Foreclosure Fairness Program

Washington State Department of Commerce

ANNUAL REPORT ON PROGRAM PERFORMANCE PER RCW 61.24.163

COMMUNITY ECONOMIC OPPORTUNITIES
FORECLOSURE FAIRNESS PROGRAM

December 2020

REPORT TO THE LEGISLATURE

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Acknowledgments

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Special thanks to the Dispute Resolution Centers, Northwest Justice Project, mediators, attorneys and housing counselors who collaborate with the Department of Commerce to implement and deliver the Foreclosure Fairness Program

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FORECLOSURE FAIRNESS PROGRAM

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Executive Summary

Overview

This report provides Foreclosure Fairness Program (FFP) data to satisfy RCW 61.24.163 and additional programmatic context and background. The full text of the legislative reporting requirements is below:

> 18) Beginning December 1, 2012, and every year thereafter, the department shall report annually to the Legislature on:
>
> (a) The performance of the program, including the numbers of borrowers who are referred to mediation by a housing counselor or attorney;
>
> (b) The results of the mediation program, including the number of mediations requested by housing counselors and attorneys, the number of certifications of good faith issued, the number of borrowers and beneficiaries who failed to mediate in good faith, and the reasons for the failure to mediate in good faith, if known, the numbers of loans restructured or modified, the change in the borrower's monthly payment for principal and interest and the number of principal write-downs and interest rate reductions, and, to the extent practical, the number of borrowers who report a default within a year of restructuring or modification;
>
> (c) The information received by housing counselors regarding outcomes of foreclosures; and
>
> (d) Any recommendations for changes to the statutes regarding the mediation program.

Although the data provided in this report reflects program activity for fiscal year 2020, the report narrative and recommendations also acknowledge the impact of the COVID-19 pandemic on the state economy and thus on the foreclosure arena going forward. The Program Outcomes section contains several tables reflecting the FFP outcomes, which respond directly to the statutory language. The Challenges section addresses significant issues related to funding, reporting and the possibility of increased beneficiary exemptions.

Table 1: Locations of Annual Reporting Requirements in this Report

Subsection	Proviso	Location in Report
(a)	"The performance of the program, including the numbers of borrowers who are referred to mediation by a housing counselor or attorney."	Table 2
(b)	"The results of the mediation program, including the number of mediations requested by housing counselors and attorneys."	Tables 4, 5 and 6
(b)	"The number of certifications of good faith issued, the number of borrowers and beneficiaries who failed to mediate in good faith, and the reasons for the failure to mediate in good faith, if known, the numbers of loans restructured or modified."	Table 7

Subsection	Proviso	Location in Report
(b)	"The change in the borrower's monthly payment for principal and interest, and the number of principal write-downs and interest rate reductions."[1]	Table 4
(b)	"To the extent practical, the number of borrowers who report a default within a year of restructuring or modification."	Commerce conducted a survey in 2014, which determined that this information is not available.
(c)	"The information received by housing counselors regarding outcomes of foreclosures."	Table 3
(d)	"Any recommendations for changes to the statutes regarding the mediation program."	Recommendations

Summary of Issues and Recommendations

Stakeholder Issues and Recommendations

The Washington State Department of Commerce (Commerce) is one of four state agencies and several stakeholders that meet regularly to make recommendations on program implementation. The group is actively considering recommending changes to the Legislature to address the following issues:

- **Change the trigger for beneficiary fees back to issuances of Notice of Default:** The Notice of Trustee Sale's timing has resulted in significantly lower fees.
- **Beneficiary exemptions:** Legislative action will prevent the possibility of beneficiaries, not normally eligible to be exempt from paying fees or from engaging in mediation, from claiming these exemptions due to the decreased foreclosure activity. The Legislature should suspend these exemptions during calendar year 2021.

Commerce Recommendation

- **Allow Commerce to report required data on the web:** Commerce recommends that starting with fiscal year 2021, the program provides the required data quarterly on the program's website instead of providing an annual report in the form of a document. The required data is better suited to a web-based format. This will also ensure stakeholders have up-to-date information on the program's outcomes.

[1] Chapter 61.24.163 RCW requires Commerce to report on “the change in the borrower’s monthly payment for principal and interest.” This data is contained in private documents that are not available to Commerce and, therefore, is not included in this report.

