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OHIO & KENTUCKY

The Chapter 13 Meeting of Creditors

United States Bankruptcy Court
Northern District of Ohio
7th Biennial Bench-Bar Retreat

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Holiday Inn, Independence

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I. General Benefits of Attending the 341 Meeting

Benefits gained from attendance at the initial meeting of creditors to be considered include:

- providing an opportunity to develop and finalize a foreclosure prevention alternative (such as a mortgage loan modification or repayment plan);
- having the ability to determine the debtor's intentions about a property and in Chapter 7 cases, the opportunity to have the debtor execute a reaffirmation agreement if he or she wants to retain the property;
- investigating whether there are grounds for objecting to the confirmation of a reorganization plan, questioning the feasibility of the plan, or investigating any potential fraud or "bad faith";
- presenting a Proof of Claim for consideration in the development of a reorganization plan and assessing the debtor's ability to reorganize;
- obtaining information about the receipt of rental income, if applicable; and
- being able to alert the trustee about deficiencies in a reorganization plan, prior filings involving the same collateral, or problems related to discharging the debt.

Whenever the debtor's answers to preliminary questions raised at the 341 Meeting of Creditors give rise to additional concern, the bankruptcy attorney should explore the possibility of obtaining an order from the bankruptcy court authorizing a broader examination of the debtor's financial affairs under Rule 2004 of the Federal Rules of Bankruptcy Procedure

II. Aspire to file Proofs of Claim prior to 341 Meeting

A. Statutory Requirements:

1. 11 U.S.C. §101(5). A claim is defined by the Code in Section 101(5) as a "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured." 11 U.S.C. § 101(5)(A). Section 101 also defines a claim as a right to an equitable remedy for breach of performance if such breach gives rise to a right of payment. 11 U.S.C. Section 101(5)(B).

2. 11 U.S.C. § 501. A creditor or an indenture trustee may file a proof of claim. If a creditor does not timely file a proof of such creditor's claim, an entity that is liable to such creditor with the debtor, or that has secured such creditor, may file a proof of such claim. If a creditor does not timely file a proof of such creditor's claim, the debtor or the trustee may file a proof of such claim.

3. 11 U.S.C. § 502(a). Provides that "a claim or interest, proof of which is filed under section 501 . . . is deemed allowed, unless a party in interest . . . objects."

4. 11 U.S.C. §502. If an objection to a claim is made, the court, after notice and a hearing, shall determine the amount of the claim. The grounds for disallowance of claims are listed in section 502(b), including the ground that a claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured. **Procedural defects are not listed as a ground for disallowing a claim**.

B. Amendments to the Federal Rules of Bankruptcy Procedure.

1. On April 26, 2011, the United States Supreme Court adopted amendments to Federal Rule of Bankruptcy Procedure Rule 3001(c), and approved new rule 3002.1. The rule amendments and new rule were transmitted to Congress in accordance with the Rules Enabling Act and took effect on December 1, 2011.
2. Summary of the 2011 Changes:

Amended Rule 3001(c) and new Rule 3002.1 impose upon creditors significantly increased burdens and requirements, particularly for those creditors with claims secured by a lien on an individual debtor's principal residence. The revisions to Rule 3001(c) set forth in greater detail the supporting information that now must be filed with a proof of claim. Rule 3002.1 deals with a Chapter 13 debtor's ability, under §1322(b)(5) of the Bankruptcy Code, to cure a default on a home mortgage loan and maintain payments.

3. Rule 3001. Proof of Claim (Effective December 1, 2011)

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(c) SUPPORTING INFORMATION.

(1) *Claim Based on a Writing*. When a claim, or an interest in property of the debtor securing the claim, is based on a writing, the original or a duplicate shall be filed with the proof of claim. If the writing has been lost or destroyed, a statement of the circumstances of the loss or destruction shall be filed with the claim.

(2) *Additional Requirements in an Individual Debtor Case; Sanctions for Failure to Comply*. In a case in which the debtor is an individual:

(A) If, in addition to its principal amount, a claim includes interest, fees, expenses, or other charges incurred before the petition was filed, an itemized statement of the interest, fees, expenses, or charges shall be filed with the proof of claim.

(B) If a security interest is claimed in the debtor's property, a statement of the

amount necessary to cure any default as of the date of the petition shall be filed with the proof of claim.

(C) If a security interest is claimed in property that is the debtor's principal residence, the attachment prescribed by the appropriate Official Form shall be filed with the proof of claim. If an escrow account has been established in connection with the claim, an escrow account statement prepared as of the date the petition was filed and in a form consistent with applicable nonbankruptcy law shall be filed with the attachment to the proof of claim.

(D) If the holder of a claim fails to provide any information required by this subdivision (c), the court may, after notice and hearing, take either or both of the following actions:

(i) preclude the holder from presenting the omitted information, in any form, as evidence in any contested matter or adversary proceeding in the case, unless the court determines that the failure was substantially justified or is harmless; or

(ii) award other appropriate relief, including reasonable expenses and attorney's fees caused by the failure.

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C. Top 10 Best Practices in filing proofs of claim

1. Think before you act. Use Good judgment – No form over substance.
2. Identify the proper Name of the Creditor aka the entity to whom the debtor owed money.
3. When filing initial proofs of claim, state the mortgage arrearage up to the date of the filing date of the bankruptcy petition, <u>unless the plan or trustee indicates otherwise</u>.
4. File Entry of Appearance and Request for Notice.
5. Comply with Local Rules. Attach the Court mandated worksheet.
6. No Non-public personal information included on filings
    - No social security numbers on Notes or Mortgages
    - Loan numbers redacted
7. Read and verify information before signing.
8. Itemize, Itemize, Itemize with the Goal of Transparency in mind.
9. Use Trustee Initiative Worksheet to review POCS and make sure in compliance with April 2009 Guidelines to Chapter 13 Trustees.
10. Have client perform escrow analysis.

