

## North Carolina's Emergency Measures to Reduce Home Foreclosures<sup>1</sup>

### I. INTRODUCTION

To avoid as many as 25,000 foreclosures on subprime loans in the state over the next two years, North Carolina passed foreclosure prevention legislation.<sup>2</sup> The Emergency Program to Reduce Home Foreclosure Act (Act),<sup>3</sup> which went into effect on November 1, 2008, is too new to judge how effectively it will reduce foreclosures across the state before it expires on October 31, 2010. The Act raises many issues: how does it benefit homeowners who are facing foreclosure? How does it benefit lenders whose debtors have defaulted? How does the Act differ from and coordinate with similar legislation passed in other states and by the federal government?

This Note will analyze the benefits and drawbacks of the Act and compare it to similar programs in other jurisdictions. Part II of the Note will discuss the foreclosure emergency that North Carolina faces.<sup>4</sup> Part III will detail the provisions of the Act, with attention to the new pre-foreclosure filing requirements and the State Home Foreclosure Prevention Project, as well as the additional requirements and responsibilities that the Act gives to the North Carolina Office of the Commissioner of Banks (NCOCOB).<sup>5</sup> Part IV will analyze the ways in which the Act

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1. Full disclosure: the author of this Note is a trained volunteer for the State Home Foreclosure Prevention Project, a project created by the Act analyzed in this Note. In September, 2008, the author attended six hours of training.

2. Press Release, N.C. Office of the Governor, Gov. Easley Signs Bills to Help Citizens Avoid Home Foreclosures: First of its Kind Program Aims to Drastically Reduce North Carolina Foreclosure Actions (Aug. 18, 2008), <http://www.governor.state.nc.us/News/PressReleases/Default.asp> (follow "August 2008" drop-down boxes; then follow "Aug. 18: FULL STORY" hyperlink).

3. Emergency Program to Reduce Home Foreclosures Act, ch. 226, 2008 N.C. Sess. Laws (to be codified at N.C. GEN. STAT. § 45-100) [hereinafter N.C. Act].

4. *Id.* The preamble states: "Whereas, it will benefit both borrowers and lenders in the State of North Carolina if every effort is made to bring the parties together to seek solutions and avoid foreclosures." See *infra* notes 9-71 and accompanying text.

5. See *infra* notes 72-96 and accompanying text.

benefits homeowners and mortgage lenders, including a comparison of the Act to similar programs in other states.<sup>6</sup> Part V will discuss the interrelation of the Act with present and proposed federal legislation, voluntary efforts at foreclosure prevention by lenders, and the possibility of preemption by federal law.<sup>7</sup> Finally, Part VI will conclude that the Act carefully balances the competing interests of homeowners and mortgage lenders, benefiting both parties and making federal preemption less likely.<sup>8</sup>

## II. THE FORECLOSURE EMERGENCY IN NORTH CAROLINA

### A. *The Role of Subprime Loans in the Foreclosure Emergency*

Subprime lending, described as the “democratization of credit” by former Federal Reserve Chairman Alan Greenspan, offers the possibility of homeownership to borrowers whom lenders consider more likely to default on their mortgages.<sup>9</sup> In a subprime loan, a borrower offsets this credit risk by paying higher interest rates.<sup>10</sup> “In . . . its simplest form, what makes a loan subprime is the existence of a premium above the prevailing prime market rate that a borrower must pay.”<sup>11</sup>

Homeowners often struggle to maintain payments on subprime loans for the duration of their mortgages because of the high interest rates.<sup>12</sup> Many subprime loans are adjustable-rate mortgages (ARMs), in which the interest rate starts at a low, “teaser” level before resetting to a higher, fluctuating, market-

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6. See *infra* notes 97-173 and accompanying text.

7. See *infra* notes 174-195 and accompanying text.

8. See *infra* notes 196-204 and accompanying text.

9. ELLEN SCHLOEMER ET AL., CTR. FOR RESPONSIBLE LENDING, LOSING GROUND: FORECLOSURES IN THE SUBPRIME MARKET AND THEIR COST TO HOMEOWNERS 8 (2006), <http://www.responsiblelending.org/pdfs/foreclosure-paper-report-2-17.pdf>.

10. *Id.* at 7. Accord James R. Hagerty, *Foreclosures, Overdue Mortgages Increase Again: Troubles Extent Into Prime Loans Via Option ARMs*, WALL ST. J., Sept. 6, 2008, at A3.

11. Souphala Chomsengphet & Anthony Pennington-Cross, *The Evolution of the Subprime Mortgage Market*, FED. RES. BANK ST. LOUIS REV. 31, 36 (Jan./Feb. 2006), available at <http://research.stlouisfed.org/publications/review/06/01/ChomPennCross.pdf>.

12. SCHLOEMER ET AL., *supra* note 9, at 7.

based rate a few years later.<sup>13</sup> As mortgage payments rise to the fully-indexed rate (in extreme cases causing a forty percent increase in the payment from their introductory rate),<sup>14</sup> borrowers become less likely to repay the mortgage and more likely to default.<sup>15</sup> Most of the subprime loans that went into foreclosure by early 2008 defaulted because they were already too expensive for the homeowners even before the ARM interest rates had reset.<sup>16</sup> The increase in ARM interest rates has been “a driving factor” in raising the default rate in prime loans,<sup>17</sup> but the ARM has not yet adjusted for many of the subprime loans.<sup>18</sup> Borrowers are becoming delinquent on subprime ARMs months and even years in advance of the scheduled reset date.<sup>19</sup> Since the ARMs are causing many delinquencies at the introductory rate,<sup>20</sup> when the rates finally do increase, the foreclosure rate on subprime loans is expected to get much higher.

The U.S. demand for subprime mortgages escalated around the turn of the twenty-first century: \$665 billion worth of subprime loans were extended in 2005, up from \$35 billion in 1994.<sup>21</sup> The increase in demand came not only from home buyers, but also from investors around the world interested in investment vehicles backed by bundles of mortgages in the U.S. housing market.<sup>22</sup> The

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13. Hagerty, *supra* note 10.

14. SCHLOEMER ET AL., *supra* note 9, at 26-27.

15. STATE FORECLOSURE PREVENTION WORKING GROUP, ANALYSIS OF SUBPRIME MORTGAGE SERVICING PERFORMANCE: DATA REPORT NO. 1, at 11 (Feb. 2008), <http://www.csbs.org/Content/NavigationMenu/Home/StateForeclosurePreventionWorkGroupDataReport.pdf> [hereinafter DATA REPORT NO. 1].

16. *Id.* at 1, 11.

17. Hagerty, *supra* note 10.

18. DATA REPORT NO. 1, *supra* note 15, at 1-2, 11.

19. STATE FORECLOSURE PREVENTION WORKING GROUP, ANALYSIS OF SUBPRIME MORTGAGE SERVICING PERFORMANCE: DATA REPORT NO. 3, at 4 (Sept. 2008), <http://www.csbs.org/Content/NavigationMenu/Home/SFPWGReport3.pdf> [hereinafter DATA REPORT NO. 3] (finding specifically that one-third “of the subprime loans facing reset in the 3rd quarter of 2009 are already delinquent in May 2008, up from 29% in January 2008 and 22% in October 2007”).

20. DATA REPORT NO. 1, *supra* note 15, at 11.

21. SCHLOEMER ET AL., *supra* note 9, at 7. See also Chomslengphet & Pennington-Cross, *supra* note 11, at 37 (finding the development from \$65 billion in 1995 to \$332 billion in 2003, based on data from *Inside B&C Lending*).

22. *This American Life: The Giant Pool of Money*, Program #355 (PRI radio broadcast May 9, 2008), available at [http://www.thislife.org/Radio\\_Episode.aspx?episode=355](http://www.thislife.org/Radio_Episode.aspx?episode=355).

investment vehicles combined various sorts of mortgages with other investments and sold tranches to investors with small percentages of each mortgage in the bundle.<sup>23</sup> Investors sought tranches that included large amounts of the riskier subprime loans because of their high interest rates combined with some highly-rated investments with low interest rates for stability.<sup>24</sup> The demand for subprime mortgages was so strong that, as early as 2005, the Office of the Comptroller of the Currency (OCC), the regulator of national banks, noted the “clear trend toward easing of underwriting standards as banks stretch for volume and yield” of mortgages.<sup>25</sup>

Investors’ demand for mortgage-backed securities has dropped as home prices have fallen (often to less than the amount of the outstanding mortgage),<sup>26</sup> resulting in the current mortgage crisis.<sup>27</sup> Homeowners in default have been foreclosed upon, costing the U.S. economy more than \$300 billion by the end of 2007<sup>28</sup> and an estimated \$500 billion by the middle of 2008.<sup>29</sup> Foreclosure filings are continuing to rise across the country, with a three percent increase from the second to third quarters of 2008, and a seventy-one percent increase from the third quarter of 2007 to the third quarter of 2008.<sup>30</sup> Economists anticipate that the trend

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23. *Id.* Accord Jessica Holzer et al., *FDIC’s Bair Suggests Guarantees for Loans*, WALL ST. J., Oct. 23, 2008, [http://online.wsj.com/article/SB122477138431362499.html?mod=rss\\_whats\\_news\\_us](http://online.wsj.com/article/SB122477138431362499.html?mod=rss_whats_news_us) (link no longer connects to this article; source on file with Banking Journal).

