Date of Hearing: March 3, 2025

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Avelino Valencia, Chair
AB 238 (Harabedian) – As Introduced January 13, 2025

SUBJECT: Mortgage forbearance: state of emergency: wildfire

SUMMARY: Establishes the Mortgage Deferment Act to require mortgage servicers to offer up to 360 days of mortgage forbearance for borrowers affected by the January 2025 Los Angeles-area wildfires.

Specifically, **this bill**:

1) Makes the following definitions for the purposes of the Mortgage Deferment Act:

   a) "Borrower" means a natural person who is a mortgageor or trustor or confirmed successor in interest, or a person who holds a power of attorney for such a natural person.

   b) "Mortgage loan" means a loan that is secured by a mortgage and is made for financing to create a or preserve the long-term affordability of a residential structure in the state, or a buy-down mortgage loan secured by a mortgage, of an owner-occupied unit in the state.

   c) "Mortgage servicer" means a person or entity who directly services a loan or who is responsible for interacting with the borrower, managing the loan account on a daily basis, including collecting and crediting periodic loan payments, managing any escrow account, or enforcing the note and security instrument.

   d) "Wildfire disaster" means the conditions described in the proclamation of a state of emergency issued by Governor Gavin Newsom on January 7, 2025.

2) Authorizes a borrower experiencing direct or indirect financial hardship due to the wildfire disaster to request mortgage forbearance by submitting a request to the mortgage servicer and affirming that the borrower is experiencing a financial hardship.

3) Requires a mortgage servicer to grant the forbearance requested under 2) for up to 180 days without any additional documentation other than the borrower's attestation and to extend that forbearance an additional 180 days at the request of the borrower.

4) Prohibits a mortgage servicer from initiating any judicial or nonjudicial foreclosure process, move for a foreclosure judgment or order of sale, or execute a foreclosure-related eviction or foreclosure sale.

5) Contains an urgency clause so provisions take effect immediately.

EXISTING LAW:

1) Provides the following protections, among others, for homeowners facing the nonjudicial foreclosure of their homes:

a) Prohibits a mortgage servicer from recording a notice of default until at least 30 days after making contact, as specified, with a borrower to discuss options for avoiding foreclosure. (Civil Code Section 2923.5)

b) Prohibits a mortgage servicer from taking specified acts related to foreclosure while a borrower's application for a loan modification is pending. (Civil Code Section 2924.11)

2) Requires licensure and oversight by Department of Financial Protection and Innovation (DFPI), as specified, for persons who service federally related residential mortgage loans secured by properties with one-to-four family residences. (Division 20 of the Financial Code, commencing with Section 50000)

FISCAL EFFECT: Unknown. This bill is keyed Fiscal by Legislative Counsel.

COMMENTS:

1) Purpose

According to the author:

> The Mortgage Deferment Act provides essential relief to homeowners facing financial hardship due to the Los Angeles wildfires. By mandating up to 12 months of mortgage forbearance with no added fees, penalties, or interest, this legislation ensures that families have the time and flexibility to recover without the immediate threat of foreclosure.
>
> Given the long-term nature of wildfire recovery, short-term assistance is insufficient. This act establishes clear, accessible relief, preventing financial ruin and stabilizing communities. Long term, uniform action is necessary to protect homeowners and mitigate the economic fallout of this disaster.

2) Background:

a) Los Angeles wildfires.

California has faced an alarming increase in destructive wildfires. Most of the largest and devastating fires have taken place within the last decade, culminating in a particularly severe outbreak in recent years. This period has witnessed some of the worst wildfires in the state's recorded history.

More recently, January 2025 wildfires, often referred to as firestorms due to the intense hurricane-force winds that helped the fires quickly spread, destroyed more than 16,000 structures and has led to widespread hardship for victims and the surrounding communities. According to an analysis by the Los Angeles Times, real estate losses from the two largest fires – Palisades and Eaton – could exceed $30 billion, and the fires caused the displacement of approximately 13,000 households.

b) The residential mortgage market.

Mortgage loans fall under two primary categories: conforming and nonconforming. Whether or not a mortgage loan is conforming or nonconforming can have an impact on eligibility requirements, interest rates, loan amounts, and mortgage insurance requirements, among other loan features.