D. U.S. TRUSTEE INITITATIVE MORTGAGE CLAIM REVIEW CHECKLIST

- o NAME(S) ON MORTGAGE DIFFER(S) FROM DEBTOR(S)' NAME(S)

- o ACCOUNT NUMBER NOT STATED ON CLAIM
- o COLLATERAL NOT IDENTIFIED
- o NO MORTGAGE INCLUDED WITH CLAIM
- o NO NOTE INCLUDED WITH CLAIM
- o MORTGAGE AND/OR NOTE DOES NOT CONTAIN INFORMATION REFLECTING A PERFECTED SECURITY INTEREST OR DEED BOOK/PAGE REFERENCE
- o NAME OF ACTUAL CREDITOR HOLDING THE MORTGAGE DOES NOT APPEAR ON THE CLAIM FACE
- o NAME OF CREDITOR ON CLAIM FACE IS NOT SUPPORTED BY THE DOCUMENTS ATTACHED TO THE CLAIM (NOTE, MORTGAGE, ASSIGNMENT OF CLAIM)

ARREARAGE

- o ARREARAGE NOT ITEMIZED
- o ARREARAGE FIGURE CONTAINS MATHEMATICAL ERROR(S)
- o PREPETITION ARREARAGE IS NOT AS OF FILING DATE OF BANKRUPTCY PETITION
- o POSTPETITION ARREARAGES ARE INCLUDED IN THE PREPETITION ARREARAGE CLAIM

COSTS/FEES

- o APPEARS TO HAVE EXCESSIVE FEES
- o FEES NOT ITEMIZED
- o FEES/COSTS APPEAR TO BE THROUGH A DATE OTHER THAN THE PETITION FILING

PAYMENT ISSUES

- o CURRENT MONTHLY PAYMENT NOT PROVIDED OR NOT ITEMIZED
- o PRINCIPAL BALANCE IS NOT STATED
- o INTEREST RATE NOT STATED

ESCROW ISSUES

- o CLAIM INCLUDES ESCROW ADVANCE(S) WHILE STATED MORTGAGE PAYMENT DOES NOT APPEAR TO INCLUDE ESCROW COMPONENT

III. National Association of Chapter Thirteen Trustee's Best Practices

A. The NACTT Mortgage Committee is comprised of Chapter 13 trustees, mortgage servicers, mortgagees and creditors' counsel. The committee's mission is to foster communication between the parties, resolve differences and to recommend best practices of conduct for all stakeholders with the goal to improve the bankruptcy system.

B. Best Practices for Trustees and Mortgage Servicers in Chapter 13

1. If servicers/mortgagees include a flat fee cost in the proof of claim for review of the Chapter 13 plan prior to confirmation and for the preparation of the proof of claim, it should be reasonable and fairly reflect the attorney's fee incurred.

2. If servicers/mortgagees include attorney fees for pursuing relief from stay, such fees should be clearly identified as well as how such fees are to be paid in any agreed order resolving a Motion for Relief from Stay or any other matter before the court.

3. Servicers/mortgagees should analyze the loan for escrow changes upon the filing of a bankruptcy case and each year thereafter. A copy of the escrow analysis should be provided to the debtor and filed with the Bankruptcy Court by the servicers/mortgagee or their representative each year.

4. Servicers/mortgagees should not include any pre petition cost or fees or pre petition negative escrow in any post petition escrow analysis. These amounts should be included in the pre-petition claim amount unless the payment of such fee or cost was actually made by the servicer.

5. Servicers/mortgagees should attach a statement to a formal notice of payment change outlining all post petition contractual costs and fees not previously approved by the court and due and owing since the prior escrow analysis or date of filing whichever is later. This statement need not contain fees, costs, charges and expenses that are awarded or approved by the Bankruptcy Court order. In absence of any objection or challenge to such fees, the trustee should take appropriate steps to cause such fees to be paid as part of Debtor's Chapter 13 plan.

6. Servicers/mortgagees should supply and maintain a contact for debtor's counsel and trustee's for the purpose of restructuring, modifying a mortgage, or other loss mitigation assistance including a short sale or deed in lieu of foreclosure. The contact should be an individual or group with the ability to implement or assess with objective criteria a loss mitigation modification after filing of a chapter 13 petition with the goal of keeping the Debtor in the house and the success of the bankruptcy.

7. Servicers/mortgagees should provide a dedicated phone line and contact for Chapter 13 Trustee inquiry use only.

8. Servicers/mortgagees should monitor post petition payments. If the mortgage is paid post petition current then the servicers/mortgagees should not seek to recover late fees. No late fees should be recovered or demanded for systemic delay but should be limited to actual debtor default.

9. Pre petition payments should be tracked as applied to pre petition arrears, post petition payments should be tracked as applied to post petition ongoing mortgage payments.

10. Servicers/mortgagees should file a notice and reason of any payment change with the court and provide same to the Debtor

11. Servicers/mortgagees are required to file with court a notice of any protective advances made in reference to a mortgage claim, such as non escrow insurance premiums or taxes. Such notice should be provided to the debtors and filed with the court.

12. Servicers/mortgagees should review the Trustee web site or NDC for payment discrepancies with their system prior to the filing of a Motion for Relief from Stay in Trustee pay jurisdictions.

13. Servicers/mortgagees should review the Trustee web site or NDC at the close or discharge of the bankruptcy for payment discrepancies with their system in Trustee pay jurisdictions.

14. Servicers/mortgagees should clearly identify if the loan is an escrowed or escrowed loan and break out the monthly payment consisting of Principal, Interest, Escrow and PMI components.

