

The State of Foreclosure in the State of Florida

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How Did We Get Here and Where Are We Going?

A whopping 9,000 Americans are losing their homes to foreclosure each day. At the beginning of the crisis, based on then-anticipated subprime and Alt A interest rate resets, analysts predicted an aggregate 2 million Americans would lose their homes. Initially, interest rate resets were the single largest predictor of frequency for new foreclosure filings. Once the crisis spread to other areas in our economy, however, unemployment (i.e., people not being able to pay their mortgage due to lack of income), value reductions (i.e., people defaulting and walking away due to being underwater in their property), and the credit crunch (i.e., inability to refinance) became more significant influencers in the frequency of foreclosures. The most unique thing about Florida foreclosures is the sheer volume of new cases and number of borrowers underwater. As we will discuss, Florida is also among the first states on a statewide bases, along with Ohio, to explore (and in some judicial circuits implement) mandatory mediation. Unless and until the Florida Supreme Court adopts uniform standards, each Judicial Circuit will employ its own processes and procedures as long as they are in conformance with applicable statutes, federal, and case law.

Since then, what began as more or less an isolated subprime mortgage crisis has, of course, expanded into our nation's broader economy, eroding credit, depreciating property and other asset values, increasing unemployment, and decimating consumer confidence, spending and ultimately GDP. The result so far? The total number of homes lost is now anticipated to reach as many as 6 million with another 2 million Americans ending up underwater and an aggregate \$4 million in home equity lost forever.

For purposes of discussion here, we will focus on the defense of residential foreclosures in Florida.

Statistic released confirm that Florida is among the top four states leading the nation, along with California, Nevada, and Arizona, in the number of foreclosures. Perhaps the biggest difference between these now infamous states and others was the high percentage of speculative investing due to their collective geographic predisposition toward second homes, retirement buyers, and/or vacation rentals. Because of this "artificial demand," prices

in these locations and the number of units being added to supply rose more dramatically during the bubble than in other less sexy places. Price and supply-demand will accordingly take longer and endure more severe correction, often resulting in more foreclosures, before stabilizing. Those properties were most prevalent in areas like Miami-Dade, which is among the top foreclosure hotspots within the state of Florida; 75 percent of the county's new cases filed each month are foreclosures. Still, experts predict most markets will begin to recover, or at least stop deteriorating further, toward the end of 2009. And already we are starting to see increased demand among first time homeowners, in part because of pent-up demand, low interest rates, attractive prices, the \$8,000 credit, and because as long as you buy right, it still makes more sense to own than to rent.

The Basics

Foreclosure is a legal procedure with roots going back to English common law pursuant to which a lender takes title to a parcel of real estate following a borrower's failure to comply with a mortgage loan agreement entered into with the lender. The most frequent failure is a default in payment under the promissory note, but in some cases, particularly commercial loans, defaults under other agreement terms are common. For example, a developer default may be triggered if multiple buyers of the units the developer planned to build for resale cancel their purchase contracts or an anchor tenant reneges on their lease, or if the construction involves too many changes, runs over budget, or takes longer than the agreed time frame for completion or an existing shopping center or office building loan default may be triggered if tenant vacancy rate rises above a preset level.

Which Foreclosure Theory Does Your State Follow?

Foreclosure processes vary, depending upon whether your state uses mortgages or deeds of trust for financing real estate.

- Those states using mortgages generally conduct judicial foreclosures, effectuating the foreclosure via the state's court system. These are also referred to as lien theory states since a mortgage grants a mortgagee a lien, as opposed to title or some other interest, in the real estate.

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- Those using deeds of trust utilize out-of-court, non-judicial, procedures defined by state law. Also referred to as trustee or title theory, in these states, title to the financed real estate is essentially held by a trustee until the loan is repaid.
- Some use a hybrid of both.

Non-judicial foreclosures tend to proceed more quickly than judicial foreclosures, but each state has its own laws or statutes setting forth the exact amount of time within which each step in the process may and must be completed. Current anticipated and actual time frames will, of course, also be impacted by how busy the courts are at any given time.

The Judicial Foreclosure Process in a Nutshell

The attorney for a mortgagee (lender) in a judicial foreclosure typically initiates a lawsuit against the mortgagor (borrower) by filing a complaint and a *lis pendens* (lawsuit pending notice) with the clerk of the court for the county in which the property is located.

The complaint will reflect the alleged default, if monetary, how much money is owed, and why mortgagee should be allowed to foreclose and must be delivered to the mortgagee in accordance with the state laws which typically require service by a process server or, if that is not possible, by publication. The complaint must name and be served on anyone with an interest in the real estate as a defendant.

The *lis pendens* is also recorded in the local public records to give the public (potential buyers and lenders) notice that a lawsuit is now pending against the property.

While judicial circuits are exploring the possibility of requiring the parties to attempt mediation before proceeding with foreclosure litigation, for the time being in most jurisdictions, once a mortgagor has been served, he has three basic options:

1. Do nothing, in which case the mortgagee's attorney will request and the judge will likely grant, a default judgment and set a date for the sale (discussed below); or

2. File an answer to the complaint with no real affirmative defenses (reasons why what the mortgagee claims the alleged default should not be treated as such) and no counterclaims (allegations of wrongdoing against the mortgagee), in which case the mortgagee's attorney will request and the judge will likely grant a summary judgment (essentially agreeing that there is no issue to discuss and therefore no reason for further hearings) and order the foreclosure sale; or
3. File an answer to the complaint with realistic affirmative defenses and/or counterclaims, in which case the judge will likely set a date for a hearing during which each party will present their case and the judge may rule in favor of the mortgagee granting a sale, in favor of the mortgagor oftentimes dismissing the case, or that further discovery and hearings with the judge will be needed in order for him to make a decision.

