You’ve just inherited the family home, where you’ve not lived for many years, after the unfortunate but inevitable passing of your last living parent. You know there is a mortgage loan for the property. You have many questions, which may generally be summarized “What are my options, how does this work, and what happens now?”

A Commonplace Scenario

Dad passed years ago, and Mom inherited his interests in the family home. Mom just passed away, and Daughter has inherited all interests in the family home, although she has not lived there for 20 years. The mortgage loan on the family home. Daughter knows of the existence of the mortgage loan, with an associated lien on the family home, but she doesn’t know much more and doesn’t have any specialized knowledge or experience with mortgage loans, deeds of trust, or similar issues. Daughter never wanted to be the executor, so Cousin Sally is performing that role.

Daughter finds a mortgage loan statement from Questionable Loan Servicing, LLC. It appears that Mom had not paid the mortgage for the last few months before her death; the loan statement lists the account as delinquent to the tune of $5,000.00, with an unpaid balance of $225,000.00. A week later, Daughter calls Questionable Loan Servicing, LLC, who won’t speak to her without Mom’s authorization. The fact that Mom isn’t alive to give that permission doesn’t seem to have the impact it should with Questionable’s customer service representative. However, good news! Since Daughter says she inherited the house, she must be the Executor; if the Executor provides certain formal documents, Questionable will speak to the Executor about the mortgage loan status, options, and any other relevant issues. “No, I’m not Executor, but I’ve been told by the attorney that I own the property and should be able to deal with the mortgage loan.”

Questionable’s earnest and well-intentioned customer service representative promises to look into the situation and send written information which will clarify if and how Daughter may be able to deal with the mortgage loan and get access to the loan account. Daughter confirms her own mailing address and says she’ll wait for the documents. Three weeks later, Daughter finds five different letters from Questionable, all sent to the family home; they are:

1. a letter to Mom which says that $232,500.00 is now due and that the matter has been referred to an attorney to initiate foreclosure proceedings;
2. a letter to Mom which says that Questionable may be able to assist with foreclosure-avoidance options;
3. a letter to Daughter which says Questionable cannot talk to her until she provides proper legal authorization;
4. a letter to the Executor which says that the Executor should provide Questionable with Mom’s death certificate, a copy of the trust (but there was no trust!), and the property deed which shows who the new owner is (but there is no such deed!); and
5. a letter to Mom’s Estate which reminds everyone that the loan has a “due upon conveyance” clause, and that if ownership of the home is transferred without the mortgage loan note-holder’s permission, the loan could be accelerated and be called due in full.

Daughter, now completely discouraged, begins to slowly knock her head against the nearest wall and contemplates opening another bottle of Mom’s scotch. What can she do? What should she do? Will they ever talk to her? Can they foreclose? Does she need to refinance? Does she really own the home? Can they sue her over the unpaid mortgage? What a mess.

Heirs Interacting with the Mortgage Loan Servicer

It’s almost impossible to figure any of this out if the mortgage loan servicer won’t provide information and recognize you as the owner, or at least as an individual authorized to have access to the loan account, so getting that access almost always needs to be the first step. Here is the most relevant part of the Code of Federal Regulations on the issue of a mortgage loan servicer’s duties in such scenarios:

(a) Reasonable policies and procedures. A servicer shall maintain policies and procedures that are reasonably designed to achieve the objectives set forth in paragraph (b) of this section.

(b) Objectives. (1) Accessing and providing timely and accurate information. The policies and procedures required by paragraph (a) of this section shall be reasonably designed to ensure that the servicer can:

(vi) Upon notification of the death of a borrower, promptly identify and facilitate communication with the successor in interest of the deceased borrower with respect to the property secured by the deceased borrower’s mortgage loan.