15. Servicers/mortgagees should identify nontraditional mortgage loans in their proof of claims. Loans with options should identify on the proof of claim the type of loan as well as the various contractual payment options available during the bankruptcy to the borrower/Debtor.

16. Trustees should initiate a communication with mortgage servicers when questions arise in a review of a post petition escrow analysis.

17. United States Trustees and Trustee Education Network should modify the requirements of the financial management class regarding adjustable rate mortgages, the calculation of mortgage escrows and, in particular, the potential of increased mortgage payments resulting from increased taxes, interest rate hikes and/or mortgage premiums.

18. Trustee voucher checks, check stubs or vouchers provided with any other form of payment contain the following information, except to the extent prevented from doing so by local rule:

    a. The Name of the debtor and case number.

    b. The trustee's claim number.

    c. The mortgagee's account number (to the extent provided on the proof of claim).

    d. If the mortgagee account number is not available, e.g. not contained on the proof of claim, at least one other piece of identifying information e.g., property address.

    e. The amount of the payment.

    f. Whether the payment is for the ongoing mortgage payment or the mortgage arrearage.

g. If for the mortgage arrears, the balance owing on the arrears claim after application of the payment.

h. If the trustee has set up a separate claim for post-petition charges of the mortgagee, that the voucher clearly identify that fact.

i. If any portion of the payment on arrears is intended to pay interest on the mortgage arrears, the amount of that interest portion of the payment.

j. If the mortgage is to be paid off during the bankruptcy under the confirmed plan through payments by the trustee, e.g., a total debt claim, the portions of each payment which represent principal and interest, and the balance owing on the claim after application of the payment.

19. There is a movement among servicers to redact all but the last four numbers of the mortgagors' loan numbers on proofs of claim, because those claims are public records. While mortgage servicers in general want as much information as possible on the vouchers, the mortgage servicers on the Working Group felt that if the voucher had the bankruptcy case number, the name of the debtor and the redacted loan number from their filed claim, they would be able to post the payment. Using the account number to the extent provided in a filed proof of claim also insures that trustees are not disclosing information on their website that is not already disclosed in the public record.

20. Voucher Narrative re Payments**:** The Working Group places particular emphasis on f. above. The voucher should identify if a payment is for the regular mortgage payment or for the mortgage arrearage in consistent language. While Chapter 13 trustee disbursement applications focus on the claims to be paid, mortgage servicer computer systems focus on their mortgagor account number. Posting of receipts, whether or not the account is in bankruptcy, is typically handled by a Cash Processing group or department of the mortgage servicer. Those departments focus on the account number on the voucher and the narrative on the voucher for that account number to determine if the payment is for the regular mortgage payment or the mortgage arrearage.

21. Mortgage Arrearage Claims: When filing their initial proofs of claim, mortgage servicers should state their mortgage arrearage up to the date of the filing date of the bankruptcy petition, unless the plan or trustee indicates otherwise, or local rule provides otherwise. The Chapter 13 Trustee will use the mortgage arrearage claim to set up the arrearage balance on the claim, which in turn will show up as the "balance" on the voucher check, absent objection to the claim.

IV. LEGAL INTERESTS AND MODIFICATION OF SECURITIZED LOANS

A. Note and Mortgage Basics

A promissory note is usually a negotiable instrument, which provides the person entitled to enforce the note the right to payment of the obligation it represents. OHIO REV.CODE §§ 1303.03, 1303.31; see also U.C.C. §§ 3-104, 3-301 (2002). Article 3 governs negotiable instruments – it defines what a negotiable instrument is and defines how ownership of those pieces of paper is transferred. See § 3-104(a) ("an unconditional promise or order to pay a fixed amount of money, with or without interest . . . .").

A person is entitled to enforce a note when that person falls into one of the following categories (note: a "person" under OHIO REV.CODE § 1301.01 "includes an individual or an organization." See also U.C.C. § 1-201 (2002)):

1. "The holder of the instrument." ORC §1303.31(A)(1) [UCC 3-301].

    a. In order to demonstrate that it is a "holder" of a note payable to a third party, a party must show that the note was "negotiated." §1303.21(A); See also UCC 3-201. Negotiation of a note may be effectuated by: (1) either a blank indorsement or a special indorsement, and (2) transfer of possession. *See,* ORC §§1303.21(B), 1303.24 (UCC § 3-204), and 1303.25 (UCC § 3-205).

       Once a note is endorsed, its negotiation is complete upon transfer of possession. OHIO REV.CODE §§ 1303.24(A)(1)(a), 1303.21(A); see also U.C.C. §§ 3-204, 3-201 (2002). The transfer of possession requires physical delivery of the note "for the purpose of giving the person receiving delivery the right to enforce the instrument." OHIO REV.CODE §§ 1303.22(A) and cmt. 1, 1301.01(N); see also U.C.C. §§ 3-203 cmt. 1, 1-201 (2002). However, "... possession alone does not establish that the party [in possession of a note] is entitled to receive payments under it." Citizens Fed. Sav., 78 Ohio App.3d at 287.

       A note may be endorsed by an allonge, which is a paper "affixed to the instrument," which then becomes part of the instrument. OHIO REV.CODE § 1303.24(A)(2); see also U.C.C. § 3-204 (2002); Adams v. Madison Realty Dev., Inc., 853 F .2d 163, 167 (3d Cir.1988) (discussing why an endorsement written on a separate piece of paper must be affixed to the note). An allonge may be subject to challenge if it is not "so firmly affixed to the instrument as to become an extension or part of it." *See,* ORC §1303.22, official comment (UCC 3-203).