Discovery is the legal process by which each side is allowed an opportunity to gather information about the facts surrounding the case from the other side and third parties (such as witnesses) before starting a trial. There are several different types of discovery. For example, interrogatories are written questions one side gives to the other to respond to, also in writing. Requests for production are written requests one side gives the other to produce various documents and information. And depositions are questions one side asks the other (or third parties such as witnesses), which are documented word-for-word by the court reporter. One or more of the parties may subpoena an individual to appear and testify.

When the judge orders the foreclosure sale, a writ will be issued authorizing the foreclosure sale (sometimes referred to as a sheriff's sale). Foreclosure sales, conducted in an auction format, are open to the public, and are generally held in a public place such as on the courthouse steps or in front of the property. State laws vary with regard to payment methods and time frames, but generally require cash or a substantial deposit to be paid prior to a person being allowed to bid at a foreclosure sale and the balance to be paid later that day or, in some states, within thirty days. The highest bidder will, of course, become the owner of the property, and receive a certificate

of title subject to the mortgagor and junior lien holder redemption rights and the judge's confirmation of the sale, after which a clerk's deed (sometimes referred to as a sheriff's deed) will be recorded in the county public records vesting title to the property in the highest bidder. If the owner or a tenant is still occupying the property, eviction steps may then be necessary.

The right to pay off the mortgage being foreclosed and own the property will also vary by state. The time allowed to redeem foreclosed property varies from state to state from zero days all the way up to almost a year and obviously has a big impact on how long a mortgagor can stay in his home as well as the potential risk and expense involved in foreclosures for both mortgagees and for foreclosure investors.

Most judgments granting foreclosure will include provision for reimbursement of the mortgagee's attorney fees and other costs incurred in connection with the foreclosure.

The Non-Judicial Foreclosure Process in a Nutshell

In contrast, deeds of trust, used in non-judicial states, contain a power-of-sale clause enabling the trustee to initiate a foreclosure sale without having to file a lawsuit or otherwise go to court as is required in states that adhere to the judicial theory for foreclosures. Typically, the trustee must first issue a notice of default informing the trustor (borrower). Some non-judicial states also require that a notice of default be recorded in the local public records.

As is the case in judicial foreclosure states, the trustor has three basic options;

1. Do nothing, in which case the trustee will likely begin taking necessary steps to sell the property;
2. Respond with no real defenses or allegations against the lender; or,
3. Respond with realistic answers and allegations against the lender.

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Assuming the trustee moves forward, again depending on the state's specific laws, a notice of sale may be mailed to the trustor, posted in public places, recorded in the local public records, or published in local legal publications. After the legally required period has expired, a public auction will be held. Again with the highest bidder becoming the owner of the property subject to the redemption period and receipt of a deed. Auctions of non-judicial foreclosures will generally require cash, or cash equivalent at the sale, or very shortly thereafter. The various non-judicial foreclosure states have different procedures. For example, some do not require a notice of default, but start with a notice of sale. Others require only the publication of the notice of sale to announce the sale, with no direct owner notification required.

A chart indicating which states follow the judicial foreclosure theory and which follow the non-judicial theory is included for your convenience.

Judicial v. Trustee or Non-Judicial By State

State	Security Instrument	Foreclosure Type	Initial Step	# of Months	Redemption	Deficiency
Alabama	Mortgage	Non-judicial	Publication	1	12 MM	Allowed
Alaska	Trust Deed	Non-judicial	Notice of Default	3	None	Allowed
Arizona	Trust Deed	Non-judicial	Notice of Sale	3	None	Allowed
Arkansas	Mortgage	Judicial	Complaint	4	None	Allowed
California	Trust Deed	Non-judicial	Notice of Default	4	None	Prohibited
Colorado	Trust Deed	Non-judicial	Notice of Default	2	75 DD	Allowed
Connecticut	Mortgage	Strict	Complaint	5	None	Allowed
Delaware	Mortgage	Judicial	Complaint	3	None	Allowed

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Dist. of Col.	Trust Deed	Non-judicial	Notice of Default	2	None	Allowed
Florida	Mortgage	Judicial	Complaint	5	None	Allowed
Georgia	Security Deed	Non-judicial	Publication	2	None	Allowed
Hawaii	Mortgage	Non-judicial	Publication	3	None	Allowed
Idaho	Trust Deed	Non-judicial	Notice of Default	5	None	Allowed
Illinois	Mortgage	Judicial	Complaint	7	None	Allowed
Indiana	Mortgage	Judicial	Complaint	5	3 MM	Allowed
Iowa	Mortgage	Judicial	Petition	5	6 MM	Allowed
Kansas	Mortgage	Judicial	Complaint	4	6-12 MM	Allowed
Kentucky	Mortgage	Judicial	Complaint	6	None	Allowed
Louisiana	Mortgage	Exec Process	Petition	2	None	Allowed
Maine	Mortgage	Judicial	Complaint	6	None	Allowed
Maryland	Trust Deed	Non-judicial	Notice	2	None	Allowed
Massachusetts	Mortgage	Judicial	Complaint	3	None	Allowed
Michigan	Mortgage	Non-judicial	Publication	2	6 MM	Allowed
Minnesota	Mortgage	Non-judicial	Publication	2	6 MM	Prohibited
Mississippi	Trust Deed	Non-judicial	Publication	2	None	Prohibited
Missouri	Trust Deed	Non-judicial	Publication	2	None	Allowed
Montana	Trust Deed	Non-judicial	Notice	5	None	Prohibited
Nebraska	Mortgage	Judicial	Petition	5	None	Allowed

