

Mortgage Lenders and Servicers Should Evaluate and Streamline Their Pre-Foreclosure Notice Procedures to Avoid Pitfalls

By Marc A. Goldich



Marc A. Goldich is a member of the Commercial Litigation Group at Reed Smith LLP and resident in the Philadelphia office. Mr. Goldich's trial and litigation experience has been broad-based, encompassing commercial matters and financial services litigation, including defending individual and consumer class actions challenging mortgage servicer and mortgage lender pre-foreclosure notice procedures. Mr. Goldich has won multimillion-dollar verdicts in commercial cases as a plaintiff and has also successfully defended complex commercial cases for major private and public companies and individuals. Mr. Goldich has extensive experience counseling mortgage lenders and servicers on their pre-foreclosure practices and procedures.

Mr. Goldich has been recognized for his contributions to the "Prisoner Civil Rights Panel" and listed in the annual "Pro Bono Honor Roll" of the U.S.D.C. for the Eastern District of Pennsylvania. To that end, for his work on behalf of indigent clients, Mr. Goldich has been named an "Unsung Hero" by *The Legal Intelligencer*. Most recently, Mr. Goldich was selected for inclusion in the 2013 Pennsylvania Rising Stars list of Pennsylvania Super Lawyers. Mr. Goldich was also selected as a "2013 Lawyer on the Fast Track"—a coveted award bestowed on Pennsylvania lawyers by *The Legal Intelligencer*.

I. Introduction

Home mortgage lenders, assignees and servicers (hereinafter, creditors) are facing what appears to be an increasing influx of both individual and putative class action lawsuits brought by defaulted borrowers who allege that the pre-foreclosure notices the borrowers received violated various state and federal consumer protection laws.¹

In Pennsylvania, for example, financial institutions often find themselves defending against claims that their pre-foreclosure notice practices violate: Pennsylvania's Loan Interest and Protection Law (Act 6);² Pennsylvania's Housing Finance Agency Law (Act 91);³ the Pennsylvania Unfair Trade Practices and Consumer Protection Law (UTPCPL);⁴ and/or other federal and state consumer protection laws.⁵ Typically, these suits involve a wide range of claims, *e.g.*, from purported deviations in the language of the creditor's notice as compared to that promulgated by the legislature, to an assessment of allegedly improper fees. In the current legal environment, it is reasonable to assume that there is no

prospective end in sight to the spread of these types of challenges to creditor's pre-foreclosure notice practices.

That being said, based upon experience counseling clients on their internal pre-foreclosure notice procedures, it seems clear that the proactive implementation by creditors of selected best practices with respect to pre-foreclosure notices may help to provide "safe harbor" protections from potential liability in these types of cases.⁶ Thus, creditors may wish to proactively consider reviewing their pre-foreclosure notice templates and streamlining their pre-foreclosure notice processes in order to coordinate a well-defined and universal system with their foreclosure counsel or perhaps even bring the pre-foreclosure notice process entirely in-house. To illustrate these points, this article provides a brief overview of the minefield that Pennsylvania pre-foreclosure notice law has become.

II. Act 6

Under Act 6,⁷ before a mortgage lender may commence a foreclosure action in Pennsylvania, it must provide the residential mortgage debtor with a Notice of Intention to Foreclose (NOI).⁸ The

1. See, *e.g.*, Claire Alexis Ward, *Throw the Book at Them: Testing Mortgagor Remedies in Foreclosure Proceedings after U.S. Bank v. Ibanez*, 66 Consumer Fin. L.Q. Rep. 269 (2012).

2. 41 P.S. §§ 101 *et seq.*

3. 35 P.S. §§ 1680.401c *et seq.*

4. 73 P.S. §§ 201-1 *et seq.*

5. See, *e.g.*; Scott D. Samlin & Rinaldo Martinez, *California Homeowner Bill of Rights*, 66 Consumer Fin. L.Q. Rep. 409 (2012). In view of these developments, creditors nationwide may wish to periodically conduct state-specific reviews of the often rapidly-changing foreclosure requirements in an effort to establish best practices and reduce potential exposure to affirmative claims.