24. *This American Life*, *supra* note 22.

25. NATIONAL CREDIT COMMITTEE, OFFICE OF THE COMPTROLLER OF THE CURRENCY, 2005 SURVEY OF CREDIT UNDERWRITING PRACTICES (2005), <http://www.occ.treas.gov/2005Underwriting/CreditUnderwriting2005.htm>.

26. *See Where Homes Are Worth Less Than the Mortgage* (multimedia interactive map), N.Y. TIMES, Nov. 10, 2008, [http://www.nytimes.com/interactive/2008/11/10/business/20081111\\_MORTGAGES.html](http://www.nytimes.com/interactive/2008/11/10/business/20081111_MORTGAGES.html).

27. *This American Life*, *supra* note 22.

28. MARK E. PEARCE, N.C. OFFICE OF THE COMMISSION OF BANKS, RISING FORECLOSURES IN NORTH CAROLINA: HOUSE FORECLOSURE COMMITTEE, (Jan. 23, 2008), <http://www.nccob.org/NR/rdonlyres/63F9E8B2-3FB4-4693-80BE-EC2931F6E700/0/HouseForeclosureCommitteeJanuary2008.pdf>. Accord Holzer et al., *supra* note 23.

29. Email from Will Corbett, Staff Attorney, N.C. Office of Comm’r of Banks, to potential volunteers for the State Home Foreclosure Prevention Project, UNC School of Law, Duke Law, and NCCU School of Law (Oct. 21, 2008, 9:19 AM EST) (on file with Banking Journal) [hereinafter Corbett Email].

30. David Benoit, *Foreclosure Filings Rise 71%*, WALL ST. J., Oct. 23, 2008, <http://online.wsj.com/article/SB122475248587362063.html>.

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will continue to worsen, with expectations varying between two million more to over four million more foreclosures from 2008 to 2010.<sup>31</sup>

While homeowners of all mortgage types have faced foreclosure in the mortgage crisis, subprime loan holders are dramatically more likely to be affected.<sup>32</sup> As of May 2008, over 300,000 subprime loans (constituting more than twenty-seven percent of all seriously delinquent subprime loans) were in foreclosure, compared with fewer than 80,000 prime loans (or fifteen percent of all delinquent prime loans) that started foreclosure proceedings by that date.<sup>33</sup> Many of the borrowers who funded their real estate purchases with subprime loans face an extreme need for help to avoid foreclosure.

*B. State Governments' Research on Subprime Mortgage Foreclosures*

The NCOCOB regulates most of the mortgage lenders in North Carolina by granting licenses to over one thousand mortgage companies, including "8 of the top 20 mortgage lenders" in the state.<sup>34</sup> Reacting to the foreclosure emergency in 2007, representatives of the NCOCOB and the North Carolina Attorney General joined with colleagues in ten other states to create the State Foreclosure Prevention Working Group (Working Group).<sup>35</sup>

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31. PEARCE, *supra* note 28.

32. DATA REPORT NO. 1, *supra* note 15. See generally Hagerty, *supra* note 10 (discussing foreclosures on prime borrowers).

33. DATA REPORT NO. 3, *supra* note 19, at Appendix 4-5. See also OFFICE OF THE COMPTROLLER OF THE CURRENCY & OFFICE OF THRIFT SUPERVISION, OCC AND OTS MORTGAGE METRICS REPORT: DISCLOSURE OF NATIONAL BANK AND FEDERAL THRIFT MORTGAGE LOAN DATA, JANUARY-JUNE 2008, at 9 (U.S. Dep't of the Treasury ed., Sept. 2008), available at <http://www.occ.treas.gov/ftp/release/2008-105a.pdf> (reporting that, in the first half of 2008, the percentage of all mortgage loans regulated by national banks and federal thrifts that were seriously delinquent was between two and three percent each month, whereas between ten and twelve percent of subprime loans were seriously delinquent).

34. PEARCE, *supra* note 28.

35. DATA REPORT NO. 1, *supra* note 15, at 4; STATE FORECLOSURE PREVENTION WORKING GROUP, ANALYSIS OF SUBPRIME MORTGAGE SERVICING PERFORMANCE: DATA REPORT NO. 2 (Apr. 2008), <http://www.csbs.org/Content/NavigationMenu/Home/StateForeclosureApril2008.pdf> [hereinafter DATA REPORT NO. 2]; DATA REPORT NO. 3, *supra* note 19 (noting the participation in the Working Group of Arizona, California, Colorado, Iowa, Illinois, Massachusetts, Michigan, Ohio and

The Working Group studies “unnecessary” foreclosures: those where delinquent borrowers have not abandoned the home but are actively trying to pay, and where lenders benefit from renegotiating instead of foreclosing on the home.<sup>36</sup> The Working Group’s findings suggest that the best potential solution for the foreclosure crisis is to make renegotiation a viable alternative to foreclosure.<sup>37</sup> Renegotiation is often the best solution for both lenders and borrowers; otherwise, in foreclosure, homeowners are forced to move, and lenders can lose up to forty percent of the value of the mortgage.<sup>38</sup> But renegotiation is particularly challenging for subprime loans that have been divided up into securities: they no longer have just one owner.<sup>39</sup> Instead, borrowers often deal with mortgage servicers, the organizations who receive the homeowners’ payments.<sup>40</sup> Servicers are often not as motivated to renegotiate as the homeowners or a direct lender would be.<sup>41</sup> In fact, some have a financial disincentive to renegotiate because they are often paid double the standard fee for servicing a loan in default.<sup>42</sup> As a result, while some servicers report renegotiating with forty percent of their delinquent borrowers, others report renegotiating with as few as ten percent.<sup>43</sup>

The Working Group found that neither party is currently taking full advantage of the renegotiation process.<sup>44</sup> In September 2008, they reported that over three-quarters of borrowers facing foreclosure are not in renegotiations with lenders.<sup>45</sup> Those delinquent homeowners who manage to keep their homes do so by

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Texas (each represented by the state Attorney General); New York (represented, like North Carolina, by the state Attorney General and state bank regulators); and the Conference of State Bank Supervisors).

36. DATA REPORT NO. 1, *supra* note 15, at 4.

37. *Id.*

38. Press Release, N.C. Office of the Governor, *supra* note 2.

39. Holzer et al., *supra* note 23.

40. Steven Seidenberg, *Homing in on Foreclosure*, A.B.A. J., July 2008, at 54, 58.

41. *Id.* See also John D. Geanakoplos & Susan P. Koniak, Op-Ed., *Mortgage Justice is Blind*, N.Y. TIMES, Oct. 30, 2008, at A39, available at <http://www.nytimes.com/2008/10/30/opinion/30geanakoplos.html?scp=1&sq=mortgage%20justice%20is%20blind&st=cse> (recommending a government-sponsored trustee instead of a servicer to renegotiate mortgages that have been split into investment securities).

42. Seidenberg, *supra* note 40, at 58.

43. DATA REPORT NO. 3, *supra* note 19, at 11.

44. See DATA REPORT NO. 1, *supra* note 15.

45. DATA REPORT NO. 3, *supra* note 19, at 2, 7.

independently finding ways to catch up on their arrears, despite the onerous terms of their mortgages.<sup>46</sup> Lenders, recognizing that they can gain more by renegotiating loans than foreclosing,<sup>47</sup> are willing to modify the loans, or permit servicers to modify for them, sixty-five percent of the time.<sup>48</sup> Renegotiation may involve modification, where the terms of the loan are changed permanently (e.g., to lower the interest rate or principal due) or the creation of a payment plan, where the delinquent payments are rescheduled (either during the life of the loan or added to the end) but the original terms of the loan are generally intact.<sup>49</sup> Modifications are generally more beneficial to troubled homeowners, and lenders appear increasingly likely to offer loan modifications instead of payment plans.<sup>50</sup>

Even though modifying a mortgage loan can be in the best interests of both parties overall, it is not a perfect solution.<sup>51</sup> The Working Group found that twenty percent of homeowners who renegotiated their mortgage loans also defaulted under the new terms,<sup>52</sup> and others in the mortgage industry claim that the recidivism rate is as high as fifty percent.<sup>53</sup> The Working Group

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46. *Id.* at 7; DATA REPORT NO. 1, *supra* note 15, at 2, 13.

47. Press Release, North Carolina Attorney General, Hotline to help North Carolinians facing foreclosure (Feb. 4, 2008), <http://www.ncdoj.com/DocumentStreamerClient?directory=PressReleases/&file=foreclosure%20assistance%20hotline.pdf>. See also OFFICE OF THE COMPTROLLER OF THE CURRENCY, *supra* note 33, at 12 (finding, from a collection of information on loss mitigation from the institutions with the most mortgage servicing, which included nine national banks and five federal thrifts, that there was an increase nationwide in lenders helping homeowners mitigate their loss instead of foreclosing, with over 250,000 loss mitigation plans started in the first half of 2008 alone).