The Consumer Financial Protection Bureau (the “CFPB”) has defined “successor in interest” in this context to mean “the spouse, child, or heir of a deceased borrower or other party with an interest in the property.” The CFPB requires loan servicers to follow the requirements as explained in the above-referenced CFR, and has formally observed that the existence of and compliance with such policies and procedures in scenarios involving transfer of ownership due to death is important to “reduce the number of unnecessary defaults and foreclosures...."
The same CFPB bulletin provides practical examples of actions the loan servicer should take to be in compliance, thus also providing successors in interest like Daughter insight into what can be done from the other side of the equation. In summary, Daughter should at a minimum provide a copy of the death certificate, any and all documents which evidence her as the heir / new owner (no, in North Carolina this would not include a deed in her name, which shouldn’t exist), and even copies of the CFR and CFPB items cited herein.

Daughter needs to be persistent, be patient (to a certain extent), to maintain good documentation, and to try to make sure the loan servicer’s various departments are appropriately communicating with each other and with external parties (such as any substitute trustee and/or law firm retained to handle a foreclosure of the family home). If the loan servicer fails to effectively cooperate, Daughter should consider filing a complaint with the CFPB and perhaps the North Carolina Commissioner of Banks. The bureaucratic roadblocks are often formidably Byzantine, and I can personally vouch for some of the horror stories which arise from dealing with loan servicers.

**Does the Heir, as new Owner, Need to be “Approved” by the Creditor in Order to Avoid Foreclosure?**

Most people don’t realize that mortgage loan agreements and/or deeds of trust often have a “due upon conveyance” clause (often called a “due on sale” clause, with such description being an incomplete one). These contractual clauses, in essence, allow the creditor to call the mortgage loan due if ownership of the associated real property is conveyed to someone else without creditor’s permission. There are good and understandable reasons for such clauses. However, for your typical residential property, these clauses are not enforceable when the conveyance occurred due to death of the previous owner and the resulting conveyance was to a relative. In our scenario, the creditor cannot call the loan due and/or foreclose merely because Daughter is now the owner, with the creditor not having approved her ownership.

Independent of any due on conveyance clause, the heir’s ownership of the property does not in any way need to be approved by the mortgage loan creditor or anyone else in relation to the loan or the deed of trust. The rights to own real property and to pass it down to subsequent generations are very strongly protected ones.

**Must the Heir Pay the Mortgage Loan?**

In our scenario, Daughter may wonder if, merely by becoming the owner, she has now somehow become obligated to pay the mortgage loan. The answer is no, but barring some other agreement, if the loan isn’t paid in accordance with the contractual loan terms, the creditor can accelerate the loan and foreclose via the deed of trust just as if Mom was still alive and still the owner. Unfortunately, mortgage loan agreements typically don’t contain any type of “grace period” which allows for missed payments during times of confusion and transition such as the death of the borrower.

So the bad news is that the loan does need to be paid if Daughter wants to keep the property. However, unless Daughter has formally agreed to become personally liable for the loan, the creditor cannot pursue her personally for money or any other damages if the loan is not paid as agreed.

One somewhat miscellaneous factor to consider is that a foreclosure case may contain the Daughter as a respondent, and if a foreclosure occurred it is at least possible that her credit report (arguably incorrectly / illegally) would reflect a “foreclosure.”

**Can the Heir Refinance or Modify the Loan? Can the Heir Sell the Property or Otherwise Dispose of it?**

Although most people seem to think of refinancing as just restructuring the loan, of course a refinance is an entirely new loan, even if it’s with the same lender. By contrast, a modification is an amendment of the current loan terms. Refinances are treated very differently as compared to modifications in the context of inherited properties.

In our scenario, the mortgage loan is delinquent and a foreclosure case appears to be in the works. Daughter’s right to refinance the family home is not restricted due to the mortgage loan being delinquent, and even the existence of a foreclosure case would not restrict said rights. She, as owner of the property, is free to refinance the property by seeking a new loan which would pay off the pre-existing loan and result in the pre-existing deed of trust being canceled. This new loan would presumably have Daughter as the borrower and the fact that she inherited the property would be of little to no relevance.

With regard to modifying the loan Mom had on the property, yes, Daughter can try to negotiate a modification of the same. In almost every instance in which Daughter seeks a modification of the loan, the creditor will require her to personally become an obligor on the loan in exchange for offering modification terms. We might normally say the creditor would require her to “assume” the loan, but word choice matters in this context, as explained in a following section.