2. A non-holder in possession of the instrument who has the rights of a holder."

ORC §1303.31(A)(2); See also UCC § 3-301. A person may be entitled to enforce a negotiable instrument if it has possession of the note without proper endorsement(s); however, proof that the person has rightful possession is required. OHIO REV.CODE § 1303.22, cmt. 1; see also U.C.C. § 3-203, cmt. 1.

a. This includes a person that acquired the rights of a holder by transfer of the note without any indorsement; thus, a person may acquire the status of a holder (including the holder's right to enforce) by acquiring the instrument from a holder. §1303.22; See also UCC § 3-203 and 22 Richard A. Lord, *Williston on Contracts* §60:36 (4th ed. 2008).

b. Certain other persons not in possession of the note, *e.g.*, situations where the note has been lost, stolen, or destroyed. ORC §§1303.31(A)(3) (UCC 3-301) and 1303.38 (UCC 3-309).

3. The corresponding right to foreclose the mortgage lien – Once a party establishes that it is entitled to enforce the note, that party is automatically entitled to enforce (often times foreclosure) the corresponding mortgage, because "a transfer of the note by the owner, as to vest legal title in the indorsee, will carry with it equitable ownership of the mortgage." Kernohan v. Manss (1895), 53 Ohio St. 118, 133, 41 N.E. 258; see, also, U.S. Bank Nat'l Ass'n v. Marcino, 7th Dist. No. 08 JE 2, 2009-Ohio-1178, ¶53 ("[v]arious sections of the Uniform Commercial Code, as adopted in Ohio, support the conclusion that the owner of a promissory note should be recognized as the owner of the related mortgage.").

B. Securitization

1. Securitized transactions date back to the early 1970s and were the sales of pooled mortgage loans by the Government National Mortgage Association (Ginnie Mae). These transactions were followed by the Federal Home Loan Mortgage Corporation (Freddie Mac) and Federal National Mortgage Association (Fannie Mae) in the early 1980s. In connection with securitization, the word "security" does not mean what it traditionally might have meant under corporate laws or commerce: a secured instrument. The word "security" here means a financial claim which is generally manifested in form of a document, its essential feature being marketability. To ensure marketability, the instrument must have general acceptability as a store of value. Hence, it is generally either rated by credit rating agencies, or it is secured by charge over substantial assets. Further, to ensure liquidity, the instrument is generally made in homogenous lots.

2. The entity that securitizes its assets is called the **originator**: the name signifies the fact that the entity was responsible for originating the claims that

are to be ultimately securitized. There is no distinctive name for the investors who invest their money in the instrument and they are simply called **investors**.

3. **Ownership of Securitized Loans.** In any mortgage securitization, ownership of the loans or receivables (or in securitization terminology, the "collateral") is separated from the lender that accumulated the collateral pool (often called the "sponsor" of the securitization) in order to protect investors in the event of a bankruptcy of the sponsor. In order to reach this result, the sponsor typically sells the collateral (e.g., the mortgage loans) to a special-purpose subsidiary (often called the "depositor"), which in turn conveys ownership to a trustee of a trust. The trust is established to issue fixed-income securities, to cause the loans to be serviced, and to make payments to the security holders funded solely from collections on the loans. The security holders have no interest in the underlying loans. They are secured creditors of the trust; the loans are the collateral for the trusts obligations; and the trustee owns the collateral.

4. **Mortgage-Backed Securities ("MBS").** Each mortgage securitization trust generally issues several classes of MBS which are designed to represent different degrees of risk, and as a result, pay different rates of interest. The ratings agencies assign credit ratings to the different MBS classes, which may range, say, from AAA (or equivalent) down through several lower-rated classes, to an unrated, not publicly-issued lowest class (call it "C"). The ratings are based largely on two general areas of risk considerations. The first consists of the characteristics of the underlying loans and the projections of likelihood of default and prepayment in the loan pool. The second area consists of the respective rights of the different classes of MBS, as established in the trust documents, in terms of priority of (a) distribution of cash and (b) allocation of the losses (typically incurred whenever a loan is liquidated in foreclosure).

   a. Cash Distribution Priorities. Mortgage securitization trust documents usually provide an order of priority for the distribution of the cash collected by the servicer each month. Basically that order is:

      1. To reimburse the servicer's out-of-pocket advances, and to the servicer's fee, which is a percentage of the interest portion of the payments actually collected by the servicer in that month;
      2. To pay in full the payments due to holders of the Class AAA bonds;
      3. To pay the next-lower class of MBS-holders their monthly distributions in full; and so on down each MBS class (e.g., AA, A, BBB, BB, C) in order.

b. **Loss Allocation Priorities.** **S**ecuritization documents typically allocate loan losses in reverse order of priority from the bottom up. Thus, losses are applied 100% to Class C until all of the C-class securities have been reduced to zero, then to Class B, and so on. If all losses were allocated pro-rata across all of the securities issued by the trust, then all of the MBS would carry the same degree of risk, and hence the same interest rate and credit rating.

C. Loan Modification

1. From the perspective of MBS holders, a modification that reduces the interest rate has the effect of reducing the trust's cash receipts, compared to what would have been received had the mortgage note been collected according to its original terms. That lowest-class security would receive monthly distributions reduced, for the remainder of the life of the modified mortgage, by an amount equal to the amount of reduction in that particular borrower's monthly payment.

2. **Contractual Terms- Pooling and Servicing Agreement.** The contract governing the servicer's obligations to the securitization trustee, are governed by the "pooling and servicing agreement." The pooling and servicing agreement contains express provisions addressing the servicer's ability to grant loan modifications. While some variations exist, the pooling and servicing agreement are standardized for the most part. Most securitizations are structured to be what the Internal Revenue Code defines as a "Real Estate Mortgage Investment Conduit" ("REMIC") and must adhere to the requirements of REMIC statutes in order to avoid risking tax consequences. While the REMIC regulations generally restrict substitution and significant modification of loans, a safe harbor in the regulations permits modifications that are "<u>occasioned by default or a reasonably foreseeable default</u>". More restrictive variations occasionally occur: some agreements may raise the threshold to a requirement that default be at least "imminent," and occasionally a provision placing an overall cap–such as 5% of the securitized pool–on the number of loans that the servicer may modify under any circumstance.