Program Outcomes

Background on Data

Data from Commerce reflect FFP performance for state fiscal years 2012 through 2020, the life of the FFP so far. State fiscal year data gives a snapshot of certain functions within the Foreclosure Fairness Program. Still, it does not always reflect the full impact on borrowers, neighborhoods and communities as some mediations span several years. In some cases, the tables below compare data from the FFP's life to data from the state fiscal year 2020 to provide a complete picture of program performance.

Program Outcomes

The following tables and figures show data as required in statute. See Table 1 for a crosswalk of statutory reporting requirements as they relate to the tables below. Table 2 reflects an overview of mediation referrals the FFP received.

Table 2: Mediation Referrals since Program Start and Fiscal Year 2020

Mediation Referrals	Cases Since Program Start, FY 2012-2020	Cases FY 2020
Total Mediation Referrals Received	11,830	441
Referred by Housing Counselors	5,143 (43%)	267 (60%)
Referred by Attorneys (Private and Civil Legal Aid)	6,687 (57%)	174 (40%)
Cases Assigned to Mediators (Includes Cases That Have Been Mediated, Closed, or Currently Pending an Outcome)	10,692	421
Cases Complete/Closed	10,188	514
Cases Ineligible for Mediation (Typically Because the Beneficiary was Exempt or the Referral Missed the Window of Eligibility in Statute)	1,197	23

Source: Washington State Department of Commerce (^uncharacteristically low due to the protections provided to homeowners in the Cares Act)

Table 3: Housing Counseling Agencies' Overall Outcomes in Fiscal Year 2020

Category Description	Cases in FY 2020
Outputs	
Clients	2236
Referrals to Other Services	363
Outcomes	
Pending Outcomes (Still in Counseling)	1278
Withdrawals from Counseling	57
Home Retention Agreements	502
Non-Retention Agreements	52
No Agreements	332
Foreclosures	15

Source: Washington State Housing Finance Commission

Tables 4, 5 and 6 reflect all certified cases' outcomes since the inception of the program, with numbers for fiscal year 2020 highlighted. These tables contain data from the FFP database and include referrals from both housing counselors and private attorneys.

Table 4: Mediation Session Outcomes Where Agreement was Reached

Outcomes	Cases in FY 2012-2020	Cases in FY 2020
Mediation Session(s) Occurred – Agreement Reached	3018	144
Borrower Stayed in Home (Subcategories Below Are Not Mutually Exclusive)	2327	100
Reinstatements	207	16
Repayments	71	8
Extensions	199	7
Adjusted Rate to Fixed Rate	229	7
Amortization Extensions	506	15
Interest Rate Reductions	955	19
Principal Reductions	118	1

Outcomes	Cases in FY 2012-2020	Cases in FY 2020
Monthly Principal Payment Reductions	380	6
Monthly Interest Payment Reductions	268	2
Refinances	64	5
Other Loan Structures/Modifications	906	35
Principal Forbearances	175	2
Interest Forbearances/Write-offs	45	1
Fees and Penalties Forbearances/Write-offs	35	0
Other Forbearances[2]	70	6

Source: Washington State Department of Commerce

Table 5: Outcomes in Which No Mediation Occurred

Outcomes in Which No Mediation Occurred	Cases FY 2012-2020	Cases FY 2020
Number of Mediations in Which No Mediation Occurred	4166	285
Home-Retention Agreement Reached Before Session	2194	153
Non-retention Agreement Reached Before Session	291	24
Borrower Withdrew from Mediation (Not Included in Other Categories)	677	30

Source: Washington State Department of Commerce

[2] Because of the way the certification is structured, Commerce is not able to identify unique restructures and modifications.

Table 6: Mediation Session Outcomes — Borrower Did Not Stay in Home

Non-retention (Categories Are Not Mutually Exclusive)	Cases FY 2012-2020	Cases FY 2020
Deeds in Lieu	55	0
Short Sales	236	5
Voluntary Surrenders	48	1
Cash for Keys	30	0
Other Non-retention Agreements	438	38

Source: Washington State Department of Commerce

Table 7: Mediation Session Outcomes — Findings of Not in Good Faith

Findings of Not in Good Faith	Cases FY 2012-2020	Cases FY 2020
Borrower Not in Good Faith[3]	731	62
Beneficiary Not in Good Faith	343	7
Both Borrower and Beneficiary Not in Good Faith[4]	31	1

[3] Typically, reported reasons for lack of good faith for either or both the borrower and beneficiary include: lack of timely or accurate provisioning of documents to the mediator and other party; failure to appear at or participate in mediation; failure to pay the mandated share of the mediation fee; beneficiary's representative was not been authorized to make binding decisions.
[4] Even though the certification specifically tracks parties "not in good faith," multiple outcomes are not explicitly tracked as being in "good faith."

