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SUBJECT

Tenancy: rental payment default: state of emergency: COVID-19

DIGEST

This bill enables small landlords, homeowners, and tenants in financial distress because of the COVID-19 pandemic, to temporarily defer their mortgage or rental payments until, it is hoped, the worst of the public health emergency passes and its financial consequences begin to ease. The bill also establishes timelines and a framework for full repayment of any amounts deferred.

EXECUTIVE SUMMARY

The COVID-19 pandemic has caused widespread unemployment, business closures, and an economic contraction that threatens to metastasize into a potentially catastrophic wave of evictions and foreclosures. To date, the combination of a judicially-imposed freeze on most evictions and federal financial assistance have combined to forestall such a calamity. However, the judicial moratorium is scheduled to end on September 1, 2020, much of the federal assistance has expired, and it is uncertain whether more federal help will materialize. Where they have not done so already, it is highly likely that many tenants and homeowners will soon default on their mortgage or rent payments. If tenants cannot pay their rents, many landlords will be unable to keep up on their mortgage payments also. Evictions and foreclosures would ensue, leading to residential overcrowding and a dramatic increase in homelessness, two things that, on top of everything else, would likely undermine efforts to contain further COVID-19 spread.

This bill proposes a comprehensive solution intended to stave off catastrophic levels of eviction and foreclosure. In effect, it allows small landlords, homeowners, and tenants who are in financial distress as a result of the COVID-19 pandemic to defer rent and mortgage payments until after, it is hoped, the worst of the pandemic has passed.

Specifically, under the bill:

Temporary Protections for Tenants (including mobilehome owners):

- From March 4, 2020 to April 1, 2021 – Tenants get protection from eviction for falling behind on rent and any other payments due under the lease if, within 15 days of the landlord's demand for payment, the tenant submits an attestation to the landlord declaring that they cannot pay because of COVID-19. Tenants still owe their landlords any amount unpaid, but tenants cannot be evicted or sued for not paying it. Voluntary agreements to repay are fine but cannot include penalties, costs, or interest.

- From April 1, 2021 to April 1, 2022 – Tenants must now pay rent and any other payments due under the lease within 15 days of a demand from the landlord or face eviction, but tenants cannot be evicted for any unpaid balance left over from March 4, 2020 to April 1, 2021. Voluntary repayment of that leftover balance is still fine.

- April 1, 2022 onward – The usual landlord/tenant rules snap back into place. If a tenant still owes the landlord any unpaid balance leftover from March 4, 2020 to April 1, 2021, the landlord can now sue the tenant to recover any amount permissible under the lease.

Temporary Protections for Homeowners (including mobilehome owners):

- At any time from the enactment of the bill to April 1, 2021, homeowners with privately backed loans can, based on the submission of an attestation to their lender declaring that they cannot pay because of COVID-19, receive up to 12 months of mortgage forbearance, but any forbearance already received between March 4, 2020 and enactment of the bill can be counted against the 12 months. If the homeowner's post-forbearance repayment options all require increased monthly payments or the payment of a lump sum prior to the maturity of the loan, the lender must tell the borrower, with specificity, why the lender cannot offer an option that does not require such terms. Financially distressed homeowners with federally-backed loans are only guaranteed forbearance if they request it prior to December 31, 2020 and their lender only has to comply with federal laws regarding notifications to consumers.

Temporary Protections for Small Landlords (defined to exclude real estate investment trusts and corporations, except where they own affordable housing):

- One to Four Unit Buildings: Treated the same as homeowners, above.

- Five or More Unit ("Multi-Family") Buildings: At any time from enactment of the bill until April 1, 2021, multi-family landlords with privately-backed loans can, based on the submission of an attestation to their lender saying they cannot pay because of COVID-19, receive up to six months of mortgage forbearance, but any forbearance already received between March 4, 2020 and enactment of the bill can be counted against the six months. The lender can demand documentation of reduction in rental revenue compared to pre-COVID times and can require partial payment during forbearance if the multi-family landlord still has positive net operating income. Financially distressed multi-family landlords with federally-backed loans are only guaranteed forbearance if they request it prior to December 31, 2020.

Note that this timeline would change slightly in the increasingly unlikely event that the Governor declared an end to the statewide COVID-19 state of emergency before December 31, 2020.

The bill is sponsored by the California Rural Legal Assistance Foundation, Housing Now! California, the Leadership Counsel for Justice and Accountability, PolicyLink, Public Advocates, Public Counsel, and the Western Center on Law and Poverty. Support comes from tenant advocates, consumer advocates, groups representing homeowners, and anti-poverty organizations. Opposition comes from landlord associations, who welcome the possibility of mortgage forbearance but worry it might not hold up to legal challenge, leaving them with a set of tenant protections they believe are too onerous, are subject to abuse, and that would curtail their ability to derive revenue from their rental property too much and for too long. Further opposition comes from bankers, lenders, and loan servicers, who assert that the loan payment forbearance provisions in the bill are unconstitutional and would, at least in some cases, put them in a precarious financial position.

NOTE REGARDING INPUT FROM OTHER SENATE POLICY COMMITTEES

Due to the COVID-19 Pandemic and the unprecedented nature of the 2020 Legislative Session, all Senate Policy Committees are working under a compressed timeline. This timeline does not allow this bill to be referred and heard by more than one committee, as a typical timeline would allow. In order to fully vet the contents of this measure for the benefit of Senators and the public, this analysis includes information from the Senate Committee on Banking and Financial Institutions. That information can be found in Comment 3.

PROPOSED CHANGES TO THE LAW

Existing law:

1) Provides, pursuant to the CARES Act, that, as to federally backed mortgages securing one-to-four unit properties, a lender must provide up to 360 days forbearance to a borrower who requests such forbearance during the period beginning March 13, 2020 and ending at an undefined time (but likely December 31, 2020), subject only to an affirmation from the borrower that the borrower has a financial hardship due to the COVID-19 pandemic. (15 U.S.C. § 9056.)

2) Provides, pursuant to the CARES Act, that, as to federally backed mortgages securing multifamily (five or more units) properties, a lender must provide up to 90 days forbearance to a borrower who requests such forbearance during the period beginning March 13, 2020 and ending when the nationwide COVID-19 state of emergency ends or December 31, 2020, whichever is earlier, subject only to an affirmation from the borrower that the borrower has a financial hardship due to the COVID-19 pandemic and a requirement that the lender document the hardship. (15 U.S.C. § 9057.)

3) Requires a lender, pursuant to the Homeowner Bill of Rights, to undertake steps to explore loan modification and loss mitigation with a borrower, including, but not limited to, contacting a mortgage borrower 30 days before recording any Notice of Default, to discuss options for avoiding foreclosure. (Civ. Code § 2923.55.)

4) Specifies that a tenant is guilty of an unlawful detainer and subject to court-ordered eviction if, within three days of a demand to vacate the premises or pay rent that lawfully accrued within the last 12 months, the tenant does neither. (Code of Civ. Proc. § 1161(2).)

5) Specifies that a tenant is guilty of an unlawful detainer and subject to court-ordered eviction if, within three days of a demand to vacate the premises or comply with a material obligation under the lease other than the payment of rent, the tenant does neither. (Code of Civ. Proc. § 1161(3).)

6) Authorizes a mobilehome park to terminate the tenancy of a mobilehome owner in the mobilehome park for non-payment of rent, utility charges, or reasonable incidental service charges only when:
   a) the amount has been due for five days;
   b) the park thereafter serves the mobilehome owner with a demand to pay the amount due or vacate the premises within three days, unless the mobilehome park owner has already been served with three or more three-day notices of this type in the last 12 months;

c) the mobilehome owner neither vacates nor pays within the three days given; and
d) the park also gives the mobilehome owner a 60 day notice terminating the tenancy. (Civ. Code § 798.56(e).)

7) Provides, pursuant to the CARES Act, that, as to properties subject to a federally-backed mortgage, the landlord may not seek to evict a tenant for non-payment of rent or other fees or charges for 120 days after March 27, 2020 and, thereafter, can only require the tenant to vacate upon 30 days' notice. (15 U.S.C. § 9058.)

This bill:

1) Makes a series of findings and declarations regarding the economic consequences of the COVID-19 pandemic and the resulting threat of widespread residential evictions and foreclosures.

2) Establishes a legal framework through which small landlords, homeowners, and mobile home owners may request up to 360 days of forbearance on a mortgage or loan secured by a one-to-four unit residence or rental property during a specified period ending April 2021 at the latest. Requires mortgage servicers and mobilehome lienholders to provide such forbearance upon the borrower's submission of an attestation affirming that the requester has a COVID-19 related financial hardship, subject to specified procedures. Allows borrowers to enforce their rights under this framework in court and directs courts to award the borrower attorney's fees if the borrower successfully obtains injunctive relief to stop a foreclosure sale.