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Nevada	Trust Deed	Non-judicial	Notice of Default	4	None	Allowed
New Hampshire	Mortgage	Non-judicial	Notice of Sale	2	None	Allowed
New Jersey	Mortgage	Judicial	Complaint	3	10 DD	Allowed
New Mexico	Mortgage	Judicial	Complaint	4	None	Allowed
New York	Mortgage	Judicial	Complaint	4	None	Allowed
North Carolina	Trust Deed	Non-judicial	Notice Hearing	2	None	Allowed
North Dakota	Mortgage	Judicial	Complaint	3	60 DD	Prohibited
Ohio	Mortgage	Judicial	Complaint	5	None	Allowed
Oklahoma	Mortgage	Judicial	Complaint	4	None	Allowed
Oregon	Trust Deed	Both	Publication	6	365	Allowed
Pennsylvania	Mortgage	Judicial	Complaint	3	None	Allowed
Rhode Island	Mortgage	Non-judicial	Publication	2	None	Allowed
South Carolina	Mortgage	Judicial	Complaint	6	None	Allowed
South Dakota	Mortgage	Judicial	Complaint	3	180 DD	Allowed
Tennessee	Trust Deed	Non-judicial	Publication	2	None	Allowed
Texas	Trust Deed	Non-judicial	Publication	2	None	Allowed
Utah	Trust Deed	Non-judicial	Notice of Default	4	None	Allowed

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Vermont	Mortgage	Judicial	Complaint	7	None	Allowed
Virginia	Trust Deed	Non-judicial	Publication	2	None	Allowed
Washington	Trust Deed	Non-judicial	Notice of Default	4	None	Allowed
West Virginia	Trust Deed	Non-judicial	Publication	2	None	Prohibited
Wisconsin	Mortgage	Judicial	Complaint	Varies	None	Allowed
Wyoming	Mortgage	Non-judicial	Publication	2	3 MM	Allowed

Foreclosure Alternatives Including the Voluntary Repossession

During the course of a judicial or non-judicial foreclosure, various workout alternatives including a short sale, modification, refinance, forbearance, cash for keys, or a deed-in-lieu of foreclosure, bankruptcy, mediation or voluntary repossession may become relevant.

Statistics available distinguishing foreclosures on primary residence verses other property types are questionable since it is well known that many borrowers lied on their loan application to obtain a primary residence, as opposed to an income property or second home mortgage, since primary residence loans tend to carry lower interest rates, presumably due to the lower risk of a borrower defaulting, and typically require less down payment for the same reason. This is one of the reasons it can be difficult to determine with any real certainty what foreclosure defense strategies or alternatives are statistically most often employed for various property types. Whatever the statistics currently are, they will no doubt shift as the commercial real estate market becomes an increasingly bigger part of the foreclosure problem.

While some homestead property owners do employ a voluntary repossession strategy such as deed-in-lieu of foreclosure, or cash for keys, these foreclosure alternatives tend to be more comfortably accepted in the context of commercial real estate, income properties, or second homes.

One reason is, of course, the fact that emotions tend to run higher when a borrower's home is involved. In contrast, the decision-making process involving foreclosure of non-homestead properties tends to be more about pure business and what makes the most economic sense.

Homeowners also tend to think ahead less and be less proactive in addressing the foreclosure of their home, sometimes seemingly preferring to bury their heads in the sand, in comparison to commercial property, income property and second home owners, perhaps in part because they are embarrassed or perhaps less sophisticated and therefore simply unaware of the alternatives.

In the case of cash for keys, for a variety of reasons, most lenders will discuss the option only if the borrower brings it up, rendering that genre of voluntary repossession significantly less common at this point in time. Certainly, many homeowners do not appear to realize a voluntary repossession may enable them to buy a new home again sooner than allowing the foreclosure to proceed.

The fact that both refinance and loan modification qualification criteria for each property type differ no doubt influences the strategy options available to distressed property owners. And now that Uncle Sam has brought a seat up to the table, the bailout options and other programs available for one property type verses others have been magnified even further. For the most part, the administration's goals have seemed to focus on keeping people in their homes and, in fact, are sometimes subsidized at the expense of income property and second home owners.

Renting a property to cover at least part of the mortgage payment and other expenses is also a more viable option for second or vacations homes than it is for primary residences. Presumably, second homes and vacation properties are located in more popular areas, in terms of attracting seasonal or vacation rental tenants, can generate more revenue and, of course, are not occupied by the owner all of the time and hence do not require the owner to relocate or otherwise greatly disrupt his or her home and family life.

On a primary residence, unless the lender has a temporary post-foreclosure rental program in place, agreeing to a deed-in-lieu of foreclosure, or cash for keys, requires a homeowner to find another place to live, whereas in the

case of an income property or vacation home, a voluntary repossession involves relatively minor impact on daily family, friends, and neighbors.

The Special Importance of Preliminary New Foreclosure Case Review

Generally, the best-case scenario for borrower's counsel is of course to get the case settled before racking up litigation costs and putting the client through the emotional foreclosure litigation wringer. Creating a downside for lender or lender's counsel from day one can be at least, if not more, effective than well plead affirmative defenses and counterclaims. A preliminary review of all cases from the perspective of the initial transaction table, loan funding, assignment(s), pooling and securitization, may very well reveal serious flaws that unfortunately occurred at a much higher frequency given the high volume of closings that occurred during the real estate bubble, at each of these stages.

