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FEDERAL LAW REQUIRES CREDITORS TO PROVIDE COUNSELING ASSISTANCE INFORMATION TO DELINQUENT HOMEOWNERS

Paul H. Schieber*

I. Introduction

On February 5, 1988, former President Reagan signed the Housing and Community Development Act of 1987 (the "Act").¹ Buried deep within the Act is a little-known benefit for mortgagors. Section 169 of the Act requires that a creditor of a home loan notify the delinquent homeowner about counseling assistance if the homeowner is unable to correct a delinquency due to an involuntary loss of employment.² Section 169 applies to most federally-insured and federally-guaranteed home loans, as well as to all conventional home loans, regardless of the loan's size.³ In order to qualify under the Act, the homeowner's home loan must be secured by a single-family dwelling which is the homeowner's principal residence.⁴ Unfortunately, the Department of Housing and Urban Development ("HUD") has complicated Section 169 by issuing non-binding compliance guidelines which offer advice that are internally contradictory. Also, at least one state has already enacted legislation requiring that creditors provide similar notice about state agencies which provide counseling assistance.

Neither Section 169 nor HUD's guidelines specify in what form the counseling information should be given or when the creditor must give this information to the homeowner. Moreover, neither Section 169 nor HUD's guidelines state the ramifications of a creditor's failure to provide this notice. However, a homeowner undergoing a foreclosure proceeding should have his or her attorney determine whether the creditor has complied with the required notice procedures. If the creditor has not complied, the homeowner may be able to delay the foreclosure proceeding in order to obtain counseling assistance.

II. Legislative Background

Section 106 of the Housing and Urban Development Act of 1968⁵ authorized HUD to provide, or to contract for private parties to provide, counseling services for homeowners with mortgages insured by the Federal Housing Administration ("FHA") under the National Housing Act.⁶ Congress passed this legislation to help insured homeowners meet their mortgage obligations.

In 1986, Representative James A. Traficant introduced legislation that was to become Section 169 of the Housing and Community Development Act of 1987. Congressman Traficant had served as sheriff of Mahoning County, Ohio, prior to his election to Congress. According to Traficant, one of his responsibilities as sheriff was to conduct residential mortgage foreclosures, a task he found particularly distasteful. In his first year in the House of Representatives, Traficant introduced this legislation in an effort to make foreclosures more difficult or, at least, more palatable to consumers. Section 169 expanded the scope of HUD's original counseling assistance program beyond mortgages secured under the FHA mortgage insurance program.

III. Scope of Coverage

Section 169 applies to most federally-insured or federally-guaranteed home loans (*e.g.*, FHA and Veteran's Administration loans), and all home loans provided by private creditors.⁷ Section 169 does not apply to Farmers Home Administration loans assisted under Title V of the Housing Act of 1949 (primarily loans and insurance programs for rural housing administered by the Farmers Home Administration).⁸ A home loan is defined under Section 169 as "a loan secured by a mortgage or

lien on residential property."⁹ The section does not differentiate between home loans secured by a first mortgage and home loans secured by subsequent mortgages or liens, including home equity loans. Nor does Section 169 distinguish between home loans used to purchase the residence and home loans used for other purposes.

HUD's guidelines state that the home loan must be secured by a "one-family dwelling."¹⁰ However, both Section 169¹¹ and the guidelines¹² provide that the dwelling may be divided into as many as four units. Therefore, the term "dwelling" includes two-, three-, and four-unit properties, condominiums and cooperative housing projects.¹³ Also, the residence that secures the home loan, or one unit on the property that secures the loan, must be the homeowner's principal residence.¹⁴ HUD has defined a principal residence as "a residential property occupied by the mortgagor as his or her primary residence more than half the time during the year immediately preceding any notice of mortgage delinquency, or (if the mortgage is less than a year old) . . . more than half the time since the debt was incurred."¹⁵ Therefore, counseling assistance information need not be provided for purely investment properties or vacation homes.

The duties created by the Act apply to all creditors of delinquent homeowners.¹⁶ Section 169 defines "creditor" to include not only the original lender, but also anyone who is responsible for collecting the payments.¹⁷ In addition, the Act applies not only to lending and

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collecting institutions, but to individual lenders as well. Consequently, if an individual holds a mortgage on even one residential property, for example, in the instance of an owner financed sale, that owner-lender must comply with the Act.

A homeowner is entitled to receive the counseling information if the homeowner is unable to meet his or her mortgage payments due to the involuntary loss of, or reduction in, employment either of the homeowner or of someone who contributes to the homeowner's income.¹⁸ Neither Section 169 nor HUD's guidelines state whether the homeowner is obligated to inform the creditor that the delinquency is due to a loss of employment, or whether the creditor has the obligation to discover the cause of the delinquency. However, HUD's guidelines do state that "[c]reditors may find it more convenient and less costly to provide the notice . . . to all delinquent homeowners, rather than to those that they first determine to meet the loss [or] reduction of income standard" ¹⁹ Thus, HUD's guidelines appear to indicate that the creditor is obligated to discover the cause of the homeowner's delinquency.