48. DATA REPORT NO. 2, *supra* note 35, at 2. This 65% rate in January 2008 is an increase from 45% as of October 2007. Accord DATA REPORT NO. 1, *supra* note 15, at 1, 12.

49. Mike Ferullo, *HOPE NOW Reports Record Number of Loan Modifications, Repayment Plans*, Banking Rep. (BNA) (Aug. 4, 2008).

50. OFFICE OF THE COMPTROLLER OF THE CURRENCY, *supra* note 33, at 3. Loan modifications represented approximately 33% of all loss mitigation actions in January 2008 and almost 50% of all loss mitigation actions by June 2008. Accord DATA REPORT NO. 2, *supra* note 35, at 2; DATA REPORT NO. 3, *supra* note 19, at 8.

51. Kate Berry, *Why Foreclosure Relief Worries Many Servicers*, AMERICAN BANKER, Nov. 5, 2008, § Mortgages, at 1, available at <http://www.americanbanker.com/article.html?id=20081104WSJ8UA22&queryid=1137336523&hitnum=1>.

52. DATA REPORT NO. 3, *supra* note 19, at 3.

53. Berry, *supra* note 51 (quoting Fred Cannon of Keefe, Bruyette & Woods, Inc., who states "It's well known within the industry that modified loans have a recidivism rate of 50%.")

blames the recidivism on ineffective, “band-aid modifications” that are not reducing the homeowners’ payments or addressing the crisis.<sup>54</sup> Although lenders receive less profit on the renegotiated loan than they would under the terms of the original mortgage, and although some debtors continue to default, lenders benefit from good-faith renegotiation because they would typically lose even more if they were to foreclose on the home.<sup>55</sup>

However, even though renegotiation would be in the best interests of both the borrowers and the lenders, they are not coming together to renegotiate most of the mortgages facing foreclosure.<sup>56</sup> Lawmakers can potentially avoid more unnecessary foreclosures if they can find a way to unite lenders and homeowners for renegotiation.<sup>57</sup>

C. *The Act as North Carolina’s Response to the Foreclosure Emergency*

North Carolina has a history of creating laws to protect homeowners and other borrowers against abusive credit practices.<sup>58</sup> This has helped to keep the foreclosure rate in North Carolina lower than the national average:<sup>59</sup> North Carolina has fewer subprime loans, non-traditional mortgages, adjustable rate loans, and mortgage fraud than most states.<sup>60</sup> Specifically, North Carolina is “45<sup>th</sup> in [the] nation in concentration of subprime lending *in 2005*” and “33<sup>rd</sup> out of 44 reporting states [on mortgage fraud] in 2006.”<sup>61</sup> Despite the state’s careful consumer protection

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54. DATA REPORT NO. 3, *supra* note 19, at 9-10.

55. Geanakoplos & Koniak, *supra* note 41.

56. See DATA REPORT NO. 1, *supra* note 15.

57. *See id.*

58. PEARCE, *supra* note 28; accord Corbett Email, *supra* note 29. North Carolina’s consumer protection laws include the Predatory Lending Act of 1999, N.C. GEN. STAT. § 24-1.1E; Act of Aug. 29, 2001, ch. 393, 2001 N.C. Sess. Laws (codified at N.C. GEN. STAT. § 53-243.01 (2007)) (regulating mortgage brokers and bankers); N.C. GEN. STAT. § 24-10.2 (prohibiting “flipping”); N.C. GEN. STAT. § 24-11F (defining “rate spread loans”); Act to Regulate Mortgage Servicing, ch. 228, 2008 N.C. Sess. Laws (to be codified at N.C. GEN. STAT. § 53-243.01); and N.C. Act, *supra* note 3.

59. PEARCE, *supra* note 28; Press Release, North Carolina Attorney General, *supra* note 47.

60. PEARCE, *supra* note 28 (stating that “Strong Laws and Balanced Growth have reduced NC’s susceptibility to crisis”).

61. *Id.*

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and the relatively low level of foreclosures in North Carolina, the rate of foreclosures in North Carolina is climbing.<sup>62</sup> The foreclosure rate in 2007 was up 9.4% over the 2006 rate, and the NCOCOB anticipates that in 2008, the foreclosure rate in North Carolina will rise by an additional twenty percent, with as many as 60,000 foreclosure starts in the state, as the overall economy worsens.<sup>63</sup>

The NCOCOB noted in early 2008 that, compared to other states, “[p]ro-active legislation and balanced growth have put NC in [a] good position to weather [the] foreclosure storm.”<sup>64</sup> Nonetheless, North Carolina actively has sought to avoid unnecessary foreclosures through negotiation and counseling with homeowners. In February 2008, the Attorney General’s office created a telephone hotline to provide defaulting homeowners with free counseling about foreclosure avoidance options.<sup>65</sup> The NCOCOB asked the North Carolina General Assembly to respond to the impending foreclosure crisis, beginning in April 2008 with a hearing before the House Select Committee on Rising Foreclosures.<sup>66</sup> The state worked with community groups and mortgage industry leaders to create the principles to guide its future actions.<sup>67</sup> These principles include: improving communication between homeowners and lenders, encouraging renegotiations without requiring them, focusing efforts on “willing homeowners who have a realistic possibility of retaining their homes,” and avoiding a foreclosure moratorium.<sup>68</sup> Based on these principles, the NCOCOB asked the General Assembly to support more homeowner counseling programs and to “[t]emporarily increase judicial review of foreclosures for certain types of subprime or non-traditional loans originated in 2005-2007.”<sup>69</sup> The General Assembly responded by filing in late May 2008 the bill

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62. *Id.*; Press Release, North Carolina Attorney General, *supra* note 47.

63. PEARCE, *supra* note 28; *accord* Corbett Email, *supra* note 29.

64. PEARCE, *supra* note 28.

65. Press Release, North Carolina Attorney General, *supra* note 47.

66. Corbett Email, *supra* note 29.

67. *Id.*

68. Will Corbett, Staff Attorney, N.C. Office of the Comm’r of Banks, Speech on State Home Foreclosure Prevention Project at UNC School of Law (Oct. 21, 2008) [hereinafter Corbett Speech].

69. PEARCE, *supra* note 28.

that would become the Act; it was enacted into law in August 2008.<sup>70</sup> By September 2008, North Carolina's default notices dropped sixty-six percent.<sup>71</sup>

### III. NORTH CAROLINA'S PASSAGE OF THE EMERGENCY PROGRAM TO REDUCE HOME FORECLOSURES ACT

As Governor Mike Easley explained, "[o]ur goal is to help borrowers and lenders together so that the family gets to keep their home and the bank does not lose money on the loan."<sup>72</sup> The Act seeks to achieve this in two main ways. First, it requires lenders to provide written notices to homeowners forty-five days ahead of filing for foreclosure on subprime loans, and to file such notices electronically with the North Carolina court system.<sup>73</sup> Second, it encourages homeowners and lenders to renegotiate the mortgage during the forty-five day delay, which the NCOCOB may extend for thirty additional days.<sup>74</sup>

The Act, which is effective between November 1, 2008 and October 31, 2010,<sup>75</sup> applies only to subprime loans, defined as a residential mortgage created in 2005, 2006 or 2007 that would qualify as a rate spread home loan.<sup>76</sup> According to the North Carolina General Statutes, a rate spread home loan on a first mortgage has an annual percentage rate at least 1.75 percentage points above the prevailing market interest rate (based on Freddie Mac mortgage commitment data published weekly in the Federal Reserve Board's Statistical Release H.15) and at least three percent greater than the yield on U.S. Treasury securities (based on the Home Mortgage Disclosure Act triggers).<sup>77</sup>

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70. N.C. Act, *supra* note 3.