D. Loss mitigation and Bankruptcy

1. Borrowers in bankruptcy are increasingly requesting loan modifications. A servicer-offered modification can reduce a fixed rate, fix an adjustable interest rate, extend the term of the note, and capitalize outstanding delinquencies and fees. Further, the US Treasury Department, as it continues to revamp the Home Affordable Modification Program (HAMP), now encourages "principal write-downs" on loans.

2. **Welcome to Bankruptcy Letter** - One of the best methods to initiate action to process modifications on active Bankruptcy loans is to prepare a loss mitigation

letter/package to send to Debtor's counsel at the outset of the Bankruptcy Case. Such a letter or package will detail the various workout options that may be available to the Debtor, should he or she qualify. The loss mitigation letter may be sent concurrently with, or after sending, a Proof of Claim, Motion for Relief from Stay or other Bankruptcy filing. Sending such a letter is much more successful in the Bankruptcy context as often times the borrower is represented by legal counsel for the first time.

3. **Chapter 7 Cases**

In a chapter 7 proceeding, the debtor's property becomes property of the bankruptcy estate; and the chapter 7 trustee has control of the property to sell, dispose, or abandon as she deems in the best interest of creditors. A loan modification may be done in a chapter 7 case. An abandonment of the property from the trustee and relief from the automatic stay is desirable before the finalization of a loan modification. After all, modifying a loan secured by a piece of real property that the Trustee intends to administer is futile. The loan modification can also be incorporated into a reaffirmation agreement where the changed or modified terms would be set forth. Official Bankruptcy Forms B240A/B ALT (Form 240A/B ALT) (Reaffirmation Agreement) (04/10) provide opportunities for modified loan terms.

In most jurisdictions, a loan modification may also be done after a discharge of the debts. The key to remember in this instance is that the loan modification **cannot** reimpose personal liability upon the borrower. The loan modification needs to specifically recognize the discharge and indicate that the modification is not obligating the borrower personally on the debt. With respect to HAMP modifications, if the Debtor has received a chapter 7 bankruptcy discharge and did not reaffirm the mortgage debt, the following language must be inserted in the Home Affordable Modification Agreement:

> "I was discharged in a chapter 7 bankruptcy proceeding subsequent to the execution of the Loan Documents. Based on this representation, Lender agrees that I will not have personal liability on the debt pursuant to this Agreement."

4. **Chapter 13 Cases**

In Ohio's bankruptcy courts, loss mitigation can take place at any time during the bankruptcy case. If borrowers are in the HAMP trial payment period when the bankruptcy is filed, it might not be finalized prior to plan confirmation, so some courts have been continuing the confirmation hearing to allow for completion of the HAMP process. Plan confirmation most often occurs within 60 to 75 days of the petition filing. Under this approach, the plan that is ultimately confirmed and the budget that is filed are accurate, and represent the current financial snapshot of the debtor. Where the court will not continue confirmation, the plan must comply with the Bankruptcy code (e.g. provide for cure of the arrearage and maintenance of post-

petition payments).

5. Many of the Courts in Ohio and across the country are still working through the logistics of the best way to effectuate loss mitigation in a Bankruptcy. Arguably, Court approval is needed in all Bankruptcy cases. An example of what some Courts want to take place in a Chapter 13 case can be found in the requirements instituted by the Chapter 13 Trustee in Cincinnati where the Trustee wants the Debtors to prepare/file:

   - "proposed" motion to modify plan;
   - amended schedules I & J (evidencing the proposed budget);
   - the above documents along with Application to Incur Debt, so that the Trustee can make an informed decision regarding the loan modification; and
   - a proposed Loan Modification Agreement and/or documentation evidencing the proposed Loan Modification must be submitted with the Application to Incur debt, otherwise the Application to Incur Debt may be denied by the Trustee.

   Further, in many instances, a Motion to Approve Loan Modification is advisable before finalizing loan-modifications as often times, the entry of an order granting such a Motion, coupled with an Amended Proof of Claim, allows a Chapter 13 Trustee to discontinue payments on a creditor's pre-petition arrearage claim and in certain jurisdictions, discontinue post-petition conduit payments.

V. The National Mortgage Settlement

A. Overview and Highlights of the National Mortgage Settlement

1. On February 9, 2012, the Attorney General announced that the federal government and 49 states (Borrowers from Oklahoma will not be eligible for any of the relief directly to homeowners because Oklahoma elected not to join the settlement) had reached a settlement agreement with the nation's five largest mortgage servicers to address mortgage servicing, foreclosure, and bankruptcy abuses (the "National Mortgage Settlement"):

- Ally/GMAC
- Bank of America
- Citi
- JP Morgan Chase
- Wells Fargo
  - On March 5, 2014, the CFPB announced a Consent Judgment with the largest nonbank mortgage loan servicer in the country, Ocwen Financial Corporation, and

its subsidiary, Ocwen Loan Servicing. It also covers two companies previously purchased by Ocwen, Litton Loan Servicing LP and Homeward Residential Holdings LLC (previously known as American Home Mortgage Servicing, Inc. or AHMSI). The consent order required that Ocwen follow the servicing standards set up by the 2012 National Mortgage Settlement with the five largest banks.

- On December 8, 2014, the CFPB announced a Consent Judgment with SunTrust Mortgage, Inc., which also requires that SunTrust follow the servicing standards set up by the 2012 National Mortgage Settlement.

Loans owned by Fannie Mae or Freddie Mac are not impacted by this settlement.