Under Section 169, the creditor has two duties to the eligible homeowner: (1) to inform the homeowner of the creditor's own counseling assistance services, if available, and (2) to provide to the homeowner a list of HUD-approved mortgage counseling agencies.²⁰ Section 169 only requires creditors to notify homeowners of the counseling assistance services, and does not obligate the lender to actually provide the counseling services.²¹ HUD has provided no guidance as to the format in which this information is to be provided to the homeowner. However, HUD has published a list of approved homeownership counseling agencies for each state and, in some states, for particular local communities.²²

IV. Timing of Notice

Section 169 does not specify when the creditor must provide the counseling information to the homeowner. HUD, however, has given limited but somewhat conflicting guidance. HUD recommends that notice "be provided at the earliest point that a creditor, as part of normal business practice, communicates the fact of the delinquent status of the homeowner's account to the homeowner."²³ If followed, this recommendation may prove cumbersome and unnecessary.

In practice, the time when delinquency notices are sent varies from creditor to creditor. A creditor may send a notice at the end of the payment grace period, or at any time when a payment is late. Frequently, creditors send delinquency notices merely to inform homeowners that their payments are overdue. At the time of the first notice a creditor may not anticipate, nor may there be any real risk, that the homeowner will default on the loan.

HUD has informally acknowledged that it may be unnecessary to send the counseling information with the first notice, and has suggested that creditors send the counseling information with a 45-day delinquency notice. This advice works well for creditors who regularly send 45-day default notices. However, it does not clarify the obligations of creditors who send only 30- and 60-day notices. Are those creditors now required to adopt a third, 45-day notice, or will the 60-day notice be sufficient? HUD's advice is unclear and, considering the additional expense to creditors and ultimately to homeowners, the required timing of the notice should be clarified.

On the one hand, the creditor must send the homeowner notice of counseling services "sufficiently in advance of any adverse action taken as a result of default to afford the homeowner time to take advantage of the possible assistance that counseling services can pro-

vide."²⁴ In most cases, 60-day notices would meet this definition. On the other hand, there might be cases where a 60-day notice would be insufficient for homeowners to arrange and take advantage of a counselor's advice. How much notice the homeowner needs in order to take advantage of the counseling services depends upon how soon the lender will foreclose on the loan.

Therefore, until HUD clarifies when creditors must send counseling service information, creditors would be well-advised to analyze their current notice procedures and consult with legal counsel to determine the most appropriate time for providing this information. Such consultation should be done immediately as the Act already has full legal force and effect.²⁵

V. Enforcement

Section 169 fails to provide any specific penalties for failure to comply with the counseling notice requirement. Nevertheless, a homeowner may be able to cite a creditor's failure to comply with the Section 169 as a defense in a foreclosure action. HUD has interpreted Section 169 as creating a legal duty on the part of creditors, and has suggested that "noncompliance with the law's requirements could be an actionable event that could affect the [lender's] ability to carry out foreclosure in a timely manner."²⁶ The courts' receptivity to a homeowner raising such a defense in a foreclosure proceeding is uncertain because, as yet, this defense has not been the subject of litigation.

Section 169 does not give HUD the broad power to require that all creditors comply with the notice requirement.²⁷ However, HUD has stated that it will require that all creditors of HUD-approved mortgages comply with Section 169.²⁸ Any creditor of a HUD-approved mortgage who fails to comply with Section 169 will be subject to HUD Mortgagee Review Board²⁹ jurisdiction and administrative ac-

tion.³⁰ HUD has also suggested that state or other federal agencies that have supervisory authority over home loans may enforce Section 169 upon creditors within their jurisdiction, and that homeowners may wish to pursue enforcement of the statute with those agencies.³¹

A consumer who has become delinquent or who is in default due to an involuntary loss of employment should seek counseling assistance from his or her financial institution. If counseling assistance is not provided by the institution, the homeowner should ask the creditor to provide HUD's approved counseling agency list. If a creditor fails to comply with Section 169, the homeowner should make the court aware of this fact during the foreclosure proceedings. The court may enforce Section 169 by delaying the foreclosure proceedings to allow the homeowner time to pursue counseling services.

