, providing empirical data showing that lenders rarely modify loans. According to Willen, securitization is not the root problem since lenders holding loans in portfolio also have difficulty modifying loans. He believes that lenders calculate how many loans would likely be cured and how many would redefault and conclude that modifications are more costly than foreclosures. Empirical data are not yet available on Maine’s program.

⁴ See http://www.maine.gov/pfr/consumercredit/foreclosure_resources/whatisforeclosure.html.

⁵ Funding came from removing the exemption under the real estate transfer tax for foreclosure sales and deeds in lieu of foreclosure.

⁶ See http://www.courts.state.me.us/court_info/fdp/home_fa.html.

⁷ BCCP’s budget comes from 90 percent of the tax imposed on the transfer of real property through a deed conveyed back to a lender on mortgages that are in default and sold at public auction or that the bank takes back in lieu of foreclosure. In FY 2010, the state transferred \$1.6 million to BCCP because of skyrocketing foreclosures.

⁸ See *State and Local Foreclosure Mediation Programs: Can They Save Homes?* (Washington, DC: National Consumer Law Center, September 2009).

⁹ They must produce evidence of the mortgage note, mortgage, and all assignments and endorsements of the same.

¹⁰ See <http://www.fdic.gov/consumers/loans/loanmod/loanmodguide.html>. The redefault rate is one variable included in the worksheet.

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