Some of the Traditional and More Current Borrower Foreclosure Defenses and Counterclaims

The evidence and arguments lenders put forth in foreclosure cases of course depend upon the default and other factors involved but we know will always strive to support the alleged borrower default, most often in residential foreclosure cases today a monetary default. To dispute the evidence and arguments being put forth by lenders, borrower's foreclosure defense counsel are literally doing whatever it takes. For example, alleging:

- That the borrower did not receive the lender's default and acceleration notice, or that the notice received was somehow faulty.
- That the borrower did not get some other legally required notice(s) or disclosure, either at closing or as part of the foreclosure, or that the notice the borrower received contained incorrect or incomplete information or was not properly delivered to all obligors.
- That the HUD-1 Settlement Statement contained inaccurate, incomplete, or improper information.
- That one of the many other possible TILA or HOEPA violations occurred. For example: During the real estate bubble, some amortized loan originators seem to have developed the habit of

moving fees which should have appeared on the TIL Disclosure under "Finance Charge" to instead appear under "Amount Financed," perhaps, practitioner speculate, to avoid inclusion in the APR and give the appearance of a lower cost loan.

- That lender's counsel failed to attach the original note, failed to properly name an indispensable party, failed to state a cause of action, or one of the many other allegations we've seen often over the years such as failure of a condition precedent, tortious interference, or unclean hands.
- That the lender failed to correctly apply a loan payment or imposed excessive or impermissible charges. For example, especially high inspection fees or forced place insurance that cost significantly more than what the homeowner was paying for insurance purchased on his own.
- That there was an improper or incomplete assignment of the mortgage, or that the assignment was not completed before the commencement of the foreclosure action. Some courts will automatically dismiss such cases with prejudice.
- That lender's counsel sent pleadings directly to the borrower, as opposed to borrower's counsel, even after learning the borrower was represented by counsel. Some courts will sanction lender's counsel for doing so.

New arguments emerge daily. An interesting line of defense currently developing in response to the practice of lenders' foreclosure counsel naming all unknown spouses, tenants, and heirs as defendants in a foreclosure case is the allegation by borrowers' foreclosure defense counsel that this long-accepted practice in truth unnecessarily drives up costs (since costly attempts at service of process are made on parties who oftentimes do not even exist). The purpose of this practice is, of course, to make sure that in cases in which such people do exist, the foreclosure is not delayed for failure to name them and provide notice. Unfortunately, if lenders' foreclosure counsel are required to first verify whether or not such unknown parties actually exist prior to attempting to serve them, doing so may require actually sending someone to the property to inquire, adding even more to the cost. This is however, an excellent example of the creative arguments emerging from the borrower's residential foreclosure defense "camp" everyday.

And the Winner is...TILA and HOEPA Violations

TILA (Truth in Lending Act, 15 U.S.C. § 1601 *et seq.*) and HOEPA (Pub. L. No. 103-325, an amendment to TILA crafted to provide additional protections for borrowers of high-cost loans including subprime mortgage loans) violations are particularly troubling for lenders nowadays since if properly pleaded, they allow a borrower to rescind the mortgage loan or, as is more often the case (since rescission requires return of the mortgage loan money, an impossibility for most borrowers) to utilize the right to rescind the mortgage loan as leverage in negotiating a modification.

If a mortgage loan is rescinded, it essentially becomes an unsecured debt. In other words, the mortgage lien on the home no longer exists but the borrower is still obligated to repay the mortgage loan amount borrowed under the promissory note, minus possible credits, which we will discuss shortly. More specifically, if, for example, the TILA disclosure in a RESPA refinance was not provided within three days of the loan closing or was incorrect or incomplete, the borrower may have cause to rescind the loan for up to three years from the closing date!

Sometimes the news for borrower-clients gets even better. TILA provides for penalties for lender TILA violations that may be credited against the amount a borrower has to tender and repay. For example, a potential \$2,000 penalty may be imposed against a lender for failing to disclose information on the TILA notice, or for failing to rescind a loan when properly requested. Under other circumstances, the lender may be held liable for a refund of loan costs, closing costs and/or mortgage payments, all of which can be credited against mortgage loan amount required to be tendered in repayment. And attorney fees and costs are all statutory in TILA cases. What's more, HOEPA protections, which provide for even more penalties, may also apply if aggregate loan costs exceeded 8 percent of the original mortgage loan amount, which allows for even more penalties. For example, under HOEPA, if a borrower is entitled to rescind a mortgage loan, a lender may be penalized for each of the following: prepayment penalty, default interest, negative amortization, among other features.

In short, borrower's foreclosure defense counsel are pulling a lot of old tricks and some new ones out of their proverbial hats to delay residential foreclosures on behalf of their clients.

