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TO THE  
HOUSE COMMITTEE ON  
CONSUMER PROTECTION AND COMMERCE  
THE TWENTY-EIGHTH STATE LEGISLATURE  
REGULAR SESSION OF 2015

Wednesday, February 11, 2015  
2:30 p.m.

TESTIMONY ON H.B. 371  
RELATING TO FORECLOSURES

THE HONORABLE ANGUS L.K. MCKELVEY, CHAIR,  
AND MEMBERS OF THE COMMITTEE:

My name is Iris Ikeda, Commissioner of Financial Institutions (“Commissioner”), offering comments on H.B. 371, Relating to Foreclosures, on behalf of the Department of Commerce and Consumer Affairs (“DCCA” or the “Department”).

H.B. 371 would prohibit a mortgage creditor from executing on any asset of the debtor beyond the asset that is secured by a mortgage.

The bill would prohibit a financial institution from collecting on the full amount of debt owed from its mortgage loan with a consumer. As the state regulator of financial institutions, the Division of Financial Institutions (“DFI”) reviews loan portfolios to determine

if the banks are in compliance with state and federal laws, rules and guidelines. One factor in reviewing loan files is validating that banks underwrite the loans in a safe and sound manner taking into account a consumer's income and debts and whether the consumer can afford to take on a mortgage debt. DFI also reviews the bank's books and records to check compliance with loss mitigation programs including the process used in foreclosure procedures.

The typical foreclosure process takes about three years from the time the borrower is in default to the sale of the house in foreclosure. In foreclosure status, if the bank cannot recoup its investment by selling the house, the balance is converted to an unsecured debt against the debtor. If the bank cannot collect on the full mortgage related debt, the bank will re-evaluate the underwriting process and mortgage program(s) it offers consumers. From the regulator's point of view, the bank will not be able to safely continue to make residential loans at its current level because the bank will have to reserve more capital to reserve for anticipated losses, i.e. not being able to collect on its debt. If this cycle continues, there will be a reduction in capital for residential loans that banks can safely make for consumers. The more capital reserved by the bank, the fewer loans they are able to make.

Thank you for the opportunity to provide comments on this measure. I would be pleased to respond to any questions you may have.



*Mortgage Bankers Association of Hawaii*  
*P.O. Box 4129, Honolulu, Hawaii 96812*

February 10, 2015

The Honorable Angus L.K. McKelvey, Chair,  
The Honorable Justin H. Woodson, Vice Chair, and  
Members of the House Committee on Consumer Protection & Commerce  
State Capitol, Room 325  
Honolulu, Hawaii 96813

Re: House Bill 371 Relating to Foreclosures

**Chair McKelvey, Vice Chair Woodson and Members of the House Committee on Consumer Protection & Commerce:**

I am Linda Nakamura, representing the Mortgage Bankers Association of Hawaii ("MBAH"). The MBAH is a voluntary organization of individuals involved in the real estate lending industry in Hawaii. Our membership consists of employees of banks, savings institutions, mortgage bankers, mortgage brokers, financial institutions, and companies whose business depends upon the ongoing health of the financial services industry of Hawaii. The members of the MBAH originate or support the origination of the vast majority of residential and commercial real estate mortgage loans in Hawaii. When, and if, the MBAH testifies on legislation, it is related only to mortgage lending.

The MBAH opposes House Bill 371 Relating to Foreclosures.

The MBAH opposes House Bill 371 because mortgage lenders will be stripped of any deficiency judgment if a mortgage lender completes a judicial foreclosure and the mortgage property is sold for less than the mortgage lender is owed on the note.

Mortgage lenders are in the business of making mortgage loans to provide housing and real estate investments to consumers. Mortgage lenders are not in the business of making mortgage loans to foreclose on a consumer. When a consumer defaults on a mortgage, mortgage lenders work with the consumer to avoid foreclosure. Mortgage lenders will work with the consumer on a repayment plan, modification, short sale or a deed in lieu of foreclosure.

When a mortgage lender provides a mortgage loan to a consumer, an appraisal of the asset that is to secure the mortgage loan is completed. The appraisal is of a point in time and the mortgage lender relies on that appraisal to calculate loan to value. Loan to value by definition is the ratio of the percentage of the property's value that is mortgaged. Current industry standard for loan to value is 80%. The mortgage lender does not make

any assumptions with respect to the future valuation of the asset. It relies on the appraisal to calculate the loan to value to make a credit decision. House Bill 371 may force mortgage lenders to require a lower loan to value ratio to mitigate the risk of not being able to collect on any potential deficiency judgment.

As stated above, mortgage lenders are in the business of making mortgage loans to consumers. During bad economic times, property values decline. Both owner occupied homeowners and investors will have the easy option of walking away from the properties with no recourse as there is no incentive to work with the mortgage lender to avoid foreclosure. This will lead to strategic defaults whereby borrowers who are not past due on their mortgage see no reason to continue to make payments on a property that has decreased in value. Many real estate investors purchase condominium units in Hawaii. This bill may leave condominium projects with many empty units as real estate investors walk away from bad investments.

