

The Honorable Robert N. Herkes, Chair
The Honorable Glenn Wakai, Vice Chair
House Committee on Consumer Protection and Commerce

Hearing : Wednesday, February 18, 2009, 2:00 p.m.
State Capitol, Conference Room 325

IN SUPPORT OF HB 304

Chair and Members of the Committees:

My name is Ryker Wada, representing the Legal Aid Society of Hawai'i ("LASH"). I am advocating for our clients who include the working poor, seniors, citizens with English as a second language, disabled and other low and moderate income families who are consumers. We are testifying in support of HB 304 as it would strengthen protections for consumers in the State of Hawaii.

I supervise a housing counseling program in the Consumer Unit at the Legal Aid Society of Hawaii. The Homeownership Counseling Project provides advice to individuals and families about homeownership issues. Specifically the project provides information on how to prepare yourself before purchasing a home and what to do if you are in danger of losing your home through foreclosure. In the past Fiscal Year we serviced more than 200 clients in our Project and more than 70 in the past 2 months.

HB 304 seeks to require that a mortgagee using a power of sale provision to foreclose upon a homeowner's property allow a longer time period after contacting a homeowner before continuing to foreclose upon the property.

In some cases, homeowners who are faced with foreclosure simply do not have enough time to complete all that is required by the mortgagee in order to save their homes. HB 304 would create a vehicle by which homeowners would be allowed more time to save their homes, and provided their options by the own mortgagee.

LASH anticipates a growing number of foreclosures in the coming years as the so-called exotic mortgage products mature and consumers are not able to keep up with their adjusted mortgage payments or find a suitable refinance. With the growing number of foreclosures, there will only be an increase in the number of homeowners and tenants who are harmfully displaced by the foreclosure process.

The Legal Aid Society of Hawaii supports HB 304 and its efforts to protect homeowners and renters from a swift foreclosure process.

Conclusion:

We appreciate these committees' recognition of the need to protect consumers in the State of Hawaii. HB 304 attempts to strengthen protections for consumers by giving homeowners more time to find appropriate solutions to their potential foreclosure problems. We support HB 304 and its attempts to protect homeowners in the State of Hawaii. Thank you for the opportunity to testify.



HAWAII BANKERS ASSOCIATION

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Presentation to the House Committee on Consumer
Protection and Commerce
Wednesday, February 18, 2009, at 2:00 p.m.

Testimony for HB 304 Relating to Foreclosures

TO: The Honorable Robert Herkes, Chair
The Honorable Glenn Wakai, Vice Chair
Members of the House Committee on Consumer Protection and Commerce

My name is Neal Okabayashi and I testify for the Hawaii Bankers Association. While we are sympathetic to the intent of this bill to help those in a foreclosure, we believe that given the myriad of programs by both the federal government and lenders, the bill is not needed.

Hawaii has been very fortunate in avoiding the number of foreclosures prevalent in certain mainland states. In part, that has been due to the conservative lending of local banks but also in part to the strength of our economy. Unfortunately, as our economy deteriorates, we can expect foreclosures to increase because the reasons for loan defaults basically remain the same: job loss or underemployment, health issues, death and divorce – three factors worsened by economic downturns. Complicating this effort is that many nonbanks, as well as some banks, made nontraditional mortgages which have led to borrowers with no or little equity in a property which tends to reduce any incentive to try to work out problems with the lender.

During the heydays of mortgage lending, mainland lenders had the largest market share. For example, in 2006, the local lenders (primarily banks and credit unions) were about 27% of the market while mainland banks and nonbanks were about 55% of the market. Because of the turmoil in the credit markets and demise of certain mainland lenders, local banks and credit unions were about 50% of the market last year and mainland lenders were about about 35% of the market. Because of the imprecision of the figures provided by Title Guaranty, these figures are just estimates.

Thankfully, the local lenders are not well represented in foreclosures. Our sense is that, perhaps as a consequence of the large market share of mainland lenders during a time of low rates and high home prices, mainland lenders like Countrywide and WAMU (seized by federal banking regulators and sold to JP Morgan Chase) are much more involved in foreclosure proceedings than local lenders.