3) Establishes a legal framework through which small landlords may request up to 180 days of forbearance on a mortgage or loan secured by a rental property of five or more units during a specified period ending April 2021 at the latest. Requires mortgage servicers to provide such forbearance upon the borrower's submission of documentation showing a COVID-19 related financial hardship, as specified and subject to specified conditions. Authorizes mortgage servicers to require partial payment in the amount of any positive net operating expenses. Allows borrowers to enforce their rights under this framework in court.

4) Allows a tenant to be evicted for any lawful reason, except that:
a) as to non-payment of a financial obligation under the lease that accrued between March 4, 2020 and the earlier of 90 days after the end of the state of emergency or April 1, 2021, the tenant can only be evicted if, in response to a specified 15-day notice, the tenant does not pay the demanded amount, vacate, or sign and deliver an attestation of COVID-19 related financial hardship, as defined;

b) as to non-payment of rent for the 12-month period immediately following the period described in (a), the tenant can only be evicted if, in response to a specified 15 day notice, the tenant does not pay the demanded amount or vacate.

5) Provides that a landlord and tenant may enter into a voluntary agreement for repayment of any non-payment of financial obligation under the lease that accrued between March 4, 2020 and the earlier of 90 days after the end of the state of emergency or April 1, 2021, provided that the agreement is limited to the unpaid amount only, among other conditions.

6) Prohibits a landlord from suing a tenant for any non-payment of financial obligation under the lease that accrued between March 4, 2020 and the earlier of 90 days after the end of the state of emergency, or April 1, 2021, until 15 months after the end of the state of emergency, or April 1, 2022, whichever is earlier. Authorizes a landlord bringing such a suit to seek all damages available to the landlord pursuant to the lease, including, but not limited to, interest, attorney's fees, court costs, and late payment penalties.

7) Specifies that, if a local initiative, ordinance, regulation, or other policy conflicts with (4),(5), or (6), the provision that provides greater protection to tenants shall control.

8) Contains a severability clause.

COMMENTS

1. Basic framework

This bill is one of several bills gutted and amended this past summer in order to try to address the impact from the COVID-19 pandemic on residential housing. In its original form, the bill focused exclusively on protecting tenants. It proposed to provide a guarantee to financially distressed tenants that, whatever other difficulties they might be facing, they would not have to worry about being evicted from their homes in the midst of the pandemic. The justification for shielding tenants against eviction was both humanitarian and a matter of public health: forcing people into crowded living conditions or out onto the streets would only facilitate further spread of COVID-19.

Few quarreled with the rationale behind the proposed policy. Nonetheless, the bill received understandable criticism from landlords for being unbalanced. While the bill called for tenants to pay their landlords back in full after the worst of the COVID-19 economic fallout passed, it did not provide answers for how landlords were supposed to keep up with their bills in the meantime. Larger landlords with more financial cushion to rely upon and greater access to credit might be able to operate for several months with reduced rental revenue, but smaller landlords of the proverbial "mom-and-pop" variety expressed fear that they would be driven out of business or into foreclosure.

To try to address this imbalance, the author has now amended the bill to include a component providing temporary mortgage forbearance for small landlords and homeowners, including mobilehome owners. As a result, while aspects of the bill can be questioned for a variety of policy and legal reasons detailed in this analysis, it can accurately be described as a comprehensive plan to try to minimize the number of Californians who will lose their homes to eviction and foreclosure as a result of the economic fallout from the COVID-19 pandemic. In simplified terms, that plan offers financially distressed tenants, homeowners, and small landlords temporary deferral of payment obligations until, it is hoped, the economy recovers and it becomes possible for everyone to pay off their debts over time.

2. Analysis of the bill's mortgage and mobilehome loan forbearance provisions

As explained in greater depth in the contribution of the Senate Banking and Financial Institutions Committee contribution to this analysis at Comment 3, there are essentially two general categories of loans for residential housing: those that are owned, insured, or guaranteed by an agency within the federal government ("federally-backed" mortgages or loans), and those that are not ("non-federally backed" or "privately-backed" mortgages or loans. Since the federal agencies have a financial stake in federally-backed loans, the federal government maintains authority to regulate much about how those loans are handled. According to the Senate Banking and Financial Institutions Committee, roughly 70 to 80 percent of California mortgages are federally-backed. The remainder are not.

a. Where things stand today

Pursuant to the CARES Act and agency guidance emanating from it, the federal government has exercised its authority over federally-backed loans to establish the following temporary forbearance regime. Starting March 13, 2020, when the federal government declared a nationwide state of emergency in response to COVID-19, and presumably continuing until December 31, 2020,[1] owners of property with one to four residential units on it and a federally-backed mortgage may request forbearance on their loan payments by calling or writing to their mortgage servicer. (CARES Act § 4022(b).) So long as the borrower "affirms" that they are "experiencing a financial hardship during the COVID–19 emergency," the mortgage servicer must "with no additional documentation required other than the borrower's attestation," provide the borrower with up to 180 days of forbearance, with an option to extend that forbearance

[1] Due to what may have been a drafting oversight, Section 4022 of the CARES Act does not actually define the "covered period" during which its provisions apply, but the related Section 4023 of the bill defines "covered period" to mean March 13, 2020 until the nationwide state of emergency ends or December 31, 2020, whichever comes earlier. (CARES Act § 4023(f)(5).)

for up to an additional 180 days. (*Ibid*.) During the forbearance, the mortgage servicer is forbidden from charging the borrower any fees, penalties, or interest beyond the amounts scheduled or calculated as if the borrower made all contractual payments on time and in full under the terms of the mortgage contract. (CARES Act § 4022(c).)

The CARES Act also provides access to forbearance for landlords who have federally-backed mortgages on multifamily housing, meaning buildings with five or more residential units. The process and terms of the multifamily forbearance are stricter, however. Unlike the one-to-four unit context, where the mortgage servicer is prohibited from requesting anything from the mortgage servicer other than an attestation of financial hardship due to COVID-19, in the multifamily context mortgage servicers are supposed to "document" the financial hardship involved. (CARES Act § 4023(c).) Similarly, whereas in the one-to-four unit context the borrower has a right to up to 360 days of forbearance, the CARES Act limits multifamily borrowers to 90 days of forbearance, though some federal agencies have since extended this to 180 days. (*Ibid*.)

The CARES Act does not specify the terms on which the borrower must make up the amount unpaid once the forbearance ends. Initially, there were reports that some mortgage servicers were requiring borrowers to make an immediate lump sum payment for the full deferred amount, but federal agency guidelines have since clarified that mortgage servicers are not supposed to do that.

In sum, the CARES Act creates a simple framework that generally allows distressed borrowers to obtain forbearance from their mortgage servicer quickly and easily upon request. Critically, however, *the CARES Act does not cover privately-backed loans*. This means that, while financially distressed California borrowers – be they landlords or homeowners – with federally-backed loans on one-to-four unit properties can be rest assured that they can currently obtain forbearance upon request and will probably be able to do so for the remainder of the calendar year, their counterparts with privately backed mortgages have no such guarantee. Similarly, landlords operating multifamily buildings with federally-backed mortgages can expect to obtain up to six months forbearance, subject only to the requirement that they "document" their financial hardship, while their counterparts with privately-backed mortgages are at the mercy of their mortgage servicer. For the time being, it appears that most servicers have been willing to work with their borrowers on privately-backed mortgages voluntarily, but as things stand, such borrowers have no guarantee of that.

b. How the bill would work

The forbearance components of this bill build around, but largely reflect the CARES Act provisions described above. Importantly, in fact, the bill contains a safe harbor clause specifying that any mortgage servicer who complies with the CARES Act, and any amendments or agency guidance relating to it, is deemed to be in compliance with the bill as well.

In contrast to the CARES Act, however, this bill has three major differences and some more nuanced ones. The first major difference is that the bill's access to forbearance upon request is limited to homeowners and small landlords, only. Through the bill's definition of "borrower," corporations and real estate investment trusts are excluded from benefiting from the bill. Thus, landlords resembling the proverbial "mom-and-pops" are covered by the bill, while corporate landlords are not.

The second major difference from the CARES Act is that this bill would also apply to privately-backed loans. Thus, a borrower who owns a one-to-four unit residential property subject to a privately-backed mortgage would be able to get up to 360 days' worth of forbearance upon request, just as their counterparts with federally-backed mortgages now can. Similarly, borrowers with privately-backed multifamily loans would have access to up to 180 days forbearance just the same as their federally-backed counterparts.

The third major difference between this bill and the CARES Act is that this bill would extend out the period in which borrowers could obtain forbearance upon request to 90 days after the statewide emergency ends or April 1, 2021, whichever is earlier. By contrast, the window for requesting forbearance under the CARES Act closes when the nationwide state of emergency ends or December 31, 2020, whichever is earlier.

