

# The Jerome N. Frank Legal Services Organization

YALE LAW SCHOOL

## Testimony of P. Solange Hilfinger-Pardo In Support of House Bill 5567

Good morning Senator Winfield, Representative Lesser and other members of the Committee. Thank you for your time today. My name is Solange Hilfinger-Pardo. I am a second-year law student in the Mortgage Foreclosure Litigation Clinic at Yale Law School. Our Clinic provides legal assistance to homeowners fighting foreclosure who cannot afford private counsel. I am here today on behalf of the Clinic to express our support of House Bill 5567, An Act Concerning Alternatives To Foreclosures.

This Act achieves two changes that we believe will be vital for certain homeowners facing foreclosure. First, it creates a method by which senior lienholders and homeowners can come to a workout without facing the threat of hold ups by underwater junior lienholders. Second, it opens up the existing foreclosure by market sale provisions to homeowners already in foreclosure.

Both these measures are important ways for homeowners with underwater properties to avoid foreclosure. Connecticut is home to four cities in the top one hundred towns with the highest negative equity in the country: Hartford, Bridgeport, Waterbury, and New Haven. As of 2014, Hartford was the “most underwater” city in the nation, with a negative equity rate of 56%.<sup>1</sup> Voluntary mortgage modifications, short sales and deeds-in-lieu are almost always a better way for a mortgagee to realize value when the property is underwater and over-leveraged.

Allowing junior lienholders to exert holdout pressure is value destroying. Junior lienholders have incentives to hold up beneficial resolutions such as modifications, deeds-in-lieu or short sales in order to receive a payout, even if their lien is entirely underwater. Without a means for subordinating junior liens, entirely underwater junior lienholders can exert hostage power to prevent economically efficient workouts, harming first mortgagees, as well as the housing market generally. The Clinic and the Connecticut Fair Housing Center have witnessed second mortgagees demand—and receive—payoffs of thousands of dollars to cooperate with a workout. In other cases, the time it took to seek this cooperation caused a deal to fall through. In the context of loan modifications, senior lienholders and homeowners have no practical ability to circumvent junior lienholders who are demanding payouts and threatening to block modifications. In such situations, their only choice is to pay or let the home enter an unnecessary foreclosure.

This bill will allow more homeowners to avoid foreclosure. In a random sampling of Connecticut Fair Housing Center foreclosure prevention intakes from 2013 and 2014, 12% reported having second mortgages that were completely underwater, and many more had junior liens that were underwater. These are homeowners whose outcomes could be significantly improved through the enactment of this bill. They would not be forced to pay out junior lienholders who made a bad bet on the property in order to obtain a loan modification. Nor would they ever be forced into foreclosure when an alternative preferable to both the homeowner and the first mortgagee exists.

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<sup>1</sup> Haas Institute, *Underwater America*, U.C. Berkley (2014), 14.

The foreclosure by market sale provisions already provide for junior liens to be subordinated in order to allow the sale to go forward. This bill would allow homeowners already in foreclosure to utilize these tools for avoiding foreclosure. Given that many homeowners do not always pursue alternatives to foreclosure prior to entering the foreclosure process, this bill will allow mortgagees to better preserve property value and give homeowners additional means of avoiding foreclosure.

We have some suggestions for slight amendments to the bill's language as it currently stands. These changes accomplish the same objectives as before but in ways that may be more accommodating of other stakeholders, namely mortgagees, who would be affected by this bill. The amended bill also clarifies some of the language in the raised bill and would simplify its administration. We are attaching our suggested amendments to this testimony.

We watch homeowners struggle through foreclosure day in, day out. Modifications, deeds-in-lieu, or short sales often provide significantly better outcomes for both the homeowner and the first mortgagee. We support this bill because we believe it helps achieve those outcomes. Thank you for the opportunity to testify today.