This Bill may harm the future of mortgage lending as well as the real estate market in Hawaii.

Thank you for the opportunity to present this testimony.

LINDA NAKAMURA  
Mortgage Bankers Association of Hawaii

Presentation To  
Committee on Consumer Protection and Commerce  
February 11, 2015 at 2:30 pm  
State Capitol Conference Room 325

**Testimony in Opposition to House Bill No. 371  
Relating to Foreclosures**

TO: The Honorable Angus L. K. McKelvey, Chair  
The Honorable Justine H. Woodson, Vice Chair  
Members of the Committee

My name is Edward Pei and I am the Executive Director of the Hawaii Bankers Association (HBA). HBA is the trade association representing eleven FDIC insured depository institutions with branch offices in the State of Hawaii.

HBA is opposed to this Bill that will prohibit mortgage lenders from pursuing the balance owed to the lender by homeowners after a judicial foreclosure action in which the sale of the home resulted in a remaining balance, or deficiency. Currently, lenders will seek to obtain a judgment for the balance owed to pursue recovery. Without this recourse, lenders will have to look critically at altering their credit policies and underwriting guidelines, likely resulting in requiring larger down payments (lower loan to value ratio), and/or tighter underwriting standards. Experience has shown that borrowers making larger down payments are less likely to default. But, larger down payments would also result in fewer consumers being able to afford to buy a home in Hawaii, even if they have the monthly cash flow to service their debt.

The testimony submitted by the Hawaii Financial Services Association and the Mortgage Bankers Association articulates very well the problems with this Bill as well as the unintended consequences if this Bill becomes law. We agree completely with their testimony and the reasons this Bill should not pass out of your Committee.

It is ironic that this Bill, seemingly designed to assist consumers, may ultimately hurt the prospective new home buyer. Actually, if anything, this Bill only protects the wealthier homeowner with other assets that actually could be used to continue mortgage payments, shielding those assets from attachment.

Thank you very much for the opportunity to submit this testimony and we would be happy to respond to any questions.



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February 11, 2015

Rep. Angus L.K. McKelvey, Chair  
Rep. Justin H. Woodson, Vice Chair  
and members of the House Committee on Consumer Protection and Commerce  
Hawaii State Capitol  
Honolulu, Hawaii 96813

Re: **House Bill 371 (Foreclosures)**  
**Hearing Date/Time: Wednesday, February 11, 2015, 2:30 p.m.**

I am Marvin Dang, the attorney for the **Hawaii Financial Services Association** (“HFSA”). The HFSA is a trade association for Hawaii’s consumer credit industry. Its members include Hawaii financial services loan companies (which make mortgage loans and other loans, and which are regulated by the Hawaii Commissioner of Financial Institutions), mortgage lenders, and financial institutions.

The HFSA **opposes** this Bill.

The purpose of this Bill is to prohibit a mortgage creditor from executing on any asset of the debtor beyond the asset that is secured by the mortgage.

## **The Senate companion bill was deferred indefinitely.**

A companion to this House Bill, Senate Bill 1192 (Foreclosures), was heard by the Senate Committee on Commerce and Consumer Protection (“CPN”) on February 4, 2015. After the hearing, the CPN Committee deferred the Senate Bill indefinitely.

## **Important things to know about loss mitigation and foreclosures.**

At the outset, we want to emphasize that a foreclosure action is the last resort for a lender when a borrower’s mortgage loan is delinquent. Before commencing a foreclosure action, a lender will consider many “loss mitigation” alternatives to foreclosure, such as loan modification, reinstatement, forbearance (temporarily suspending or reducing payments), deed-in-lieu of foreclosure, or short sale.

The federal Consumer Financial Protection Bureau (“CFPB”) issued a rule effective January 10, 2014 requiring most servicers to provide loss mitigation options to delinquent borrowers prior to foreclosure. The CFPB rule has the force and effect of law. Servicers cannot foreclose until the mortgage is 120 days past due. Servicers are required to establish and follow loss mitigation procedures. These procedures must acknowledge a borrower’s application for loss mitigation options within 5 business days of receipt of an application. If the application is not complete, the borrower must be provided with a list of information or documentation that is required to complete the application. Even after a foreclosure has started, the CFPB rule requires servicers to evaluate a borrower for loss mitigation options if the loss mitigation application is received 37 days before a scheduled foreclosure sale date. Servicers must complete the loss mitigation evaluation within 30 days of receipt of a complete loss mitigation application and provide the borrower with a written decision.

