FORECLOSURE MEDIATION IN NEVADA: WHY HASN'T IT WORKED?

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The Nevada Foreclosure Mediation Law[1] was enacted in 2009 in order to "keep Nevadans in their homes" through the foreclosure crisis that saw Nevada leading the nation in real estate foreclosures and 48 percent of Nevada homeowners "under water," owing more on their homes than the homes were worth. Assembly Speaker Barbara Buckley, who sponsored the legislation, cited an estimate that the law would save 17,700 homes from foreclosure.[2] But, two years later Buckley, no longer in the assembly, reported that Nevada continued to lead the nation in foreclosures and that now 65 percent of Nevada homeowners are under water.[3]

Under the statutory scheme, if a homeowner facing foreclosure elects mediation, the Supreme Court's Administrative Office of the Courts (AOC), acting as Mediation Administrator, appoints a trained mediator to conduct a mediation session. The beneficiary cannot proceed further with the foreclosure until it obtains a certificate from the Mediation Administrator stating either that the homeowner failed to attend the mediation or that the parties, while acting in good faith, were unable to reach an agreement modifying the loan.[4]

The beneficiary must attend - either in person or through a representative with authority to negotiate a loan modification. The beneficiary must also provide documentation showing that it is in fact the entity to whom the money is owed and must participate in the process in good faith. If the beneficiary fails to meet any of these requirements, the mediator is required to prepare and submit to the Mediation Administrator a petition and recommendation concerning the imposition of sanctions against the beneficiary or its representative. The district court may then impose sanctions *including ordering that the underlying loan be modified on terms set by the court*.[5]

The law expresses a public policy encouraging loan modification as a solution to the foreclosure crisis. An underwater homeowner's best option may be to default on the loan, permit the foreclosure to proceed and then vacate the home. Why continue paying for a home that costs more than it is worth? But the homeowner's decision to walk away is problematic for the beneficiary. Not only does the beneficiary pay the costs of the foreclosure, it must then sell the property in a seriously deflated market, paying taxes and maintaining the property in the interim. In such cases, modifying the terms of the loan, such as by reducing principal, might be in the best interest of both parties and would benefit the community by stabilizing real estate values.

How many homes has the Foreclosure Mediation Law saved? No one knows. Published AOC statistics show that approximately 28 percent of the 13,813 mediations completed through September 2011 resulted in agreements under which the homeowner remained in the home. But the statistics do not reveal the nature of such agreements. How many were for actual loan modifications as opposed to, for example, agreements for the homeowner to cure the default. How many were for permanent, as opposed to temporary, modifications? How many agreements, if any, resulted in principal reductions? Meanwhile, the AOC has denied a nonprofit corporation's requests under the Nevada Public Records Act to permit inspection of the records containing this information, contending that the records are confidential.

Why hasn't the law resulted in more loan modifications?

Foreclosure mediation in practice differs considerably from the process envisioned by the legislature. Contrary to the legislative intent, loan servicers, not beneficiaries, participate in many mediations. In addition, the current procedures homeowners must follow to obtain sanctions differ from what the legislature intended.

Loan servicers

A loan servicer is a company that acts as an intermediary, collecting payments from the homeowner and distributing them to the beneficiary. If the homeowner defaults, the servicer handles the foreclosure, charging the beneficiary a fee for its services. This creates a conflict of interest between the beneficiary and the servicer.[6]

Servicer participation in the mediation as the purported representative of the beneficiary is common but contrary to the legislature's intent. As Buckley explained in 2009, one of the problems that stood in the way of voluntary loan modifications prior to the Foreclosure Mediation Law was that in many cases, the loans had been sold so many times it was unclear who the beneficiary was. To address this problem, Buckley assured the legislature, "We are going to clarify the language to make it absolutely clear that the lenders, and not the intermediaries, are the ones required to come to the mediation."[7] But no such clarification appears either in the statute or the Foreclosure Mediation Rules (FMRs).

Not only do servicers participate in the mediations, they are actively involved in the development of AOC procedures related to mediation. Servicers, such as Bank of America, are represented on the Foreclosure Mediation Advisory Committee created under FMR 22 to evaluate the effectiveness of the mediation program. The program manager meets regularly with servicers' representatives to obtain their input. The AOC retained a law firm to advise it regarding the Foreclosure Mediation Program, but that law firm boasts a 125-year attorney-client relationship with Wells Fargo Bank, a servicer.