The settlement provides benefits to borrowers whose loans are owned by the settling banks as well as to many of the borrowers whose loans they service.

On April 4, 2012, the United States District Court for the District of Columbia entered orders approving the settlement. The National Mortgage Settlement settles certain state and federal investigations relating to mortgage servicing abuses including abuses in the bankruptcy process.

The settlement provides as much as $25 billion in relief to distressed borrowers and direct payments to states and the federal government. It is the largest multistate settlement since the Tobacco Settlement in 1998.

General information concerning the National Mortgage Settlement including settlement documents, general FAQs, and other important documents can be found at:

www.nationalmortgagesettlement.com

2. The settlement makes important progress in the following areas, according to the National Consumer Law Center:

- Establishing strong standards for how mortgage servicers handle loan modifications, including requiring a review of a loan modification application prior to initiation of any foreclosure. Setting limitations on abusive fees and charges, including late fees, title and appraisal fees, and forceplaced insurance;
- Providing some principal reductions to struggling homeowners, including those in lower-income areas and communities of color;
- Preserving a homeowner's right to defend a foreclosure against mortgage company and servicer abuses.
- Forbidding waiver of claims in the loan modification context; and
- Allowing homeowners to pursue independent litigation against mortgage servicers for abusive acts.

The settlement **does not**:

- Release any criminal liability or grant any criminal immunity.
- Release any private claims by individuals or any class action claims.
- Release claims related to the securitization of mortgage backed securities that were at the heart of the financial crisis.
- Release claims against Mortgage Electronic Registration Systems or MERSCORP.
- Release any claims by a state that chooses not to sign the settlement.
- End state attorneys general investigations of Wall Street related to financial fraud or the financial crisis.

3. Timing of Settlement Relief

- March 1, 2012: Loan modifications can receive credit
- October 3, 2012: All servicing standards implemented

4. Servicing Standards

The Banks must implement extensive new mortgage servicing standards, **including provisions specific to borrowers in bankruptcy**.

Joseph A. Smith, Jr., Monitor of the National Mortgage Settlement, announced on October 2, 2012 that the five banks participating in the Settlement are now required to be in full compliance with the agreement's 304 servicing standards, or rules that guide their interaction with consumers. In response to this deadline, he released the following statement:

> ***"Today is the 180th day since the entry of the consent judgments comprising the National Mortgage Servicing Settlement. As of today, the five banks subject to the Settlement are required to operate in full compliance with its servicing standards. I will conduct careful and thorough reviews of the banks' processes to assure and verify that they are compliant with the Settlement's rules."***

The servicing standards require, among other things:

• A single point of contact at each Bank for borrowers in bankruptcy, who want information or assistance when they fall behind on their mortgage payments;

• New processes to ensure that the Banks provide accurate information about the amount those borrowers in bankruptcy owe on their mortgages;

• Better dispute resolution processes;

• Clear itemization of the principal, interest, fees, expenses and other charges incurred prior to bankruptcy that the Banks claim in bankruptcy cases;

• Prompt posting of payments and proper designation of pre-and post- petition payments and charges;

• Timely disclosure of fees, expenses, and charges incurred after a ` borrower files for

chapter 13 bankruptcy.

a. Accuracy of Filed Documents

- All pleadings, proofs of claim, affidavits, sworn statements, and declarations filed in judicial foreclosure or bankruptcy cases, and in notices of default or sale in non-judicial foreclosures, must be:
    - "accurate and complete and are supported by competent and reliable evidence"

- If proof of claim or stay relief motion in case pending before Settlement contains materially inaccurate information, servicer must:
    - file an amended claim or motion, at servicer's expense, within 30 days of acquiring knowledge of the inaccuracy
    - not collect any attorney fees or other charges for preparation or submission of proof of claim or motion for relief that is later withdrawn or denied as a result of a "substantial misstatement" as to the amount due

b. Affidavits, Sworn Statements, and Declarations Must:

- Be based on personal knowledge or reliance on business records as allowed under the Federal Rules of Evidence
- Not contain false or unsubstantiated information, but statements based on information and belief are allowed if so stated
- Accurately identify affiant/declarant by name, employer, and title
- Be signed BY HAND and dated (signature stamps and other mechanical signatures prohibited except for electronic filing)

c. Proofs of Claim

- Servicers required to attach to proof of claim the "Loan Documents," which include:
    - original or duplicate of note, including all indorsements;
    - a copy of any mortgage or deed of trust (including, if applicable, evidence of recordation in applicable land records); and
    - copies of any assignments of mortgage or deed of trust required to demonstrate the right to enforce the borrower's note under applicable state law

- **Servicers must also attach to proof of claim:**
    - affidavit if note has been lost or destroyed
    - **statement setting forth basis for asserting that applicable party has right to foreclose**
        - must have procedures to ensure servicer or foreclosing entity has "documented enforceable interest" in note and mortgage under state law, or is otherwise a proper party to the foreclosure action
    - Official Form 10 (Attachment A) as required by Bankruptcy Rule 3001(c)(2)(C)

        - must comply with all other requirements in Rule 3001

d. Motions for Relief from Stay

<u>Motion must:</u>

- Include “Loan Documents” or state that they are attached to a filed proof of claim
- State the basis for the moving party’s right to foreclose
- Disclose whether debtor is being evaluated for a loss mitigation option
- Disclose terms of any trial period or permanent loan modification plan pending at time of motion
- Motion shall have attached an affidavit, sworn statement or declaration setting forth:
    - whether there are any prepetition or post-petition defaults
    - if default, a description of any default, and a detailed itemization of all amounts owed, the prepetition and post-petition arrearages, and each fee or charge applied to such pre-petition amount or post-petition amount; and
    - an up-to-date statement of all amounts claimed and the amount necessary to cure any default

e. Federal Rules of Bankruptcy Procedure

- Settlement imposes sanction separate from that available under Bankruptcy Rule 3002.1(i):
    - if servicer fails to provide payment change notice as required by Rule 3002.1(b), servicer shall waive and not collect any late charge or other fees imposed solely as a result of the borrower’s failure to timely make the changed payment
    - If servicer fails to timely provide notice of fees, as required by 3002.1(c) and Rule 3002.1(g), the fees are deemed waived and may not be collected from the borrower
        - exception for “independent charges” - fees paid by servicer that are authorized by borrower or advanced by servicer for taxes, HOA fees, liens or insurance

f. Payment Application in Ch. 13 Cases.