Attachment to  
Testimony of  
P. Solange Hilfinger-Parolo:  
Suggested Amendments

General Assembly

**Raised Bill No. 5567**

February Session, 2016

LCO No. 2602



Referred to Committee on BANKING

Introduced by:  
(BA)

**AN ACT CONCERNING ALTERNATIVES TO FORECLOSURES.**

Be it enacted by the Senate and House of Representatives in General Assembly convened:

- 1 Section 1. (NEW) (*Effective from passage*) For purposes of this section  
2 and sections 2 to 6, inclusive, of this act:
- 3 (1) "Mortgage" has the same meaning as provided in section 49-24a  
4 of the general statutes, as amended by this act;
- 5 (2) "Mortgagee" has the same meaning as provided in section 49-24a  
6 of the general statutes, as amended by this act;
- 7 (3) "Mortgagor" has the same meaning as provided in section 49-24a  
8 of the general statutes, as amended by this act;
- 9 (4) "Residential real property" has the same meaning as provided in  
10 section 49-24a of the general statutes, as amended by this act;
- 11 (5) "Senior lien" means the first security interest placed upon a  
12 property to secure payment of a debt or performance of an obligation  
13 before one or more junior liens;

14 (6) "Junior lien" means a security interest placed upon a property to  
15 secure payment of a debt or performance of an obligation after a senior  
16 lien is placed on such property;

17 (7) "Lienholder" means a person who holds a security interest in real  
18 property;

19 (8) "Underwater mortgage" means a mortgage where the debt  
20 associated with such mortgage, along with any senior lien, exceeds the  
21 fair market value of the mortgaged property as determined by a court  
22 in accordance with sections 4 and 5 of this act.

23 Sec. 2. (NEW) (*Effective from passage*) Notwithstanding any provision  
24 of the general statutes, any underwater mortgage on residential real  
25 property may be modified, and the value increased, without the  
26 consent of the holders of junior encumbrances and without loss of  
27 priority for the full amount of the loan modified, provided such  
28 modification is approved by the court through entry of judgment of  
29 loss mitigation in accordance with sections 3 to 5, inclusive, of this act.

*Such a judgment may only be entered in a foreclosure action against the residential property*

30 Sec. 3. (NEW) (*Effective from passage*) A mortgagor of an underwater  
31 mortgage may elect to transfer the subject property to a mortgagee in  
32 satisfaction of the mortgagor's obligation to the mortgagee by agreeing  
33 to transfer such property in a record executed by both parties. Any  
34 transfer agreement shall: (1) Transfer to the mortgagee all interests in  
35 the property except for the interests reserved to the mortgagor in the  
36 transfer agreement or the interests held by more senior mortgagees or  
37 lienholders; (2) discharge the mortgage; *and contemplate the termination of*  
38 in the property subordinate to that of the lienholder party to the  
39 transfer agreement; *and (4) be conditioned on a court's entry of a*  
40 judgment of loss mitigation under sections 4 and 5 of this act.

41 Sec. 4. (NEW) (*Effective from passage*) A mortgagee or mortgagor may  
42 file a motion for judgment of loss mitigation following a modification  
43 under section 2 of this act or execution of an agreement under section 3  
44 of this act. Upon motion of the mortgagee or mortgagor and with the

45 consent of the counterparty, the court, after notice and hearing, may  
 46 render a judgment of loss mitigation approving the modification or  
 47 transfer. Such judgment shall be a final judgment for purposes of  
 48 appeal. The only issues at such hearing shall be (1) a finding of the fair  
 49 market value of the residential property, which may be determined by  
 50 an appraisal, conducted by a court-appointed disinterested real estate  
 51 appraiser, (2) a finding of the fair market value of any priority liens on  
 52 such property, (3) the mortgagor's debt, (4) <sup>held by the mortgagee,</sup> whether the mortgage is an  
 53 ~~underwater mortgage~~, and (5) whether the contemplated transaction  
 54 was agreed to in good faith and for the purposes of mitigation <sup>being</sup> the  
 55 losses such mortgagor and mortgagee would incur through a  
 56 judgment of foreclosure. If the court renders a judgment of loss  
 57 mitigation, immediately after the expiration of any applicable appeal  
 58 period or after the disposition of such an appeal that affirms the  
 59 judgment, then either, as applicable (A) the mortgage held by the  
 60 mortgagee shall be increased as contemplated in such judgment and  
 61 any junior lienholder's lien shall be deemed subordinated to such  
 62 mortgage, in the same order as existed prior to the subordination, ~~or~~  
 63 (B) the transfer contemplated in the transfer agreement shall be  
 64 effectuated. The mortgagor and mortgagee shall, thirty days after the  
 65 modification or transfer, submit the judgment of loss mitigation to the  
 66 town clerk for recording in accordance with title 7 of the general  
 67 statutes.