Beyond these major differences, the bill diverges from the CARES Act in subtler ways as well. For example, the bill requires mortgage servicers to provide borrowers with notices throughout the forbearance process that let them know about their rights and what they can likely expect to happen when they emerge from forbearance. Of particular importance, the notifications are intended to alert borrowers early if the mortgage servicer knows that the borrower will have to make higher monthly principal and interest payments when the forbearance is over or if the borrower will be required to make a lump sum payment before the maturity of the loan in order to avoid default. Another difference between the bill and the CARES Act is that the bill provides great specificity about what mortgage servicers can require of multifamily borrowers in order to prove financial hardship. Specifically, the bill states that a mortgage servicer can require the borrower to document a 10 percent reduction in gross rental revenues when compared against the pre-COVID-19 period. Yet another example of the difference between the CARES Act and the bill is that the bill gives mortgage servicers the option, in the multifamily context only, to require partial payments from borrowers in forbearance in the amount of any net positive operating income.

As to all of these differences between the CARES Act and the bill, however, it is critical to bear in mind the impact of the safe harbor clause: these differences will in most instance apply only to privately-backed loans since, as to federally-backed loans, the safe harbor means that compliance with the CARES Act is sufficient to comply with the bill.

Borrowers are authorized to enforce their rights pursuant to the bill in court if they are likely to suffer material harm from a violation. To help protect homeowners and small landlords, in particular, from losing their properties due to a violation of the bill, the bill provides for an automatic award of attorney's fees to a prevailing borrower in the one-to-four context who obtains an injunction to stop the sale of their property through foreclosure. Any other award of attorney's fees to prevailing borrowers under the bill are left to the discretion of the court.

Opponents of the bill argue that expanding the universe of financially distressed homeowners and small landlords with access to forbearance upon request would likely result in reduced access to credit overall. This point is developed further in the contribution to this analysis by the Senate Committee on Banking and Financial Institutions in Comment 3, below. With regard to this concern, it is important to bear in mind that the bill's provisions do not apply to mortgages originating after the operative date of the bill. Thus, lenders would not have to factor costs of the bill into future loans. Finally, even assuming that the bill would result in some constriction in the availability of credit, as a policy matter, that would need to be weighed against the economic harm that could very well result if additional borrowers are *not* able to obtain forbearance. As the California Chamber of Commerce puts it in their letter opposing this bill: "[f]oreclosures will place additional strains on banks, lenders, and the larger housing market - which will not help home buyers or California's economic recovery."

c. Constitutional considerations

In their opposition to this bill, several trade associations associated with banking and lending argue that California lacks legal authority to regulate mortgage and other loan forbearance in the manner this bill purports to do. They raise three primary constitutional claims for that belief. First, they claim that such interference with existing mortgage and loan agreements violates the Contracts Clauses of both the state and federal constitutions. Second, they assert that, at least as to federally chartered banks, federal law regulates the field of mortgages, finance, and lending such that California is preempted, under the Supremacy Clause, from enacting the sort of forbearance measures contained in this bill. Third, they argue that the bill has the effect of an unconstitutional taking of property because, they allege, it regulates in such a way as to deprive banks of economic return on their investment without just compensation.

i. Contracts Clause

The Contracts Clause of the U.S. Constitution provides that "[n]o state shall … pass any Law impairing the Obligation of Contracts." (U.S. Const. Art. I, § 10, cl. 1). The California Constitution, similarly, declares that "[a]… law impairing the obligation of contracts may not be passed." (Cal. Const., art. 1, § 9.) Because the two provisions are parallel, the same legal analysis applies to both. (*Campanelli v. Allstate Life Ins. Co.* (9th Cir. 2003) 322 F.3d 1086, 1097, citing *Calfarm Ins. Co. v. Deukmejian* (1989) 48 Cal.3d 805.)

Though the contract clauses speak in absolute terms, courts have long held that they do not in fact prohibit all state action that results in the modification of a contract. (*Lyon v. Flournoy* (1969) 271 Cal.App.2d 774, 782.) Instead, as the U.S. Supreme Court recently articulated in *Sveen v. Melin* (2018) 138 S. Ct. 1815, whether a state law violates the Contracts Clause must be determined through a two-step test. The threshold question is whether the state law operates as a "substantial impairment of a contractual relationship." If not, the state law does not violate the Contracts Clause. If so, then the state law may still be constitutional if it is drawn in an "appropriate" and "reasonable" way to advance "a significant and legitimate public purpose." (*Id*. at 1821-22.)

Applying this basic standard to the bill, it seems likely that a court would find that requiring forbearance on a mortgage constitutes a substantial interference with the underlying contractual bargain. Borrowers promised to pay certain amounts at certain intervals and the bill would at least temporarily disrupt that schedule. Under the second part of the *Sveen v. Melin* test, however, it seems doubtful that a court would find the bill unconstitutional. Staving off the serious threat of housing loss due to a global pandemic is an eminently significant and legitimate public purpose" and the bill goes about it in a way that is both appropriate and reasonable. The measures are temporary in nature, respond to an emergency situation, and provide a pathway for both parties to the contract to obtain the full benefit of their bargain, albeit after a delay until that emergency abates. These are the types of considerations that the U.S. Supreme Court has taken into account when upholding the constitutionality of state laws that postponed mortgage foreclosures in the past. (*Home Building and Loan Assn. v. Blaisdell* (1934) 290 U.S. 398.)

ii. Regulatory takings

Under both the California and federal constitutions, the state cannot deprive anyone of property without providing adequate compensation. (U.S. Const., Amend. V; Cal. Const., art. I, § 7.) Although the bill does not propose any physical taking of property, judicial precedent establishes both that a contract can, in at least some instances, be a basis for a property right (*Lynch v. United States* (1934) 292 U. S. 571, 579) and that regulations can, under extreme circumstances, result in the legal equivalent of taking property. Such situations are known as regulatory takings.

The seminal case on regulatory takings is *Penn Central Transportation Company v. City of New York* (1978) 438 U.S. 104. In that case, the U.S. Supreme Court explained that applying the rule against regulatory takings involves "essentially ad hoc, factual inquiries." Still, the court set forth a general standard to be followed when determining whether a regulatory taking has occurred:

> The economic impact of the regulation on the claimant and, particularly, the extent to which the regulation has interfered with distinct investment-backed expectations are relevant

> considerations. So too, is the character of the governmental action. A 'taking' may more readily be found when the interference with property can be characterized as a physical invasion by government than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good." (*Id*. at 124.)

This bill adjusts the timing of mortgage payments in order to promote the collective interest in avoiding widespread foreclosures in the midst of a pandemic. Moreover, since the required forbearance is temporary and does not ultimately relieve the borrower from paying off the mortgage in full, it seems doubtful that a court would conclude that the bill undermines investment-backed expectations. In short, the bill does not appear to deprive anyone of the financial benefit of their bargain, it just requires them to wait out the worst of a public health and economic crisis in order to do so.

iii. Preemption.

Federal law supersedes state law where language in the federal statute reveals an explicit congressional intent to pre-empt state law, where the federal statute's structure and purpose or nonspecific statutory language reveal a clear pre-emptive intent, or where federal law may be in irreconcilable conflict with state law because compliance with both statutes is a physical impossibility or the state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress. (*Barnett Bank, N.A. v. Nelson* (1996) 517 U.S. 25, 31.)

There are two principal ways in which this bill runs the potential risk of straying beyond what is permissible under preemption doctrine. The first has to do with federally-backed mortgages. Such mortgages, as previously discussed, are owned, insured, or guaranteed by the federal government. Therefore, anything within the bill that instructs mortgage servicers on how to handle federally-backed loans could potentially be construed as a state telling the federal government how to manage the loans it is backing. And, if what the bill requires conflicted in any way with the federal government's own rules for how to manage those loans, the bill would certainly be preempted at least to the extent of the conflict. The bill seeks to sidestep this potential problem entirely by simply setting up a safe harbor with respect to federally-backed loans. Under this safe harbor, so long as a mortgage servicer follows federal law when servicing a federally-backed loan, the bill deems the servicer to be in compliance with the terms of the bill. This safe harbor eliminates what would otherwise be perhaps the most obvious potential preemption problem with the bill, but it raises policy questions in the process. Those questions are addressed as part of the discussion on points for further evaluation, below.

The second potential preemption problem relates to how the bill's forbearance provisions operate with respect to any mortgage, whether federally or privately-backed.

These mortgages could originate from a California financial institution, in which case California has clear authority over them. However, national banks and financial institutions from other states also create these mortgages. When a loan originates outside of California, California's authority to regulate the mortgages is more limited.