It is also our feeling that a substantial portion of foreclosures in Hawaii are of investors, especially in resort areas. Those borrowers relied on the income stream from the rental pool to make mortgage payments and as tourism turned down, they found the rental pool income stream to be insufficient to make payments.

Lenders are actually very active in foreclosure mitigation programs because lenders are hurt by foreclosures and would prefer alternatives such as deferrals and loan modifications but

sell the property, the lender's alternatives are reduced. In Hawaii, just as in some mainland states such as California, many of the foreclosures are of investors, especially those in resort areas who relied on a rental income stream to pay the loan. Our sense, which is anecdotal, is that more than half of our foreclosures are investors.

As for banks, because we are regulated by a federal banking agency, we have less flexibility on loans made with a loan-to-value greater than 80%, meaning the down payment was less than 20%. In such cases, we are required to obtain private mortgage insurance from an insurer when we make the loan, and any modification must be approved by the insurer.

There are other programs. A coalition of mortgage servicers, lenders, housing counselors and investors have come together to form the Hope Now Alliance, which has produced a set of loan mitigation guidelines similar to the FDIC program.

The FHA has a program aimed at facilitating loan modifications called Hope for Homeowners.

The Federal Reserve System has taken unprecedented steps to reduce the short term interest rates which have an indirect downward push on mortgage rates. Such steps, along with President Obama's stimulus plan which is intended to reduce unemployment or at least reduce the rate of unemployment, will improve the economic climate which is the best foreclosure mitigation program. The Federal Reserve also announced its plan to purchase up to 600 billion dollars in mortgage related debt which has the impact of lowering mortgage rates, which would have two beneficial effects: increase housing prices and reduce mortgage rates, both of which will help borrowers refinance their loans. The stimulus plan about to go to conference also includes a tax credit for homebuyers which would help stabilize and provide an upward lift to home prices, thus helping existing homeowners.

Mitigation programs must have two prongs. One is to increase the ability of borrowers to refinance loans, and the Federal Reserve and this administration have taken those steps. The other is exploring modification of the loan or forbearance, and the lenders have taken those steps.

While lenders are actively pursuing mitigation strategies, we are mindful that we are in an economy that is not conducive to mitigation. Housing prices have dropped which impacts those who paid less than 20% down but in some cases, even those who did pay 20% down. Chairman Ben Bernanke testified before Congress on December 4, 2008 that the available evidence indicates the two most important factors in default are affordability (which depends on both the income of the borrower and the monthly payment) and the borrower's equity in the property. Thus, for those with little or no equity in the property, or even underwater, there are challenges to resurrecting the loan and a bill such as this does not improve the situation.

We are in the midst of the worst economy since the depression. Lenders are actively attempting to help. Passage of measures such as this create downward pressures on lenders and the last thing we need to do is to pressure the financials of a lender who at the heart of our economic system. At the end of the day, the best foreclosure mitigation program is to jump start the economy and create jobs.

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February 18, 2009

Rep. Robert N. Herkes, Chair
and members of the House Committee on Consumer Protection & Commerce
Hawaii State Capitol
Honolulu, Hawaii 96813

Re: **House Bill 304 (Foreclosures)**
Hearing Date/Time: Wednesday, February 18, 2009, 2:00 P.M.

I am the attorney for the **Hawaii Financial Services Association** ("HFSA"). The HFSA is the trade association for Hawaii's financial services loan companies which are regulated by the Hawaii Commissioner of Financial Institutions under the Code of Financial Institutions (Chapter 412, Article 9 of the Hawaii Revised Statutes).

The HFSA wants to **comment** on this Bill.

The purpose of this Bill is to provide a vehicle to allow more time to a defaulting mortgagor facing foreclosure.

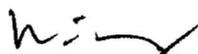
Based on my experience as an attorney in private practice who has actively handled foreclosures for 31 years since 1978, I would like to make the following comments:

1. This Bill provides that in the case of a judicial foreclosure on real property, the court shall allow at least an unspecified number of days between the assessment and judgment. A judicial foreclosure is an equitable proceeding. For this reason, if a mortgagor (borrower) shows good cause to the judge why there should be a delay, the judge already has the power to stay, i.e. delay, the appointment of a foreclosure commissioner or the confirmation of a sale.