Challenges

First Years of the Program

The Foreclosure Fairness Program was initiated in 2011 in response to the significant number of foreclosures resulting from the Great Recession. The program provided an opportunity for borrowers facing foreclosure to demand mediation with their lenders (referred to as beneficiaries in the statute) to look for alternatives to foreclosure. In 2013, the second full year of the program's operation, there were more than 37,000[5] foreclosures statewide, and the program received more than 2,500[6] referrals. As the state recovered from the recession, both the number of foreclosures and the number of referrals declined steadily. With the economy struggling again, the state faces the prospect of a significant increase in foreclosures.

The CARES Act Protections

In fiscal year 2019, the last year for which we have a full year of program activity unaffected by COVID, we received 560 referrals. During fiscal year 2020, the number of referrals was at a comparable pace through the 3rd quarter, when COVID reached Washington State. At that time, due to recommendations from the Department of Financial Institutions (DFI) and the significant protections provided to homeowners through the federal CARES Act, foreclosure activity all but ceased, and the number of referrals in the 4th quarter was 38, compared to 154 during the 4th quarter of fiscal year 2019.

The CARES Act provides significant protections for most homeowners facing foreclosure. The CARES Act covers all federally backed mortgages estimated by the DFI to be approximately 90% of all mortgages in Washington.

There are various protections for borrowers with federally backed mortgages regarding foreclosure, eviction and if and when forbearance can be entered. In addition, most of these protections are scheduled to expire on Dec. 31, 2020.

The Washington State Department of Financial Institutions has issued some recommendations for lenders holding notes for mortgages that are not federally backed and therefore not eligible for the protections provided by the CARES Act. These recommendations are valid through December 31, 2020.[7] Though not a requirement, our anecdotal experience is that lenders of mortgages not federally backed are providing some form of relief to their borrowers.

The Impact of CARES Act Protections on the Foreclosure Fairness Program

The CARES Act has had several major impacts on the Foreclosure Fairness Program. While the number of referrals for mediation has significantly dropped, the legal aid and housing counselor organizations are experiencing an increase in the number of calls from homeowners seeking to understand their options. As the FPP is currently funded by the fees lenders pay to record a Notice of Trustee Sale, and foreclosures have essentially stopped, the program's funding has disappeared.

[5] From unpublished data provided by Zillow.
[6] From the Commerce Foreclosure Fairness Program database.
[7] Washington State Department of Financial Institutions, " Second Amended Guidance to Washington State Regulated and Exempt Residential Mortgage Loan Servicers Regarding Support for Consumers Impacted by COVID-19," https://dfi.wa.gov/sites/default/files/second-amended-servicer-guidance.pdf

As borrowers facing foreclosure come out of forbearance, they will likely be referred to the program with between seven to thirteen monthly payments in arrears. Currently, most lenders have underwriting criteria that require borrowers to have proof of sufficient income to repay a modified loan. As of this writing, we are not aware of any specific underwriting standard in place that would account for income loss due to the pandemic while borrowers seek to modify their loans. The conversations between borrower and beneficiary are likely to be difficult, and it is anticipated that many borrowers will seek the assistance of the Foreclosure Fairness Program to gain some balance in those negotiations.

The Long Term Effects of the Economic Downturn Caused by the COVID -19 Pandemic

The recession that began in late 2007 was fundamentally caused by the collapse of one sector of the economy, the residential housing market, due to the promotion of subprime lending and other questionable practices. Although there was significant unemployment and lost wealth due to increased foreclosures, the nation and our region began a slow and steady return to a robust economy once these underlying issues were resolved. Many experts expect the economic downturn caused by COVID to be significantly deeper. At the height of the Great Recession, the Gross Domestic Product (GDP) dropped 4.3%.[8] As of June 30, 2020, the GDP had dropped 32.9%.[9] That's almost one-third of the economy lost. In July of 2020, the unemployment rate in Washington State had risen to 10.3%.[10] This rate has surpassed the unemployment rate of 10% seen at the height of the Great Recession.[11] With so many businesses closed for good and so many jobs permanently lost, the road back to economic health may be much longer than we experienced after the Great Recession. There is no agreement among experts as to what shape that recovery will take.[12]

