LARSON • KING | LITIGATION REDEFINED

For More Information Contact:

Michael Steinlage
msteinlage@larsonking.com

Hilary Loynes
hloynes@larsonking.com

2800 Wells Fargo Place
St. Paul, MN 55101
phone 651-312-65xx
fax 651-312-6618

Minnesota Foreclosure Law Amended to Prevent "Dual Tracking"

Earlier this year, the Minnesota foreclosure by advertisement statute was amended to require that a mortgagee have completed the process of considering a borrower for loss mitigation prior to proceeding to foreclose. The statute also prohibits "dual tracking" of loss mitigation and foreclosure activities in connection with a loan. The loss mitigation requirement in the new law went into effect August 1, 2013. The "dual tracking" prohibition goes into effect on October 31, 2013. Minn. Stat. § 582.043 Loss Mitigation; Mortgage Foreclosure Dual Tracking.

Loss Mitigation Requirements

The statute imposes requirements intended to ensure that mortgagors have an opportunity to be considered for any loss mitigation options that are available to borrowers before a loan is referred for foreclosure. The requirements begin with the duty to notify a mortgagor <u>in writing</u> of "available loss mitigation options offered by the servicer that are applicable to the mortgagor's loan." *Id.* at subd. 5(1). This could potentially include options available through government programs such as HAMP, settlements with federal and state authorities, and any private loss mitigation options that a servicer may offer.

If a mortgagor requests a loan modification or other "loss mitigation option," the statute imposes additional requirements on the servicer. Specifically, the servicer must:

- exercise reasonable diligence in obtaining documents and information from the mortgagor to complete a loss mitigation application,
- facilitate the submission and review of loss mitigation applications, and
- give the mortgagor a reasonable amount of time to provide the required documents.

Id. at subd. 5(2).

Once an application has been timely received, the servicer must evaluate the mortgagor for all available loss mitigation options before it can refer the loan to foreclosure counsel. *Id.* at subd. 5(3). If the mortgagor is eligible, the servicer must timely offer the mortgagor a loan modification. If the mortgagor is not eligible for a loan modification, the statute requires the servicer to offer any other available "loss mitigation option" for which the mortgagor qualifies. *Id.* at subd. 5(4). "Loss mitigation option" is broadly defined to include temporary or permanent loan modifications, forbearance agreements, repayment agreements, principal reduction, capitalization of arrears, and "any other relief, intended to allow a mortgagor to retain ownership of the property."

How compliance with these requirements will be measured remains to be seen. Where the loss mitigation option exists through a government program or national settlement, compliance with the requirements of the program or settlement should suffice to establish that the servicer has complied with this provision. How compliance will be measured for private loss mitigation options is less clear, although borrowers will likely look to the servicing standards implemented by the CFPB as a starting point. Whatever standards emerge, mortgagors will most assuredly argue that a servicer's compliance should be measured against the "strict compliance" standard traditionally applied to statutory foreclosure requirements that exist for the borrower's benefit.[1]

"Dual Tracking"

Dual tracking is the practice by which a lender continues to pursue foreclosure while a borrower is applying for a mortgage modification. Subdivision 6 of the new statute purports to prohibit the practice by imposing a moratorium during which a servicer may not move forward with foreclosure. The moratorium can arise in different situations, all tied to receipt of a loss mitigation application from the borrower.

- When a servicer receives a loss mitigation application, and the loan <u>has not</u> already been referred to foreclosure counsel, the servicer shall not refer the loan to foreclosure while the application is pending. *Id.* at subd. 6(a).

- When a loan has already been referred to foreclosure prior to receipt of a loss mitigation application <u>but the foreclosure sale has not been scheduled</u>, a servicer may not move forward with foreclosure while the application is pending. *Id.* at subd. 6(b).

- When a loss mitigation application is received <u>after the foreclosure sale is scheduled</u> but "before midnight of the seventh business day prior to the foreclosure sale date, the servicer must halt the foreclosure sale and evaluate the application. *Id.* at subd. 6(c).

If one of the above situations occurs, the servicer may move forward with foreclosure only after one of the following conditions is met: (1) the mortgagor is not eligible for any loss mitigation option, the servicer has informed the mortgagor of that, and the applicable appeal period has expired or the appeal has been properly denied; (2) a written offer was made and a written acceptance was required and the mortgagor fails to respond with within the timeframe specified or within 14 days from the date of the offer; or (3) the mortgagor, in writing, declines a loss mitigation offer. *Id.*

Larson • King, LLP
30 East Seventh Street | Suite 2800 | Saint Paul, MN 55101
Main: (651) 312-6500 | Toll Free: (877) 373-5501 | Fax: (651) 312-6618

The dual tracking obligation further prohibits a servicer from moving forward with foreclosure if the mortgagor is in compliance with the terms of a loss mitigation option, or a short sale has been approved by all necessary parties and proof of funds has been provided to the servicer. *Id.* at (d)(1) and (2).