68 Sec. 5. (NEW) (Effective from passage) If the court does not enter a  
 69 judgment of loss mitigation, then the modification or transfer  
 70 contemplated by the mortgagor and mortgagee under section 2 or 3 of  
 71 this act shall not be consummated. In the event of such nonentry, (1)  
 72 the mortgagor may, if eligible, petition for inclusion in the foreclosure  
 73 mediation program set forth in sections 49-31k to 49-31o, inclusive, of  
 74 the general statutes, provided the mortgagor did not substantially  
 75 contribute to the events <sup>or circumstances</sup> leading to such denial, and the court (A) gives  
 76 consideration to any testimony or affidavits the parties <sup>shall</sup> submit in  
 77 support of or in opposition to such petition, and (B) finds <sup>may</sup> that (1) such

a finding that the mortgagor is eligible for such a judgment

or (C) the judge shall enter an order listing the reasons behind a decision not to subordinate the junior liens as contemplated in subsection (A)

in order to grant such petition

78 petition is <sup>not</sup> motivated primarily by a desire to delay entry of a judgment  
79 of foreclosure, and (ii) it is highly probable the parties will reach an  
80 agreement through mediation, and (2) the mortgagee shall have the  
81 right to request the entry of a judgment of foreclosure in accordance  
82 with the other provisions of law, including the provisions governing  
83 strict foreclosure.

84 Sec. 6. (NEW) (*Effective from passage*) Nothing in sections 2 to 5,  
85 inclusive, of this act shall be construed as eliminating the debt or any  
86 judgment associated with an affected junior lien.

87 Sec. 7. Subsection (a) of section 49-24b of the general statutes is  
88 repealed and the following is substituted in lieu thereof (*Effective from*  
89 *passage*):

90 (a) On and after January 1, 2015, a mortgagee who desires to  
91 foreclose upon a mortgage encumbering residential real property of a  
92 mortgagor shall give notice to the mortgagor by registered or certified  
93 mail, postage prepaid, at the address of the residential real property  
94 that is secured by such mortgage, in accordance with the relevant  
95 notice provisions of this chapter and chapter 134. No such mortgagee  
96 may commence a foreclosure of a mortgage prior to mailing such  
97 notice. Such notice shall advise the mortgagor of his or her  
98 delinquency or other default under the mortgage and that the  
99 mortgagor has the option to contact the mortgagee to discuss whether  
100 the property may, by mutual consent of the mortgagee and mortgagor,  
101 be marketed for sale pursuant to a listing agreement established in  
102 accordance with section 49-24d. Such notice shall also advise the  
103 mortgagor (1) of the mailing address, telephone number, facsimile  
104 number and electronic mail address that should be used to contact the  
105 mortgagee; (2) of a date not less than sixty days after the date of such  
106 notice by which the mortgagor must initiate such contact, with  
107 contemporaneous confirmation in writing of the election to pursue  
108 such option sent to the designated mailing address or electronic mail  
109 address of the mortgagee; (3) that the mortgagor should contact a real

110 estate agent licensed under chapter 392 to discuss the feasibility of  
 111 listing the property for sale pursuant to the foreclosure by market sale  
 112 process; (4) that, if the mortgagor and mortgagee both agree to proceed  
 113 with further discussions concerning an acceptable listing agreement,  
 114 the mortgagor must first permit an appraisal to be obtained in  
 115 accordance with section 49-24c for purposes of verifying eligibility for  
 116 foreclosure by market sale; (5) that the appraisal will require both an  
 117 interior and exterior inspection of the property; (6) that the terms and  
 118 conditions of the listing agreement, including the duration and listing  
 119 price, must be acceptable to both the mortgagee and mortgagor; (7)  
 120 that the terms and conditions of any offer to purchase, including the  
 121 purchase price and any contingencies, must be acceptable to both the  
 122 mortgagor and mortgagee; (8) that if an acceptable offer is received,  
 123 the mortgagor will sign an agreement to sell the property through a  
 124 foreclosure by market sale; and (9) in bold print and at least ten-point  
 125 font, that if the mortgagor consents to a foreclosure by market sale, the  
 126 mortgagor will not be eligible for foreclosure mediation in any type of  
 127 foreclosure action that is commenced following the giving of such  
 128 consent. The notice provided under this subsection may be combined  
 129 with and delivered at the same time as any other notice required by  
 130 subsection (a) of section 8-265ee or federal law. <sup>should</sup> If the mortgagor and  
 131 mortgagee by their mutual consent choose to enter into discussions  
 132 regarding the possibility of marketing the property pursuant to a  
 133 listing agreement established in accordance with section 49-24d, at any  
 134 point subsequent to the commencement of a foreclosure action,  
 135 nothing in this section, sections 1 to 6, inclusive, of this act or section  
 136 49-24e, as amended by this act, shall be construed as prohibiting the  
 137 parties from entering into such listing agreement.