The Effects of the Economic Downturn Caused by the COVID-19 Pandemic on Program Funding

Currently, the sole source of funding for the Foreclosure Fairness Program comes from the fees beneficiaries pay when they record a Notice of Trustee Sale. Because of the forbearance provisions and moratoriums on federally backed mortgages in the CARES Act, Notices of Trustee Sales are not recorded. Thus funding for the Program has disappeared.

We expect to see a significant, perhaps exponential, increase in referrals to the program as borrowers emerge from forbearances with arrears due and the need to modify their loans. However, a unique feature of the Foreclosure Fairness Program is that foreclosure activity is halted by statute when a borrower is referred into mediation. This also prevents a Notice of Trustee Sale from being recorded. When the program successfully finds an agreement between the beneficiary and borrower, historically 50% of the time, if one has not already been recorded, a Notice of Trustee Sale is prevented. All funding questions and solutions remain fluid and are being addressed in stakeholder meetings held at the time of this writing and expected to continue into 2021.

Before fiscal year 2018, the program was funded by fees beneficiaries paid for each Notice of Default (NOD) issued in Washington State. However, the NOD is not a publicly recorded document, and there is no way to reconcile the number of NODs issued with the number of fees received. In 2018, the funding mechanism shifted to fees paid by beneficiaries for each Notice of Trustee Sale recorded in Washington State to remedy

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[8] Federal Reserve History, "The Great Recession," https://www.federalreservehistory.org/essays/great_recession_of_200709
[9] Bureau of Economic Analysis, "Gross Domestic Product, Second Quarter 2020 (Advance Estimate) and Annual Update," (June 30, 2020), https://www.bea.gov/news/blog/2020-07-30/gross-domestic-product-second-quarter-2020-advance-estimate-and-annual-update
[10] Washington State Employment Security Department, "Monthly employment report," https://esd.wa.gov/labormarketinfo/monthly-employment-report
[11] Washington State Office of Financial Management, "Unemployment rates," https://www.ofm.wa.gov/washington-data-research/statewide-data/washington-trends/economic-trends/unemployment-rates
[12] The Brookings Institution, "The ABCs of the post-COVID economic recovery," (May 4, 2020), https://www.brookings.edu/blog/up-front/2020/05/04/the-abcs-of-the-post-covid-economic-recovery/

this situation. These are public documents and so could be reconciled with the number of fees paid. However, as stated above, this funding mechanism's flaw became apparent when most foreclosures were halted.

Addressing the Potential Increase in Beneficiaries Exempt from Fees

Another factor that may harm funding for the FPP is a reduction of fees collected as more beneficiaries become eligible to be exempt from fees in calendar year 2021. Currently, by statute, beneficiaries may apply to be exempt from paying fees into the FPP if they have recorded fewer than 50 notices of trustee sales in Washington during the previous calendar year. The CARES Act was signed into law at the end of March 2020, and foreclosures in our state plummeted for three-quarters of calendar year 2020. It is reasonable to assume that many beneficiaries not normally eligible for the exemption will be eligible due to the pandemic's unique circumstances.

Summary of Funding Issues

- CARES Act protections and DFI recommendations suspended most foreclosure activity, and beneficiary fees tied to recordings of Notices of Trustee Sales disappeared.

- Before COVID, it became clear that there was a structural flaw in the funding mechanism as the program's success reduced the number of Notices of Trustee Sales recorded, which resulted in decreased funding.

- A consequence of the suspension of foreclosure activity is beneficiaries not normally eligible to be exempt from fees will now qualify for this exemption in 2021, further crippling the funding of the program

Possible Solutions to Funding Issues

For a borrower to be eligible for mediation, they must have been issued a Notice of Default by the beneficiary. Moving the trigger for beneficiary fees back to the NOD will eliminate the program's problem of being a victim of its success. Currently, the NOD is not a recorded document. To reconcile the number of NODs issued with the amount of beneficiary fees received, this information will need to be reported directly to Commerce with a partial exemption from public disclosure to protect borrowers' privacy. The aggregate data would be available to the public.