In the context of state regulations and their application to national banks, the U.S. Supreme Court has clarified that preemption applies when a state law prevents or significantly interferes with a national banks exercise of its powers. (*Barnett Bank, supra,* 517 U.S. 25 at 33.) Based on this general standard, the Office of the Comptroller of the Currency (OCC) has issued rules explaining what states can and cannot do with respect to national banks. In broad strokes, these rules allow states to legislate in the area of debt collection but prohibit states from passing laws that govern the terms of credit. As the opponents to the bill have pointed out, the OCC recently issued a bulletin highlighting these rules as a reminder to states considering legislation along the lines of this bill.[2] The OCC stated that:

> [F]ederal law preempts state and local laws that impermissibly conflict with banks' exercise of federally authorized powers under the standard set forth in *Barnett Bank of Marion County, N.A. v. Nelson*. Consistent with this standard, OCC regulations provide examples of the types of state laws that do not apply to banks' lending and deposit-taking activities. These include state law limitations on: terms of credit, such as the schedule for repayment and interest, amortization of loans, balance, payments due, minimum payments, and term to maturity; disbursements and repayments; and processing, origination, and servicing mortgages. OCC regulations also address interest and non-interest fees. (Footnotes omitted.)

On the one hand, this bill does not require mortgage servicers to offer any particular kind of repayment arrangement postforbearance. Instead, the bill simply requires the servicer to notify the borrower if the servicer reasonably believes that only more challenging repayments terms will be available to the borrower, such as higher monthly payments or the need to make a lump sum payment before the end of the mortgage. On the other hand, the bill's prohibition on charging fees, penalties, and some forms of interest during the forbearance period arguably runs afoul of the OCC's rule. The mere fact that the bill requires servicers to provide forbearance at all may do so as well. Certainly, the forbearance component of the bill is likely to be challenged in court, if enacted.

[2] *OCC Bulletin 2020-62: COVID-19 Relief Programs: Preemption* (Jun. 17, 2020) Office of the Comptroller of the Currency https://www.occ.treas.gov/news-issuances/bulletins/2020/bulletin-2020-62.html (as of Aug. 15, 2020).

It may be possible for California to argue that, even if the bill does violate the OCC rules, those rules themselves do not properly reflect the standard set forth in *Barnett Bank.* A court reviewing the matter could conclude that states actually have greater latitude to legislate in this area than the OCC believes, particularly if the state is enacting temporary measures in response to an emergency, as this bill does.[3]

The forbearance component of the bill might be on stronger legal footing, for example, if it were restructured in such a way that it nests the deferred payment program within California's non-judicial foreclosure process. That process formally begins with the recording of a Notice of Default in the county where the property is located. (Civ. Code § 2924(a)(1).) With that in mind, the bill could direct county recorders not to record a Notice of Default for that property unless it were accompanied by a declaration from the loan servicer that the borrower has not sought forbearance.

d. Points for further evaluation

The forgoing discussion of this bill's residential mortgage and mobilehome loan forbearance components reveal an approach that, while providing the much needed balance to the tenant protection components, may still need some refinement. Additional concerns are also articulated in the contribution to this analysis submitted by the Senate Banking and Financial Institutions Committee, which can be found at comment 3, below. Notwithstanding these concerns, given the gravity of what is at stake and the short timeframe left for the Legislature to act, there is a strong argument that this bill constitutes a critical part of the final discussion.

Assuming that the bill moves forward, the Committee should continue to provide the author with its guidance as to the primary remaining issues left for consideration in relation to the forbearance component of the bill. Those remaining issues may be summarized as follows.

i. How widely to apply the bill's safe harbor provisions?

The safe harbor provisions in the bill in print deem a mortgage servicer in compliance with the bill, with respect to any federally-backed loan, as long as the mortgage servicer complies with the terms of the CARES Act and any related federal agency guidelines as they evolve. This approach has at least two virtues that justify keeping the safe harbor provision in the bill as is. It gives borrowers with privately backed loans the possibility of an additional three months, until April 1, 2021, to obtain forbearance on request if they need it. In addition, as explained earlier in this analysis, it avoids some of the thornier preemption questions that the bill might otherwise prompt.

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[3] *See* Krishnamurthy, *Don't Bank on Preemption for AB 2501* (Jun. 4, 2020) The Daily Journal https://www.dailyjournal.com/articles/357956-don-t-bank-on-preemption-for-ab-2501 (as of Aug. 15, 2020).

Yet the current approach to the safe harbor also has drawbacks. One criticism, well-articulated in the contribution to this analysis by the Senate Banking and Financial Institutions Committee, is that the safe harbor in the bill in print would result in an unlevel playing field: borrowers with federally-backed loans would get three months' less time to request forbearance compared to borrowers with privately-backed loans, and the federally-backed borrowers would not necessarily receive the bill's consumer-friendly notifications. To be fair to the bill, however, it should also be highlighted that an unlevel playing field *already exists*, albeit in the reverse direction. As things stand today, a borrower with a federally-backed loan is guaranteed to get forbearance based on little more than a phone call to the mortgage servicer, whereas borrowers with privately-backed loans have no guarantee of any assistance at all. Thus, from the borrower's point of view, the differing standards set up by the current safe harbor in the bill may be arbitrary, out of the borrower's control, and potentially confusing, but they are not really any more so than the status quo.

It may also bear noting that Congress or the federal agencies may at some point extend the period in which borrowers on federally-backed loans may get forbearance on request through April 1, 2021. In several cases, the federal agencies have already extended the length of forbearance available to borrowers whose loans they back. If that were to happen, then all loans would be treated the same under the safe harbor in the bill even as it is presently written. It is even possible that passage of this bill would induce such a result at the federal level.

Another criticism of the current safe harbor comes from the loan servicers themselves. From their perspective, the bill's distinct treatment of federally and privately-backed loans is inefficient. Whatever the rules are going to be, the mortgage servicers would like them to be consistent, so that they can operate under a single set of procedures.

There are two ways that the safe harbor could be revised to achieve this consistency. One option would be to expand the existing safe harbor to include privately-backed loans. Under this approach, a mortgage servicer servicing a privately-backed loan would be deemed in compliance with the bill so long as the mortgage servicer treated the borrower the same way it has to treat a borrower with a federally-backed loan. Since the exact treatment required on a federally-backed loan varies somewhat depending on which federal agency is backing the loan, it would be necessary to designate one federal agency's rules – presumably Fannie Mae's – to serve as the standard for privately-backed loans.

While this approach has the appeal of consistency and "leveling the playing field," it is critical to note that it would also render much of the other components of the bill moot. Because mortgage servicers would only have to follow the CARES Act and agency guidance whether the loan is privately-backed or federally-backed, they would never have to comply with the bill's consumer notification requirements and, unless the federal rules changed, they would not have to offer forbearance to anyone after

December 31, 2020, when the window to request forbearance under the CARES Act closes. Moreover, if the period in which distressed borrowers can obtain forbearance upon request ends in December 2020 rather than April 2021, the Legislature will not have any opportunity to step in and extend the period should economic conditions fail to improve in the interim.

As an alternative approach, the safe harbor could be done away with altogether. That option achieves the consistency and level playing field objectives. It has the added benefit, from the borrowers' perspective, of ensuring that all financially distressed borrowers, regardless of loan type, would be able to obtain forbearance upon request all the way until April 1, 2021. Similarly, eliminating the safe harbor altogether would mean that all borrowers get the benefit of the bill's consumer notification provisions. The downside to eliminating the safe harbor is not inconsequential, however. Without the safe harbor, the bill would be telling mortgage servicers how to handle federally-backed loans, a posture that could be especially difficult to defend if challenged on preemption grounds.

ii. What to do about smaller lending institutions?

Some smaller mortgage servicers, such as credit unions, carry a significant number of mortgage loans in portfolio, meaning that they remain on the institution's books rather than being sold to investors or insured or guaranteed by the federal government. Such entities assert that they are at particular financial risk if they are forced to provide full forbearance to large numbers of their borrowers. They worry, therefore, that application of this bill to them could lead to a significant reduction in their ability to lend to members, at best, and regulatory actions up to and including forced mergers, at worst. The author reports a healthy back and forth with the credit unions and small mortgage servicers over a possible exemption from the bill, but no definitive result has come out of those negotiations yet. One option would be to exempt lending institutions by the number of foreclosures they undertake annually, as was done under the California Homeowner Bill of Rights, but if foreclosure numbers remain low, this exemption might sweep too broadly, leaving many homeowners and landlords without access to the forbearance. Alternatively, the exemption could be based on the institution's size.

3. <u>Comments from the Senate Banking and Financial Institutions Committee</u>

"The provisions of this bill that impose requirements on mortgage servicers with respect to offers of forbearance and actions that must be taken post-forbearance on both single-family and multi-family mortgages are within the shared jurisdiction of the Senate Banking and Financial Institutions Committee with the Senate Judiciary Committee. From the perspective of the Senate Banking and Financial Institutions Committee, these well-intentioned provisions raise at least three key policy concerns: creation of an unlevel playing field among mortgage servicers; a likely reduction in the availability of mortgage credit and likely concurrent increase in the cost of that mortgage credit; and the risk of federal pre-emption challenges.