A conforming loan "conforms" to the standards established by Fannie Mae and Freddie Mac, which are government-sponsored entities (GSEs) that support mortgage lending through the secondary market. When a lender funds a conforming loan, it then sells that loan to a GSE. The GSE will then often repackage the loan and sell it to investors on the open market. This process in which the GSE is a constant purchaser of mortgages promotes a more stable mortgage market, and a significant majority (around 70%) of mortgages are supported by the GSEs. Their central role means that guidelines and policies establishes by the GSEs typically set the tone for the entire industry.

A nonconforming loan, in contrast, does not meet the standards of the GSEs. These loans, also called jumbo loans or portfolio loans, often have different requirements and terms than conforming loans. In many cases, the loan amount exceeds the dollar amount of a conforming loan. These loans, by not being backed by the GSEs, tend to be riskier for lenders.

c) Mortgage servicers.

Generally speaking, a mortgage servicer handles the day-to-day task of managing a mortgage loan. The servicer processes loan payments, responds to borrower questions, and keeps track of principal and interest paid. In many cases, the mortgage servicer is not the lender and is servicing the loan on behalf of the lender or investor.

Mortgage servicers also work with homeowners affected by natural disasters and monitor and control the disbursement of insurance proceeds. For those servicers that follow Fannie Mae's guidelines, then the servicer typically obtains details on the property damage and the necessary repairs, discusses the plans for repair with the borrower, issues a check for any amounts designated for personal property or living expenses, and then disburse the insurance loss proceeds according to a set procedure. Following this, servicers will typically review and approve the final plans for repair and monitor and inspect repairs as they are completed.[1]

d) Forbearance.

Mortgage forbearance provides borrowers temporary relief when they experience an unexpected hardship or income shock. Under a forbearance plan, a borrower can enter into an agreement with the lender that allows the borrower to pause or reduce mortgage payments during the period of hardship. The borrower will still owe the full amount and repays the missed payments at a later time (typically with interest).

Forbearance helps both the borrower and the lender by avoiding a foreclosure. The borrower is able overcome the initial hardship and get back on track, and the lender does not need to start the lengthy and expensive process of foreclosure. Throughout this

[1] https://servicing-guide.fanniemae.com/THE-SERVICING-GUIDE/Part-B-Escrow-Taxes-Assessments-and-Insurance/Chapter-B-5-Property-and-Flood-Insurance-Loss-Events/B-5-01-Insured-Loss-Events/1040963581/B-5-01-Insured-Loss-Events-07-14-2021.htm

process, the mortgage servicer acts as the point of contact and manages the forbearance agreement, often checking in with the borrower and negotiating the eventual repayment process.

At the same time, forbearance is not without risks for the borrower. For example, the mortgage still accrues interest during the forbearance period, meaning that it can cost borrowers more in the end to pause payments. And, the loan terms do not change. Thus, forbearance is considered one tool in the toolkit, which includes loan modifications, to keep a homeowner in their home. The success of forbearance depends on whether or not the borrower hardship is truly short-term and whether home and property are stable or appreciating.

The GSEs publish forbearance guidelines for borrowers affected by a natural disaster. Under Fannie Mae's guidelines, for example, a servicer may offer an initial forbearance plan term of up to three months through a more streamlined process, so long as the property is located in a FEMA-Declared Disaster Area and the mortgage loan was current or less than two months delinquent at the time the disaster event occurred. And, the servicer must request approval from Fannie if the cumulative term of forbearance exceeds 12 months.[2]

3) Wildfire-related mortgage forbearance agreement.

On January 23, 2025, Governor Newsom announced a commitment from 270 state-chartered banks, credit unions, and mortgage lenders and servicers to provide 90 days of forbearance for families affected by the Los Angeles wildfires. By January 30, 2025, the commitment had grown to include 400 financial institutions. The announcement included:

- 90-day mortgage payment forbearance periods, streamlined processes for requesting initial relief without submitting forms or documents, payment options that do not require immediate repayment of unpaid amounts (i.e., no balloon payments) at the end of the forbearance period, and the opportunity for additional relief.
- Relief from mortgage-related late fees accruing during the forbearance period for 90 days.
- Protection from new foreclosures or evictions for at least 60 days.
- Institutions will not report late payments of forborne amounts to credit agencies

4) CARES Act and learned lessons from ambitious forbearance plans

AB 238 is modeled after federal legislation requiring forbearance during the COVID-19 pandemic. Specifically, the federal CARES Act provided a mortgage payment forbearance option for all borrowers who, either directly or indirectly, suffer a financial hardship due to the novel coronavirus (COVID-19) national emergency. As part of that process, no documentation was required to prove hardship beyond an attestation that the borrower was suffering from that hardship. Under the CARES Act, a borrower was eligible for up to 180 days of forbearance, and that could be extended another 180 days.