The Commercial Real Estate Market between a Rock and a Hard Place

Since the latest buzz is about doom and gloom in the commercial real estate market, which will of course translate to an increase in commercial foreclosures, a word about them is appropriate. Since commercial mortgage loans typically carry five to ten year maturity dates, the commercial market has been most threatened by the credit crunch, reduced consumer confidence, decreased spending and GDP, and increased tenant vacancy rates, which together make refinancing virtually impossible when the mortgage loans mature. The CMBS market itself is a \$900 billion industry with securitized or conduit debt coming in at a higher 60 percent of the commercial mortgage loan market. Through 2009, \$400 billion commercial mortgage loans will mature and another \$1.4 trillion between 2010 and 2012. But issues of affordable new CMBS products are extremely hard to come by. Securitized CMBS or MBS, particularly those held in REMIC trusts, but also any subject to restrictive pooling and servicing agreements, involve added challenges for legal practitioners because of the restrictions placed on work-out options, including modifications, contained in the pooling and servicing agreements, and IRS Section 860A and 860G REMIC trust provisions discussed in more detail below. So essentially commercial mortgage loans are maturing, there are no affordable refinance options and the loans cannot be modified. We knew all along there would be surprises as these SPV's played out their natural and unnatural lives. But even the surprises are surprising some commercial real estate borrowers who had no idea what they were getting themselves into. This is a significant issue considering that U.S. commercial real estate is a \$6.5 trillion industry with 4 billion square feet in office space, 13 billion square feet in industrial space, 9.5 billion square feet in shopping space, 4.4 million hotel rooms, and 33 million square feet in rental apartments. The impact that tremors in such a large industry can potentially have on the broader economy is tremendous. For example, shopping centers alone account for \$2.25 trillion in sales and \$125 billion in state sales tax and 40 percent of local government taxes come from commercial real estate in general.

CMBS PSAs and REMIC Trusts

Many securitized commercial mortgages are owned by a trust that elects treatment, for tax purposes, as a pass through real estate mortgage

investment conduit, or "REMIC" under I.R.C. §§ 860A through G. The trusts typically hold a pool of commercial mortgages; a typical pool might contain one hundred different loans. The Code imposes a variety of restrictions on REMIC trusts, which unknowing borrowers are discovering as they approach their lenders for commercial loan work-outs. For example, unlike CDOs, the REMIC mortgage pool has to be "static," in other words, the trust cannot trade loans in and out of the pool. And a significant loan modification, such as one a borrower might ask for as part of a loan workout, could be considered a loan "substitution" under the Code, which would effectively terminate the REMIC status, causing the trust to be taxed as a corporation with a 100 percent "prohibited transaction" tax. Substantial modifications would include changes in yield, timing for payment, obligors, co-obligors, security/credit enhancement, or debt instrument priority, and would most certainly not be agreed to by the servicer. An important exception may apply if the original loan documents contemplated such future modifications in anticipation of a borrower's future actions. Commercial mortgage loan documents should therefore be carefully reviewed by borrower's commercial real estate foreclosure counsel for these provisions. There are likewise certain modifications that typically fall under the REMIC radar, and there is generally more flexibility for a loan that is in default or at risk of default.

Among the primary documents involved in REMIC trusts is, of course, the PSA (Pooling and Servicing Agreement). The parties to the PSA are the depositor (the entity that sells the mortgage loans to the trust), the master servicer, the special servicer, and the trustee. The PSA will include a "servicing standard" that must be followed, and obligates the servicer to maximize investor recovery on the loan to the CMBS certificate holders on a present value basis. The PSA may grant the master servicer less authority over loan assumptions and modifications than would otherwise be allowed by the REMIC rules for performing loans. The PSA may also require approval from others, such as ratings agencies that play an important role in assumptions and modifications that may affect the flow of payments from the underlying real estate. Master servicers may therefore be required by the PSA to consult with the ratings agency and even required to obtain a "no downgrade letter" if any serving action might affect rating. A legal opinion might also be required to insure REMIC status is not impacted. When REMICs are involved, commercial real estate borrowers may deliberately

default to try to circumvent the REMIC restrictions or file bankruptcy, in hopes that a judge will grant relief from the REMIC structure.

Some of the factors involved in analyzing a CMBS default from the lender view include:

- Cause of default, property business aspects, financial operating statements, management capabilities, other factors that could be affecting the property.
- Rights under loan documents, right to replace management, control cashflow/lockbox, control budgets, approve leases, other collateral such as letters of credit, reserves, or guarantees.
- Legal remedies; foreclosure, appointment of receiver, activation of assignment of leases, etc.
- Possibility of consensual remedies such as a debt restructuring and forbearance, sale or property, refinance or paydown.
- Leverage can be accomplished by way of cash management/lockbox (hard or soft or springing), assignment of leases, initiating foreclosure to trigger receivership, involuntary bankruptcy, etc., but risks include potential lender liability, mortgagee in possession, tenants withholding rent or vacating, etc.

The CMBS servicer often has a big impact on workouts. Within the master servicing organizations, there is often a division of servicing functions such as monitoring of payments, escrow analysis, financial statement review, reserve advancement, etc. Once in default, the loan is sent to a special servicer with expertise in loan work-outs and often a financial interest in the CMBS trust that owns loans, thereby creating more of an alignment of economic interests (for that particular owner, but not perhaps for others). On the other hand, as the new guy on the scene, the special servicer often has limited background knowledge or history of the loan, collateral, or borrower.

CMBS borrowers are almost always bankruptcy remote. They are entities set up for the sole purpose of owning and operating a certain piece of real estate. They have restrictions in their organizational documents precluding them from engaging in any other kind of business or incurring any other debt and keeping them separate from any affiliates. They may also have

separate directors. The purpose is to minimize the chances that the borrower will file bankruptcy. And if he does, the mortgage lender will probably be the only significant creditor. This means the lender has more leverage in workouts and bankruptcy negotiations.

Commercial mortgage loan lenders are running into some of the following issues, much to borrower benefit:

- The loan assignment documents are improper, meaning the loan was not correctly assigned to the trust.
- The loan file itself may be incomplete.
- There may be a conflict of interest between the servicer and the trust.
- Bankruptcy remote is not necessarily bankruptcy proof.