2. This Bill provides that in a non-judicial foreclosure on real property, the mortgagee (lender) allow at least an unspecified number of days after contact is made with the mortgagor before filing a notice of default. During the first 120 days in which a loan is in default, lenders generally make reasonable attempts to contact the mortgagor (borrower) and to work on alternatives to foreclosure. A lender should not be forced to follow a rigid statutory procedure when a lender is working with a mortgagor (borrower) to avoid foreclosure on a defaulted loan.

3. Parts of this Bill would make changes to Part II of Chapter 667 of the Hawaii Revised Statutes ("HRS"). Part II is the "Alternate Power of Sale Foreclosure Provisions". I was involved in drafting Part II during the 1997 and 1998 legislative sessions. However, before the legislation passed in 1998, the legislature made certain changes to Part II that made it unusable and unworkable. As a result, no lender uses the Part II alternate power of sale provisions which are in the HRS Sections 667-21 through 667-51. Instead, all non-judicial foreclosures use the provisions in HRS Sections 667-5 through 667-10, much of which were first enacted 135 years ago in 1874.

We are willing to work with your Committee to revise Part II of Chapter 667 and this Bill as needed. Thank you for considering our comments.


MARVIN S.C. DANG
Attorney for Hawaii Financial Services Association

(MSCD/hfsa)

Testimony of the Collection Law Section of the Hawaii State Bar Association

Dear Members of the Hawaii State Legislature:

My name is David Rosen, I am an attorney in private practice with over 10 years of experience in handling foreclosure and Landlord/Tenant legal matters in Hawaii. In that capacity, I am one of probably a dozen or so attorneys, which handle the bulk of foreclosures, both judicial and nonjudicial, in the entire state.

I am also a member of the Collection Law Section of the Hawaii State Bar Association, which is a voluntary organization made up of attorney, real estate professionals, and members of Hawaii's lending and debt collection communities. It is on behalf of this organization that I testify here today.

Like you, we are well aware of the financial upheaval currently taking place. And, like you, we wish that more could be done to help those who are being affected through these difficult times. However, many of the Bills that have been proposed will not only not provide assistance, but may actually make things significantly worse – and not just for homeowners/borrowers, but also for innocent third parties such as homeowners who are paying their mortgages, but who live in associations where there are a significant number of foreclosures.

As a starting point, let me note that this is not the first time that Hawaii has experienced high foreclosure rates. However, it is important to allow this process to run its course under the legal and financial systems currently in place. With respect to Hawaii's foreclosure and Landlord/Tenant laws, and as someone who has been involved with them for over a decade, I can honestly say that the laws as they currently stand are working.

Could they be improved? Yes. But, rather than attempting to do so in reaction to the current situation, which could add uncertainty and confusion, it would be better to take a more circumspect and prospective approach so that, in the quest to help, more harm is not done.

With respect to the specific legislation that has been introduced this Session, there are so many Bills pending in both Houses that rather than referring to specific Bill numbers and discussing why they may be problematic, I have attempted to classify the various Bills by their intent and to address issues related to each category.

- Bills to assist tenants residing in properties being sold through foreclosure (HB 202, HB 331, HB 443, HB 522, HB 525 and SB 784, SB 1068).
- Bills to delay the foreclosure process and/or to require lenders to take certain actions (HB 304, HB 976, HB 1347, HB 1825 and SB 1213, 1328, SB 1623).
- Bills to allow greater recoveries by condominium associations of legal fees (SB 573) and assessments (HB 876 and SB 572).