71. Benoit, *supra* note 30.

72. Press Release, N.C. Office of the Governor, *supra* note 2.

73. N.C. Act, *supra* note 3, § 1; *accord* Corbett Email, *supra* note 29.

74. N.C. Act, *supra* note 3, § 1; Press Release, N.C. Office of the Governor, *supra* note 2.

75. N.C. Act, *supra* note 3, § 6.

76. N.C. Act, *supra* note 3, § 1.

77. *Id.* (defining subprime loans as those created at any point in years 2005, 2006 and 2007 that "would meet the definition of a rate spread home loan under G.S. 24-1.1F(a)(7), if that section had been in effect when the loan was originated.") N.C. GEN. STAT. § 24-1.1F(a)(7) also includes mortgages for subordinate liens as those that both are 3.75 percentage points above the prevailing market interest rate and

A. *The Notice and Filing Requirements in the Act*

The Act requires that a pre-foreclosure notice be sent to borrowers of subprime loans forty-five days prior to the filing of a notice of hearing.<sup>78</sup> The notice must supply the homeowner with the amount past due, the total amount required to bring the loan current, information on “the availability of resources to avoid foreclosure,” and contact data for the borrower’s mortgage lender and/or mortgage servicer, counseling agencies within the state, and the NCOCOB.<sup>79</sup> Then, within three business days, creditors must submit information on the loan electronically to the state to be compiled in a nonpublic database.<sup>80</sup> The NCOCOB may request additional information on the loan “to prioritize efforts to reach borrowers most likely to avoid foreclosure and to prevent delay for defaults where foreclosure is unavoidable.”<sup>81</sup>

B. *The Role of the North Carolina Office of the Commissioner of Banks in the Act*

The Act grants additional rights, powers, and responsibilities to the NCOCOB. First, the NCOCOB will establish and run the State Home Foreclosure Prevention Project (Project)<sup>82</sup> with input from representatives from homeowner groups as well as the mortgage industry. The Act states that “the purpose of the Project is to seek solutions to avoid foreclosures for certain subprime loans.”<sup>83</sup> Because the NCOCOB has discovered that many subprime loans in North Carolina violate state and federal laws, a key component of the Project will be the legal review of thousands of subprime loans.<sup>84</sup> The Project uses NCOCOB paralegals and trained legal volunteers, including law

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have an annual percentage rate at least five percent greater than the yield on U.S. Treasury securities. *Accord* Memorandum from the N.C. Bankers Ass’n to the *Legal Memorandum* Mailing List (Sept. 10, 2008) (on file with Banking Journal).

78. N.C. Act, *supra* note 3, §§ 1-2.

79. N.C. Act, *supra* note 3, § 1.

80. *Id.*

81. *Id.*

82. *Id.*; Corbett Email, *supra* note 29.

83. N.C. Act, *supra* note 3, § 1.

84. Corbett Email, *supra* note 29.

students, all subject to a confidentiality agreement, to begin the process.<sup>85</sup> They enter the values from the NCOCOB database into a computer program that indicates whether the terms of a given loan exhibit “red flags” (because the terms approach violations of North Carolina’s or federal lending laws) for further review by the NCOCOB staff.<sup>86</sup> Then NCOCOB attorneys conduct an extensive legal compliance review of the flagged loans to determine whether there are violations, and if so, to engage in conversations with the mortgage servicer, the licensed entity, and a housing counselor to remedy the violation.<sup>87</sup> In cases of egregious violations, the NCOCOB can bring a suit to enforce the disgorgement of certain terms in a mortgage or revoke illegal terms entirely.<sup>88</sup> In addition to the legal review process, the Project has a consumer education component, including a media campaign on television and the internet.<sup>89</sup>

Second, after analyzing a loan, if the NCOCOB determines that the loan is “appropriate for efforts to avoid foreclosure,” and that “further efforts by the State Home Foreclosure Prevention Project offer a reasonable prospect to avoid foreclosure on primary residences,” the NCOCOB has the power to extend the foreclosure process one time for thirty days.<sup>90</sup>

The third requirement for the NCOCOB is to report on the program’s effectiveness and recommendations to the General Assembly before May 1 in 2009 and 2010.<sup>91</sup> The Act creates an additional reporting requirement for the State Banking Commission, obliging it to report on the program’s implementation to the Joint Legislative Commission on

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85. Will Corbett, Staff Attorney, N.C. Office of the Comm’r of Banks, Student Volunteer Training for the State Home Foreclosure Prevention Project at UNC School of Law (Sept. 30, 2008) [hereinafter Training].

86. *Id.*; Email from Will Corbett, Staff Attorney, N.C. Office of Comm’r of Banks, to potential volunteers for the State Home Foreclosure Prevention Project, UNC School of Law, Duke Law, and NCCU School of Law (Sept. 24, 2008, 3:30 PM EST) (on file with Banking Journal).

87. Training, *supra* note 85.

88. Corbett Speech, *supra* note 68.

89. Corbett Email, *supra* note 29.

90. N.C. Act, *supra* note 3, § 1.

91. N.C. Act, *supra* note 3, § 5.

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Governmental Operations by February 15, 2009, less than four months after the Act takes effect.<sup>92</sup>

C. *Funding of the Act*

The North Carolina General Assembly funded the Act with one million dollars.<sup>93</sup> The General Assembly earmarked \$400,000 to implement the Project,<sup>94</sup> and the NCOCOB will use \$600,000 for grants to nonprofit financial counseling agencies.<sup>95</sup> In addition to the legislated funding, the NCOCOB is willing to spend up to \$1.5 million more “to hire additional professional and administrative staff to assist struggling homeowners.”<sup>96</sup>

IV. THE BENEFITS OF THE ACT TO NORTH CAROLINA’S  
HOMEOWNERS AND LENDERS COMPARED WITH SIMILAR STATE  
LAWS

North Carolina is not the only state that has enacted some form of foreclosure prevention.<sup>97</sup> Certain aspects of the North Carolina Act support subprime homeowners more than they are supported in other states;<sup>98</sup> others aspects promote the rights of North Carolina’s mortgage lenders more than in other

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92. N.C. Act, *supra* note 3, § 4; Current Operations and Capital Improvements Appropriations Act of 2008, ch. 107, § 13.6B, 2008 N.C. Sess. Laws (to be codified as amended in scattered sections of N.C. GEN. STAT. § 143C).

93. N.C. Act, *supra* note 3, § 4; Current Operations and Capital Improvements Appropriations Act of 2008 § 13.6B.

94. N.C. Act, *supra* note 3, § 4; Current Operations and Capital Improvements Appropriations Act of 2008 §§ 6.9A, 13.6B.

95. N.C. Act, *supra* note 3, § 4; Current Operations and Capital Improvements Appropriations Act of 2008 § 13.6B.

96. Vicki Lee Parker, *Help Available in Foreclosure*, NEWS & OBSERVER, Aug. 19, 2008, <http://www.newsobserver.com/business/story/1183872.html>.

97. N.C. Act, *supra* note 3. Other states’ foreclosure prevention statutes (including those that passed in California, Colorado, Connecticut, Georgia, Hawaii, Illinois, Kentucky, Louisiana, Maine, Maryland, Michigan, New Jersey, New York, Pennsylvania, and Washington state) may be more or less comprehensive than the North Carolina Act or include measures that are covered elsewhere in the North Carolina General Statutes. Still other jurisdictions (including Ohio and the city of Philadelphia) have foreclosure prevention programs that were created by the judiciary, not passed through the legislature. *See infra* notes 101-159 and accompanying text.

98. *See infra* notes 165-167 and accompanying text.

jurisdictions.<sup>99</sup> Overall, the North Carolina Act balances the rights of homeowners and mortgage lenders by seeking to stop foreclosures and resolve the loan default in other, more mutually-beneficial ways than foreclosure on the borrower's home.<sup>100</sup>

#### A. Foreclosure Prevention Legislation in Various States

##### 1. Delay or Moratorium on Foreclosure

Delay periods in foreclosure prevention statutes in other states range from thirty days to a moratorium of five months, compared to North Carolina's forty-five day delay period and refusal of a moratorium.<sup>101</sup> Maryland's statute, passed in April 2008, created a five-month moratorium.<sup>102</sup> New York requires a ninety-day delay before initiating foreclosure proceedings.<sup>103</sup> Several other state foreclosure prevention acts have created longer delays before foreclosure than the forty-five day period in North Carolina.<sup>104</sup> Some other states, however, only require lenders to

99. See *infra* notes 168-173 and accompanying text.

100. See *infra* notes 160-164 and accompanying text.

101. Compare N.C. Act, *supra* note 3, § 1 with Nicholas Confessore & Jeremy W. Peters, *A Proposal from Albany on Stemming Foreclosures*, N.Y. TIMES, June 20, 2008, <http://www.nytimes.com/2008/06/20/nyregion/20albany.html?scp=8&sq=Nicholas+Confessore+%26+Jeremy+W.+Peters&st=nyt>, and Manny Fernandez, *In Confronting the Foreclosure Crisis, a Bill Strikes a Balance*, N.Y. TIMES, June 22, 2008, <http://www.nytimes.com/2008/06/22/nyregion/22housing.html?scp=1&sq=In+Confronting+the+Foreclosure+Crisis%2C+a+Bill+Strikes+a+Balance&st=nyt> (noting in both that New Yorkers considered, but did not pass, a year-long moratorium).

102. Cheyenne Hopkins, *Foreclosure Moves Open Gray Area in Preemption*, AM. BANKER, Apr. 21, 2008, available at <http://www.americanbanker.com/article.html?id=20080418T8I3STMP&queryid=1118817646&hitnum=1>.

103. Act of Aug. 5, 2008, ch. 472, § 2, 2008 N.Y. Laws (to be codified as amended in scattered sections of N.Y. BANKING LAW, N.Y. C.P.L.R., AND N.Y. REAL PROP. ACTS. LAW ) [hereinafter N.Y. Act]; see also Fernandez, *supra* note 101 (describing how the New York State Assembly originally passed the foreclosure prevention bill with a one-year moratorium).

