

Banking and Finance Law Daily Wrap Up, DEBT COLLECTION—The CFPB is gearing up to battle ‘zombie mortgages’, (Apr. 26, 2023)

Banking and Finance Law Daily Wrap Up

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A CFPB advisory opinion clarifies that a debt collector bringing a state foreclosure action on a time-barred mortgage debt may violate the Fair Debt Collection Practices Act and its implementing regulation.

The Consumer Financial Protection Bureau has [issued](#) an [advisory opinion](#) that sets the stage for its battle against so-called “zombie mortgages.” In light of a series of actions by debt collectors attempting to foreclose on silent second mortgages, also called “zombie mortgages,” that consumers thought were satisfied long ago and that may be unenforceable in court, the agency has issued guidance. The advisory opinion reminds debt collectors covered by the Fair Debt Collection Practices Act (FDCPA) and its implementing Regulation F that they are prohibited from suing or threatening to sue to collect a time-barred debt and that this prohibition applies even if the debt collector does not know that the debt is time-barred.

Zombie mortgages and the 2008 financial crisis. According to the advisory opinion and the CFPB’s press release, many lenders originated mortgages to consumers without considering their ability to repay the loans in the time leading up to the 2008 financial crisis. One common piggyback mortgage product, an 80/20 loan, involved a first lien loan for 80 percent of the value of the home and a second lien loan for the remaining 20 percent of the valuation. After housing prices began to decline in 2005, refinancing became more difficult, and homeowners began to default. Many second mortgage holders charged their defaulted loans off as uncollectible and stopped communicating with the homeowners, as the mortgage holders recognized that a foreclosure would not generate enough money to cover even the first mortgage. Some sold the loans to debt buyers, often for pennies on the dollar. Many borrowers concluded that their second mortgages had been modified along with their first mortgages, discharged in bankruptcy, or forgiven because they had not received any notices or periodic statements for years. In a [blog post](#) on the matter, the CFPB notes that zombie second mortgages “tend to particularly affect older borrowers, lower-income borrowers, and borrowers in communities of color.”

In recent years, as prices have increased, some borrowers are hearing from companies claiming to own or have the right to collect on their long-dormant second mortgages. According to the CFPB, these companies often demand the outstanding balance on the second mortgage, plus fees and interest, and threaten to foreclose if the borrower does not pay. However, because of the amount of time that has elapsed, some of these debts have become time-barred because an applicable state statute of limitations has expired. In most states, consumers can raise this as an affirmative defense to preclude the debt collector from recovering on the debt using judicial processes such as foreclosure.

Advisory opinion. The CFPB’s advisory opinion clarifies that covered debt collectors, including individual and entities seeking to collect defaulted mortgage loans and many of the attorneys bringing foreclosure actions on their behalf, may not sue or threaten to sue to collect on time-barred debt. Because Regulation F’s prohibition on suits and threats of suit on time-barred debt is subject to a strict liability standard, the debt collector violates the prohibition even if the debt collector neither knew nor should have known that a debt was time-barred. Accordingly, a debt collector who brings or threatens to bring a state-court foreclosure action with respect to a time-barred mortgage debt may violate the FDCPA and Regulation F.

“The CFPB is concerned about homeowners who survived the 2008 financial crisis but who are now facing foreclosure threats and other collection activity because of long-dormant second mortgages,” the CFPB writes in its guidance. “These borrowers are often told that they face a choice between entering into onerous payment plans or losing their homes and the equity they have diligently built since the financial crisis.”

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