

Loan Modifications – Workout Plans and Modification

March 24, 2016

E. Andrew Keeney, Esq.
Kaufman & Canoles, P.C.





E. Andrew Keeney, Esq.

Kaufman & Canoles, P.C.

150 West Main Street, Suite 2100

Norfolk, VA 23510

(757) 624-3153

eakeeney@kaufcan.com

<http://www.kaufmanandcanoles.com/movies/credit-unions.html>

Schedule

- Greetings & Overview
- Workout Agreement/Lender Liability
- Foreclosures as Seen by NCUA
- Foreclosure Procedures
- Deed in Lieu
- Short Sales
- REO



Due Diligence Before Loan Modifications

- Get copies of all of your loan documents
- Review all loans, even those that are not delinquent
- If they are delinquent – WHY?
- Forbearance/Modification agreement
- Decision point – 3 paths:
 - Member cures the delinquency & the loan is reinstated as current
 - Credit union & member negotiate a resolution
 - Member does not address the delinquency, becomes further delinquent & credit union forecloses
- Get the deed
 - Short sale
 - Deed in lieu
 - Foreclosure
- Stay on schedule

4



Loan Extension Policies

(according to NCUA)

- Loan extension policies should address the qualifications & procedures for granting extension agreements, including:
 - Documentation of the reasons for granting extension
 - Identification of the persons with the authority to approve extensions
 - Require that the member demonstrate a “reasonable ability” to meet his or her payment obligation following the extension
 - Limitations on the frequency of extension agreements

Loan Modifications vs Loan Refinance

6



Strategies Including Loan Modifications or Extensions

7



Loan Restructuring

The Workout & Workout Agreement

- Initial Actions
 - Learn the facts
 - Talk to member to learn initial problem & discuss desired result(s)
 - Assess what you already know
 - Order the necessary searches & documents
 - Preliminary analysis – look at the current situation as both a modification & as if you were doing due diligence on a loan to a new borrower

Loan Restructuring (continued)

- Re-read member's loan & security documents with the information you learned from the searches and initial analysis questions in mind
- Visit/inspect property
- In person meeting with members
- Wells Fargo example
- Suggested form letter and agreements available



Standstill Agreement

Agreement whereby a lender makes no further collection efforts on an unpaid loan, acting in the belief that foreclosure would jeopardize the ability of a borrower in financial difficulty to repay any portion of the debt. Such agreements are found most frequently in loans secured by real estate, whether both parties agree that a renegotiated loan is better than a defaulted borrower.

The Workout & Workout Agreement

- Drafting the workout agreement – forms available
 - Begin by outlining the provisions that concern you or use a standard form
 - Basic types of changes (“Business Terms” vs. “Technical Points”)
 - Specific provisions and issues
 - Provision stating that the original documents, except as inconsistent with the Workout Agreement, remain in full force & effect
 - Disclaimer stating that the Workout Agreement was drafted by both parties & that both parties were given the opportunity to be represented by counsel
 - Indemnification & hold harmless clause

11



Alternative Measures

- Extend the loan
- Lower the payment
- Lower the interest rate
- Set up escrow account for taxes & insurance
- Principal forbearance with the mortgage essentially being divided into 2 loans – borrower makes regular payments on 1 smaller loan & the other loan becomes a 0 interest loan that is paid back when the home is sold
- Currently 78.5% refi requests turned down
- Just Say No!!!!

12



Alternative Measures (cont.)