We also want to highlight that the number of foreclosure actions which were filed in Hawaii courts in 2014 decreased 39% from the number of filings in 2013. (See the newspaper article “Isle

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foreclosures decreased 39% during 2014” in the Sunday, February 1, 2015 Honolulu Star-Advertiser on page D2.)

**This Bill will allow borrowers to shield their assets from deficiency judgments.**

Under this Bill, if a lender decides to foreclose judicially on a real property that is collateral for a mortgage loan that’s in default, and if that property is sold at a foreclosure auction for less than the amount to pay off the loan, the lender will be barred from obtaining a deficiency judgment against the borrower.

Without a deficiency judgment against the borrower, the lender will not be able to execute on or garnish any other assets of the borrower. That’s even though the borrower might own other real property, be flush with cash in savings accounts, or have a steady flow of money from salary, rents, dividends, and other sources. Those assets will be shielded from deficiency judgments.

**Problematic coverage of this Bill.**

This Bill is problematic. First, it affects all mortgage loans that are already in existence. We understand that there could be constitutional issues involving this retroactive coverage.

Second, under this Bill an asset-rich borrower (individual or entity), whose delinquent mortgage loan is secured by commercial or industrial properties, will benefit when a lender can’t pursue that borrower’s other assets. We contend that such a borrower shouldn’t receive that benefit.

Third, this Bill will insulate from a deficiency judgment a well-off investor-borrower with residential property as collateral for a mortgage loan and who has other assets. We assert that such an investor should not be so insulated.

Fourth, with this Bill, an affluent homeowner-borrower who owns and later acquires other assets or who has abundant sources of income will have those other assets and income protected from a deficiency judgment. We do not agree that such a homeowner should be protected.

**There could be negative unintended consequences if this Bill becomes law.**

Because this Bill prohibits lenders from pursuing deficiencies after foreclosures, lenders will have to absorb the monetary losses. The following negative unintended consequences could result:

● **Future borrowers, including potential homeowners, could be negatively impacted.** The lending industry standard for the “loan-to-value ratio” (i.e. the ratio of the dollar amount of the loan to the value of the property) for residential mortgage loans is 80%. Because of this Bill, lenders might have tighten their loan underwriting standards. If the loan-to-value ratio is lowered below 80%, future borrowers will have to put more money down for purchases or will need to have more equity in their properties for refinancings. Potential first-time homebuyers without cash for larger downpayments won’t be able to buy properties when they can’t qualify for loans.

If lenders need to set aside more money as reserves for loan losses, lenders could have less money available to lend. Future borrowers and potential homeowners could be negatively impacted.

● **There could be harm to Hawaii’s economy and Hawaii’s real estate and lending industries.** If potential buyers can’t get mortgage loans, they might not be able to purchase properties. When it’s harder for property owners to sell their properties, there will be uncertainty in and harm to Hawaii’s economy and real estate industry.

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If mortgage lenders are barred from recovering deficiencies by attaching or garnishing the other assets of the defaulted borrowers, there will be negative financial impacts for lenders. That's because lenders will have to fully absorb the losses.

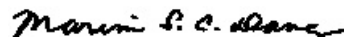
● **This Bill will encourage and unfairly reward “strategic defaults”**. A “strategic default” occurs when a borrower decides not to pay a mortgage loan even though the borrower has the ability to make the payments. Because of this Bill, the other assets owned by the strategic defaulter will be protected. The strategic defaulter will have an incentive to “walk away” from the contractual obligation to repay the loan knowing that the lender will be unable to get a deficiency judgment after a foreclosure sale. Strategic defaulters will be unfairly rewarded.

**Conclusion.**

In conclusion , this Bill appears to be fundamentally flawed. It does not seem to constitute sound public policy.

**Accordingly, we ask that your Committee “hold” this Bill and not pass it.**

Thank you for considering our testimony.



MARVIN S.C. DANG  
Attorney for Hawaii Financial Services Association





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Testimony to the House Committee on Consumer Protection and Commerce  
February 11, 2015

In opposition to HB 371, Relating to Foreclosures

To: The Honorable Angus McKelvey, Chair  
The Honorable Justin Woodson, Vice-Chair  
Members of the Committee

My name is Stefanie Sakamoto, and I am testifying on behalf of the Hawaii Credit Union League, the local trade association for 70 Hawaii credit unions, representing approximately 804,000 credit union members across the state.

This bill would prohibit a mortgage creditor from executing on any asset of the debtor beyond the asset that is secured by the mortgage.

Approximately 50 credit unions in Hawaii currently offer mortgages.

Because credit unions are not-for-profit financial cooperatives owned by their members, the inability of a credit union to seek a deficiency judgment would have to be borne by the other members of the credit union. This could adversely affect the future lending ability of the credit union, or the financial soundness of the credit union.

We also agree with the testimony submitted by the Hawaii Financial Services Association, and the Mortgage Bankers Association of Hawaii.

Thank you for the opportunity to comment.