Sanctions

AOC statistics reveal that in 5,771, or approximately 42 percent, of the mediations completed through September 2011, the beneficiary failed to comply with its obligations under the statute. In such cases, the mediator is required to recommend sanctions and the district court must determine what sanctions are appropriate.[8] AOC statistics do not disclose how many

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of these cases have resulted in sanctions, but it is believed to be only a very small fraction of the nearly 6,000 cases where mediators found beneficiaries noncompliant.

Why are sanctions so rare?

First, since homeowners are not advised of their right to obtain sanctions in these cases or the procedures they must follow to do so, very few homeowners actually seek the sanctions they are entitled to under the law.

Next, in practice the procedure for obtaining sanctions is considerably more onerous than the legislature intended. Supreme Court Justice James Hardesty, then Chief Justice, explained to the 2009 legislature that the procedure for district court review of mediators' recommendations for sanctions would be no different than district court review of recommendations from masters and discovery commissioners.[9] Under such procedures, a party dissatisfied with the recommendation may file objections with the court, which may then hold a hearing to determine whether to adopt the recommendation.[10] Thus the burden would be on the party objecting to the recommendation to file objections and convince the court that the recommendation ought not to be adopted. In the absence of an objection, the court would normally adopt the recommendation.

In practice, however, at least until very recently, the AOC prohibited mediators from preparing and submitting petitions and recommendations concerning sanctions, as the AOC interpreted the Foreclosure Mediation Law as neither requiring nor permitting the mediator to recommend *specific* sanctions against beneficiaries or their representatives.

Also, the Foreclosure Mediation Rules make no provisions for the mediator's petitions and recommendations required by the law. Therefore, a homeowner seeking sanctions must file a "petition for judicial review" under FMR 21 under which the homeowner does not have the advantage of a mediator's recommendation. As the party seeking relief, the homeowner bears the burden of convincing the court considering a Rule 21 petition that sanctions are appropriate. FMR 19(1) and FMR 21(1) imply that a homeowner seeking sanctions must prove that lender acted in "bad faith" although the term "bad faith" does not appear anywhere in the Foreclosure Mediation Law. In addition, FMR 21(5) requires the court to apply a de novo standard of review when considering a Rule 21 petition, meaning that the homeowner must meet his burden of proof without the benefit of the mediator's determination. But FMR 1(5) prohibits the homeowner from making a record of the mediation on which the homeowner could otherwise rely to demonstrate what occurred at the mediation. The AOC tells mediators they may not testify at the hearings on such petitions and instructs them to destroy their notes of the mediations, leaving the homeowner with only scant evidence with which to meet the burden of proof.

Conclusion

The Foreclosure Mediation Law has not been applied as intended and therefore has failed in its objective of keeping Nevadans in their homes through the foreclosure crisis. ■

1 AB 149 (Nev. 2009), now codified as NRS 107.086.
2 Hearing on A.B. 149 Before Joint Comm. on Commerce and Labor, 75th Leg. (Nev., Feb. 11, 2009), page 4; Hearing on A.B. 149 Before Sen. Comm. on Commerce and Labor, 75th Leg. (Nev., May 18, 2009), page 9.
3 Hearing on A.B. 300 Before the Assembly Comm. on Commerce and Labor, 76th Leg. (Nev., March 23, 2011), Exh. F, [PowerPoint presentation by Barbara Buckley], page 2.
4 NRS 107.086(2)(c), (6), and (7).
5 NRS 107.086(5).
6 See, Thompson, Diane E., *Foreclosing Incentives: How Servicer Incentives Discourage Loan Modifications*, 86 Wash. Law Rev. 755 (2011).
7 Hearing on A.B. 149 Before Joint Comm. on Commerce and Labor, 75th Leg. (Nev., Feb. 11, 2009), pp. 5, 12.
8 NRS 107.086(5); *Pasillas, supra.*
9 Hearing on A.B. 149 Before Assembly Ways and Means Committee, 75th Leg. (Nev., April 27, 2009) (testimony of Chief Justice Hardesty).
10 See, e.g., NRCP 16.1(d), NRCP 53(e).

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