VI. Relationship to Similar State Law

Pennsylvania has passed the Homeowner's Emergency Mortgage Assistance Act,³² commonly referred to as "Act 91," which requires homeownership counseling notices parallel to those required under the federal statute. Act 91 applies to most residential mortgages and liens on real property located in Pennsylvania.³³ The property securing the home loan must be the homeowner's principal residence,³⁴ and be a one- or two-family owner-occupied residence.³⁵ Act 91 excludes mortgages secured by the Federal Housing Administration under Title II of the National Housing Act,³⁶ and mortgages given by a non-corporate seller.³⁷

Pennsylvania creditors must provide the notice promulgated by the Pennsylvania Housing Finance Agency to delinquent homeowners no earlier than 60 days into delinquency.³⁸ The notice must inform the homeowner of state-approved homeownership counseling services, and that the homeowner has 30 days to meet with his or her creditor to attempt to resolve the delinquency or default by restructuring

the loan payment schedule.³⁹ Act 91 precludes creditors from instituting foreclosure proceedings before the notice is sent.⁴⁰ In addition, if the homeowner chooses to meet with the homeownership counseling agency, the agency must send the creditor a notice that the creditor may not institute foreclosure proceedings until 30 days after the homeowner has met with the agency.⁴¹

The Pennsylvania Housing Finance Agency recently wrote to HUD asking that HUD accept compliance with Act 91 as compliance with Section 169. HUD has not yet responded to this request. At least for now, Pennsylvania creditors must comply with both the Act 91 requirements and the Section 169 requirements under the federal Act.

VII. Conclusion

The Section 169 of the Housing and Community Development Act of 1987 requires all creditors to provide information on counseling assistance to homeowners whose home loan payments become delinquent due to an involuntary loss of employment. Neither Section 169 nor the subsequent HUD advisory statements give creditors adequate guidance about how early they must give the notice to homeowners. Without further clarification, creditors may inadvertently fail to comply with Section 169. As a result, creditors are well advised to seek the advice of counsel in designing a course of action to comply with Section 169. Improper action on the part of the creditor could provide a homeowner with a new defense in foreclosure proceedings.

9. 12 U.S.C. § 1701x(c)(6)(C).
10. 54 Fed. Reg. at 20964.
11. 12 U.S.C. § 1701x(c)(6)(E).
12. 54 Fed. Reg. at 20964.
13. 12 U.S.C. § 1701x(c)(6)(E).
14. *Id.* at § 1701x(c)(4)(A).
15. 54 Fed. Reg. at 20964.
16. 12 U.S.C. § 1701x(c)(5).
17. *Id.* at § 1701x(c)(6)(A).
18. *Id.* at § 1701x(c)(4)(C).
19. 54 Fed. Reg. at 20964.
20. *Id.*
21. *Id.*
22. 54 Fed. Reg. 20967-21037.
23. 54 Fed. Reg. at 20965.
24. *Id.*
25. As originally enacted, Section 169 expired on September 30, 1989. 12 U.S.C. § 1701x(c)(9). However, on November 5, 1989, President Bush signed a bill into law which extends the Section 169 requirements through September 30, 1990. Pub. L. No. 101-137, Sec. 8 (1989).
26. *Id.*
27. *Id.*
28. *Id.*
29. The HUD Mortgage Review Board has the authority, pursuant to 24 C.F.R. § 25.9(j) (1989), to review and enforce claims under HUD guidelines.
30. 54 Fed. Reg. at 20965.
31. *Id.*
32. 35 Pa. Cons. Stat. Ann. §§ 1680.401c-.411c (Purdon Supp. 1989).
33. 35 Pa. Cons. Stat. Ann. § 1680.401c(a).
34. *Id.* at § 1680.401c(a)(1).
35. *Id.* at § 1680.401c(a)(2).
36. *Id.* at § 1680.401c(a)(3) (citing 12 U.S.C. §§ 1707 to 1715z-18).
37. *Id.* at § 1680.401c(a)(4).
39. *Id.* at § 1680.403c(a).
39. *Id.* at § 1680.403c(b).
40. *Id.* at § 1680.403b(a).
41. *Id.* at § 1680.403c(b).

ENDNOTES

1. Pub. L. No. 100-242, Title I, 101 Stat. 1865 (codified in scattered sections of 12 U.S.C. (1988)).
2. 12 U.S.C. § 1701x(c)(4)(C).
3. 12 U.S.C. § 1701x(c)(4)(B).
4. 54 Fed. Reg. 20964.
5. Pub. L. No. 90-448, Title I, Sec. 106, 82 Stat. 490 (codified at 12 U.S.C. § 1701x (1988)).
6. 12 U.S.C. § 1701x(a)(1).
7. *Id.* at § 1701x(c)(4)(B).
8. Pub. L. No. 81-171, Title XII, 63 Stat. 413 (codified in scattered sections of 42 U.S.C. (1982 & Supp. V 1987)).