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Document Flaws Have Put Brakes on Foreclosures

By DAVID STREITFELD

The foreclosure machinery that has forced millions of Americans out of their homes is beginning to seize up as some lenders and their lawyers are accused of cutting corners in their pursuit of rapid home repossessions.

Evictions are expected to slow sharply, housing analysts said, as state and national law enforcement officials shine a light on questionable foreclosure methods revealed by two of the country's biggest home lenders in the last two weeks.

Even lenders with no known problems are expected to approach defaulting homeowners more cautiously and look more aggressively for resolutions short of outright eviction.

Despite the turmoil, some economists said the breakdown could ultimately lay the groundwork for a real estate recovery.

Stricken neighborhoods across the country, for example, could benefit. One big factor undermining home sales is fear of a large number of foreclosed homes coming to the market. If the foreclosures are delayed or never happen, housing prices might find a floor.

"Maybe this is like shock therapy," said the economist Karl E. Case. "Maybe this will actually get the lenders to the table and encourage them to work out deals that are to the benefit of everybody."

While such a happy ending is possible, the near term is more likely to produce paralysis and confusion.

As more defaulting homeowners become aware of the lenders' problems, they are expected to hire lawyers and challenge the proceedings against them. And if completed foreclosures were not properly done, families who bought the troubled homes could be vulnerable to claims by the former owners.

Apparently alarmed about such a possibility, one of the major title insurance companies, Old Republic National Title, has sent a bulletin to agents saying that "until further notice" it would not insure title to properties foreclosed upon by GMAC Mortgage, the country's fourth-largest home lender and one of the two big lenders at the center of the current controversy.

GMAC declined to comment, and Old Republic representatives did not return calls.

GMAC has acknowledged legal missteps in processing mortgages, and JPMorgan Chase has acknowledged the possibility of missteps, and both have suspended all foreclosures in the 23 states where they need a court's approval. That's 56,000 in the case of Chase alone; GMAC declined to provide a number.

Attorneys general in half a dozen states are demanding action or opening investigations. The Treasury Department said Thursday it was asking regulators to look into "these troubling developments."

"We're seeing a fundamental breakdown in the system, because no one cared that much about getting things right," said Representative Alan Grayson, a Democrat of Florida, who unsuccessfully asked the Florida Supreme Court to halt all foreclosures in that state.

Wall Street was examining the impact the disclosures could have on the lenders. Moody's Investors Service has placed the servicer ratings of GMAC and Chase on review for possible downgrade.

The federal government has been the majority owner of GMAC since supplying $17 billion to prevent the lender's failure during the financial crisis.

Other lenders said Thursday that their foreclosure filings, including the crucial affidavits, had been properly done.

A Citigroup spokesman said the lender required "annual training for our foreclosure employees on the proper execution of affidavits, including having personal knowledge of the information in the affidavit."

A Wells Fargo spokeswoman said "the affidavits we sign are accurate." A spokesman for Bank of America, Rick Simon, said, "We do not have anything to tell you at this time."

GMAC and Chase are in trouble because, overwhelmed with foreclosures, they tried to process them as quickly and cheaply as possible, defense lawyers say. The companies say they are reviewing their procedures to take care of any violations.

The missteps stemmed from the affidavits the lenders file as they seek a quick or summary judgment in thousands of foreclosure cases. The affidavits state certain facts about the case, including the amount owed, which the signer indicates he has personal knowledge of. Without the affidavit, the lender would have to prove the facts at trial.

In depositions taken by lawyers for homeowners, executives at GMAC and Chase said they or their teams signed 10,000 or more affidavits and related documents a month. That did not give them time to review the cases.

Defense lawyers say the disclosures are symptomatic of the carelessness, if not outright fraud, that lenders have been exhibiting for years in their rush to file cases. Many necessary documents have disappeared, with defense lawyers saying the lenders often do not even have standing to foreclose.

In a number of pending cases in Florida, defense lawyers there said, GMAC has already withdrawn affidavits. The lawyers said they would try to have the cases thrown out for possible fraud, although they acknowledged that might be difficult.

GMAC said it would refile the affidavits. Chase said it had not withdrawn any affidavits.

“The way the plaintiffs’ lawyers have handled this has corrupted our legal system,” said Thomas Cox, a Maine lawyer whose deposition of a GMAC executive in June helped prompt the current disclosures. “They tried to manufacture foreclosures the way you’d manufacture cars, on an assembly line. It can’t be done that way.”

Mr. Cox is representing pro bono a rural woman who is in foreclosure on a $82,000 mortgage. The plaintiff in the case is Fannie Mae, the mortgage holding company that failed during the financial crisis and is now under government conservatorship. GMAC serviced the loan for Fannie Mae.

This week, the judge in the case set aside his summary judgment in favor of Fannie when he read Mr. Cox’s deposition of a GMAC executive, Jeffrey Stephan, who said he never reviewed the file he had signed. The case will now go to trial.

“I don’t think they are going to give up easily,” said Mr. Cox.

As the foreclosure crisis has deepened, the length of time borrowers spend waiting for the end has lengthened.

In January 2009 the time between the owner’s first missed payment and eviction was 319 days, according to LPS Applied Analytics. By August it was 478 days.

Since spring, the data firm says, the lenders have been trying to clear their backlog. They have stepped up the rate at which they put defaulting owners into the formal foreclosure process. In August, they started 283,000 foreclosures, up from 220,000 in April.

Now, as the lenders are pressed to examine more closely their filings, those foreclosure starts are likely to fall, prolonging the owner’s time in limbo. Many borrowers use this period, when they are living in their home but not paying for it, to try and get their financial house back in order.