138 Sec. 8. Subsections (a) and (b) of section 49-24e of the general  
 139 statutes are repealed and the following is substituted in lieu thereof  
 140 (*Effective from passage*):

141 (a) If a mortgagor executes a listing agreement that is acceptable to  
 142 both the mortgagee and mortgagor pursuant to section 49-24d and

143 receives an offer to purchase the residential real property that  
 144 encompasses a price, terms and conditions that are acceptable to both  
 145 the mortgagor and the mortgagee, the mortgagor shall execute a  
 146 contract for sale with the purchaser that shall reflect the agreed-upon  
 147 price, terms and conditions and be contingent upon the completion of  
 148 the foreclosure by market sale in accordance with sections 49-24 to 49-  
 149 24g, inclusive, as amended by this act, and sections 49-26 to 49-28,  
 150 inclusive, [ and 49-31t.] If an offer is received, but is unacceptable to  
 151 the mortgagee, the mortgagee shall provide the mortgagor with  
 152 written notice of its decision and, without limiting the breadth of its  
 153 discretion, a general explanation of the reason or reasons for such  
 154 decision. Such notice shall not be required in instances where the offer  
 155 is unacceptable to the mortgagor. The mortgagor shall, not later than  
 156 five days after the date of the execution of the purchase and sale  
 157 contract, provide the mortgagee with a copy of such contract along  
 158 with written documentation, in a form and substance acceptable to the  
 159 mortgagee, evidencing the mortgagor's consent to the filing of a  
 160 motion for judgment of foreclosure by market sale.

161 (b) Unless otherwise prohibited by applicable law, not later than  
 162 thirty days after the receipt of such contract and the documentation  
 163 evidencing consent, or not later than thirty days after the satisfaction  
 164 or expiration of any contingencies in the contract that must either have  
 165 been satisfied or expired before the foreclosure action may be  
 166 commenced to consummate the sale, whichever thirty-day time frame  
 167 is later, the mortgagee shall commence a foreclosure by writ, summons  
 168 and complaint. Any such complaint shall claim, in the prayer for relief,  
 169 a foreclosure of the mortgage pursuant to sections 49-24 to 49-24g,  
 170 inclusive, as amended by this act, and sections 49-26 to 49-28,  
 171 inclusive, [and 49-31t,] and shall contain a copy of the contract between  
 172 the mortgagor and the purchaser as well as a copy of the appraisal  
 173 obtained pursuant to section 49-24c. If the mortgagee, commenced a  
 174 foreclosure action <sup>or at</sup> prior to the time of such receipt, satisfaction or  
 175 expiration, then, not later than thirty days after the most recent receipt,

has already  
 latest of such

176 satisfaction or expiration, the mortgagee shall make a motion for  
177 judgment of foreclosure by market sale in accordance with the  
178 provisions of section 49-24f and attach the contract and appraisal to the  
179 motion. No mortgagee may require the employ or use of a particular  
180 list of persons licensed under chapter 392 as a condition of approval of  
181 an offer. No mortgagee may require the use of an auction or other  
182 alternative method of sale as a condition of approval of an offer once  
183 the listing agreement required pursuant to section 49-24d has been  
184 executed by the mortgagor. Nothing in this section shall be construed  
185 as requiring either the mortgagee or mortgagor to approve any offer  
186 that is made pursuant to this section.

187 Sec. 9. Section 49-24 of the general statutes is repealed and the  
188 following is substituted in lieu thereof (*Effective from passage*):

189 All liens and mortgages affecting real property may, on the written  
190 motion of any party to any suit relating thereto, be foreclosed (1) by a  
191 decree of sale instead of a strict foreclosure at the discretion of the  
192 court before which the foreclosure proceedings are pending, or (2)  
193 with respect to mortgages, as defined in section 49-24a, as amended by  
194 this act, that are a first mortgage against the property, by a judgment of  
195 foreclosure by market sale upon the written motion of the mortgagee,  
196 as defined in section 49-24a, as amended by this act, and with consent  
197 of the mortgagor, as defined in section 49-24a, as amended by this act,  
198 in accordance with sections 49-24a to 49-24g, inclusive, as amended by  
199 this act, and sections 49-26 to 49-28, inclusive, [, and 49-31t.]