- If they'll work with us . . . we'll work with them
- Distribute the responsibilities
 - Counseling members
 - Loan rewrites, extensions & modifications
 - Collections
 - OREOs
- CEO overview, updates & responsibility

NCUA & Foreclosures

14



NCUA Letter 09-CU-19

Evaluating Residential Real Estate Mortgage Loan Programs

- Policies and procedures for all aspects of the foreclosure process
- Compliance with state laws where credit union does business
- Experienced and knowledgeable staff qualified to handle foreclosures
- Effective internal controls
- Adequate oversight, due diligence and control of third-party services performing foreclosures
- Legally compliant documentation
- Reports to the Board of Directors
- Avoid/eliminate dual tracking
- Evaluate the borrower for potential modification before proceeding into foreclosure

15



More From NCUA

- NCUA Letter 11-CU-01, Residential Mortgage Foreclosure Concerns (January 2011)
- Federal Financial Regulating Agencies Issue State of the “Making Home Affordable Loan Modification Program” (March 2009)
- Final IRPS, Appendix C of Part 471 and NCUA Written Policy Requirement on Frequency of Modifications (May 2012)

By “Loan Workout” we mean:



A loan to a borrower in financial difficulty that has been formally restructured so as to be reasonably assured of repayment (both principal and interest) and of performance according to its restructured terms. A workout loan typically involves a *re-aging, extension, deferral, renewal, or rewrite* of a loan.



Crowe Horwath. **NCUA**

17



Specific Requirements for Loan Workout Policy



- ❑ The Loan Workout Policy should be commensurate with the credit union's size and complexity and must be in line with the credit union's broader risk mitigation strategies



Crowe Horwath. **NCUA**

18



Specific Requirements for Loan Workout Policy – cont.



- ❑ Define borrower eligibility requirements (i.e. under what conditions a credit union will consider a loan workout), including establishing on the number of times an individual loan may be restructured
 - ❑ What loan types will be included in the workout program?
 - ❑ How will underlying collateral be evaluated?
 - ❑ Does the borrower need to be delinquent?
 - ❑ Is demonstration of a financial hardship sufficient for considering a loan workout?
 - ❑ Income verification? Debt ratio/DSC ratio limits?
 - ❑ When will loans be considered for multiple restructures?



Crowe Horwath. NCUA



Specific Requirements for Loan Workout Policy – cont.



- ❑ The policy must establish sound controls to ensure loan workouts are appropriately structured
 - ❑ Set aggregate program limits (for total workout portfolio and each type of workout) as a percentage of net worth that will trigger enhanced periodic reporting to the board of directors
 - ❑ Provide provisions to ensure compliance with the regulatory restriction on no additional advances or financing of interest and fees





Types of Foreclosure

- Judicial Foreclosure
- Non-Judicial/Power of Sale Foreclosure
- American College of Mortgage Attorneys
2015-2016 Mortgage Law Summary
https://www.acmaatty.org/commerce/lawSummary/MortLawSummary_pub.cfm

Non-Judicial Foreclosure

- Deed of trust must include power of sale provisions
- Terms of deed of trust control unless the provisions of the State code are stricter
- Borrower/Property Owner has no right of redemption



Prior to Foreclosure

- Engage Trustee
- Provide Records to Trustee
- Title Matters
- Appraisal
- Many state special rules

Suspending Foreclosure Sale

- Borrower can stop sale
 - Any time before the sale by paying the debt, lender's costs and reasonable attorneys' fees
 - Borrower's bankruptcy stays foreclosure proceedings
- Trustee Postponement of Sale
 - By advertisement in the same manner as the original advertisement of sale

Foreclosure Defenses

- Failure to comply with notice provisions
- Improper acceleration of the note
- Truth in lending disclosure violations (3 year rescission right)
- Lost note
- www.independentforeclosurereview.com

Other Considerations

- Servicemembers Civil Relief Act
 - NCUA Letter to Credit Unions 09-CU-12
 - Cannot foreclose on property owned by a servicemember before the servicemember's military service that secures a deed of trust during the period of military service or 9 months after without a court order
 - In an action filed during or within 9 months after a servicemember's military service, a court may stay a proceeding when the member's ability to comply with the obligation is materially affected by reason of the member's military service

After the Foreclosure

- Lender Successful Bidder
 - The proposed foreclosure deed, a copy of the proposed accounting, a "receipt" for the net sale proceeds and an invoice for the expenses of sale, including the cost of recording the foreclosure deed, is submitted to the lender.
- Third Party Successful Bidder
 - Trustee coordinates the settlement with the bidder's attorney and proceeds to closing
 - Failure to Complete Foreclosure Sale
 - The bidder's deposit is often used to pay the expenses of the foreclosure with the excess funds forwarded to the lender and the process begins again.