For purposes of this bill and the discussion below, it is important to understand that the term federally-backed mortgage does *not* speak to what type of institution originated the loan, but instead to whether a federal entity has agreed to insure or guarantee it. Generally speaking, a federally-backed loan is one that is owned, guaranteed, or insured by the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporations, the Federal Housing Administration, the United States Department of Veterans Affairs, or the United States Department of Agriculture (collectively, "the federal mortgage agencies"). Available evidence suggests that approximately 70-80% of all mortgages held by Californians are federally-backed.

Non federally-backed mortgages include those that are serviced by the same financial institution that originated them (so-called portfolio loans; estimated to comprise approximately 15% to 20% of all outstanding mortgages held by Californians) and those that are included in private securitization pools (estimated to comprise less than 5% of all outstanding mortgages held by Californians). Both federally-backed and non federally-backed mortgages may be originated and serviced by either state- or federally-regulated financial institutions. For that reason, this bill's provisions apply to all servicers of single-and multi-family residential mortgage loans, including those that are regulated at the federal level and by other states.

Application of two different sets of rules and two different timelines to mortgage servicers (creation of an unlevel playing field). Within its mortgage provisions, this bill uses the forbearance provisions of the federal CARES Act and federal guidance on post-forbearance options that was issued to servicers of federally-backed loans by the federal mortgage agencies as its floor. Thus, any servicer of a federally-backed mortgage that complies with the CARES Act and with guidance issued by that servicer's applicable federal mortgage agency is deemed to be in compliance with the applicable mortgage-related provisions of the bill. However, the mortgage provisions of this bill also include several requirements that do not appear in the CARES Act or in federal mortgage agency guidance, and this bill applies a timeline to the provision of that relief that fails to match the timeline in the CARES Act and current federal mortgage guidance. The way this bill is drafted, servicers of non federally-backed loans must follow the enhanced provisions and adhere to the timeframe in the bill, while servicers of federally-backed loans may choose which set of provisions and which timeline to follow, but are likely to follow the CARES Act and federal mortgage agency guidance and timeline for compliance and operational reasons.

This bill lacks any justification for why it applies two different sets of rules to mortgage servicers, based on whether the loans they service are federally-backed or non-federally backed; the borrowers of the properties secured by those mortgages are all similarly situated, but the protections for which they will be eligible will differ, depending on a factor outside the borrowers' control. The different sets of rules also have the potential to create confusion among borrowers, who may be uncertain about which set of protections applies to them.

If this bill's authors believe that the state has the authority to impose requirements on federally-regulated servicers and servicers regulated by other state regulators, it would be simplest if the bill applied one set of rules and one timeline to all single-family residential mortgage servicers subject to the bill's provisions and (if desired) another timeline to all multi-family residential mortgage servicers subject to the bill's provisions. In the alternative, if this bill's differential treatment of servicers of federally-backed and non federally-backed mortgages is an attempt to mitigate pre-emption claims, staff respectfully suggests that pre-emption arguments can still reasonably be raised about this bill's mortgage provisions, because the bill imposes California-specific rules on the servicing activities of federally-regulated servicers and servicers regulated by other states, and does so outside of the nonjudicial foreclosure context.

Likely reduction in the availability of mortgage credit and concurrent increase in the cost of that mortgage credit. As stated earlier, several of this bill's provisions go beyond existing federal law and federal mortgage agency guidance, and all of this bill's provisions subject the servicers covered by the bill to lawsuits for failure to comply. It is a common practice for providers of mortgage credit to tighten their underwriting standards when government imposes restrictions on the creditors' ability to collect on amounts due to them and to assert their rights under the promissory notes underlying most deeds of trust. The availability of mortgage credit has already shrunk considerably since the pandemic began,[4] due in part to federal requirements that mortgage servicers award forbearance to any borrower who requests it. Typically, when the availability of mortgage credit shrinks, only those with pristine credit can obtain new mortgages or refinance existing mortgages; in nearly all cases, those mortgages also come a cost premium. Simply stated, mortgage originators who are concerned about their ability to recoup amounts lent and who fear being sued for their servicing practices are more reluctant to lend and charge more money in exchange for their willingness to do so. By layering additional requirements on top of relief required at the federal level, and by subjecting servicers to the possibility of lawsuits for failure to comply, this bill has the very real potential to decrease the availability of mortgage credit and increase the cost of mortgage credit in California, relative to the status quo.

Pre-emption challenges. Some of this bill's opponents have asserted that its application to federally-chartered banks runs afoul of federal law. Those banks' prudential regulator (the federal Office of the Comptroller of the Currency; OCC) appears to agree with

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[4] E.g., Mortgage lenders tighten screws on credit in echo of 2008, American Banker, May 8, 2020 (https://www.americanbanker.com/articles/mortgage-lenders-tighten-screws-on-credit-in-echo-of-2008) and Mortgage Credit Tightens, Creating Drag on Any Economic Recovery, Andrew Ackerman and Nick Timiraos, Wall Street Journal, May 25, 2020) https://www.wsj.com/articles/mortgage-credit-tightens-creating-drag-on-any-economic-recovery-11590431459#:~:text=It%20isn't.,some%20of%20this%20credit%20crunch).

those arguments, based on a bulletin it issued in June of this year (https://www.occ.treas.gov/news-issuances/bulletins/2020/bulletin-2020-62.html). Without weighing the relative merits of opponents' pre-emption claims and the authors' countervailing arguments, staff observes that court challenges to this bill and the possible injunctive relief ordered by a court in connection with those challenges could undermine the good intentions of this bill's authors. Although this bill does contain a severability clause, a pre-emption challenge could result in some or all of its mortgage-related provisions being enjoined pending judicial review at the very time borrowers are most in need of its protections.

4. Analysis of the bill's rent deferral and eviction protection provisions

Currently, there are local, state, and federal rules that protect some tenants against eviction for non-payment of rent to varying degrees. An analysis of each local ordinance is beyond the scope of this analysis, but typically, these ordinances provide a moratorium against eviction for non-payment of rent during some temporary, specified period. Often these ordinances limit these protections against eviction to tenants who can provide documentation of a COVID-19 related hardship. Some of these ordinances also provide tenants with a period of several months or a year after the eviction moratorium ends in which to get caught up on the rent.

At the statewide level, the most important existing protection against eviction is the Judicial Council's Emergency Rule 1. Under that rule, landlord are free to file eviction cases with the courts, but the courts will not take the next procedural step – issuing a summons to the tenant – unless the landlord can demonstrate to the court's satisfaction that the eviction is necessary to protect public health or safety. The practical result of Emergency Rule 1 is a temporary freeze on eviction proceedings. This protects tenants for the time being, but the moment Emergency Rule 1 is rescinded, landlords will be free to file new eviction cases and pursue any cases that are already pending. The Judicial Council recently voted to rescind Emergency Rule 1 effective September 1, 2020. Absent legislative action in the interim, therefore, there will soon be no statewide protection against eviction for tenants who cannot pay rent due to the COVID-19 pandemic.

At the federal level, either through Congressional action or, more recently, through an Executive Order, the government has taken actions widely described in the press as "eviction moratoriums." As an initial matter, it is important to understand that these so-called "moratoriums" only apply to properties owned pursuant to a federally-backed mortgage. Second, there are limitations on when these federal eviction shields apply, even as to federally-backed properties. Under the CARES Act, all tenants in federally-backed properties were given 120 days of protection against eviction for non-payment of rent. (CARES Act § 4024.) That aspect of the CARES Act expired July 24, 2020. Congressional negotiations over an extension of this protection for tenants have stalled (as of publication of this analysis). President Trump has issued an Executive Order that he touted as an extension of the CARES Act eviction moratorium though in fact the Order merely directs government agencies to study whether they can extend the moratorium. It is not clear, moreover, whether President Trump actually has the legal authority, without Congressional approval, to grant such an extension. Again, however, even if President Trump's Executive Order does somehow extend the eviction moratorium, it still does not protect California tenants who do not live in federally-backed properties.

Finally, a separate provision of the CARES Act continues to shield tenants in federally-backed properties from eviction for falling behind on the rent if the landlord's mortgage is in forbearance pursuant to the CARES Act's mortgage forbearance provisions. (CARES Act § 4023(d).) It is unknown how many California tenants may be eligible for this protection. Regardless, tenants rarely know whether their landlord is in forbearance and what kind of mortgage the landlord has. This information can be difficult to obtain. As a result, even where this protection applies in theory, it may not be very effective in practice.