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[2] https://servicing-guide.fanniemae.com/svc/d2-3.2-01/forbearance-plan#P9626

The CARES Act's forbearance requirement, at the time, was an unprecedented intervention. By June 2020, around 5% of all conforming mortgages in the United States were in forbearance. Since then, a number of studies have evaluated the policy's effectiveness. These studies contain a number of takeaways relevant to the committee's consideration of AB 238:

a) Forbearance successfully helped prevent widespread foreclosures during the COVID-19 pandemic. A research brief by the Philadelphia Federal Reserve concludes: "Our overall findings are that the program mitigated a default wave like that experienced during the Great Recession of 2008–09, as both government and private lenders participated on a broad scale to provide forbearance relief to all who requested it."[3]

b) Forbearance can help stabilize the economy. A study by the Harvard Joint Center for Housing Studies found that the CARES Act's forbearance policies helped stabilize the economy by boosting local demand during the economic recovery.[4]

c) Despite the generous documentation requirements, there is little evidence of fraud or forbearance being provided to those who did not need it. According to an analysis by the Cleveland Federal Reserve, forbearance was largely used by those who would actually benefit from a pause in payments.[5] The report looked at different ways that borrowers could strategically use forbearance for personal gain and found limited evidence of widespread "gaming."

a) There were reports of some mortgage servicers not complying with the CARES Act or providing inconsistent information. The Harvard paper cited above also notes that mortgage servicers did not honor forbearance requests universally and added significant friction in the process.

5) How AB 238's documentation requirement differs from current practice.

AB 238 requires a mortgage servicer to provide forbearance without additional documentation requirements so long as the borrower provides an attestation to a financial hardship caused by the wildfire disaster. This is meant to streamline and automate forbearance requests without the case-by-case analysis that servicers currently conduct. This simple attestation is also meant to ensure fairness and equal access to the benefit.

To highlight the difference between AB 238's documentation requirements with typical practices, the below, provided by industry representatives, represents the general approach taken by servicers when considering a forbearance request:

"In current practice, when evaluating whether to extend forbearance beyond the initial 90-day period, servicers typically seek to understand if the borrower's financial hardship persists. While the exact questions may vary by servicer, they generally focus on assessing the borrower's ongoing financial situation.

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[3] https://www.philadelphiafed.org/-/media/frbp/assets/consumer-finance/reports/23-02-tracking-resolutions-of-mortgage-forbearances-and-delinquencies.pdf
[4] https://www.jchs.harvard.edu/blog/can-mortgage-forbearance-help-stabilize-economy
[5] https://www.clevelandfed.org/publications/economic-commentary/2022/ec-202211-mortgage-borrowers-use-of-covid19-forbearance-programs

Common inquiries include:

- Current Income: What is your present income level, and has it changed since the initial forbearance was granted?

- Employment Status: Are you still employed, or have there been changes in your job situation contributing to the hardship?

- Expenses: What are your current expenses, and do they continue to exceed your ability to pay the mortgage?

- Ongoing Hardship: Is the financial difficulty (e.g., caused by a wildfire or other event) still affecting your ability to make payments?

- Prospects for Improvement: Do you anticipate any upcoming changes in your financial circumstances that might alleviate the hardship?"

6) Additional policy considerations

AB 238 proposes a generous forbearance intervention that would apply to mortgage servicers of both conforming and nonconforming loans. The author's rationale for this is that current 90-day forbearance commitment is insufficient given the widespread and long-term harm caused by the fires, and a reliance on federal guidance that applies only to conforming loans will lead to inconsistencies and gaps in relief.

While this bill is modeled after the successful federal CARES Act, the underlying situation facing fire victims is different than the pandemic and thus may call for a modified approach. The author may wish to consider the following issues as the bill moves forward:

a) AB 238 could put mortgage servicers out of compliance with GSEs or other investors.

Unlike the COVID-19 era, there is not a federal law requiring streamlined and automatic forbearance for fire victims. And, most servicers are subject to GSE guidelines that were agreed to when a GSE backed a loan, and these guidelines outline how a servicer may offer forbearance during a natural disaster. The potential differences between the GSE guidelines and AB 238's requirements mean that in some situations, servicers could be forced to choose between complying with state law or with guidelines that were agreed to as part of the GSE backing process.

