Department of Legislative Services

Maryland General Assembly
2015 Session

FISCAL AND POLICY NOTE

House Bill 1197 (Delegate B. Robinson)
Rules and Executive Nominations

Real Property - Foreclosure - Owner-Occupied Residential Property - Prohibition on Collection of Deficiency

This bill prohibits a secured party, such as a mortgage lender, from obtaining a deficiency judgment or taking any other action against a mortgagor or grantor in an action to foreclose a mortgage or deed of trust on owner-occupied residential property that was recorded on or after October 1, 2015, if the proceeds of the sale, after deducting all costs and expenses allowed by the court, are insufficient to satisfy the debt and accrued interest.

Fiscal Summary

State Effect: Special fund revenues for the Department of Housing and Community Development (DHCD) decrease significantly beginning in FY 2016 due to the bill's prohibition against a secured party taking any action to collect outstanding debt following the sale of a foreclosed property, as discussed below. Expenditures are not affected.

Local Effect: The bill may negatively affect local government revenues to the extent that they are unable to collect deficiency judgments on loans secured by deeds of trust on residential properties recorded on or after October 1, 2015. However, because it is assumed that the bill applies in a limited number of cases, the impact is likely minimal. Expenditures are not affected.

Small Business Effect: Potential meaningful.

Analysis

Current Law: Under the Maryland Rules, within 30 days after a foreclosure sale of property, the person authorized to make the sale must file a complete report of the sale with the court. A party or the holder of a subordinate interest in the property may file exceptions to the sale. The court must ratify the sale if (1) the time for filing exceptions has expired and exceptions to the report either were not filed or were filed but overruled and (2) the court is satisfied that the sale was fairly and properly made. Upon ratification of the sale, the court may refer the matter to an auditor to state an account.

At any time after the sale and before final ratification of the auditor's report, any person claiming an interest in the property (or in the proceeds of the sale of the property) may file an application for the payment of that person's claim from the surplus proceeds of the sale. For owner-occupied residential property, a secured party, or any appropriate party in interest, may file a motion for a deficiency judgment within three years after the final ratification of the auditor's report, if the proceeds of the sale, after deducting all costs and expenses allowed by the court, are insufficient to satisfy the debt and accrued interest. The filing of this motion is the sole post-ratification remedy available to a secured party or a party in interest for breach of a covenant under a deed of trust, mortgage, or promissory note that is secured by owner-occupied residential property.

Background: Almost all states allow deficiency judgments under certain conditions, for certain types of property or foreclosure proceedings. However, many states restrict not only the conditions under which deficiency judgments are allowed, but also the maximum recovery for the creditors. These more restrictive states are collectively considered "nonrecourse" states. States with such restrictions include Alaska, Arizona, California, Connecticut, Idaho, Minnesota, Nevada (since 2009), North Carolina (since 2009), North Dakota, Oregon, Texas, Utah, and Washington.

The Department of Labor, Licensing, and Regulation (DLLR) reports that evidence from other states indicates that mortgage interest rates are higher in states that prohibit deficiency judgments, but by less than 50 basis points. Typically, rates are inflated by between 13 and 33 basis points, depending upon the type of home and mortgage. It is difficult to determine the historical difference in qualifications for credit between recourse and nonrecourse states because numerous factors have influenced access to credit in recent years, including the securitization of debt and competition among lenders. However, whether a lender will have recourse to recover any deficiency following foreclosure is understood to be one of the factors that lenders consider when extending credit. DLLR reports that it was unable to find information on specific loan terms in recourse compared to nonrecourse states, but noninterest costs associated with home purchasing, such as closing costs and brokers' fees, increased by $550 per $100,000 of loan amount in nonrecourse states. Additionally, while rates of default and foreclosure are lower in recourse states than in nonrecourse states, the effect is significant only when the borrower is likely to have significant assets or income:

- For borrowers with properties appraised at less than $200,000, there is no difference in the probability of default across recourse and nonrecourse states.

- For homes appraised at $300,000 to $500,000, borrowers in nonrecourse states are 59% more likely to default.

- For homes appraised at $500,000 to $750,000, borrowers in nonrecourse states are almost twice as likely to default as borrowers in recourse states.

- For homes appraised at $750,000 to $1 million, borrowers in nonrecourse states are 66% more likely to default as borrowers in recourse states.

State Fiscal Effect: Special fund revenues for DHCD decrease, potentially significantly, beginning in fiscal 2016 due to the bill's prohibition against a secured party taking any action to collect outstanding debt following the sale of a foreclosed property. This estimate is based on deficiencies submitted by DHCD to the Central Collection Unit (CCU) for collection between fiscal 2012 and 2014. DHCD advises that it does not collect deficiency judgments on the majority of loans made under the Maryland Mortgage Program, as the mortgage insurer has the first right to any deficiency judgment. However, DHCD further advises that any loan deficiency, while not pursued through the courts, is sent to CCU. Amounts later recovered by CCU, less specified collection fees, are deposited into the DHCD special fund.

The Office of the Attorney General, Consumer Protection Division, can handle the bill's requirements with existing resources, assuming 50 or fewer new complaints are generated by the bill. Since most deficiency judgments are handled without a trial or hearing, it is expected that the Judiciary can implement the bill's requirements with existing resources.

Small Business Effect: To the extent that licensed collection agencies are considered small businesses, the bill may significantly reduce the total amount of debt transferred from lenders to such agencies for the purpose of collection, resulting in a reduction in business. However, the extent of any such impact is difficult to ascertain, as the largest collection agencies handle the majority of debt collection, and the proportion of the collection industry related to foreclosures on residential property relative to debt collection as a whole is unknown.

Additional Comments: To the extent that mortgage lenders respond to the bill by instituting stricter lending requirements, home sales may decrease. A decrease in home sales could cause a reduction in State and local tax revenues related to property transfers, including State transfer taxes and local transfer and recordation taxes.

Additional Information

Prior Introductions: None.

Cross File: SB 875 (Senator Benson, *et al.*) **-** Judicial Proceedings and Finance.

Information Source(s): State Department of Assessments and Taxation; Office of Administrative Hearings; Department of Labor, Licensing, and Regulation; Judiciary (Administrative Office of the Courts); Department of Housing and Community Development; Office of the Attorney General; Department of Legislative Services

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