All of this means that (at least as of publication of this analysis) California cannot count on federal protections to shield anything more than a very small number of COVID-19 impacted tenants against eviction.

a. What this bill would do

At its most basic, this bill removes the threat that financially distressed tenants will be evicted if they fall behind on their payment obligations under the lease anytime between March 4, 2020 and 90 days after the statewide emergency ends or April 1, 2020, whichever comes sooner. However, tenants still owe their landlords this money, and landlords can sue to recover that money if it remains unpaid after a year and 90 days from the end of the state of emergency, or April 1, 2022, whichever comes sooner.

To achieve that basic outcome, the bill operates in three distinct phases. During what is hoped will be the worst of the COVID-19 pandemic, a tenant can be evicted for any lawful reason, such as breaking a material term of the lease, causing a nuisance, or damaging property. In order to evict a tenant for falling behind on their payment obligations under the lease, however, a landlord must give the tenant a 15 day notice telling the tenant to do one of three things to avoid eviction: pay up in full, vacate, or return an attestation to the landlord indicating that the tenant is in financial distress because of COVID-19 and cannot, for that reason, pay in full at that time. The notice informs the tenant that even if the tenant signs and returns the attestation, the tenant will still owe the money to the landlord and that, if the tenant does not pay the landlord back voluntarily, the tenant can eventually be sued for the unpaid amount plus any applicable penalties, fees, and interest. The notice further encourages tenants to make partial payments if they can do so while still covering their basic household expenses.

The bill thus incentivizes and encourages voluntary advance payment by the tenant, while removing the threat of eviction if tenants absolutely cannot pay.

During the second phase of the bill, when the economic impact from the COVID-19 pandemic will hopefully be starting to wane, tenants will have to remain current on their monthly rent, but cannot be evicted for any unpaid balance left over from the first phase. If the tenant does not remain current on their monthly rent during this second phase, they can be evicted under normal procedures, except that they will have a 15-day window in which to try to make up for any missed payment, rather than the usual three day window. This second phase will last for the 12 months immediately following the first phase.

In the bill's third phase, which would immediately follow the second phase, all of the currently existing landlord/tenant laws will snap back into place. Because existing law does not allow a landlord to evict a tenant for unpaid rent that accrued over a year ago, the landlord will still not be able to evict a tenant for any unpaid balance left over from the first phase. (Civ. Code § 1161(2).) However, beginning in the third phase, landlords will be able to sue their tenants for any unpaid balance still left over from the first phase, as well as any late penalties, attorney's fees, interest, costs, and any other amount that the landlord may lawfully charge to the tenant pursuant to the lease.

In this way, the bill sets up a dynamic that protects tenants from eviction during the worst of the pandemic, incentivizes tenants to repay their landlord voluntarily, and provides the landlord with a backstop in the event that the tenant does not.

b. Constitutional considerations

Just as the financial institutions opposed to this bill question whether the forbearance components of the bill would pass constitutional muster if challenged in court, the landlords opposed to this bill likewise question whether the rent deferral and eviction protection pieces of this bill would survive constitutional scrutiny. Issues of preemption do not apply to this component of the bill, but the landlords still assert that it violates constitutional prohibitions on impairment of contracts and regulatory takings.

i. Contracts clause

As already discussed in relation to the forbearance component of this bill, whether a state law violates the Contracts Clause must be determined through the two-step *Sveen v. Melin* test. The threshold question is whether the state law operates as a "substantial impairment of a contractual relationship." If not, the state law does not violate the Contracts Clause. If so, then the state law may still be constitutional if it is drawn in an "appropriate" and "reasonable" way to advance "a significant and legitimate public purpose." *(Sveen v. Melin* (2018) __ U.S. __; 138 S. Ct. 1815, at 1821-22.)

It seems likely that a court would conclude that temporary deferral of rent payments is a substantial interference with a rental contract. The temporary removal of summary eviction proceedings as a remedy for breach of the lease may be a harder call, since the summary eviction process is a legislative creation and landlords could still seek to recover possession of the property through an action in ejectment.

Regardless, both rent deferral and the eviction protections would appear to have strong arguments for constitutionality under the second step in the *Sveen v. Melin* test. It would be difficult to convince a court that keeping tenants housed during a pandemic is not a significant and legitimate public purpose, especially given that things like access to good sanitation, sheltering in place, and self-quarantine of sick individuals are critical to preventing further spread of the disease.

That leaves only the question of whether the bill is a reasonable and appropriate way to achieve the goal. In that regard, this bill shares a number of characteristics with state laws that have previously been upheld by the courts, despite a finding that they interfered with contracts. (*See, e.g., Home Building and Loan Assn. v. Blaisdell* (1934) 290 U.S. 398.)The bill is responsive to an emergency situation and temporary in nature: all the usual landlord-tenant laws snap back into place by April 1, 2022 at the latest. The bill also provides a mechanism for landlords to recover interest and all amounts owed to them under the lease in the end.

ii. Regulatory takings

As discussed under the constitutional analysis of the forbearance component in Comment 2, the standard for determining whether a regulatory taking has occurred is a fact specific inquiry. However, courts will generally look at the economic impact of the regulation on the claimant, the extent to which the regulation has interfered with distinct investment-backed expectations, and the character of the governmental action. (*Penn Central Transportation Co. v. City of New York* (1978) 438 U.S. 104, 124.) If the government action seems like the equivalent of a physical invasion of property, then a taking will be found more readily than if the impact on the person alleging a taking simply results from some public program adjusting the benefits and burdens of economic life to promote the common good. (*Ibid.*)

It is unlikely that a court would conclude that this bill's rent deferral and eviction protections are the functional equivalent of a physical taking. The bill is far more aptly described as a public program that adjusts the benefits and burdens of economic life in order to help avoid widespread evictions during a pandemic. While requiring landlords to wait out the present public health and economic emergency, the bill does not ultimately prevent them from seeking all amounts to which they were entitled under the contract. There may be tenants who escape paying these amounts because they are judgment proof or because the landlord opts not to pursue the debt in court, but these are considerations inherent in any contractual situation, not the creation of this bill.

c. Points for further evaluation

A recurring point of criticism among opponents of the bill's rent deferral and eviction protection component is that the method for establishing who is a financially distressed tenant is, to them, inadequate. Opponents raise the specter of a well-to-do tenant using the guise of solidarity with "rent strikers" to take advantage of the bill's provisions. As it appears in print, the bill only requires a tenant to sign and return an attestation affirming that the tenant is unable to pay the rent or other financial obligations under the lease because of the COVID-19 pandemic. Critics of the bill point out that the attestation is not even sworn under penalty of perjury. They assert that many tenants who actually can pay the rent will simply lie, sign the attestation, and thereby get out of paying rent.

There are several policy reasons that support why the bill currently only requires an attestation. First, the process is modeled after the way that the CARES Act treats homeowners and landlords with mortgages on properties with one-to-four units. As discussed earlier in this analysis, the CARES Act not only allows borrowers to obtain mortgage forbearance merely by affirming that they have a financial hardship due to COVID-19, it actually prohibits mortgage servicers from asking the borrowers for anything further. Demanding something different from tenants would open up the bill to legitimate criticism that it subjects tenants to barriers from relief that it does not erect for homeowners and small landlords.

Second, while requiring tenants to submit evidence to document their claim of hardship might prevent some unscrupulous people from deferring rent when they do not truly need to, such a requirement also raises serious risks that many people who legitimately need the help will be unable to access it. In ordinary times, some of California's most vulnerable residents might have a difficult time documenting their financial situation. An undocumented worker paid under the table in cash will not be able to produce evidence of a reduction in pay, for instance, and is unlikely to be able to obtain a letter verifying previous employment. Under COVID-19 conditions, these kinds of practical barriers to gathering evidence and documentation are even more problematic and widespread. Many businesses have closed their doors, temporarily or for good. How is a tenant supposed to obtain documentation of a loss in wages from an employer that no longer exists? Many other businesses are still operating but are doing so remotely. To obtain documentation from such an employer, a tenant would have to have access to the internet, which is not universal. Ready access to a printer or scanner would also facilitate gathering and submitting documentation, but few people have such equipment at home. For this reason, should the Committee decide to recommend the insertion of a hardship documentation requirement into the bill, or should the author elect to do so of his own accord, any such documentation requirement should include an option to self-certify the hardship. The California Apartment Association has submitted a proposal along these lines for consideration. Before immediately pushing for adoption of this proposal, however, Committee members and the author may wish to think through the costs and benefits carefully. Once self-certification is permitted as one way of documenting the hardship, the door is opened back up for unscrupulous tenants to lie, begging the question of whether anything is gained by imposing a burdensome hardship documentation regime that, for the reasons explained next, is likely to produce disputes and an increase in litigation.