Other Challenges Common to Commercial Foreclosures

Oftentimes commercial foreclosures cases are further complicated by a wide variety of other factors such as multiple borrowers, property owners or guarantors and multiple loans, conflicting inter-creditor agreements, and multiple participants in the various loans, many of whom cannot even be identified. The type of breach can also complicate a foreclosure litigation, with monetary breaches on a fully matured note absent any lender liability or interference being the least complicated. Likewise, the status of the project can add to the challenges. For example, partially completed construction projects oftentimes involve entitlements that may be expiring, unit buyers suing for the return of deposits that have been spent and to cancel their contracts, associations that cannot afford to pay their expenses, construction defects or potential ensuing successor developer liability, municipalities angry about code violations, contractors with liens, and a litany of other stumbling blocks.

What Do You Get When You Cross One Judge with 5,000 New Foreclosure Cases?

In general, the fact that judges in Florida are so overwhelmed by the large volume of residential foreclosure cases on their dockets has perhaps had the single biggest influence on the court's predisposition to those cases. More

specifically, judges are allowing far less leeway for unprepared attorneys, homeowners who wait until a foreclosure sale date is being set to respond to the existence of a foreclosure case in the first place, and strategies seemingly designed merely to delay the case where no legitimate issue of fact or law exists. That given, although, as we will discuss, delay can play a vital role in foreclosure defense, relatively speaking it is more important than ever to do whatever is needed to position a case so that all issues can be resolved as quickly as possible, and judges today are more prone than before to refuse to rule on cases “piecemeal” particularly if they can save time in the long and short run by requiring the parties to wait and have all issues resolved at once. Likewise, judges today are far less forgiving than they once may have been of lender’s or borrower’s counsel who cause delay by not following procedure or responding to opposing parties in a timely manner.

Some cases that may be of interest include:

Nationstar Mortgage, LLC v. Willie E. Knox and Linda M. Knox

United States Court of Appeals, Fifth Circuit, No. 08-60887

Issue: Mortgage Lending

Brief, filed December 22, 2008

Marion Johnson and Vivian Johnson v. D and D Home Loans, et al.

United States Court of Appeals, Fourth Circuit, No. 08-1421

Issue: Mortgage Lending

Brief, filed July 14, 2008

Jackson, et al., on behalf of themselves and all others similarly situated v. Mortgage Electronic Registration Systems Inc., and Stanek, Sheriff of Hennepin County

Minnesota Supreme Court, No. A08-397

Issue: Mortgage Lending

Brief, filed June 2, 2008

Moua vs. Rand

United States Court of Appeals, Eighth Circuit, No. 07-2544

Issue: Mortgage Lending

Brief, filed October 15, 2007

Cuomo v. The Clearing House Association LLC (Appeal)

United States Supreme Court, No. No. 08-453

Issue: Mortgage Lending

Amicus Brief, filed March 4, 2009

The Clearing House Association L.L.P. v. Cuomo (Motion for rehearing en banc)

United States Court of Appeals, Second Circuit, No. 05-5996

Issue: Mortgage Lending

Amicus Brief, filed February 8, 2008

Watters v Wachovia Bank

U.S. Supreme Court, No. 05-1342

Issue: Mortgage Lending

Amicus Brief, filed September 1, 2006

Also, over the course of the past year, many judges who once allowed telephonic appearance are no longer allowing such hearings.

Looking Ahead, Mandatory Mediation

Among the most significant and recent evolution is mandatory mediation. The primary drive behind mandatory mediation is, of course, the huge backlog of court cases. As we've mentioned, Florida is already well along the road to mandatory mediation in residential real estate foreclosure cases. Ohio has been doing it for some time and other states are following suit. Some hope this will save homes, shorten the foreclosure process, and alleviate the strain on court dockets and resources for other types of cases. Statewide Florida foreclosures are currently taking an average of 300 days to complete; twice the prior average timeframe.

The following summary of the current status of mandatory mediation in various Florida judicial circuits is provided courtesy of the Collins Center.

1st Circuit, Escambia, Santa Rosa, Okaloosa and Walton Counties –
Effective March 17, 2008 with implementation on April 1, 2008, all owner-occupied residential foreclosure actions must file Form "A" with the action

9th Circuit, Orange and Osceola Counties – Effective February 25, 2009, at option of the court, a foreclosure case may be referred for mediation. At the time plaintiff/lender files foreclosure, defendant/homeowner must be served with a form notice providing lender contact information for loan workout department and notice of homeowner's right to mediation. Orange County Bar provides a list of certified mediators. Plaintiff pays cost of mediation at \$275 for two hours and \$100 per hour thereafter, with one-half of the cost recoverable.

11th Circuit, Miami-Dade County – Effective May 1, 2009, upon filing a homestead residential foreclosure action the plaintiff/lender must include a fee for \$750 payable to the Collins Center. Failure to pay the fee results in dismissal without prejudice. When the Collins Center receives the fee, they have 30 days to find the homeowner/defendant to “substantiate the foreclosure action and advise of availability of financial counseling and mediation.” The Collins Center shall advise the court if they are unable to locate the homeowner and the court may set final hearing or enter summary judgment. If the homeowner is found by the Collins Center, the homeowner may be referred to a HUD Counselor. The HUD Counselor has twenty-one days to help the homeowner complete financial forms provided by the Collins Center. The homeowner's financial forms are provided to the lender/plaintiff by the Collins Center. The mediator will be paid \$350. If the mediation does not occur for one of the specific reasons stated in the administrative order, the plaintiff/lender will be refunded the mediator fee of \$350. Within five days of the original service, parties may stipulate to not using the mediation services. (See 1st and 19th Circuits.)