28



Distribution of Foreclosure Sale Proceeds

- Foreclosure sale expenses (including trustee's commission)
- Discharge all taxes, levies and assessments, with costs and interest that have priority over the lien of the deed of trust
- Current real estate taxes pro-rated to date of sale
- Discharge in the order of their priority, if any, the remaining debts and obligations secured by the deed
- Any liens of record inferior to the deed of trust under which sale is made
- Remaining proceeds go to the borrower

29



Deficiency Judgment

- Credit Union may recover the difference between foreclosure sale proceeds and the unpaid amount of the original loan (plus collection expenses) depending on state law.

After the Sale

- Eviction
 - Owner
- Rights of Tenants
 - Residential Tenants
 - Commercial Tenants
 - Attornment and Non-Disturbance Agreements
- Insurance
- Property Management

Deed in Lieu of Foreclosure

32



Deed in Lieu of Foreclosure – When Is It Appropriate?

- Member hands over keys
- Member transfers all the collateral to the credit union
- Deed in lieu is more appropriate when property value is less than the debt
- Deed in lieu is used best when the title is clean

How a Deed in Lieu of Foreclosure Works

- Member & credit union execute transfer documents
- Property insurance by credit union
- Credit union obtains physical possession including the keys
- Deed of trust often remains in place until the property is sold
- Credit union obtains new owner's title insurance policies

34



Advantages & Disadvantages of Deed in Lieu

- Advantages
 - Quick
 - Inexpensive
 - Consensual
 - Limited publicity for the member
 - No litigation
- Disadvantages
 - Existing liens are not extinguished
 - Transfer taxes
 - Fraudulent conveyance risk
 - Title insurance

35



Short Sales

36





Short Sales

- Why are short sales important as an option?
- What effect is the short sale on the credit union's bottom line?
- Short sales defined
- Deficiency
- Promissory Note Obligations
- Release of collateral but not the note



- “We are a member-owned, not-for-profit organization. Therefore, the individuals harmed by losses suffered by the credit union are not stockholders but other credit union members, some of whom are facing similar financial circumstances. Credit unions and credit in general are about shared responsibility, and we expect our members to accept responsibility for any shortfall in the pay off of a real estate loan.”

- PenFed Credit Union

Real Estate Owned (REO)

- Property owned by a lender after an unsuccessful sale at a foreclosure auction and held in inventory.
- Other real estate; other real estate owned. Generally, foreclosed property held by lending institutions.
- An account at banks or credit unions that includes property other than real estate used for credit union operations.

1099

- Once the credit union suffers a loss can they notify IRS via a 1099?
- Gross income does not include any amount which (but for this subsection) would be includible in gross income by reason of the discharge (in whole or in part) of indebtedness of the taxpayer if the indebtedness discharged is qualified principal residence indebtedness which is discharged before 1/1/13.
- This exclusion was added by the Mortgage Forgiveness Debt Relief Act of 2007.
- There are limitations (e.g. must be acquisition indebtedness, must be directly related to a decline in the value of the residence or to the financial condition of the taxpayer) that come in play.

41





E. Andrew Keeney, Esq.

Kaufman & Canoles, P.C.

150 West Main Street, Suite 2100

Norfolk, VA 23510

(757) 624-3153

eakeeney@kaufcan.com

<http://www.kaufmanandcanoles.com/movies/credit-unions.html>

Loan Modifications – Workout Plans and Modification

March 24, 2016

E. Andrew Keeney, Esq.
Kaufman & Canoles, P.C.

43