I. Proposed legislation to address the issues relating to tenants.

There is no disputing that tenants renting properties being sold through foreclosure are innocent parties that are being affected and could use assistance. To address this issue without creating unintended consequences that might (i) increase the number of foreclosures by injuring borrowers, (ii) shift the cost to innocent association members, or (iii) create added liability to lenders and the purchasers of foreclosure properties, which could drive down property values further, we would propose the following modest changes to HRS § 521 (the Residential Landlord Tenant Code):

a. Require landlords facing foreclosure to provide a tenant with a pre-auction notice, at least two weeks prior to the first known auction, that: (1) the property is in foreclosure and that the tenant may need to vacate the property 30 days after an auction is completed, should that occur; (2) if a foreclosure auction occurs, any lease agreement between landlord and tenant will terminate on that date; (3) unless and until an auction occurs, the tenant shall remain obligated to perform under any rental agreement that exists and to pay the landlord any amounts owed; and (4) tenant's obligation to perform under any rental agreement shall terminate immediately and tenant shall be permitted to credit any deposit paid to landlord against any payment obligations tenant may owe landlord, unless landlord provides tenant with proof that tenant's deposit is secure (e.g., in a segregated trust account) or has already been applied against amounts owed by tenant.

b. A landlord's failure to provide the aforementioned pre-auction notice to a tenant within 5 days of (i) receiving personal notice of a foreclosure auction from the foreclosing party, or (ii) receiving an inquiry from a tenant about a foreclosure action on the property, shall result in tenant having the right to terminate any rental agreement immediately and to receive a prompt (i.e., within 5 days of a written demand from the tenant) refund of any deposit held by landlord. Tenant shall serve landlord with an election to terminate a lease agreement, apply a deposit to amounts owed or that will be owed, or to demand a refund of a deposit in writing at the address to which tenant delivers rent payments or such other address as previously designated by landlord to tenant in writing.

c. Allow tenants 30 days to vacate, from the date on which the tenant is given a post-auction notice stating that a foreclosure sale has occurred and the tenant will need to vacate the premises within 30 days. Said notice may be given by the foreclosing party, the prior owner, the prior landlord or property manager, or the party purchasing the property at the foreclosure sale. Said notice shall be in writing, posted on and mailed to the property, and effective as of the date of delivery whether or not it is accepted by the tenant.

d. Confirm that following a foreclosure sale and during the 30 day period following the post-auction notice described above, a tenant will not be liable to pay rent to anyone, but may be held liable to the new owner for any damage to the property and for any legal fees and costs should the tenant fail to vacate the property at the end of said 30 day period.

e. A landlord may not apply a tenant's deposit to cover any rent for a period following a foreclosure sale.

f. Confirm that any party carrying out a foreclosure action and/or any purchaser at a foreclosure sale shall: (i) be permitted, but not required, to give the post-auction notice to a tenant immediately upon the completion of the auction; (ii) have absolutely no liability to a prior owner or a tenant for any reason prior to the expiration of the post-auction notice 30 day period or during or as a result of any eviction proceeding that may follow; and (iii) have a reasonable right to inspect the property immediately upon becoming the lawful owner of the property.

II. Proposed legislation to delay the foreclosure process and/or to require lenders to take certain actions.

As I have previously stated, Hawaii's existing foreclosure and Landlord/Tenant laws are functioning adequately and are allowing for sufficient time for borrowers wishing to negotiate with their lenders and/or associations. While certain individuals may believe that their lender or association is behaving unfairly or unreasonably, these situations make up a small percentage of the total number of accounts and loans in default and where a foreclosure action is undertaken.

In fact, in the vast majority of cases, a lender or an association is going to exhaust all efforts to work out a modification or other arrangements prior to referring a matter to legal counsel and/or proceeding with foreclosure. It is, therefore, extremely rare for a matter to be referred to foreclosure within 60 days of an account going into default. More often, it may be 3-6 months before either a judicial or non-judicial foreclosure action is initiated. Thereafter, it may be a minimum of 3-6 months before an auction is held. Quite often, it may be more than a year before a foreclosure action is completed.

The reason it takes this long is that it is neither in the interests of an association or a lender to foreclose under current economic conditions. Not only is a foreclosing association or lender highly likely to take a substantial loss on their account/loan once the account is in default, but the foreclosure process itself is also expensive.