200 Sec. 10. Section 49-24a of the general statutes is repealed and the  
201 following is substituted in lieu thereof (*Effective from passage*):

202 For purposes of a foreclosure by market sale in accordance with this  
203 section [,] and sections 49-24b to 49-24g, inclusive, as amended by this  
204 act: [, and section 49-31t:]

205 (1) "Mortgage" means a mortgage deed, deed of trust or other  
206 equivalent consensual security interest on residential real property

207 securing a loan made primarily for personal, family or household  
208 purposes that is first in priority over any other mortgages or liens  
209 encumbering the residential real property, except those liens that are  
210 given priority over a mortgage pursuant to state or federal law;

211 (2) "Mortgagee" means the owner or servicer of the debt secured by  
212 a mortgage;

213 (3) "Mortgagor" means the owner-occupant of residential real  
214 property located in this state who is also the borrower under the loan  
215 that is secured by a mortgage, other than a reverse annuity mortgage,  
216 encumbering such residential real property that is the primary  
217 residence of such owner-occupant, where the amount due on such  
218 mortgage loan, including accrued interest, late charges and other  
219 amounts secured by the mortgage, when added to amounts for which  
220 there is a prior lien by operation of law, exceeds the appraised value of  
221 the property; and

222 (4) "Residential real property" means a one-to-four-family dwelling  
223 occupied as a residence by a mortgagor.

224 Sec. 11. Subsection (b) of section 49-24b of the general statutes is  
225 repealed and the following is substituted in lieu thereof (*Effective from*  
226 *passage*):

227 (b) At any time after the date provided in the notice required under  
228 subsection (a) of this section, the foreclosure of the mortgagor's  
229 mortgage may continue without any further restriction or requirement,  
230 provided the mortgagee files an affidavit with the court stating that the  
231 notice provisions of said subsection have been complied with and that  
232 either the mortgagor failed to confirm his or her election in accordance  
233 with said subsection by the date disclosed in the notice or that  
234 discussions were initiated, but (1) the mortgagee and mortgagor were  
235 unable to reach a mutually acceptable agreement to proceed; (2) based  
236 on the appraisal obtained pursuant to section 49-24c, the property does  
237 not appear to be subject to a mortgage that is eligible for foreclosure by

238 market sale; (3) the mortgagor did not grant reasonable interior access  
 239 for the appraisal required by section 49-24c; (4) the mortgagee and  
 240 mortgagor were unable to reach an agreement as to a mutually  
 241 acceptable listing agreement pursuant to section 49-24d; (5) a listing  
 242 agreement was executed, but no offers to purchase were received; (6)  
 243 an offer or offers were received, but were unacceptable to either or  
 244 both the mortgagee and mortgagor; or (7) other circumstances exist  
 245 that would allow the mortgagee or mortgagor to elect not to proceed  
 246 with a foreclosure by market sale pursuant to sections 49-24 to 49-24g,  
 247 inclusive, as amended by this act, and sections 49-26 to 49-28,  
 248 inclusive, [and 49-31t,] or that would otherwise make the mortgage  
 249 ineligible for foreclosure by market sale. The affidavit required by this  
 250 subsection may be combined with the affidavit required by subsection  
 251 (b) of section 8-265ee.

252 Sec. 12. Section 49-31t of the general statutes is repealed. (*Effective*  
 253 *from passage*)

This act shall take effect as follows and shall amend the following sections:		
Section 1	<i>from passage</i>	New section
Sec. 2	<i>from passage</i>	New section
Sec. 3	<i>from passage</i>	New section
Sec. 4	<i>from passage</i>	New section
Sec. 5	<i>from passage</i>	New section
Sec. 6	<i>from passage</i>	New section
Sec. 7	<i>from passage</i>	49-24b(a)
Sec. 8	<i>from passage</i>	49-24e(a) and (b)
Sec. 9	<i>from passage</i>	49-24
Sec. 10	<i>from passage</i>	49-24a
Sec. 11	<i>from passage</i>	49-24b(b)
Sec. 12	<i>from passage</i>	Repealer section

**Statement of Purpose:**

To facilitate alternatives to foreclosure that are mutually agreeable to mortgagors and mortgagees with senior encumbrances.

*[Proposed deletions are enclosed in brackets. Proposed additions are indicated by underline, except that when the entire text of a bill or resolution or a section of a bill or resolution is new, it is not underlined.]*