6. See *supra* note 5, and discussion below.

7. See *supra* note 2.

8. 41 P.S. § 403 (2012). Given the existence of case law focusing on excessive technicalities, it stands to reason that Pennsylvania courts would interpret the definition of residential mortgage debtor to include a broad range of individuals, including those who may not be named obligors or otherwise identified in the servicer's internal system. Indeed, the Supreme Court of Pennsylvania has held that purchasers of property at a tax upset sale were "residential mortgage debtors" within the meaning of Act 6 because they were successive record owners and notified the

(Continued on next page)

provisions of Act 6 apply to all residential mortgages, including land installment contracts.⁹ A “residential mortgage” as defined in Act 6 is a loan evidenced by a security document and secured by a lien upon real property in Pennsylvania that contains “two or fewer residential units or on which two or fewer residential units are to be constructed and shall include such an obligation on a residential condominium unit” and where the original amount owed was equal to or less than the “base figure.”¹⁰ The “base figure” used to be \$50,000 but gradually¹¹ has been raised to \$234,692 and may be adjusted further by the Department of Banking.¹²

Thus, the NOI is not required in instances where the original bona fide principal amount owed is above the current base figure of \$234,692 or if the property does not otherwise fit within the definition of residential real property (*i.e.*, a property with more than two residential units, other than a condominium unit, would not fit within the Act 6 definition

of residential real property). Note that it does not matter if the principal amount owed by the borrower has dropped below the “base figure.” The only relevant point of measure is the amount owed by the borrower when the loan was first made.¹³

What must the NOI contain? Section 403(c) mandates that the NOI must, clearly and conspicuously:¹⁴ (1) identify the particular obligation or real estate security interest; (2) state the nature of the default; (3) advise the debtor of the right to cure the default as provided in section 404 and specify exactly what performance including what sum of money must be tendered to cure the default; (4) advise the debtor of the time needed to cure the default; (5) advise the debtor as to the methods by which the debtor’s ownership or possession of the real estate may be terminated; and (6) advise the debtor of the right, if any, to transfer or refinance.¹⁵

Section 404(b) in turn provides, in relevant part: “To cure a default under this section, a residential mortgage debtor shall: (1) Pay or tender in the form of cash, cashier’s check or certified check, all sums which would have been due at the time of payment or tender in the absence of default and the exercise of an acceleration clause, if any[;] (2) Perform any other obligation which he would have been bound to perform in the absence of default or the exercise of an acceleration clause, if any[;] (3) Pay or tender any reasonable fees allowed under section 406 and the reasonable costs of proceeding

to foreclosure as specified in writing by the residential mortgage lender actually incurred to the date of payment[; and] (4) Pay any reasonable late penalty, if provided for in the security document.”¹⁶

The Pennsylvania Department of Banking, the regulator charged with promulgating regulations to implement Act 6, has published a model form NOI at 10 Pa. Code section 7.4.¹⁷ The model form NOI published by the Department of Banking is specifically authorized by a statute which provides that the form adopted by the Secretary’s regulations “shall be interpreted as satisfying the requirements of [section] 403....”¹⁸ Although the published model form NOI satisfies the requirements of section 403, this does not mean that use of the model form is mandatory. The Pennsylvania Code section setting forth the model form NOI specifically uses permissive language stating that a mortgage lender’s notice “may” be in the form published by the Department of Banking.¹⁹ One court considered the argument that the form is mandatory but did not rule upon it.²⁰ Although use of the model form in itself will not insulate a lender from incorrect or omitted information, reliance on a

8. (Continued from previous page)

mortgagee of their interest in the property. *Marra v. Stocker*, 532 Pa. 187, 615 A.2d 326 (1992).

9. 41 P.S. § 403(a); see also *Anderson Contracting Co. v. Daugherty*, 417 A.2d 1227, 1232, 274 Pa. Super. 13, 23 (1979) (holding that land installment contracts are residential mortgages for purposes of Act 6).

