Cullen | Dykman

New State Law Imposes Obligations on Financial Institutions When Selling or Transferring Mortgage Loans Subject to a Pending Loan Modification

August 23, 2019

Joseph D. Simon

Garden City

New York State has enacted a new law that imposes obligations on banks and financial institutions when selling or transferring a mortgage loan subject to a pending loan modification. The new law takes effect on November 12, 2019 and applies to mortgages entered into on or after such date.

This law imposes two obligations: one obligation on the seller/transferee of the loan, and one obligation on the new mortgage servicer once the loan is sold or transferred. First, if the loan is transferred during the loan modification application process, the new law requires the bank or financial institution selling or transferring the loan to provide the borrower with a written list of all the documents relating to such modification application that were provided to the bank or financial institution to which such mortgage was sold or transferred.

Second, if a borrower has been approved in writing for a first lien loan modification or other modification to avoid foreclosure, and the servicing of such loan is transferred or sold to another mortgage servicer, New York State law will now require the subsequent mortgage servicer to assume all duties and obligations related to any previously approved first lien loan modification or other foreclosure prevention alternative. This is intended to ensure that if the loan is sold or transferred after a borrower has been approved for a modification of a mortgage, that the subsequent mortgage servicer honors the terms and conditions of the approval.

According to the legislative memorandum accompanying this new law, the law “is necessary in light of the growing loan modification crisis enveloping New York State. The modification process is difficult enough, so New York State must provide a mechanism to ensure that banks and financial institutions treat homeowners in a fair and equitable manner during the course of this difficult process.”

Please note, however, that the law leaves several unanswered questions. First, the law applies to both banks and financial institutions, but does not define the term “financial institution,” leaving some uncertainty as to whether

it applies to all financial institutions regardless of charter, as well as to mortgage companies and other types of lenders. Second, the law applies to a “mortgage” that is the subject of a loan modification, but does not define “mortgage.” The law’s legislative memorandum indicates an intent to protect “homeowners,” but the plain reading of the law has no such limitation. Accordingly, this law appears to cover any type of mortgage subject to a loan modification, including commercial mortgages. Third, it is not clear what the potential consequences are for a bank or financial institution that violates the law. The Department of Financial Services has enforcement authority over the law, but it’s not clear whether a borrower could successfully bring a lawsuit directly against a lender for a violation, or successfully raise a violation of the law as a defense to a foreclosure action. We will monitor any developments on these issues.

If you have any questions regarding this new law, please feel free to contact Joseph D. Simon at (516) 357-3710 or via email at jsimon@cullenanddykman.com, Elizabeth A. Murphy at (516) 296-9154 or via email at emurphy@cullenanddykman.com, or Mandy Xu at (516) 357-3850 or via email at mxu@cullenanddykman.com.

Practices

- Banking and Financial Services

Industries

- Financial Institutions

Attorneys

- Elizabeth A. Murphy
- Joseph D. Simon