Private Right of Action

The new law creates a private right of action to enjoin or set aside a foreclosure sale for violation of the new requirements. It also allows a mortgagor who successfully pursues an action under the section to recover reasonable attorneys' fees and costs. *Id.* at subd. 7(a).

In order to pursue a cause of action against a servicer, a mortgagor must record a lis pendens prior to the expiration of his or her redemption period; failure to do so creates a presumption that the servicer complied with this section. *Id.* at subd. 7(b). Following the expiration of the redemption period, the foreclosure sale becomes valid and effective as against allegations that the servicer did not comply with the above requirements. Minn. Stat. §582.25(23). Therefore, in most cases, the statute of limitations on a claim under this section is only six months after the foreclosure sale is held.

Interplay with Minnesota Credit Agreement Statute

While the statute is not explicit in this regard, it is reasonable to assume that in order for a borrower to rely on continuing compliance with a loss mitigation option as grounds for avoiding foreclosure, the loss mitigation option must meet the requirements of the Minnesota Credit Agreement statute. Minnesota Statute section 513.33 provides: "a debtor may not maintain an action on a credit agreement unless the agreement is in writing, expresses, consideration, sets forth the relevant terms and conditions, and is signed by the creditor and debtor." Minn. Stat. § 513.33 (2010). The statute defines a credit agreement as "an agreement to lend or forebear repayment of money, goods, or things in action, to otherwise extend credit, or to make any other financial accommodation." (*Id.*) Courts have consistently held that an agreement to modify a loan or forebear on its enforcement qualifies as a credit agreement under Minn. Stat. § 513.33.[2]

Impairment of Private Contract Rights

The legislature made clear that the statute does not require servicers to provide mortgagors with any specific loan modification option. Minn. Stat. § 582.043, subd. 2. This was done in part to head off claims that the requirements impair the contract rights of lenders in violation of the contracts clause of the United States and Minnesota Constitutions. But, by prohibiting dual tracking and delaying foreclosure, that is arguably what the new law has done.

Larson • King, LLP
30 East Seventh Street | Suite 2800 | Saint Paul, MN 55101
Main: (651) 312-6500 | Toll Free: (877) 373-5501 | Fax: (651) 312-6618

Interestingly, this is not the first time Minnesota has tested the constitutional limits on state power by enacting laws that suspend or delay creditor remedies. In *Home Building & Loan Association v. Blaisdell*, the United States Supreme Court considered a Minnesota law enacted during the Great Depression which authorized courts to extend the period of redemption following a foreclosure sale for such additional time as the court deemed "just and equitable."[3] Although conceding that the obligations of the mortgage contract were impaired by the act, the United States Supreme Court held that the impairment was within the police power of the state as called into exercise by the public economic emergency that the Legislature found to exist at the time.

The law at issue in *Blaisdell* was distinguishable from the current statute in several material respects. The statute in *Blaisdell*, by its terms, only remained in effect for a limited period of time. See *Blaisdell*, 290 U.S. 398 ("The act is to remain in effect 'only during the continuance of the emergency and in no event beyond May 1, 1935.'") The law in *Blaisdell* also provided that the lender was entitled to receive the reasonable value of the income from the property during the time that the redemption period was extended. No similar provisions or protections exist in the Legislature's current enactment.

Conclusion

Like many laws enacted in response to the foreclosure crisis, the new requirements, while well-intentioned, are fraught with ambiguity and uncertainty. To the extent the criteria to qualify for loss mitigation options offered by a servicer are not clear and well-documented, servicers would be well advised to do so, to be in position to establish compliance with the new requirements.

Endnotes:

1 *See, e.g. Jackson v. MERS*, 770 N.W.2d 487, 494 (Minn. 2009); *Holmes v. Crummett*, 13 N.W. 924 (Minn. 1882).

2 *See e.g. Rural Am. Bank of Greenwald v. Herickhoff*, 485 N.W.2d 702 (Minn.1992) (noting that the legislature intended for the statute to apply broadly to protect lenders from having to litigate claims of oral promises).

3 *Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398 (1934)*

Larson • King, LLP
30 East Seventh Street | Suite 2800 | Saint Paul, MN 55101
Main: (651) 312-6500 | Toll Free: (877) 373-5501 | Fax: (651) 312-6618