- Servicers must ensure prompt and proper application of payments made on prepetition arrearage and post-petition payment amounts
- Debtor is to be treated as being current so long as making payments in accordance with confirmed plan and any later effective payment change notices
- Throughout the case, servicer is required to update its records to reflect payments made during case and waiver of any fee as required under Settlement

5. Loss Mitigation During Bankruptcy.

a. Servicer may not deny any loss mitigation option to eligible borrowers on the basis that the borrower is a debtor in bankruptcy so long as borrower and any trustee cooperates in obtaining any appropriate approvals or consents.

b. Servicer shall, to the extent reasonable, extend trial period loan modification plans as necessary to accommodate delays in obtaining bankruptcy court approvals or receiving full remittance of debtor's trial period payments that have been made to a chapter 13 trustee. In the event of a trial period extension, the debtor must make a trial period payment for each month of the trial period, including any extension month.

c. When the debtor is in compliance with a trial period or permanent loan modification plan, Servicer will not object to confirmation of the debtor's chapter 13 plan, move to dismiss the pending bankruptcy case, or file a MRS solely on the basis that the debtor paid only the amounts due under the trial period or permanent loan modification plan, as opposed to the non-modified mortgage payments.

d. Transfer of Servicing of Loans Pending for Permanent Loan Modification.

- Ordinary Transfer of Servicing from Servicer to Successor Servicer or Subservicer.
  - At time of transfer or sale, Servicer shall inform successor servicer (including subservicer) whether a loan modification is pending.
  - Any contract for the transfer or sale of servicing rights shall obligate the successor servicer to accept and continue processing pending loan modification requests.
  - Any contract for the transfer or sale of servicing rights shall obligate the successor servicer to honor trial and permanent loan modification agreements entered into by prior servicer.
- Transfer of Servicing to Servicer.
  - When Servicer acquires servicing rights from another servicer, Servicer shall ensure that i.t will accept and continue to process pending loan modification requests from the prior servicer, and that it will honor trial and permanent loan modification agreements entered into by the prior servicer.

6. Compensation to Borrowers

Approximately $1.5 billion of the settlement funds will be allocated to compensation to borrowers who were foreclosed on after January 1, 2008 and before Dec. 31, 2011. The National Mortgage Settlement Administrator will mail Notice Letters and Claim Forms in late September through early October 2012 to those borrowers who lost their home due to foreclosure between January 1, 2008 and December 31 2011 and whose loans were serviced by one of the five mortgage servicers that are parties to the settlement. Debtor may be eligible to receive a payment of at least $840.00 as part of the National Mortgage Settlement. This estimated payment amount is based on 100% of all eligible borrowers

submitting claim forms, and therefore the payment you receive will very likely be higher.

a. Are these cash payments under the settlement property of the bankruptcy estate?

General Rule: Cash payments for acts occurring both pre- and post-petition become property of the Chapter 13 Bankruptcy Estate.

B. Frequently Asked Questions

1. Can borrowers in bankruptcy participate in the Settlement and receive financial assistance from other sources?

Yes. Borrowers, **including borrowers in bankruptcy**, may participate in the programs offered under the Settlement and other programs. For example, borrowers may be eligible for a separate restitution process administered by the federal banking regulators, including the Office of the Comptroller of the Currency (the "OCC"). For more information about the federal banking regulator claims process, please visit www.independentforeclosurereview.com or call 1-888-952-9105.

2. How does the Settlement address the Banks' filings in bankruptcy courts going forward?

The Settlement imposes new standards on the Banks to ensure the accuracy of information they provide to bankruptcy courts. These standards are designed to ensure that the Banks provide accurate information about the amount that borrowers in bankruptcy owe on their mortgages.

Moreover, under the new servicing standards, the Banks must implement better dispute resolution processes. If a Bank files inaccurate or misleading documents in a bankruptcy case, a borrower can use these new procedures and make a complaint with the Bank.

In addition, with respect to proofs of claim and certain affidavits attached to documents filed in bankruptcy courts, the Banks must correct any significant inaccuracies promptly and also provide notice of the correction to the affected borrower or counsel to the borrower.

3. What kind of information must the Banks provide concerning a mortgage when a borrower files for bankruptcy?

For a borrower in a chapter 13 (repayment) case, if a Bank files a proof of claim, the Bank must include an accurate and clear statement of exactly what the Bank claims the borrower owes. That statement must itemize the principal, interest, fees, expenses, and other charges that the Bank claims is owed as of the filing of the bankruptcy case.

4. How does the Settlement affect how the Banks apply mortgage payments made by borrowers in bankruptcy or a trustee?

The Banks must promptly post payments received from a borrower or trustee while a borrower is in bankruptcy and accurately designate payments between any arrearage owed before the bankruptcy filing and what is owed for regular mortgage payments after the filing. The Banks must also reconcile accounts, including funds held in suspense accounts, at the end of each bankruptcy case and update their records so they are consistent with the account reconciliation.