10. 41 P.S. § 101. “Residential Real Property” is defined under Act 6 as “real property located within [Pennsylvania] containing not more than two residential units or on which not more than two residential units are to be constructed and includes a residential condominium unit.” 41 P.S. § 101. Note that there is no requirement for the mortgagor to reside at the property. *Id.*

11. See Act of July 8, 2008, No. 57, 41 P.S. § 101 (definition of “Base Figure”) (eff. Sept. 8, 2008). Act 57 of 2008 amended Act 6 by adding a definition of “base figure,” namely §217.873, to be adjusted annually for inflation by the Department of Banking through notice published in the Pennsylvania Bulletin. See 41 P.S. § 101, as amended, Act No. 57, July 8, 2008 (eff. Sept. 8, 2008). The definition of residential mortgage was amended to increase the principal included in the definition from \$50,000 or less to the base amount or less. *Id.*

12. The November 3, 2012 Pennsylvania Bulletin Notice states:

The Department of Banking and Securities (Department), as required by the definition of “base figure” in section 101 of the act of January 30, 1974 (P.L. 13, No. 6) (41 P.S. § 101), known as the Loan Interest and Protection Law, is publishing the following notice regarding the inflation-adjusted base figure for the calendar year 2013. The Department has determined that the current base figure of \$230,110 adjusted for annual inflation using the “Consumer Price Index—All Urban Consumers: U.S. All Items 1982–84=100” published by the United States Department of Labor Bureau of Labor Statistics results in a base figure of \$234,692. This new base figure will be effective January 1, 2013, for the calendar year 2013.

42 Pa. Bulletin 6899 (Nov. 3, 2012).

13. 41 P.S. § 101. See *supra* notes 11 & 12.

14. The meaning of the words “clearly and conspicuously” in section 403(c) have been litigated. As to clarity, in *Mid-Penn Consumer Discount Company v. Chamberlain*, 8 Pa. D. & C.3d 752 (C.P. Phila. 1979), the Philadelphia Court of Common Pleas found that the creditor’s notice, while in technical compliance with Act 6, was drawn “largely in the complex and turgid language of the statute, and as such failed to advise the debtor of the rights and obligations on default, as required by Act No. 6.” *Mid-Penn*, 8 Pa. D. & C.3d 752, 755. The *Mid-Penn* court cited *Fidelity Bond and Mortgage Co. v. Clark*, 7 Pa. D. & C.3d 742, 746 (C.P. Phila. 1978) in which the same form was used and held that the information must be set forth in terms “readily understandable by a lay person.” *Mid-Penn*, 8 Pa. D. & C.3d at 754 (quoting *Fidelity Bond and Mortgage Co.*, 7 Pa. D. & C.3d at 746) (“the language of the notice must be reasonably understandable to a person of average intellect.”). As discussed *infra*, use of the form promulgated by the Department of Banking should avoid these problems. See 10 Pa. Code § 7.4.

15. 41 P.S. § 403(c)(1)-(6).

16. 41 P.S. § 404(b). Section 406 provides that “no residential mortgage lender shall contract for or receive attorney’s fees from a residential mortgage debtor except as follows: (1) Reasonable fees for services included in actual settlement cost[;] (2) Upon commencement of foreclosure or other legal action with respect to a residential mortgage, attorney’s fees which are reasonable and actually incurred by the residential mortgage lender may be charged to the residential mortgage debtor[;] (3) Prior to commencement of foreclosure or other legal action attorneys’ fees which are reasonable and actually incurred not in excess of fifty dollars (\$50) provided that no attorneys’ fees may be charged for legal expenses incurred prior to or during the thirty-day notice period provided in section 403 of this act.” 41 P.S. § 406.

17. The Department of Banking model notice provides that the notice shall, in relevant part, state the missed “monthly payments” and/or other reason for default and identify the “total amount now required to cure” the default, including all of the “late charges and other charges [which] have also accrued” as of the date of the notice. 10 Pa. Code § 7.4. The current model Act 6 notice is also posted on the Department of Banking website at http://www.portal.state.pa.us/portal/server.pt/document/1093554/notice_of_intention_to_foreclose_mortgage_aka_act_6_notice_pdf.

18. 7 P.S. § 6020-166.

19. 10 Pa. Code § 7.4.