12th Circuit, Desoto, Sarasota, and Manatee Counties – Effective December 1, 2008, on all cases filed after this date, the Homestead Foreclosure Conciliation Program (HFCCP) requires that lenders communicate with the homestead owners to explore options for litigation. The HFCCP does not require mediation, but requires lenders to schedule a phone conference with homestead owners. Lender's attorney must certify the conference was at least attempted. Pro bono attorneys make a limited appearance. There are sanctions for lenders' failure to comply in good faith with the administrative order.

12th Circuit, Desoto, Sarasota, and Manatee Counties – Effective March 9, 2009, no telephonic appearances in mortgage foreclosure cases.

14th Circuit, Bay County, the Honorable Michael Overstreet's court – Effective February 1, 2009, no telephonic appearance at mortgage foreclosure hearings and original note and mortgage to be attached.

15th Circuit, Palm Beach County – Effective November 1, 2008, if a borrower wishes to modify their loan, they must complete the Defendant's Foreclosure Questionnaire, provide a financial affidavit, two years of tax returns, three months of pay stubs and proof of living on the property. Lender must process request and respond. Borrower may also request a short sale by providing lender's attorney the sales contract, HUD 1 statement, real estate agent contacts. Mediation may then be ordered by the court upon request by either party.

17th Circuit, Broward County, The Honorable David Krathen division – Effective January 17, 2009, Judge Krathen issued an order requiring all mortgage foreclosure cases *in his division* complete a notarized form verifying, among other things, that the original note is filed or that a lost note affidavit is included and has been executed by an officer of the institution who has authority to bind the plaintiff.

18th Circuit, Brevard County – Effective February 9, 2009, if a responsive pleading seeking relief is filed by any defendant, then the case is referred to mediation before final or summary judgment hearing. Plaintiff may schedule mediation through the Supreme Court Certified Civil Mediator or the Brevard Civil Mediation Department. If the mediation department is used, the fee is \$250 paid in advance for 1.5 hours. If the matter is not resolved, the fee may be added as a cost to the final judgment. A mediation agenda is provided with options: repayment; home saver advance under Fannie Mae; forbearance; modification; sale; deed in lieu; consent judgment; reverse mortgage. A representative with authority to settle for plaintiff must be available, but can appear by phone.

18th Circuit, Seminole County – Effective January 29, 2009, if a responsive pleading seeking relief is filed by any defendant, then the case

is referred to mediation before final or summary judgment hearing. Plaintiff may schedule mediation through the Supreme Court Certified Civil Mediator or the Seminole County Court Mediation Department. If the mediation department is used, the fee is \$250 paid in advance for 1.5 hours. If the matter is not resolved, the fee may be added as a cost to the final judgment. A representative with authority to settle for plaintiff must be available, but can appear by phone.

19th Circuit, Indian River, Martin, Okeechobee, and St. Lucie Counties – Effective March 13, 2009, all owner-occupied residential foreclosure actions must file Form “A” with the action providing, among others things, a lender representative with the authority to settle. This form shall go immediately to managed mediation with the Collins Center. Plaintiff must also file a copy of the promissory note, mortgage and any pooling and servicing agreement that may affect the plaintiff’s ability to settle. Plaintiff must pay the nonrefundable managed mediation fee of \$750. Defendants will be given a list of HUD and National Foreclosure Mitigation Counseling Program counselors who can assist the defendant in preparing for the mediation. A representative of the counseling agency may accompany the defendant to the mediation. If defendant gets a legal aid or pro bono attorney, the attorney may file a limited notice of representation only through the conclusion of the mediation process. Includes a Borrowers Financial Information form that the Collins Center may require, along with other documents. (See 1st Circuit.)

The Supreme Decision on Mandatory Mediation

Because of this patchwork of mediation-related requirements among the various judicial circuits, and the vast challenges faced by national lenders and servicers trying to comply with rules that vary so much from one place to another, the Supreme Court of Florida Administrative Order, issued March 9, 2009, created a statewide taskforce to report and recommend to the Court a system of mediation or other alternate dispute resolution efforts that would protect the rights of the homeowners and lenders alike. The interim report was due by May 8, 2009. The final report is due no later than August 15, 2009.

The main point behind mediation is to allow lenders and borrowers alike a real opportunity to communicate and try to work out the problem, something both sides say is not happening and blame on each other.

Commercial real estate foreclosure cases in particular benefit from early mediation and repeat mediation sessions. This is because in most commercial real estate foreclosure cases today, the asset is illiquid and oftentimes has time sensitive issues that may affect asset value such as the expiration of development entitlements. Resolving an issue like this via mediation while concurrently continuing the foreclosure is becoming increasingly more common.

Mediation allows the parties to put their heads together in a neutral forum to try to come up with a solution that works for everyone. And who better to know the property and the parties than the parties themselves as opposed to foreclosures cases where the parties are ultimately leaving decisions up to a judge, especially if the parties hire a mediator experienced in commercial real estate to facilitate the mediation for them. Participants report early mediation of this type of commercial real estate issue yields a 90 percent success rate.

Thinking about Starting a Foreclosure Defense Practice?

Those considering expanding into the residential borrower foreclosure defense practice need to keep in mind that residential foreclosure defense clients are desperate, sometimes angry, emotional, and therefore tend to lean heavily on counsel. Often the merits of the residential foreclosure defense case and personality of the client cannot be determined until counsel is fairly heavily invested. For the most part, residential borrower foreclosure defense representation is a high-volume, low margin business. There may be conflicts for those attorneys who have or in the future may wish to handle lender representation. This type of practice is also on the radar screen for fraudulent, predatory type activity, a radar screen many will prefer to just steer clear of. A recent Florida Bar advisory has been issued, warning lawyers of non-attorneys trying to find lawyers to "team up" with for modification and related engagements.