5. How does the Settlement affect what the Banks charge after a borrower files for bankruptcy?

The Banks must timely disclose fees, expenses, and charges incurred after a borrower files a chapter 13 bankruptcy case. A Bank waives fees, expenses, and charges of which the Bank has not given timely notice to the Borrower. The Banks must also timely give notice to a borrower of any changes in payments the borrower will have to make due to, for example, interest rate adjustments or changes in the escrow amount.

6. Should a trustee administering the case of a borrower in bankruptcy seek to recover funds received by the borrower under the Settlement?

The United States Trustee Program will not seek to compel a trustee to recover payments that the trustee, in the exercise of discretion, decides not to recover. Eligible borrowers in bankruptcy may receive payments from the Banks as a part of the Settlement. A trustee should consider all relevant circumstances when deciding whether to seek turnover of the payments in a particular case. Factors to consider include:

- The payment amount and any interest of a non-debtor spouse or other person in the payment;
- The cost of recovering and administering the payment, including litigation with a borrower in bankruptcy who may seek a judicial determination regarding whether the funds are subject to administration;
- The extent to which recovering the payment will enable creditors to receive a meaningful distribution; and
- The applicability of state and federal exemptions.

7. How does the Settlement affect the trustees' review of the Banks' proofs of claim?

Generally, the Settlement will not alter a trustee's review of claims filed by the Banks. Importantly, however, the United States Trustees Program insisted that each Bank create a toll-free hotline, staffed by employees with special training in bankruptcy, that chapter 13 trustees can use to resolve issues related to the Banks' claims. More information on these hotlines will be provided as the Banks establish them.

If a trustee concludes, based on a review of a Bank's bankruptcy filings, that a Bank violated the Settlement, the trustee should contact the United States Trustee's office in the jurisdiction in which the case was filed.

C. General Loss Mitigation provisions under the Servicing Standards

These requirements are intended to apply to both government-sponsored and proprietary loss mitigation programs and shall apply to subservicers performing loss mitigation services on servicer's behalf.

1. Servicer shall be required to notify potentially eligible borrowers of currently available loss mitigation options prior to foreclosure referral. Upon the timely receipt of a complete loan modification application, Servicer shall evaluate borrowers for all available loan modification options for which they are eligible prior to referring a borrower to foreclosure and shall facilitate the submission and review of loss mitigation applications. **The foregoing notwithstanding, Servicer shall have no obligation to solicit borrowers who are in bankruptcy**.

2. Servicer shall, offer and facilitate loan modifications for borrower rather than initiate foreclosure when such loan modifications for which they are eligible are net present value (NPV) positive and meet other investor, guarantor, insurer and program requirements.

3. Servicer shall allow borrowers enrolled in a trial period plan under prior HAMP guidelines (where borrowers were not pre-qualified) and who made all required trial period payments, but were later denied a permanent modification, the opportunity to reapply for a HAMP or proprietary loan modification using current financial information.

4. Servicer shall promptly send a final modification agreement to borrowers who have enrolled in a trial period plan under current HAMP guidelines (or fully underwritten proprietary modification programs with a trial payment period) and who have made the required number of timely trial period payments, where the modification is underwritten prior to the trial period and has received any necessary investor, guarantor or insurer approvals. The borrower shall then be converted by Servicer to a permanent modification upon execution of the final modification documents consistent with applicable program guidelines, absent evidence of fraud.

5. Dual Track Restricted-if a borrower has not already been referred to foreclosure, Servicer shall not refer an eligible borrower's account to foreclosure while the borrower's complete application for any loan modification program is pending if Servicer received (a) a complete loan modification application no later than day 120 of delinquency, or (b) a substantially complete loan modification application (missing only any required documentation of hardship) no later than day 120 of delinquency and Servicer receives any required hardship documentation no later than

day 130 of delinquency.

6. Servicer shall not make a referral to foreclosure of an eligible borrower who so provided an application until:

a. Servicer determines (after the automatic review) that the borrower is not eligible for a loan modification, or

b. If borrower does not accept an offered foreclosure prevention alternative within 14 days of the evaluation notice, the earlier of (i) such 14 days, and (ii) borrower's decline of the foreclosure prevention offer.

c. If borrower accepts the loan modification resulting from Servicer's evaluation of the complete loan modification application referred to in paragraph IV.B. 1 (verbally, in writing (including e-mail responses) or by submitting the first trial modification payment) within 14 days of Servicer's offer of a loan modification, then the Servicer shall delay referral to foreclosure until (a) if the Servicer fails timely to receive the first trial period payment, the last day of timely receiving the first trial period payment, and (b) if the Servicer timely receives the first trial period payment, after the borrower breaches the trial plan.

d. If the loan modification requested by a borrower is denied, except when otherwise required by federal or state law or investor directives, if borrower is entitled to an appeal, Servicer will not proceed to a foreclosure sale until the later of (if applicable):

- expiration of the 30-day appeal period; and
- if the borrower appeals the denial, until the later of (if applicable) (i) if Servicer denies borrower's appeal, 15 days after the letter denying the appeal, (ii) if the Servicer sends borrower a letter granting his or her appeal and offering a loan modification, 14 days after the date of such offer (iii) if the borrower timely accepts the loan modification offer (verbally, in writing (including e-mail responses), or by making the first trial period payment), after the Servicer fails timely to receive the first trial period payment, and (iv) if the Servicer timely receives the first trial period payment, after the borrower breaches the trial plan.

7. Servicer shall ensure timely and accurate communication of or access to relevant loss mitigation status and changes in status to its foreclosure attorneys, bankruptcy attorneys and foreclosure trustees and, where applicable, to court-mandated mediators.

8. Single Point of Contact.

Servicer shall establish an easily accessible and reliable single point of contact ("SPOC")

for each potentially-eligible first lien mortgage borrower so that the borrower has access to an employee of Servicer to obtain information throughout the loss mitigation, loan modification and foreclosure processes.