104. Compare N.C. Act, *supra* note 3, § 1 with N.Y. Act, *supra* note 103, § 2 (New York's ninety-day delay); Act of June 12, 2008, ch. 176, § 7, 2008 Conn. Acts (Reg. Sess.) (to be codified as amended in scattered sections of CONN. GEN. STAT. §§ 8, 36) [hereinafter Conn. Act] (Connecticut's sixty-day delay); Act of June 5, 2008, ch. 440, § 1, 2008 Colo. Sess. Laws 2258 (to be codified at COLO. REV. STAT. § 38-38-102.5) [hereinafter Colo. Act] (Colorado's thirty-day delay to mail a notice, followed by an additional thirty-day delay before filing a notice of election and demand); and Act of Apr. 3, 2008, ch. 1, § 1, 2008 Md. Laws (to be codified at MD. CODE ANN., REAL PROP. § 3-104) [hereinafter Md. Act] (Maryland's delay of ninety days after default or forty-five days after filing intent to foreclose). Even the pilot program from the City

wait thirty days to foreclose or bring other legal action after filing a notice of intent.<sup>105</sup>

While North Carolina's forty-five day delay may not allow all homeowners to compile sufficient funds to stop foreclosure, it still gives homeowners a warning without being so long that it significantly disrupts the lenders' practices.<sup>106</sup> Also, lenders often oppose foreclosure moratoria because, as John M. Robbins, chairman of the Mortgage Bankers Association explained, they analyze every mortgage separately as "an individual transaction and situation, one which needs to be addressed individually between the lender and the borrower."<sup>107</sup> The North Carolina time period strikes a good balance between homeowner and lender interests.

## 2. Contact Information in Foreclosure Notice Mailing

Like the North Carolina Act, most states' laws require that foreclosure notifications provide the homeowner with the name and contact information of the lender and/or mortgage servicer so that the homeowner can attempt to renegotiate the loan.<sup>108</sup> North

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of Philadelphia has a longer window of delay than North Carolina: sheriff's sales in the city were delayed for two months while the program was being created. The city launched the pilot program in an effort to abate some of the 8,500 foreclosures that it anticipates for 2008. FIRST JUDICIAL DISTRICT OF PHILADELPHIA, COURT OF COMMON PLEAS OF PHILADELPHIA COUNTY, JOINT GENERAL COURT REGULATION NO. 2008-01, RESIDENTIAL MORTGAGE FORECLOSURE DIVERSION PILOT PROGRAM, <http://fjd.phila.gov/pdf/regs/2008/cpjgr-2008-01.pdf>; Associated Press, *Philly unveils plan to fight home foreclosures*, ABC NEWS, June 5, 2008, <http://abcnews.go.com/US/wireStory?id=5003562>.

105. Compare N.C. Act, *supra* note 3, § 1 with Act of July 8, 2008, ch. 69, § 2, 2008 Cal. Adv. Legis. Serv. (Deering) (to be codified at CAL. CIV. CODE § 2923.5) [hereinafter Cal. Act] (California's thirty-day delay after contact with the borrower or due diligence to contact the borrower) and Act of April 24, 2008, ch. 175, § 31, 2008 Ky. Acts (to be codified at KY. REV. STAT. ANN. § 198A) [hereinafter Ky. Act] (Kentucky's thirty-day delay).

106. See Hopkins, *supra* note 102.

107. Peter G. Miller, *Should We Have a Foreclosure Moratorium?*, REALTYTRAC, <http://www.realtytrac.com/ContentManagement/RealtyTracLibrary.aspx?a=b&ItemID=2268&acct=64953> (last visited Nov. 5, 2008).

108. Compare N.C. Act, *supra* note 3, § 1 with Conn. Act, *supra* note 104, § 7; Colo. Act, *supra* note 104, § 1; Act of June 3, 2008, ch. 138, § 3, 2008 Haw. Sess. Laws (to be codified at HAW. REV. STAT. § 667-5); Act of May 13, 2008, ch. 576, § 2, 2008 Ga. Laws (to be codified at GA. CODE ANN. § 44-14-7); and Md. Act, *supra* note 104, § 1. See also Save New Jersey Homes Act of 2008, ch. 86, § 6.a., 2008 N.J. Laws (to be codified at N.J. REV. STAT. § 46) [hereinafter N.J. Act] (requiring the mailing to

Carolina also recognizes that housing counselors can be influential in lowering the occurrence of foreclosures,<sup>109</sup> and the Act requires inclusion of contact information for at least one counselor in the notice mailing.<sup>110</sup> Similarly, legislation in New York and Pennsylvania requires that the notice of the filing of foreclosure also include contact information for governmental support and a list of state-approved housing counselors.<sup>111</sup> North Carolina's law encourages renegotiation by including in the foreclosure notice contact information for counselors as well as for the homeowner's mortgage lender and/or mortgage servicer.<sup>112</sup>

### 3. Housing Hotline

Several other states have created or authorized the creation of housing hotlines online or by telephone to support, guide and educate homeowners facing imminent foreclosure in finding other options,<sup>113</sup> much like the system instituted by North Carolina Attorney General.<sup>114</sup>

### 4. Negotiation Requirements between Homeowners and Lenders

Other jurisdictions have more detailed strategies for renegotiation requirements than North Carolina's Project has

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include a list of alternatives to foreclosure, "including any refinancing of the loan offered by the creditor and any renegotiation of loan terms offered by the creditor").

109. *Center for Community Capital director testifies about home foreclosures*, UNC CENTER FOR COMMUNITY CAPITAL, Feb. 26, 2008, <http://www.ccc.unc.edu/?id=news.022608&t=News>.

110. N.C. Act, *supra* note 3, § 1.

111. N.Y. Act, *supra* note 103, § 2 (requiring the inclusion of the telephone number and web address of the New York State Banking Department and a list of at least five local consumer credit counseling agencies); Act of July 8, 2008, ch. 57, § 2, 2008 Pa. Laws (to be codified as amended in scattered sections of PA. CONS. STAT.) [hereinafter Pa. Act] (requiring the inclusion of the name and telephone number of a local consumer credit counseling agency).

112. N.C. Act, *supra* note 3, § 1. *See also* N.C. Foreclosure Help, [www.ncforeclosurehelp.org](http://www.ncforeclosurehelp.org) (last visited Nov. 14, 2008) (compiling sources for government assistance).

113. *See* N.Y. Act, *supra* note 103, § 1; Cal. Act, *supra* note 105, § 2; Act of June 16, 2008, Act 228, § 1, 2008 La. Acts (to be codified at LA. REV. STAT. ANN. § 40:600.25.1) [hereinafter La. Act]; *and* Colo. Act, *supra* note 104, § 1.

114. Press Release, North Carolina Attorney General, *supra* note 47.

promulgated to date.<sup>115</sup> The New York legislation requires lenders and subprime borrowers to meet in settlement conference within sixty days of serving the borrower with legal papers, after default but before foreclosure, to discuss a renegotiation on the loan.<sup>116</sup> California requires its lenders to contact the borrowers to explore options to avoid foreclosure.<sup>117</sup> The City of Philadelphia requires a court-monitored mediation.<sup>118</sup> Other states recommend a negotiation session, which may or may not be overseen by the courts, but only require the negotiation for serious homeowners seeking further assistance from the state.<sup>119</sup> By contrast, the North Carolina Act does not mandate a meeting between the homeowner and lender or mortgage servicer; it puts the onus on the homeowner to initiate the negotiation by providing the homeowner with the servicer's or lender's contact information.<sup>120</sup>

## 5. Consumer Education Programs

Several states have created ongoing consumer education programs to deal with the foreclosure crisis, although the methods of consumer education vary.<sup>121</sup> Pennsylvania has an ongoing foreclosure study to monitor trends and provide for recommendations.<sup>122</sup> A similar program in Kentucky promotes consumer education by requiring lenders to include a brochure on

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115. Compare N.C. Act, *supra* note 3, § 1 with N.Y. Act, *supra* note 103, § 3; Pa. Act, *supra* note 111, § 2; and Conn. Act, *supra* note 104, §§ 7, 16.

116. N.Y. Act, *supra* note 103, § 3.

117. Cal. Act, *supra* note 105, § 1.

118. FIRST JUDICIAL DISTRICT OF PHILADELPHIA, COURT OF COMMON PLEAS OF PHILADELPHIA COUNTY, JOINT GENERAL COURT REGULATION NO. 2008-01, *RESIDENTIAL MORTGAGE FORECLOSURE DIVERSION PILOT PROGRAM*, <http://fjd.phila.gov/pdf/regs/2008/cpjgcr-2008-01.pdf>; Associated Press, *supra* note 104.

119. See, e.g., Pa. Act, *supra* note 111, § 2 (participation in a mediation program will delay the lender's rights to initiate foreclosure for thirty-three days and may delay for sixty days if the borrower seeks mortgage assistance payments); Conn. Act, *supra* note 104, § 16 (the mediation program is mandatory for borrowers who wish to seek emergency mortgage assistance payments); and THE SUPREME COURT OF OHIO, FORECLOSURE MEDIATION PROGRAM MODEL, [http://www.supremecourtsohio.gov/dispute\\_resolution/foreclosure/foreclosureMediation.pdf](http://www.supremecourtsohio.gov/dispute_resolution/foreclosure/foreclosureMediation.pdf) (recommended by the Chief Justice of the Ohio Supreme Court for Ohio judges to follow in foreclosure cases).