Consequently, associations and lenders have developed sophisticated mechanisms for analyzing accounts in default, determining appropriate courses of action, and endeavoring to negotiate with the property owner. These processes are constantly being adjusted to be more efficient and to take into account changing market conditions. Attempting to legislate this process would be extremely difficult and inefficient given the numerous variables unique to each account/loan. The likely result being that additional legislation would add expense to the process and would create less, rather than more, flexibility in how these matters are handled.

To the extent an overhaul of this process is desired by the Legislature, a better solution than piecemeal amendments would be to amend Hawaii's Part II (HRS § 667-21 et seq.) nonjudicial foreclosure law to make it the preferred mechanism for carrying out foreclosure actions in Hawaii. This law, which was enacted in 1998, after years of consideration and input from the various constituencies involved in the process, was rendered useless by a number of problems including a requirement that the borrower being foreclosed upon execute the conveyance deed following the auction. See HRS § 667-31(a). Thus, a foreclosure under this law could not occur without the participation of the party who was losing their property.

It should, therefore, come as no surprise that not a single foreclosure action appears to have occurred under this law. Instead, associations and lenders have been forced to foreclose under Hawaii's 1859 foreclosure law, which does not contain many of the useful provisions of the Part II law.

Consequently, if the Legislature is going to do anything this Session to reform the foreclosure process, deleting the homeowner participation requirement in HRS § 667-31(a) and making several other amendments would be a thoughtful and beneficial step since it would allow associations and lenders to proceed under the Part II law, which provides for greater clarity and less ambiguity in how nonjudicial foreclosure actions should be carried out.

III. Proposed legislation to allow greater recoveries by condominium associations and to increase efficiency of the current foreclosure process.

We take no position on this category of Bills other than to note that legal fees and assessments incurred by associations and sought to be recovered under these statutory provisions are rarely recoverable from the owner of the property being foreclosed upon. Consequently, these Bills simply shift the obligation to pay assessments to the purchaser of a foreclosed property or to the lender that is foreclosing.

To the extent that the Legislature is interested in providing greater relief to associations and their members, who are also generally innocent victims, it may want to consider allowing associations and lenders to foreclose more expeditiously, especially in instances where the borrower may not be residing in the property, may be evading service, or may be deceased. While the issue of deceased parties may seem insignificant, the problem of foreclosing against a property where one of the owners cannot be served or is deceased and who may not have any relatives willing to take responsibility for the decedent's affairs, is significant and highly problematic with respect to foreclosure actions.

Specifically, where personal service upon a borrower cannot be effectuated, the foreclosing party will generally need to file a judicial foreclosure action and open an involuntary probate if the borrower or any person with an interest in the property is deceased. A judicial foreclosure action is thousands of dollars more expensive than a nonjudicial proceeding and takes significantly longer; in many cases costing in excess of \$5-8,000 and taking more than a year to complete. Having to address issues such as serving a party whose whereabouts are unknown or who may be deceased can add \$3-10,000 or more and 3-9 months or more to the process.

To address this situation, legislation establishing what constitutes adequate notice of a foreclosure action and service upon interested parties would be highly beneficial and save lenders and associations significant costs and time while not harming borrowers or anyone else that is acting in good faith. In particular, HRS §§ 667-5 and 667-22 could be amended to clarify that adequate notice to and service upon any and all borrowers and interested parties, *including their heirs, assigns, and creditors*, in any foreclosure proceeding shall be deemed adequate and effectuated when notice of the lender's intent to foreclose is: (i) posted on the property, (ii) published in the manner required by said statutes, and (iii) personal service upon said parties is either completed or reasonably attempted: (a) at the address(es) reflected in any recorded instruments related to the property being foreclosed, or at any address(es) provided to the lender in writing; and (b) by the publishing of notice to said party(ies), their heirs,

assigns, and creditors in the manner proscribed by HRS § 634-23(3), which approval may be sought and obtained in a pending judicial action or through a special proceeding brought in the Circuit Court where the property is situated exclusively for the purpose of determining the adequacy of service under the circumstances.

Thank you for this opportunity to testify.

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On Behalf of the Collection Law Section of the Hawaii State Bar Association