Invested in America

July 7, 2013

Mr. William R. Breetz, Jr., Chairman
Uniform Law Commission Drafting Committee
Residential Real Estate Mortgage Foreclosure Process and Protections
University of Connecticut School of Law
Knight Hall Room 202
35 Elizabeth Street
Hartford, CT 06105

Re: Residential Real Estate Mortgage Foreclosure Process and Protections

Ladies and Gentlemen:

The Securities Industry & Financial Market Association ("SIFMA")[1] submits this letter to the Uniform Law Commission (the "Commission") pertaining to the Commission's discussion draft on the "Residential Real Estate Mortgage Foreclosure Process and Protections" (the "Draft"). We appreciate the opportunity that you previously provided to SIFMA and its counsel to discuss certain of our preliminary concerns about the Draft, particularly Section 607 of the draft law, Abrogation of the Holder in Due Course Rule in Foreclosures. SIFMA and its members have not yet taken a formal position on the Draft, but we would like to reiterate three particular concerns for the Commission's consideration.

As a preliminary matter, SIFMA, of course, is mindful of the continuing controversies and related public policy debates concerning home loan foreclosures. It is no small task to balance the legitimate interests of both defaulting borrowers to try to retain ownership of their homes and loan holders along with their contract servicers to try to enforce mortgage loan documents substantially in accordance with their terms. We applaud the efforts of the Commission to try to address this important public policy issues from all perspectives, and the concept of a uniform state law on foreclosure certainly appeals to SIFMA in theory.

Our **first** concern centers on the parallel but not necessarily consistent efforts of state and federal governments to limit the contractual rights of loan holders to foreclose on defaulting borrowers in accordance with the terms of the mortgage loan documents. The second is the ambiguity of the Draft concerning the repeal of other state laws that limit foreclosure. Our third concern pertains to provisions in the Draft that would eliminate or repeal the Holder in Due Course Rule in the case of home loan foreclosures. We address these concerns in more detail below.

The Draft Can Not Be Evaluated in a Vacuum

We appreciate the Commission purpose to focus on uniform state laws independent of federal initiatives to address similar problems. Nevertheless, loan holders and loan servicers must grapple and comply with both state and federal laws in dealing with defaulting home loan borrowers, irrespective of whether such

[1] SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit www.sifma.org.

laws conflict or address similar problems in different ways. As a result, it is virtually impossible for SIFMA to evaluate the merits of the Draft in a vacuum since there are other and evolving laws and legal requirements that address the exact same subject matter.

One example is the voluminous new residential loan servicing regulations and default servicing requirements issued in February 2013 by the Consumer Financial Protection Bureau ("CFPB"), including in certain cases a private right of action that may be asserted by the consumer for violations of the new servicing regulations. These new regulations are not effective until January 2014 and are based in part on the April 2011 Consent Orders between federal banking agencies and several federal- and state-chartered depository institutions, as well as the April 2012 global foreclosure settlement between five banks, 49 state attorneys general and the U.S. Department of Justice, among other federal agencies. Other examples are the detailed loss mitigation requirements required by (i) Fannie Mae and Freddie Mac on loans that they own or that back securities that they guarantee, (ii) the Federal Housing Administration on loans that it insures, (iii) the Department of Treasury under its Making Home Affordable Program, and (iv) many states that have enacted limitations on foreclosure since the financial crisis first began.

All of these are designed to afford defaulting borrowers with increased opportunities to save their homes from foreclosure. Reasonable people may disagree about the propriety or effectiveness of these foreclosure avoidance programs, but there is no doubt that individually and collectively these programs have provided defaulting consumers with material protections to limit a holder's ability to foreclose. This means that SIFMA and its members can not isolate its consideration of the Draft without contemplating whether the Draft's contents are consistent with other laws and regulations addressing the exact same issues but sometimes in different ways.

For example, under all of the federal requirements, servicers must inform borrowers of loss mitigation options and evaluate borrowers for their eligibility for available options, such as loan modifications. Only after these loss mitigation requirements have been exhausted are servicers permitted to initiate foreclosure. The Draft does not account for these federal requirements and could be interpreted effectively to require servicers to start all over again as if the borrower had not already been comprehensively considered for plausible alternatives to foreclosure, some of which may even be more comprehensive than those provided under the Draft. In our view, this inability to synchronize the protections provided to the consumers under the Draft with those provided under other laws and investor or insure requirement addressing the exact some issue unfairly burdens a lender's ability to enforce its mortgage loan documents against a defaulting borrower. *We believe the Draft, if finally enacted, should account for substantially similar protections provided to defaulting borrowers under other legal requirements so that borrowers get a fair shot to avoid foreclosure but can not "game the system" to postpone the inevitable.*

The Draft Does Not Condition Its Enactment on Other State Laws Addressing the Same Issues

We note, **second**, that the Draft does not condition its enactment on the repeal of all other state laws substantively or procedurally limiting foreclosure. It instead merely provides a "place holder" where an enacting state may elect to replace certain of its existing state laws with the Draft. Since the start of the financial crisis in 2008, virtually every state has enacted substantive and procedural laws limiting foreclosures on defaulting borrowers. Given the concern about the multiplicity of requirements, it will be particularly frustrating if the result of the Commission's efforts is the creation of duplicative and perhaps inconsistent state requirement addressing the same substantive concerns. *We believe the Draft should require the repeal of other state laws addressing the same substantive and procedural issues as a condition to its effectiveness.*

The Alternative Provisions in the Draft to Repeal or Limit the Applicability of the Holder in Due Course Rule to Home Loan Foreclosure Should Not Be Adopted in Haste

Third, we respectfully request that the Commission not act in haste to undo the protections afforded loan holders pursuant to the Holder in Due Course Rule, which insulates innocent loan holders from claims by the consumer pertaining to a third party creditor's alleged legal violations. There is a demonstrable, direct one-to-one relationship between assignee liability in the secondary residential mortgage market and the willingness of investors to purchase residential mortgage loans and mortgage-backed securities. In this regard, analogies to financing the purchase of personal property or commercial real estate are inapplicable.