120. N.C. Act, *supra* note 3, § 1.

121. E.g., *id.*; Pa. Act, *supra* note 111, § 5; and Ky. Act, *supra* note 105, § 1.

122. Pa. Act, *supra* note 111, § 5.

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the consumer education center at the time of the mortgage.<sup>123</sup> Illinois begins consumer education of homeownership in high school, requiring lessons on “the basic process of obtaining a mortgage and the concepts of fixed and adjusted rate mortgages, subprime loans, and predatory lending.”<sup>124</sup> Washington seeks to educate its citizens “of all ages” about financial institutions and products in order to provide them with “skills necessary to obtain individual financial independence, fiscal responsibility, and financial management skills.”<sup>125</sup> Finally, North Carolina’s Act will use the Project to educate consumers through a media campaign in television and internet advertisements.<sup>126</sup>

## 6. Funding Requirements

### A. FUNDING FOR CREDIT COUNSELORS

The North Carolina Act funds the nonprofit groups that will serve as approved consumer credit counseling agencies.<sup>127</sup> Colorado, Connecticut and Washington have similar provisions.<sup>128</sup> The Louisiana legislation granted permission for the creation of the Louisiana Housing Finance Agency, which may, but is not required to, provide grants to counselors.<sup>129</sup> The Kentucky Homeownership Protection Center solicits donations for funding.<sup>130</sup>

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123. Ky. Act, *supra* note 105, § 1.

124. Act of Aug. 19, 2008, ch. 863, § 5, 2007 Ill. Laws (to be codified at 105 ILL. COMP. STAT. 5/27-12.1).

125. Act of Feb. 11, 2008, ch. 3, § 2, 2008 Wash. Legis. Serv. (West) (to be codified at WASH. REV. CODE § 43.320) [hereinafter Wash. Act].

126. N.C. Act, *supra* note 3, § 1; N.C. Foreclosure Help, *supra* note 112 (including a link to Public Service Announcements at <http://www.foreclosurehelpandhope.org/ads.html>).

127. N.C. Act, *supra* note 3, § 4.

128. Conn. Act, *supra* note 104, § 14; Colo. Act, *supra* note 104, § 2; Wash. Act, *supra* note 125, § 4.

129. La. Act, *supra* note 113, § 1.

130. Ky. Act, *supra* note 105, § 1.

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## B. FUNDING FOR MORTGAGE ASSISTANCE PAYMENTS, BONDS AND LOANS

North Carolina does not provide funding to homeowners, although a few states do.<sup>131</sup> Michigan residents with annual incomes at or below sixty percent of the statewide median gross income who spend fifty percent of their finances on housing may qualify for bonds from the state,<sup>132</sup> and qualified citizens of Pennsylvania and Connecticut may apply for loans to pay their mortgage.<sup>133</sup>

### 7. Limits of the Legislation

#### A. LIMIT TO SUBPRIME LOANS ONLY

Some jurisdictions, including North Carolina, limit their legislation to specific types of loans, and while each state defines the covered mortgage loans differently, these subcategories of loans all face great hardships, like subprime, nonprime, or high-cost loans.<sup>134</sup> The New York legislation defines subprime loans as those that are 1.75 percentage points above the prevailing market interest rate, and it does not enforce prepayment penalties in the loans.<sup>135</sup> The Kentucky legislation applies only to “high-cost loans,” which include the following factors: a principal amount between \$15,000 and \$200,000; the borrower is a natural person; the mortgage is used for a home for personal, family or household purposes; the mortgage covers the borrower’s principal dwelling; and the total points and fees included with the loan are greater than the greater of \$3,000 or six percent of the value of the loan.<sup>136</sup>

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131. Compare N.C. Act, *supra* note 3 with Pa. Act, *supra* note 111, § 3; Conn. Act, *supra* note 104, §§ 2, 12; and Act of Apr. 2, 2008, Act 53, 2008 Mich. Pub. Acts (to be codified at MICH. COMP. LAWS § 32a) [hereinafter Mich. Act].

132. Mich. Act, *supra* note 131.

133. Pa. Act, *supra* note 111, § 3; Conn. Act, *supra* note 104, §§ 2, 12.

134. E.g., N.C. Act, *supra* note 3, § 1; N.Y. Act, *supra* note 103, § 2; Ky. Act, *supra* note 105, § 31; Act of Jan. 8, 2008, ch. 471, 2008 Me. Laws (to be codified at ME. REV. STAT. ANN. tit. 9-A § 1-202).

135. N.Y. Act, *supra* note 103, § 2.

136. Ky. Act, *supra* note 105, § 31.

The North Carolina Bankers Association notes that the Act limits further damage on the North Carolina housing market during the current economic downturn by limiting the application of the Act to subprime loans.<sup>137</sup> However, California's foreclosure prevention legislation applies to any residential mortgages created within the state between 2003 and 2007,<sup>138</sup> and comparable legislation in Maryland applies to any residential mortgage within the state.<sup>139</sup>

#### B. TIME LIMITS FOR THE MORTGAGES COVERED BY THE LEGISLATION

North Carolina limits the covered subprime loans to those created in 2005, 2006 and 2007.<sup>140</sup> Other jurisdictions also limit the effect of their legislation to mortgages created within a certain window, although the size of the time frame in other jurisdictions appears larger than that used in North Carolina.<sup>141</sup> The California law applies to mortgages created from 2003 through 2007.<sup>142</sup> The New York legislation applies to mortgages created on subprime loans between January 1, 2003, and September 1, 2008.<sup>143</sup> The laws in Maryland do not appear to indicate a time limit for subprime loans, and its act extends prospectively.<sup>144</sup>

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137. Memorandum from the N.C. Bankers Ass'n to the *Legal Memorandum Mailing List*, *supra* note 77.

138. Cal. Act, *supra* note 105, § 2.

139. Md. Act, *supra* note 104.

140. N.C. Act, *supra* note 3, § 1.

141. Compare N.C. Act, *supra* note 3, § 1 with N.Y. Act, *supra* note 103, § 2; Cal. Act, *supra* note 105, § 2; and Md. Act, *supra* note 104, § 3. Some New York homeowners are concerned by the law's limitation because it will not necessarily apply, like Maryland's law, to new mortgages created in the future. Fernandez, *supra* note 101. North Carolina homeowners, with a window of applicable laws nine months smaller than that in New York, may also become concerned by the Act's time restrictions. However, for the foreseeable future, no subprime loans are likely to be originated at all.

142. Cal. Act, *supra* note 105, § 2.

143. N.Y. Act, *supra* note 103, § 2.

144. Md. Act, *supra* note 104, § 3.

### C. EXPIRATION OF THE LEGISLATION

The North Carolina Act became effective on November 1, 2008, and expires on October 31, 2010.<sup>145</sup> Other states' laws have various expiration dates ranging from July 1, 2010 in Colorado to January 1, 2013 in California.<sup>146</sup> If the North Carolina Act proves ineffective over the first two years, the state does not have a long-term commitment to the program.<sup>147</sup> If the Act is successful and still needed, the NCOCOB may well lobby for its extension.

#### 8. Additional Features Not Included in North Carolina's Act

Several other state foreclosure prevention laws include features that were not part of North Carolina's Act. The features discussed below relate specifically to the content of the Act but were not included within it. Some other states' foreclosure prevention laws also cover features that are addressed elsewhere in the North Carolina General Statutes.<sup>148</sup>

### A. NOTICES BEFORE INTRODUCTORY RATES RESET

The Save New Jersey Homes Act of 2008<sup>149</sup> requires lenders to provide written notices to homeowners sixty days and thirty days in advance of resetting the introductory rate on an adjustable rate mortgage.<sup>150</sup> The notices must include a list of alternatives to foreclosure and information on the borrower's right to seek an extension of the introductory rate.<sup>151</sup> New Jersey homeowners are entitled to extend their introductory rate for an additional three years if they complete a certification and meet other requirements set out in the legislation, and they are not responsible for repaying to the lender the interest that they would have been charged until

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145. N.C. Act, *supra* note 3, § 6.

146. Cal. Act, *supra* note 105, § 2; Colo. Act, *supra* note 104, § 2.

147. See N.C. Act, *supra* note 3, § 6.

148. See, e.g., Act to Regulate Mortgage Servicing, ch. 228, 2008 N.C. Sess. Laws (to be codified at N.C. GEN. STAT. § 53-243.01).

149. N.J. Act, *supra* note 108.

150. *Id.*

151. *Id.*

they sell their homes.<sup>152</sup> The North Carolina Act does not offer this level of support to homeowners because it seeks a more balanced approach to the foreclosure crisis, working to respect lenders' rights while protecting homeowners.