20. See *Gettysburg National Bank v. Trace*, 22 Pa. D. & C.3d 474 (C.P. Adams 1982) (“We think the use of the model form should be mandatory. . . . We stop somewhat short of holding that use is mandatory.”).

properly completed form has been upheld.²¹ The Superior Court also has held that the model form is authoritative.²²

III. Act 91

Act 91,²³ also known as Pennsylvania's Housing Finance Agency Law, established the Homeowners' Emergency Mortgage Assistance Program (HEMAP), which offers mortgage assistance in the form of a special loan to homeowners facing foreclosure on property located in Pennsylvania.²⁴ Act 91 requires an additional notice (the Act 91 Notice).²⁵ The Act 91 Notice is the primary method lenders have of communicating with delinquent homeowners that there is a program that may be able

to assist them.²⁶ Unlike the NOI required by Act 6, in order for the Act 91 Notice to apply, it is required that the mortgagor reside at the subject property.²⁷ The focus of Act 6 is on whether the property is "residential real property" and whether the amount of the loan is equal to or below the base amount.²⁸ The primary focus of Act 91 is whether the mortgagor lives at the property, regardless of the loan amount.²⁹ Thus, for example, if a loan is for less than \$234,692 and the property is considered "residential real property," then Act 6 applies even if the mortgagor does not reside at the property. Conversely, if the mortgagor resides at the property, Act 91 applies, regardless of the original amount of the loan.

What must an Act 91 Notice contain? The Pennsylvania Housing Finance Agency (PHFA) has responsibility under Act 91 to establish the language and form of the Act 91 Notice.³⁰ Pursuant to this authority, the PHFA has promulgated an Act 91 Notice form. It is advised that the PHFA approved form be used, without alteration, in all instances where an Act 91 Notice is required. An August 8, 2012 announcement published by the PHFA regarding the restart of the HEMAP program specifically states that its current form "must be used by mortgagees and mortgage servicers going forward as the Program restarts. As of October 2, 2012 this Notice must be provided in accordance with the provisions of the Act."³¹ The PHFA form Act 91 Notice has not been changed since it was last

published on August 30, 2008.³² The PHFA has also made clear that "Mortgagees and mortgage servicers may not use any previously published form of the Act 91 Notice" because "[s]ending a Notice in a form that was published by the Agency prior to August 30, 2008 does not meet the requirements of the Act and will be considered defective."³³

Most notably, the PHFA has stated that "[m]ortgagees and mortgage servicers should not add additional or extraneous language to the form or place inconsistent information in the form. For example, putting the Notice on letterhead can result in conflicting contact numbers or including a payment coupon can be confusing to the homeowner. Such inappropriate practices may result in referrals under consumer protection laws."³⁴ The PHFA's announcement also stated that:

Act 70 of 2012 makes it very clear that there are serious consequences where the mortgagee or mortgage servicer does not send an Act 91 Notice to homeowners or sends a defective Notice (*i.e.:*) one that does not meet the requirements of the form Notice published by the Agency; one that does not contain all of the information required by the form of the Notice; or one that contains confusing, additional, conflicting or inappropriate information). In such cases the trial court may dismiss the foreclosure action, order the service of a corrected notice, impose a stay of the action or impose other appropriate remedies.³⁵

The Act 91 Notice also must contain a current list of counseling agencies available for the county in which the property is located. The PHFA has noted that "[creditors] should not attach a complete list of counseling agencies for all

21. See *Bankers Trust Co. v. Foust*, 621 A.2d 1054, 1057 (Pa. Super. Ct. 1993) (upholding use of the model form set forth at 10 Pa. Code § 7.4).