Addressing the Potential Increase in Beneficiaries Exempt from Mediation

Beneficiaries also have the right, by statute, to be exempt from mediations altogether if they were "not a beneficiary of deeds of trust in more than 250 trustee sales of owner-occupied residential real property that occurred in Washington State" during the previous calendar year. Again, it is possible that due to the cessation of most foreclosures, beneficiaries that under normal circumstances would not be eligible for exemptions are eligible to be exempt from mediation. This could result in the disqualification from mediation of a significant number of borrowers in 2021. We will need a legislative fix to prevent this outcome.

Preparations for Post-Forbearance Referrals - New Mediators

Before COVID-19, most mediators were not working to capacity, especially those in the larger counties. With the expected increase in foreclosures coming in 2021, the program is looking at ways to bring on mediators as needed in selected counties where there are not enough mediators. As of this writing, the program is developing an on-demand web-based training to be ready to launch in early 2021. This project is funded by CARES Act money and needs to be substantially completed by December 30, 2020. We will be working with the Dispute Resolution Centers (DRCs) and experienced independent mediators to revamp our policies and practices on training, mentoring and finally, accepting new mediators into the FPP as needed.

Report to Legislature

By statute, Commerce is required to provide an annual report to the Legislature. Since the FFP's inception, these reports have been largely static narrative documents out of sync with the FFP's fluid environment. Decision-making for the FFP is driven by an active and engaged stakeholder group including members of the Legislature, Commerce staff, borrowers' advocates (housing counselors and attorneys), beneficiaries' advocates (attorneys and trustees) and representatives from financial institutions (lenders, mortgage bankers and credit unions.) Often key meetings are held, and legislative decisions are made after the report is published.

Commerce recommends a move to a more dynamic way of reporting data on the FFP to those who need it. The current reporting structure does not meet that purpose in any meaningful way.

Commerce proposes moving the reporting mechanism on to the FFP website, where it can be in a dynamic format updated quarterly.

Recommendations

Even before COVID-19, some issues needed to be addressed concerning the FFP's funding and reporting mechanisms. The arrival of COVID-19 and the ensuing economic downturn has exacerbated these issues and surfaced others equally worrisome.

There are several proposed changes to ensure continued and adequate funding of the FFP, especially as the program prepares for a significant increase in foreclosures and mediation requests as the Federal Coronavirus Aid, Relief and Economic Security (CARES) Act protections expire. Some of the changes will repair underlying flaws in the FFP's funding mechanism, which is currently tied to fees paid by beneficiaries on the recording of Notices of Trustee Sales. Other changes would alter exemptions to fees, mediation or both for some institutions for whom these would not normally be available.

Stakeholder Issues and Recommendations

The Washington State Department of Commerce (Commerce) is one of four state agencies and several stakeholders who meet regularly to make recommendations on program implementation. The group is actively considering recommending changes to the Legislature to address the following issues.

- **Change the Trigger for Beneficiary Fees Back to Issuances of Notice of Default:** The Notice of Trustee Sale's timing has resulted in significantly lower fees.
  - Allow for beneficiaries to provide this information directly to Commerce
  - Exempt personal information in NODs from public disclosure to protect homeowners' privacy
  - Direct NOD data to be reported to the public in aggregate
- **Beneficiary Exemptions:** Legislative action is needed to prevent the possibility of beneficiaries, not normally eligible to be exempt from paying fees, claiming exemption from fees due to the decreased foreclosure activity. It is recommended that this exemption be suspended during calendar year 2021.

Recommendation Regarding Increased Exemptions from Mediation

Another exemption that needs legislative action to preserve the program is the beneficiary's exemption from mediation. When a beneficiary is exempt from mediation, any borrower with that beneficiary as note holder is ineligible for mediation. Action is needed to prevent the possibility of beneficiaries ineligible for exemptions under normal circumstances from claiming exemption from mediation due to the decreased foreclosure activity caused by the CARES Act protections. It is recommended that this exemption be temporarily suspended during calendar year 2021.

Commerce Recommendation

Statutory Requirement for the Program's Report to the Legislature

The statute is very specific as to the data the FFP is required to report to the Legislature. This data is much better suited to a dynamic web-based format. Commerce recommends that this data is provided on its website and updated quarterly starting with fiscal year 2021.