#### B. LIMIT FREQUENCY OF DELAYS ON FORECLOSURE

Several other states limit how frequently homeowners may take shelter in various aspects of the foreclosure prevention laws, including the delay on foreclosure itself.<sup>153</sup> The ninety-day foreclosure delay in New York is limited to once per twelve-month period for the same mortgage and borrower, even if the borrower has caught up in payments between occurrences of default.<sup>154</sup> The requirement to mail a notice to defaulting debtors in Colorado only applies the first time that a debtor is in default in a twelve-month period.<sup>155</sup> North Carolina does not impose any similar limitations on debtors who default repeatedly within the year.

#### C. FINANCING MORTGAGE PAYMENTS

As mentioned above, several states finance loans or bonds to assist homeowners facing foreclosure.<sup>156</sup> The North Carolina Act, like the laws in most jurisdictions, does not offer financial assistance to delinquent homeowners and only provides funding for the training and compensation of the credit counselors and agencies.<sup>157</sup>

#### D. REASONABLE BELIEF THAT THE MORTGAGOR CAN REPAY

Some of the state laws that cover future mortgages require the lender to show a reasonable belief that the mortgagor will be

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152. *Id.* *Accord State Issues: Subprime Legislation*, SECURITIES INDUSTRY AND FINANCIAL MARKETS ASS'N (SIFMA), Aug. 14, 2008, [www.sifma.org/legislation/state/subprime-legislation.html](http://www.sifma.org/legislation/state/subprime-legislation.html).

153. *E.g.*, N.Y. Act, *supra* note 103, § 2; Colo. Act, *supra* note 104, § 1.

154. N.Y. Act, *supra* note 103, § 2.

155. Colo. Act, *supra* note 104, § 1.

156. *See supra* notes 131-133 and accompanying text.

157. *Compare* N.C. Act, *supra* note 3, § 4 with La. Act, *supra* note 113, § 1; Conn. Act, *supra* note 104, § 14; and Colo. Act, *supra* note 104, § 2.

able to repay the loan before the lender can offer a subprime loan.<sup>158</sup> The New York law goes even further, requiring that mortgage lenders use a “duty of care” with a “reasonable and good-faith” effort to find an appropriate rate on a mortgage for each particular debtor and to determine whether a debtor will be able to repay a loan.<sup>159</sup> The North Carolina Act does not cover future mortgages.

*B. Benefits of the Act*

The Act is designed to encourage negotiation between homeowners and lenders so that homeowners will be able to refinance or renegotiate mortgage loans in ways that are in the best interest of all parties.<sup>160</sup> On its face, the Act balances the needs of homeowners struggling to meet mortgage payments with the rights of lenders to have their loans repaid or realize on the collateral for the loans.<sup>161</sup> The benefit of the forty-five day delay is that it warns debtors of impending foreclosures, which may allow them to catch up their mortgage payments in time to avoid foreclosure altogether.<sup>162</sup> This delay slows down the foreclosure process to give homeowners more warning of an impending foreclosure and to create more opportunities for lenders and homeowners to come up with a better, mutually-beneficial plan that does not involve foreclosure.<sup>163</sup> Also, with the information gathered through the filing system, the NCOCOB will be better informed to combat loans that do “not meet the state’s legal standards.”<sup>164</sup>

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158. See, e.g., Conn. Act, *supra* note 104, § 23 (regulating a “nonprime home loan”); Ky. Act, *supra* note 105, § 31 (regulating a “high-cost home loan”).

159. N.Y. Act, *supra* note 103, § 6; accord Confessore & Peters, *supra* note 101; Fernandez, *supra* note 101.

160. Press Release, N.C. Office of the Governor, *supra* note 2.

161. See N.C. Act, *supra* note 3.

162. See DATA REPORT NO. 1, *supra* note 15, DATA REPORT NO. 2, *supra* note 35.

163. See DATA REPORT NO. 2, *supra* note 35.

164. Parker, *supra* note 96.

### 1. Benefits to Homeowners

North Carolina's Act was created to protect homeowners. The Act ensures that subprime homeowners are informed of their rights by compelling lenders to notify them of impending foreclosures forty-five days in advance of beginning the legal action. It teaches the homeowners how to respond next by requiring that lenders' correspondence include the contact information for the mortgagee and servicer, as well as for housing counselors within the state.<sup>165</sup> In addition to the Act, the state provides and funds a housing hotline<sup>166</sup> as well as a website for consumer credit education.<sup>167</sup>

### 2. Benefits to Lenders

At the same time, the Act is considerate of the needs and rights of lenders by avoiding some of the more onerous provisions supporting homeowners in other jurisdictions.<sup>168</sup> North Carolina lawmakers did not consider a mortgage moratorium, as other states have.<sup>169</sup> While it encourages renegotiation, the Act does not require homeowners and lenders to meet in court-supervised sessions,<sup>170</sup> nor does it provide additional funding to homeowners facing impending foreclosure.<sup>171</sup> The Act does not require lenders to notify homeowners repeatedly in writing before the interest rates reset.<sup>172</sup> Finally, the Act is restricted to subprime loans, so it does not affect foreclosure proceedings for mortgage loans in more affluent spheres of North Carolina.<sup>173</sup>

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165. N.C. Act, *supra* note 3, § 1.

166. Press Release, North Carolina Attorney General, *supra* note 47.

167. N.C. Foreclosure Help, *supra* note 112.

168. *See* N.C. Act, *supra* note 3, § 1.

169. *See, e.g.*, Confessore & Peters, *supra* note 101 (noting the failed New York moratorium proposal); Hopkins, *supra* note 102 (discussing the Maryland moratorium).

170. *Compare* N.C. Act, *supra* note 3 with N.Y. Act, *supra* note 103, § 3; Pa. Act, *supra* note 111, § 2; and Conn. Act, *supra* note 104, § 16.

171. *Compare* N.C. Act, *supra* note 3 with Pa. Act, *supra* note 111, § 3; Conn. Act, *supra* note 104, § 12; and Mich. Act, *supra* note 131.

172. *Compare* N.C. Act, *supra* note 3 with N.J. Act, *supra* note 108, § 5.

173. *Compare* N.C. Act, *supra* note 3, § 1 with Cal. Act, *supra* note 105, § 2 and Md. Act, *supra* note 104.

## V. INTERRELATION WITH FEDERAL LAWS

A. *Potential Preemption of State Foreclosure Prevention Statutes by the OCC and OTS*

If state foreclosure prevention laws significantly disrupt lenders' practices and rights to reclaim their loans through foreclosure, then national lenders may increase pressure on Congress to create a federal law to pre-empt state laws.<sup>174</sup> Generally, mortgages are governed by contract law at the state level, but if state laws interfere with the collection processes and rights of national banks or federal thrifts, federal regulators in the OCC or Office of Thrift Supervision (OTS) may create an overarching rule in defense of the banks.<sup>175</sup> The 2004 OCC preemption rule warns: "state laws that obstruct, impair, or condition a national bank's ability to fully exercise its Federally authorized real estate lending powers do not apply to national banks."<sup>176</sup> To date, however, federal regulators have not preempted state foreclosure prevention laws.<sup>177</sup> The OCC elaborated in the Federal Register that "any other law that the OCC determines to interfere to only an insignificant extent with national banks' lending authority or is otherwise consistent with national banks' authority to engage in real estate lending would not be preempted."<sup>178</sup> While the federal agencies maintain the right in these policies to preempt any state foreclosure prevention law, the moderate nature of North Carolina's Act should protect it from federal preemption.

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174. Hopkins, *supra* note 102.

175. *Id.*

176. Applicability of State Law, 12 C.F.R. § 34.4 (2004).

177. Hopkins, *supra* note 102.

178. Bank Activities and Operations; Real Estate Lending and Appraisals, 69 Fed. Reg. 1904 (Jan. 13, 2004) (to be codified at 12 C.F.R. pts. 7 and 34).

*B. Federal Foreclosure Prevention Efforts*

## 1. Federal Foreclosure Prevention Legislation

The federal government responded to the foreclosure crisis before the North Carolina Act by passing the HOPE for Homeowners Program in the Housing and Economic Recovery Act<sup>179</sup> on July 30, 2008. This voluntary program<sup>180</sup> was created under the Federal Housing Administration “to allow homeowners to avoid foreclosure by reducing the principle [sic] balance outstanding, and interest rate charged, on their mortgages.”<sup>181</sup>

Then in October 2008, the Emergency Economic Stabilization Act of 2008<sup>182</sup> was passed, which affects the foreclosure crisis primarily through the federal government’s purchase of “troubled assets,” a defined term in that act that includes residential mortgages.<sup>183</sup> Federal agencies that acquire control over such mortgages (either wholly or in some form of securities or investment) will encourage servicers<sup>184</sup> to use the HOPE for Homeowners Program “or other available programs to minimize foreclosures,”<sup>185</sup> and “shall consent, where appropriate, . . . to reasonable requests for loss mitigation measures.”<sup>186</sup> When the government owns a qualified residential mortgage outright, it will implement a loan modification plan that “may include (A) reduction in interest rates; (B) reduction of loan principal; and (C) other similar modifications.”<sup>187</sup>

The federal foreclosure prevention legislation passed in the summer and fall of 2008<sup>188</sup> does not preempt the North Carolina Act. The federal laws coordinate well with the goals of and efforts

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179. Housing and Economic Recovery Act of 2008, P.L. 110-289, 122 Stat. 2654 (2008) (codified at 12 U.S.C.A. § 1715z-23 (2008)).