Daughter can sell the property whether the loan is current or not, but the loan will need to be paid off as part of the sale (barring some other agreement). Daughter also has the power to enter into other types of transactions, such as a discounted payoff (“DPO”) of the loan which allows her to own the property free and clear, or a deed-in-lieu (“DIL”) of foreclosure which transfers ownership of the property to the mortgage loan creditor. In some instances, Daughter may not bother negotiating a DIL, as the primary advantage of that resolution compared to a foreclosure is usually the waiver of the creditor’s right to seek damages from the borrower, something Daughter would not need to worry about as long as she had not formally agreed to become personally obligated on the loan.

Of course, any real property-related transaction an heir considers entering into must take into account whether there is a risk of the real property being pulled into the estate to be liquidated to obtain cash to pay creditors besides the mortgage loan creditor. In our example scenario, Mom has no other creditors and thus Daughter is not concerned with this issue.

**Should the Heir Agree to Become Personally Obligated on the Mortgage Loan?**
Obviously, what someone in Daughter’s situation “should” do depends on many factors. Let’s assume Daughter wants to maintain ownership of the family home. If she can reinstate the loan directly, typically by paying the entire amount the servicer quotes for reinstatement, she will then avoid having to consider a modification and the personal liability on the loan which would likely be required. She would then have the benefits of ownership without some of the potential negatives of having a mortgage loan.

If Daughter needs to modify the loan and the creditor will allow that without requiring her to become personally obligated on the loan, great -- but there is almost no chance of that happening. The creditor will almost certainly require her to become personally obligated in exchange for that modification.

I have been involved in cases in which the creditor would not commit to a loan modification before the heir agreed to become personally obligated. In other words, the loan servicer said “If Daughter formally agrees to become personally obligated on the loan, we will then *consider* a modification.” My response included indignant laughter and (with client’s approval) a professional commentary similar in theme to “When pigs fly.” Under almost no circumstances would I advise a client to become personally obligated on a loan unless that came along with a guaranteed outcome which suited the client’s wants and needs.

Does the Creditor have to Evaluate the Heir’s Ability to Repay the Loan?

In general, mortgage lenders are required to evaluate someone’s ability to repay (“ATR”) the loan in determining whether to allow that person to assume the mortgage loan, similar to the evaluation a loan applicant would be put through when seeking a loan to purchase real property. However, because many new owner heirs have traditionally failed such evaluations, and at least certain aspects of the federal government wanted to change that, the CFPB has formally distinguished an heir becoming obligated on the mortgage loan versus an assumption of the loan by someone in a different scenario. Heirs who come to own real property due to death of the previous owner and then seek to modify a loan are not subject to the ATR rule.

If Daughter wanted to modify the loan, and Questionable Loan Servicing, LLC (acting on behalf of the loan note-holder) wanted her to become obligated as a borrower on the loan in exchange for modified loan terms and the loan being considered back in good standing, the ATR rule need not be considered and need not serve as an obstacle. Daughter would not be “assuming” the loan for purposes of the ATR rule, although what she would be doing very much looks, sounds, and smells like an assumption and would be considered one in almost any other context.

Best Practices for Heirs (and their Representatives)

Heirs should act assertively and persistently when dealing with mortgage loan servicers and other creditor-side entities instead of passively waiting for the servicer to guide the heir forward. The more information the heir can obtain about the status of the mortgage loan and related options, and the more quickly the heir can obtain this information, the better-positioned the heir is to make decisions. If the overall circumstances indicate that the heir can’t afford the loan (perhaps even as potentially modified or refinanced) and/or if the heir doesn’t want to keep the property, it may be best to sell it “now” – before making payments toward the loan or at least before a delinquency eats further away at any equity.

Jason McGrath of Charlotte is licensed in three states, and his law firm McGrath and Spielberger, PLLC focuses on real property and business law matters in the Carolinas.