As a preliminary matter, please recognize the present fragile nature of the residential home finance system. Presently, as a result of the financial crisis, the overwhelming majority of home loan mortgage loans are insured, purchased or pooled into securities directly or indirectly guaranteed by the federal government. This is simply unsustainable. While Congress debates the future role, if any, of the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), virtually all agree that a robust private securitization market is required to provide credit to eligible borrowers at affordable rates on a long term basis. This goal will be severely compromised if investors perceive that mortgage-backed securities are backed by mortgages with impaired or limited enforceability, particularly if "defects" that affect enforceability can not be reasonably "diligenced" in advance by the purchasers.

We have actual experience on this point that is instructive. In 1994, Congress enacted the Home Ownership and Equity Protection Act ("HOEPA") by amending the Truth in Lending Act. HOEPA is principally implemented by Section 32 of Regulation Z. HOEPA imposed additional substantive responsibilities on creditors of non-purchase money residential mortgage loans that exceeded certain financial triggers based on the loan's interest rate or total points and fees. That is why Section 32 loans are referred to as "high cost" loans. The theory was that higher priced loans usually involved borrowers who were less capable of protecting themselves.

Since 1994, virtually no one knowingly makes, buys, services, or securitizes "high cost" Loans. The reason is simple. It is not the substantive requirements for such loans, which now are the norm rather than the exception. Rather, it is the federal repeal of the Holder in Due Course Rule with respect to such loans that has caused such loans to become toxic in the marketplace. The Dodd Frank Act recently expanded the number of home loans that are potentially subject to HOEPA by reducing the financial triggers, expanding the types of expenses that fall within the definition of "total points and fees" and adding purchase money loans to the mix.

An assignee of a HOEPA loan is subject to *all* claims and defenses with respect to the mortgage that the consumer could assert against the original creditor, unless the assignee can demonstrate, by a preponderance of the evidence, that a reasonable person exercising ordinary due diligence could not determine, based on the documentation, that the loan was a HOEPA loan.[2] This assignee liability provision is not limited to claims and defenses arising solely as a result of violations of HOEPA, but rather applies to *any* type of legal claim (*e.g.,* a claim arising out of a state law violation) that a consumer may assert against the originating lender, irrespective of whether the claim arises under HOEPA.[3] A number of states have passed anti-predatory lending laws that provide assignee liability similar to that found in HOEPA with similar lack of market acceptance.

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[2] 15 U.S.C. § 1641(a).

[3] There is, however, a material controversy over whether the term "all" includes the right of a consumer to file an *affirmative* claim against an assignee, independent of any *defensive* claim the consumer may assert against an assignee in the assignee's action to enforce the loan documents.

We have every reason to believe that the market will react in the same way if the Draft is successful in rendering the Holder in Due Course Rule inapplicable to home loan foreclosures. Defensive claims unrelated to the servicing of the loan can eviscerate the outstanding principal balance of a loan and essentially cause the loan to evaporate into thin air. Investors have little appetite for asset-backed loans that are not backed by enforceable assets.

We see this same debate presently being played out with respect to the CFPB's new "qualified mortgage" rules pertaining to the "ability to repay" requirements adopted under the Dodd Frank Act. Violations of these requirements exposes innocent loan holders to defenses to foreclosure with the possibility of significant actual, statutory and enhanced damages being offset against the outstanding debt to be enforced. Perhaps this is why the Federal Housing Finance Agency, the conservator for Fannie Mae and Freddie Mac, announced in May of this year that loans subject to this defense to foreclosure because they are not "qualified mortgages" will not be eligible for purchase by the GSEs.

While ordinarily a rational investor may price the heightened legal risk rather the withdraw from or reduce its participation in the capital markets, this seemingly less drastic alternative poses its own set of material legal problems for investors. First, pricing this risk could cause the loan to exceed the 3 point maximum to qualify for "qualified mortgage" status under federal law. Second, pricing a loan for lesser liquidity and higher legal risk could cause the loan to become a "high cost" loan under HOEPA, particularly under the recently adopted lower financial triggers. This is another example of how the Draft will not operate in isolation but is inextricably tied to federal law as well.

The debate goes well beyond the policy question over whom should bear the risk of a third party's origination violations as between a consumer and an innocent subsequent holder. It really boils down to whether investors will agree to bear the risk of loss on loans that are priced for the availability of enforceable collateral but where such collateral may prove to be illusory in foreclosure. And unlike the debate over whether a buyer of a defective appliance or car should be required to pay for something that simply does not work, as is the case with the FTC's Holder Rule, in this case neither the offending loan nor the house secured by the loan is necessarily itself defective and the consumer obtained, spent and received the benefit of the proceeds of the loan. Moreover, and equally importantly, there is no direct or necessary nexus between the limitation on the remedy of foreclosure and the violation that is being asserted against the holder.

Our bottom line is that the rescission of the Holder in Due Course Rules in the home loan foreclosure context could convert a secured loan into an unsecured loan. This is a risk that the mortgage capital markets in the past have been unwilling to accept. *We respectfully request that the Commission not include a repeal or limit of the Holder in Due Course Rule in the Draft.*

Thank you for your consideration.

Sincerely,

/s/

Christopher Killian
Managing Director
Securitization