Third, a requirement that tenants provide documentation of their financial hardship to their landlord would add layers of burden and paperwork to the process and is likely to lead to frequent disputes over whether or not documents produced by the tenant are sufficient. It is not hard to imagine a landlord, understandably anxious to obtain rent if at all possible, questioning the authenticity of a tenant's documents or wanting to see still further evidence. Tenants, in turn, might just as understandably object to what could quickly escalate into an invasive fishing expedition through their personal finances. Absent the creation of some kind of bureaucracy to oversee it, there is no neutral third party to resolve such disputes except for the courts. Almost inevitably, the frequency of these disputes will result in an increased burden on the judicial system at a time when it will already be facing tremendous demands. In contrast to all of this, submission of the attestation is a straightforward matter: either the tenant signed and returned the attestation or they did not.

Finally, the bill contains provisions that should dissuade rational people from trying to take advantage of the system. The bill does not excuse rent payments; it only defers them during what will – hopefully – be the worst of the pandemic. A tenant who does not get caught up voluntarily by April 1, 2022, faces not only the prospect of a lawsuit for the unpaid amount, but a bundle of interest, late payment penalties, court costs, and attorney's fees on top. This should act both as an up-front deterrent against tenants who are tempted to try to game the system and as a punishment on the back end for those who eventually succumb to that temptation. To help reinforce this point, the bill provides for tenants to receive a message of warning from the State of California when they are at the point of signing an attestation. The message reminds them that, even if they sign the attestation, they will still owe the landlord the rent and that if they take too long to do so, they may wind up having to pay interest, penalties, attorney fees and other costs in addition.

In light of the forgoing policy considerations, leaving the attestation requirement as is may represent the cleanest and simplest policy approach.

5. <u>Arguments in support of the bill</u>

According to the author:

> Before COVID-19, many California tenants struggled to pay rent, over half of renters were considered rent-burdened, paying over 30 percent of their income on rent. During the COVID-19 emergency,

> this number has only gotten worse, as the state's unemployment rate has skyrocketed. Similarly, the state's high cost of housing leaves many homeowners vulnerable to falling behind on their mortgage payments and losing their home to foreclosure. US Census Bureau data from July 9-14th indicate that over 4.3 million of California's renters report "little or no confidence" in their ability to pay next month's rent while 1.7 million California homeowners indicated "little or no confidence" about making their next mortgage payment. A failure to act could lead to widespread displacement for millions of Californians. AB 1436 provides renters and homeowners a chance to get back on their feet without the fear of losing their home, while also giving landlords and mortgage lenders a path to be made whole without having to resort to immediate evictions or foreclosures.

The sponsors of the bill write:

> Allowing […] families to be pushed out of their homes negatively impacts all of us. Without protections for renters and homeowners, the long-term effects will extend far beyond today's crisis, including widespread and deepening debt, difficulty securing replacement housing, and an increase in homelessness. […] AB 1436 allows California to transition out of the COVID-19 emergency in a way that balances the interests of renters, landlords, homeowners, banks and the state. It maintains community stability and provides a path towards equitable economic recovery.

In support of the bill, a coalition of public health organizations rights writes:

> Now, as millions of us shelter in place, the reality is inescapable: very little matters as much as a safe, stable home. And we are all connected in this. A failure to keep our families and neighbors in stable housing during this time is a failure to protect all of us from a rapidly spreading virus. Loss of housing disrupts a family's ability to "shelter in place" and practice "social distancing," which increases the likelihood of disease transmission. […] COVID is particularly dire for Black and brown renter families, many of whom face higher infection rates, job losses and reduced hours on top of existing economic precarity, and who may not be eligible for federal benefits due to immigration status. Failure to protect renters will cement racial inequities in health and wealth, setting California back a generation in our work to overcome the inequitable policy choices we made in the past.

6. Arguments in opposition to the bill

In opposition to the bill, a coalition of business organizations led by the California Chamber of Commerce writes:

> The COVID-19 pandemic and the actions taken to address the public health crisis have wreaked havoc to California's economy. Shutting down non-essential businesses and forcing residents to shelter-in-place have bankrupted Californians and businesses across the state. While we appreciate the serious health concerns that led to these actions, the California Legislature cannot rely upon the private sector to serve as both the state's tax base and economic safety net for COVID-19. AB 1436 effectively attempts to do just that by forcing rental property owners to forgo rent and serve as the safety net for millions of Californians. Further, the attempt to shift the economic fallout from the rental property owner onto national banks is fundamentally flawed and federally preempted. Only the state has the power and resources to function as a safety net to guarantee the health and welfare of its citizens.

In further opposition to the bill, a coalition of financial industry trade groups led by the California Bankers' Association, writes:

> While we appreciate the intent of the bill, we believe that it undermines the positive impacts of existing efforts and protections and may ultimately delay the speed in extending important relief to impacted borrowers. While our organizations wish to be collaborative, constructive and solutions-oriented, the measure that was recently amended a few weeks prior to the Legislature's adjournment includes provisions that are highly problematic. […]
>
> Generally, this measure: 1) struggles from a broad scope that may distract from efforts to focus on those truly in need of financial assistance; 2) fails to acknowledge that mortgage servicers are intermediaries that must adhere to contractual obligations and investor guidelines; 3) raises legal and constitutional issues, such as takings and impairment of contracts; 4) introduces the potential for preemption for federally chartered institutions; 5) imposes punitive penalties; and, 6) upends a national approach deployed through the CARES Act and federal agencies.

SUPPORT

Sponsors: California Rural Legal Assistance Foundation; Housing Now! California; Leadership Counsel for Justice and Accountability; PolicyLink; Public Advocates; Public Counsel; Western Center on Law and Poverty
Support: 99Rootz; Abundant Housing LA; ACLU of California; Active San Gabriel Valley; Affordable Housing Network of Santa Clara County; Affordable Housing Services; AIDS Healthcare Foundation; Alameda County Democratic Party; Alameda Renters Coalition; All Home; Alliance for Community Transit – Los Angeles; Alliance of Californians for Community Empowerment; Alliance San Diego; American Friends Service Committee - Los Angeles; American Federation State, County, and Municipal Employees, Local 3299; Anti-Eviction Mapping Project; Asian, Inc.; Asian Pacific Environmental Network; Rusty Bailey, Mayor, City of Riverside; Bay Area Legal Aid; Bay Area Regional Health Inequities Initiative; Bend the Arc: Jewish Action Southern California; Bend the Arc San Luis Obispo; Berkeley Rent Stabilization Board; Bet Tzedek Legal Services; Beverly-Vermont Community Land Trust; Board of Supervisors of the City and County of San Francisco; Bread Head California; London Breed, Mayor, City of San Francisco; Build Affordable Faster CA; Burbank Tenants' Rights Committee; California Community Land Trust Network; California Democratic Party Renters Council; California Environmental Justice Alliance; California Farmworker Foundation; California Federation of Teachers; California Federation of Labor; California Food Policy Advocates; California Healthy Nail Salon Collaborative; California Housing Consortium; California Latinas for Reproductive Justice; California League of Conservation Voters; California League of United Latin American Citizens; California Low Income Consumer Coalition; California Pan-Ethnic Health Network; California Partnership to End Domestic Violence; California Reinvestment Coalition; California School Employees Association; California Teachers Association; California Teamsters Public Affairs Council; California Work & Family Coalition; CA4Health; Catholic Charities Diocese of Stockton; Center for Community Action and Environmental Justice; Center on Race, Poverty & the Environment; Central California Asthma Collaborative; Central California Environmental Justice Alliance; Central Valley Air Quality Coalition; Central Valley Empowerment Alliance; Centro La Familia Advocacy Services, Inc.; Centro Legal de la Raza; ChangeLab Solutions; Chispa; City Heights CDC; City of Beverly Hills; City of West Hollywood; Clergy and Laity United for Economic Justice; ClimatePlan; Coalition for Economic Survival; Coalition for Humane Immigrant Rights; CommonSpirit Health; Community Action to Fight Asthma; Community Health Councils; Community Legal Aid SoCal; Community Legal Services in East Palo Alto; Community Power Collective; Congregations Organized for Prophetic Engagement; Consumer Advocates Against Reverse Mortgage Abuse; Consumer Reports; Contra Costa Senior Legal Services; Courage California; Cultiva La Salud; Democratic Party of the San Fernando Valley; Democratic Socialists of America, Los Angeles; Disability Rights California; Dolores Huerta Foundation; Downtown Women's Center; East Bay Community Law Center; East Bay Housing Organizations; East Yard Communities for Environmental Justice; Empowering Pacific Islander Communities; Ensuring