22. *Id.*

23. See *supra* note 3.

24. *Id.* More recently, Senate Bill No. 1433, known as the Homeowner Assistance Settlement Act, was signed into law to provide funding for the HEMAP program to restart after a brief suspension of HEMAP. See 35 P.S. § 1681.1 (Act 70). Act 70 establishes a special fund known as the Homeowner Assistance Settlement Fund to finance the Homeowner's Emergency Mortgage Assistance Program, which previously ran out of funding on August 27, 2011. 35 P.S. § 1681.3. Act 70 also addresses the failure to comply with notice requirements of the Homeowner's Emergency Mortgage Assistance Program, commonly referred to as the Act 91 notice. 35 P.S. § 1681.5. The purpose of the new law is to limit the damaging effect of the recent Pennsylvania Superior Court decision in the case of *Beneficial Consumer Discount Company v. Pamela Vukman*, 2012 PA Super 18 (Pa. Super. Ct. 2012), in which the court found that the failure of the mortgagee to comply with the Act 91 notice requirements deprived the court of jurisdiction in the foreclosure. Following the *Vukman* decision, any foreclosure judgment predicated upon a deficient Act 91 Notice (in effect between June 5, 1999 and September 8, 2008) was deemed to be void because the deficient Act 91 Notice deprived the court of jurisdiction to render the judgment. This new law however, specifically provides that, retroactive to June 5, 1999, the failure of a mortgagee to comply with the Act 91 Notice requirements does not deprive the court of jurisdiction over the foreclosure action, and does not impair the subsequent conveyance or other transfer of title of property through the foreclosure proceeding. 35 P.S. § 1681.5. The new law grants a court the right to dismiss a foreclosure action without prejudice, impose a stay on the action, or impose any other appropriate remedy to address the interests of a mortgagor who has been prejudiced by the failure of the mortgagee to comply with the Act 91 notice provisions, but limits the rights of the mortgagors seeking to overturn a foreclosure judgment rendered against them. 35 P.S. § 1681.5. Under Act 70, the mortgagor must affirmatively raise, in the action, the mortgagee's failure to comply with the Act 91 Notice requirements, before the delivery of a Sheriff's Deed or Marshal's Deed, or the delivery of a deed by the mortgagee. *Id.* Thus, the Pennsylvania Legislature and Governor Corbett enacted Senate Bill No. 1433, ensuring that title to properties acquired by purchasers through foreclosure sales affected by a deficient Act 91 Notice will remain marketable and insurable.

25. See Act 91, *supra* note 3.

26. The Pennsylvania Superior Court has stated that "[t]he purpose of an Act 91 Notice is to instruct the mortgagor of different means he may use to resolve his arrearages in order to avoid foreclosure on his property and also gives him a timetable in which such means must be accomplished. 35 P.S. § 1680.403c." *Wells Fargo v. Monroe*, 966 A.2d 1140 (PA Super 2009) (quoting *Fish v. Pennsylvania Housing Fin. Agency*, 931 A.2d 764, 767 (Pa. Cmwlth. 2007)).

27. See Act 91, *supra* at note 3. *Cf.* the scope requirements for an Act 6 NOI, cited *supra* at note 10.

28. See *supra* notes 2, 11 & 26.

29. See *supra* notes 3 & 26.

30. Specifically, section 403c states that the PHFA "shall prepare a notice which shall include all the information required by this subsection" and section 402c(a) states the Act 91 Notice "shall be given in a form and manner prescribed by the agency." 35 P.S. §§ 1680.402c(a) & 1680.403c.

31. PHFA Announcement, 48 Pa. B. 4859 (Aug. 8, 2012).

32. *Id.*

33. *Id.*

34. *Id.*

35. *Id.*

counties in Pennsylvania or for counties where the property is not located. This will only confuse homeowners and will make the Notice defective.”³⁶ As emphasized by the PHFA, only the portion of the list applicable to the borrower’s county should be attached to the Act 91 Notice. The PHFA commentary cited above makes clear that the model form it has promulgated should be used and that creditors should not modify or add language to the Act 91 Notice. To that end, additional language, inconsistent information, and even the creditor’s letterhead should be eliminated from any Act 91 Notice forms currently used by creditors.

IV. Conclusion

This is only a sampling of some of the pre-foreclosure requirements in Pennsylvania. Creditors must also be sensitive to and aware of the scope, applicable time periods, eligibility and formatting requirements, and cure provisions contained in Act 6 and Act 91. Indeed, with the large number of residential mortgage foreclosures and increased pressure from federal and state regulators and the courts to review and reform foreclosure practices and procedures,³⁷ navigating the mortgage foreclosure and litigation process has become more precarious

than ever. Moreover, with the increase in actions by federal and state regulators, multiple attorneys general, and class action plaintiffs’ attorneys, creditors need to be able to identify and utilize the most appropriate pre-foreclosure notice forms and procedures. In-house counsel should work with their legal team to identify key issues and implement best pre-foreclosure practices in order to avoid ongoing and ever-changing potential pitfalls.

36. *Id.* The current list of counseling agencies is found at <http://www.phfa.org/counseling/hemap.aspx>.

37. *See, e.g.*, Financial Crisis Inquiry Commission Report, Chapter 22, available at <http://www.gpo.gov/fdsys/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf>.