It is unclear how significant or common these conflicts will be. For example, AB 238 could make it difficult for servicers to comply with GSE documentation or borrower communication requirements, such as the requirement that a servicer must attempt to achieve "quality right party contact," which is a process to determine the reason for the forbearance request and whether or not the borrower has the ability to repay the mortgage loan debt. AB 238's simple attestation, meant to streamline and automate requests, may not satisfy the GSE quality right party contact requirement.

As another example, Fannie Mae does not allow forbearance to extend a loan's total delinquency beyond 12 months. Thus, if the borrower was already delinquent prior to the forbearance agreement, then the forbearance period must be shorter than 12 months. AB 238, in contrast, could require a servicer to provide 12 months of forbearance to a loan that is already delinquent, meaning that total delinquency could extent past the 12-month cap under the GSE guidelines. As the bill moves forward, the author will need to continue working closely with industry experts to work through these possible tensions.

b) There may be misuse by some borrowers.

The combination of AB 238's simple attestation, the automatic approval, and a prohibition on interest accruing during the forbearance period means that some borrowers who do not face financial hardship would nevertheless strategically pause mortgage payments for a financial gain. Misuse of AB 238's proposed program may be inevitable, as it is difficult to design a program with minimal red tape that also ensures every person who receives the benefit is deserving. One positive sign, however, is there appears to have been only small amounts of "gaming" of the COVID-19 era forbearance.

c) There will be legal challenges.

AB 238 in its current form will invite legal challenges from lenders and mortgage servicers. See Comment #10 for an example of the claims related to federal preemption or takings and impairments of contracts.

7) Industry-submitted proposal

Representatives from industry submitted to the author an alternative proposal that would address their concerns. Among its provisions, this proposal contains the following:

- Specifies that a servicer shall offer forbearance of up to an initial 90 days (instead of 180), which can be extended at the request of the borrower for additional periods only to the extent it does not contradict or conflict with applicable investor or insurer guidelines or contractual obligations.
- Allows for interest (but not default interest) to accrue during forbearance, consistent with typical practices. AB 238 does not allow any interest to accrue during the forbearance period.
- Allows for tolling of forbearance that has already been offered since the Los Angeles wildfire event.

The industry proposal, at first read, appears to codify current industry practices, and thus may not result in additional forbearance than what will occur already under current law. However, this proposal also includes a number of clarifying concepts and definitions that the author may wish to consider. As the publication of this analysis, the author's office was reviewing the industry proposal.

8) Author commitments and future refinement.

The author has committed to amending this bill at a later time to allow for more documentation requirements and check-ins after the first 180 days of forbearance. The author has also committed to continue discussions with industry representatives about remaining issues, such as the potential conflict with GSE guidelines, in order to fulfill his objectives of providing long-term relief to borrowers who are facing financial hardship, directly or indirectly, due to Los Angeles wildfires.

9) Support

SEIU California writes the following:

> Our more than 250,000 members who live in Los Angeles County have felt the devastating impact of these fires, and 91 have been displaced. The deferment of mortgage payments will provide relief for these members and their families as they pay for alternative housing options, easing the financial burdens and economic uncertainty they face as they secure stable certainty.

The California Apartment Association also writes in support, arguing:

> AB 238 is a crucial step in helping displaced homeowners as they secure temporary housing, file insurance claims, and plan for reconstruction, without immediate financial strain.

10) Concern

A coalition of organizations representing lenders and realtors have submitted a "letter of concern" outlining ways that AB 238, as drafted, would lead to unintended consequences. The letter states

> While we fully support the intent of this measure to provide relief to borrowers in need, we believe modifications are necessary to ensure the bill offers effective relief while minimizing unintended consequences for both borrowers and servicers. Mortgage servicers act as intermediaries and are required to follow contractual obligations and investor guidelines. If issues remain unresolved, this measure could raise concerns regarding legal and constitutional matters, including potential takings and impairments of contracts. Additionally, it could introduce the possibility of preemption for federally chartered institutions.

REGISTERED SUPPORT / OPPOSITION:

Support

Bet Tzedek Legal Services
California Apartment Association
California State Council of Service Employees International Union (seiu California)
Consumer Attorneys of California
Rise Economy

Other

California Association of Realtors
California Bankers Association
California Credit Union League
California Land Title Association
California Mortgage Association
California Mortgage Bankers Association

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