Opportunity Campaign to End Poverty in Contra Costa County; Environmental Justice Coalition for Water; Esperanza Community Housing Corporation; Every Neighborhood Partnership; Eviction Defense Collaborative; Eviction Defense Network; Faith in Action Bay Area; Faith in the Valley; Family Violence Appellate Project; Fideicomiso Comunitario Tierra Libre; First Unitarian Church of Los Angeles; Fresno Metro Black Chamber of Commerce; Fresno State Sierra Club, Tehipite Chapter; The Future Left; Eric Garcetti, Mayor, City of Los Angeles; Robert Garcia, Mayor, City of Long Beach; Greenfield Walking Group; The Greenlining Institute; Ground Game LA; Health Leads - Richmond, CA ; Hollywood NOW; Homeless Health Care Los Angeles; Housing Equality & Advocacy Resource Team; Housing Rights Center; Housing Rights Committee of San Francisco; Human Impact Partners; Inclusive Action for the City; Inland Equity Partnership; Inner City Law Center; Inquilinos Unidos; Investing in Place; The Jakara Movement; John Burton Advocates for Youth; The Kennedy Commission; Korean American Center; Koreatown Immigrant Workers Alliance; LA CAN; LA Forward; LA Más; LA Voice; Latino Coalition for a Healthy California; Latino Health Access; Latinos United for a New America; Law Foundation of Silicon Valley; Lawyers' Committee for Civil Rights of the San Francisco Bay Area; Los Angeles Homeless Services Authority; Los Angeles Tenants Union, Baldwin Leimert Crenshaw Local; Legal Aid Foundation of Los Angeles; Legal Aid of Marin; Legal Aid of Sonoma County; Legal Aid Society of San Mateo County; Sam Liccardo, Mayor, City of San Jose; Lift To Rise; LOOM; Los Angeles Alliance for a New Economy; March and Rally Los Angeles; Marin Environmental Housing Collaborative; Maternal and Child Health Access; Mental Health Advocacy Services; Mi Familia Vota; Monument Impact; Move LA; Multi-faith ACTION Coalition; National Association of Social Workers, California Chapter; National Center for Youth Law; National Housing Law Project; Natural Resources Defense Council; Neighborhood Legal Services of Los Angeles County; One Redwood City; Orange County Communities for Responsible Development; Organización en California de Líderes Campesinas, Inc.; Parable of the Sower Intentional Community Cooperative; Pasadena Tenant Union; Peace and Freedom Party of California, San Diego County Central Committee; People Acting in Community Together; People Organized for Westside Renewal; Physicians for Social Responsibility; PICO California; Politicians and Leaders of Tomorrow; Power California; Prevention Institute; Property Owners for Fair and Affordable Housing; Public Counsel; Public Health Alliance of Southern California; Public Health Justice Collective; Public Interest Law Project; Public Law Center; Miguel Pulido, Mayor, City of Santa Ana; Neighborhood Partnership Housing Services; Rancho La Paz Mobile Home Park HOA; Regional Asthma Management and Prevention; Rent and Mortgage Relief for All – San Luis Obispo; Rise Together Bay Area; Roman Catholic Diocese of Fresno; Root & Rebound; Sacred Heart Community Service; Sacred Heart Housing Action Committee; Safe Routes Partnership; SAJE; San Francisco Community Land Trust; San Francisco Renters Alliance; San Francisco Tenants Union; Libby Schaaf, Mayor, City of Oakland; Senior & Disability Action; Service Employee International Union California; Service Employees International Union, Local 1000; Showing Up for Racial Justice at Sacred Heart; Showing Up for Racial Justice, Bay Area; Sierra Business Council; Sierra Club

California; Silicon Valley De-Bug; Social Eco Education-LA; SOMOS Mayfair; South Pasadena Tenants Union; Darrell Steinberg, Mayor, City of Sacramento; Stonewall Democratic Club; Stories from the Frontline; Strategic Actions for a Just Economy; Strategic Concepts in Organizing and Policy Education; Sunflower Alliance Coordinating Committee; Teamsters Joint Council 7; TechEquity Collaborative; Tenants Together; Michael Tubbs, Mayor, City of Stockton; Unite Here! Local 19; United Auto Workers Local 230; United Auto Workers Local 2865; United Auto Workers Local 4123; United Auto Workers Local 5810; United Auto Workers Western States CAP and PAC; United Food and Commercial Workers – Western States Council; United Way of Greater Los Angeles; University Council – AFT; University of California Student Association; Urban Habitat; Valley Beth Shalom Homelessness Task Force ; Voices for Progress; Women Organizing Resources, Knowledge and Services; Working Partnerships USA; 131 individuals

OPPOSITION

Affordable Housing Management Association - Pacific Southwest; American Bankers Association; American Financial Services Association; Apple Valley Chamber of Commerce; Bay Area Homeowners Network; Beaumont Chamber of Commerce; Brea Chamber of Commerce; Building Owners and Managers Association of California; California Apartment Association; California Association of Collectors; California Association of Realtors; California Bankers Association; California Builders Alliance; California Building Industry Association; California Business Properties Association; California Chamber of Commerce; California Community Banking Network; California Council for Affordable Housing; California Credit Union League; California Downtown Association; California Escrow Association; California Financial Services Association; California Institute of Real Estate Management; California Land Title Association; California Manufactured Housing Institute; California Mortgage Association; California Mortgage Bankers Association; California Rental Housing Association; Carlsbad Chamber of Commerce; Chino Valley Chamber of Commerce; Civil Justice Association of California; Commercial Real Estate Development of California; Corona Chamber of Commerce; Downtown San Diego Partnership; Escrow Institute of California; Folsom Chamber of Commerce; Fontana Chamber of Commerce; Gilroy Chamber of Commerce; Greater Coachella Valley Chamber of Commerce; Greater Ontario Business Council; Hemet San Jacinto Chamber of Commerce; Hesperia Chamber of Commerce; Highland Chamber of Commerce; Highridge Costa; Inland Empire Economic Partnership; Lake Elsinore Valley Chamber of Commerce ; Long Beach Area Chamber of Commerce; Los Angeles Area Chamber of Commerce; Menifee Valley Chamber of Commerce; Moreno Valley Chamber of Commerce; Mortgage Bankers Association; Murrieta/Wildomar Chamber of Commerce; North Orange County Chamber of Commerce; Oceanside Chamber of Commerce; Oxnard Chamber of Commerce; Perris Valley Chamber of Commerce; Pleasanton Chamber of Commerce; Pomona Chamber of Commerce; Rancho Cordova Chamber of Commerce; Rancho Cucamonga Chamber of Commerce; Redlands Chamber of Commerce; San Gabriel Valley Economic

Partnership; Santa Rosa Metro Chamber; Securities Industry and Financial Markets Association; Silicon Valley Leadership Group; The Silicon Valley Organization; Southern California Rental Housing Association; Southwest California Legislative Council; Southwest Riverside County Association of Realtors; Temecula Valley Chamber of Commerce; Torrance Area Chamber of Commerce; United Trustees Association; Upland Chamber of Commerce; Victor Valley Chamber of Commerce; Western Manufactured Housing Communities Association; 42 individuals

RELATED LEGISLATION

Pending legislation:

SB 915 (Leyva, 2020) temporarily prohibits mobilehome parks from evicting residents who timely notify park management that they have been impacted, as defined, by COVID 19. The bill further mandates that mobilehome parks give COVID 19-impacted residents at least a year to comply with demands to repay outstanding rent, utilities or other charges, and up to a year to cure violations of park rules and regulations. The bill also prohibits parks from increasing rent or other charges during the period of repayment or cure. SB 915 is currently pending consideration on the Assembly Floor.

SB 1410 (Caballero, 2020) establishes a program under which landlords and tenants impacted economically by COVID-19 could enter into a specified agreement in lieu of rent payments. On the basis of this agreement, the landlord could apply to the Franchise Tax Board for tax credits equal in value to the rent not paid by the tenant. The tenant would be obligated to pay the amount of the unpaid rent to the Franchise Tax Board in yearly installments over ten years beginning in 2024, with specified discounts and forgiveness for low-income individuals.

AB 828 (Ting, 2020) establishes a moratorium on foreclosures for the duration of the COVID-19 state of emergency plus 90 days and prohibits evictions during a similar period except in cases addressing issues of damage to the property, nuisance, or health and safety. The bill also gives tenants who can document COVID-19 related financial hardship a one-year deferral on rent accrued during the state of emergency. AB 828 is currently pending consideration before the Senate Judiciary Committee.

Prior legislation:

SB 939 (Wiener, 2020) would have established, for specified commercial tenants, a temporary moratorium on evictions for the duration of the COVID-19 related state of emergency, and a yearlong period afterward in which to make up rental payments missed during that state of emergency. In addition, for specified businesses that have been especially impacted by the public health protocols resulting from the COVID-19 pandemic, including restaurants and bars, the bill would have created procedures for renegotiating or terminating existing leases that were based on pre-COVID-19 expectations. SB 939 died in the Senate Appropriations Committee.

AB 56 (Moore, Ch. 53, Stats. 1992) provided relief to tenants who were unable to respond to unlawful detainer actions because of court closures due to the Rodney King riots in Los Angeles.

PRIOR VOTES:

This bill was gutted and amended on June 10, 2020. All prior votes on the bill are therefore unrelated to the present content of the bill.

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