At times it seems as if every mortgage broker, financial manager, and a lot of the title agents who were doing closings during the boom are doing modifications now. We all know most of those folks are good guys. But we also know some of them were the same scammers doing fraudulent and inappropriate subprime mortgages. During the bubble, every other advertisement on TV was for what sounded like cheap mortgage money. Now the ads are all about help getting salvation from those marvelous mortgages. But that ride may be coming to an end as modification companies charging borrowers thousands of dollars and adding little or no value are finding themselves on the Fed's radar screen. The FTC has been sending warning letters to companies suspected of border-line mortgage modification practices and the FBI is investigating increasingly more cases, more specifically, a 400 percent increase so far from only a few years back. Several state bar associations have recently issued warnings to the members. It seems some of the "mod crooks" have been trying to get lawyers to team up with them, presumably to appear more legitimate and probably to justify charging higher modification fees. To accomplish this, non-lawyers are proposing a variety of agreements, even offering to hire lawyers as "in-house counsel" to provide services to the non-lawyer's customers. The bar warnings are being couched as a heads-up to the legal community to watch out for the non-lawyer bad guys, but are no doubt also a message from the bar to those lawyers that may be tempted that they better not "go there" since we all unfortunately know that a license to practice law does not automatically instill ethics and good judgment in lawyers who lacked those qualities before attending law school and passing the bar. Some of the things to bear in mind if approached with such an offer are:

- Cannot assist in the unauthorized practice of law by:
 - Providing legal services for a distressed homeowner while employed as in-house counsel for a non-lawyer company;
 - Forming a company with a non-lawyer to perform foreclosure-related services if any of the services are the practice of law; or
 - Assisting a non-lawyer individual or company in providing services that the individual or company is not authorized to provide or are otherwise illegal.

- Cannot directly contact distressed homeowners to offer representation (including by telephone or facsimile) and cannot allow someone else to directly contact distressed homeowners on the lawyer's behalf.
- Cannot accept referrals from non-lawyers acting in the guise of a "lawyer referral service."
- Must have a direct relationship with distressed homeowners who hire the lawyer for representation.
- Cannot allow a non-lawyer to choose a lawyer for a distressed homeowner or direct a lawyer's representation of a distressed homeowner.

Most practitioners will no doubt develop a questionnaire and checklist to use when reviewing and analyzing new residential foreclosure defense cases. For residential matters, these questions tend to focus on revealing fraud or predatory lending, or possible TILA or HOEPA defenses or counter-claims. Although it is not often possible, if given the opportunity to, we interview the loan originator, closing agent, client, spouse, co-borrowers guarantors, realtors and of course, the servicer can be the equivalent of winning the borrower foreclosure defense lottery.

Naturally, concerns about getting paid for residential foreclosure defense work are particularly relevant because foreclosure by definition involves clients who can't afford to pay their current financial obligations, no less obligations to their new lawyer. Attorneys are paid for this work in all kinds of ways including up-front fees, monthly retainers, hourly fees, percentage of monies saved (i.e., interest reduction, principal waived, etc.), with payments sometimes even being secured by a second mortgage on the property. A common practice has emerged whereby counsel's initial fee becomes affordable when borrowers are instructed to not pay their mortgage and instead use that money to pay counsel.

As is the case with many other practice areas, delving into residential foreclosure defense is best approached with eyes wide open.

Shari B. Olefson is a shareholder in the Fowler White Boggs Fort Lauderdale office. Since 1989, her practice has focused on real estate and business law.

She is one of only a handful of lawyers in the state who is a Florida Bar certified real estate attorney, has earned a Master of Law degree in real property, land development, and finance, and is a Florida Supreme Court Certified Circuit Civil Court Mediator. Since 1989, her practice has focused on real estate, business transactions, and advising clients on how to resolve the disputes that sometimes result from transactions and business relationships, including complex business and real estate mediation, workouts, and foreclosures.

Ms. Olefson's transactional and related conflict resolution background encompasses purchases, sales, development, construction, finance, asset preservation and loss mitigation, title agency, real estate and mortgage licensing and brokerage, commercial leasing, CMBS and REMIC workouts, RESPA compliance, 1031 exchanges, and contracts.

She has worked with all property types including retail, office, industrial, multifamily and custom residential, shopping centers, restaurant, out-parcel, marina, hotel-motel, mixed use, and raw land. Ms. Olefson's business background includes all facets of entity selection and formation, joint venture creation, mergers and acquisitions, capitalization and securitization.

She regularly advises a diverse range of clients including individuals, public and private local, national and international lenders, businesses, landlords and tenants, developers, investors, buyers, sellers, and borrowers. Ms. Olefson also represents lending and investment institutions creating loan programs and structuring and restructuring loan portfolios and commercial transactions. Her expertise is likewise sought by lenders, developers, and investors in connection with special assets in deacquisition, default resolution, workout negotiation, mediation and, documentation.

Ms. Olefson enjoys long-standing relationships with clients throughout Florida, the United States, and internationally, attesting to her dependability, technical skill, business acumen, and dedication to servicing client needs. She's the author of Foreclosure Nation: Mortgaging the American Dream (Prometheus Books, N.Y., 2009) as well as numerous formal and informal presentations and writings, and is a frequent speaker and writer for industry organizations and associations including the Florida Bar CLE Program.

Acknowledgement: *The author would like to acknowledge Monique Ross and Any McGrotty for their assistance in preparing this chapter.*