180. Housing and Economic Recovery Act § 1715z-23(e)(4)(C).

181. Housing and Economic Recovery Act § 1715z-23(b)(2).

182. Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, 122 Stat 2765 (2008) (to be codified at 12 U.S.C.A. § 5202).

183. Emergency Economic Stabilization Act § 3(9).

184. Emergency Economic Stabilization Act § 110(c).

185. Emergency Economic Stabilization Act § 109(a).

186. Emergency Economic Stabilization Act § 109(c).

187. Emergency Economic Stabilization Act § 110(b)(2).

188. Housing and Economic Recovery Act, 12 U.S.C.A. § 1715z-23 (2008); Emergency Economic Stabilization Act.

behind North Carolina's Act. The Act's requirement that the lender provide the homeowner with advance notice of foreclosure and contact information for the lender should give the homeowner the opportunity to learn about state and federal programs and assistance that may be available.

## 2. Proposed Federal Foreclosure Prevention Legislation

The federal government is developing additional policies to stem the increasing foreclosure rates. Federal agencies, led by the Federal Deposit Insurance Corporation (FDIC), are developing a plan in which lenders that systematically modify their mortgage loans according to government standards would receive the government's guarantee to insure them if the modification failed.<sup>189</sup> The Working Group has encouraged the systematic approach to renegotiation.<sup>190</sup> The plan echoes the method that the FDIC used for systematically modifying delinquent mortgage loans at IndyMac over the summer of 2008.<sup>191</sup> However, if this national plan goes through, it would be implemented by the cooperation of federal agencies, including the FDIC, Department of the Treasury (Treasury), and Office of Management and Budget, and funded, up to \$50 billion, by the Treasury.<sup>192</sup> This plan also appears to coordinate with the North Carolina Act and not preempt its provisions, although until the plans are codified, it is impossible to know exactly how it could interact with the provisions of the Act.

## 3. Voluntary Efforts by Lenders

Several national lending institutions are also considering ways to decrease foreclosure rates by systematically modifying

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189. Joe Adler, *Plan to Guarantee Modified Mortgages Makes Headway*, AM. BANKER, Oct. 30, 2008, § Washington, at 1, available at <http://www.americanbanker.com/article.html?id=2008102924R6BH2K&queryid=489741752&hitnum=1>. Accord Holzer et al., *supra* note 23.

190. DATA REPORT NO. 3, *supra* note 19, at 3.

191. Adler, *supra* note 189. Accord Moira Herbst, *Foreclosures: Feds to the Rescue?* BUSINESSWEEK, Oct. 30, 2008, [http://www.businessweek.com/bwdaily/dnflash/content/oct2008/db20081029\\_246033.htm](http://www.businessweek.com/bwdaily/dnflash/content/oct2008/db20081029_246033.htm).

192. Adler, *supra* note 189. Accord Michael R. Crittenden & Jessica Holzer, *Relief Nears for 3 Million Strapped Homeowners*, WALL ST. J., Oct. 30, 2008, at A3.

their loans<sup>193</sup> and even instituting a foreclosure moratorium.<sup>194</sup> These voluntary efforts have not yet been successful in slowing the foreclosure rate across the country,<sup>195</sup> but they may become more influential as more lenders work to prevent foreclosures. However, much like the enacted and proposed federal laws, these measures will supplement and not override the efforts made by the North Carolina Act to slow the foreclosure rate in the state.

## VI. CONCLUSION

The North Carolina Act balances homeowners' rights with lenders' rights through provisions that generally fall within the range of what other jurisdictions' laws have done.<sup>196</sup> One such provision is the Act's requirement for lenders to wait for forty-five days after notifying homeowners of an impending foreclosure, in between some states' thirty-day waiting period and others' sixty- or ninety-day period.<sup>197</sup> Another example is the Act's expiration date: it falls four months after the expiration of the Colorado legislation, but several years before California's act expires in 2013.<sup>198</sup> The law also proves its moderation by measures that are not included. By not restricting the forty-five day delay before filing a foreclosure to once per twelve-month period, as some jurisdictions have done, North Carolina is more permissive of

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193. Robin Sidel, *Massive Effort to Save Mortgages*, WALL ST. J., Nov. 1, 2008, <http://online.wsj.com/article/SB122549543952589677.html> (noting that major lending institutions, including J.P. Morgan Chase & Co., Bank of America Corp., and Wachovia Corp. (now a subsidiary of Wells Fargo & Co.) are systematically modifying or planning to systematically modify their delinquent mortgage loans); Ruth Simon, *Citi to Modify Terms for U.S. Mortgages*, WALL ST. J., Nov. 11, 2008, <http://online.wsj.com/article/SB122636776229916053.html> (reporting on modifications planned by Citigroup Inc.).

194. Simon, *supra* note 193 (noting that Citigroup, Inc. is not pursuing foreclosures that it has started for over 16,000 homeowners).

195. Holzer et al., *supra* note 23.

196. Compare N.C. Act, *supra* note 3 with, e.g., N.Y. Act, *supra* note 103; Cal. Act, *supra* note 105; Conn. Act, *supra* note 104; Colo. Act, *supra* note 104; Ky. Act, *supra* note 105; and Md. Act, *supra* note 104.

197. Compare N.C. Act, *supra* note 3, § 1 with N.Y. Act, *supra* note 103, § 2; Cal. Act, *supra* note 105, § 2; Conn. Act, *supra* note 104, § 7; Colo. Act, *supra* note 104, § 1; Ky. Act, *supra* note 105, § 31; and Md. Act, *supra* note 104, §§ 3, 7.

198. Compare N.C. Act, *supra* note 3, § 6 with Cal. Act, *supra* note 105, § 2 and Colo. Act, *supra* note 104, § 2.

delinquent homeowners than other states.<sup>199</sup> However, by limiting the additional thirty-day extension to one time per homeowner, the Act is stricter than others.<sup>200</sup> The Act would probably better reflect and respond to the realities of mortgage delinquencies if it had limited foreclosure delays to once a year but allowed more than one extension per homeowner. Nonetheless, the provisions that the Act does contain balance what homeowners and lenders would each prefer.

North Carolina's moderation may protect homeowners more than it appears. Because the Act is considerate of lenders' rights, it does not encourage federal preemption to support lenders that other, more homeowner-focused acts might.<sup>201</sup> Furthermore, some acts may have gone so far to protect homeowners that they may end up harming homeowners as well as failing to protect lenders.<sup>202</sup> For example, representatives from Fannie Mae and Freddie Mac have indicated that they will not buy New York subprime loans because of the costs and risks that come to them as purchasers from the additional regulation.<sup>203</sup> That disclosure concerned mortgage brokers in New York who feared that other, smaller banks would also be hesitant, if not entirely unwilling, to take the mortgages because they doubt that they would have any opportunity to sell them.<sup>204</sup> This scenario could not occur under North Carolina's Act, both because its provisions are more supportive of lenders and because it does not apply to mortgages created after 2007. In that way, the moderation of the North Carolina Act makes it more beneficial to homeowners overall.

North Carolina has made a noble step toward alleviating one of the greatest economic harms of this decade by dealing directly with the problem of foreclosures, especially in subprime mortgages. The Act protects homeowners and lenders alike by seeking to avoid foreclosures, allowing homeowners to keep their

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199. *E.g.*, N.Y. Act, *supra* note 103, § 2, Colo. Act, *supra* note 104, § 1.

200. N.C. Act, *supra* note 3, § 1.

201. Bob Tedeschi, *Shying Away from N.Y. Loans*, N.Y. TIMES, Sept. 6, 2008, at RE9, available at <http://www.nytimes.com/2008/09/07/realestate/07mort.html?scp=1&sq=shying%20away%20from%20NY%20loans&st=cse>.

202. *E.g.*, N.Y. Act, *supra* note 103.

203. Tedeschi, *supra* note 201.

204. *Id.*

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homes and equity, and permitting lenders to negotiate another option to receive their payments that may be more beneficial and lucrative in the long run than repossessing the home. Whether the Act will reduce foreclosures dramatically in North Carolina remains unclear at this time, but the Act contains moderate provisions that are not as extreme as in other jurisdictions. While the Act's provisions do not go as far toward supporting homeowners as some other jurisdictions' laws do, the North Carolina Act protects and provides guidance to homeowners while not diverging substantially from lenders' rights and goals. The Act also works well in conjunction with federal legislation and proposals to ease the foreclosure crisis. North Carolina's Act looks as though it will be a strong measure to reduce many of the foreclosures that the state otherwise would have faced by 2010.

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