

Legislative Analysis



NONRECOURSE MORTGAGE LOANS

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House Bill 5446

Sponsor: Rep. Rudy Hobbs

Committee: Commerce

Complete to 3-12-12

A SUMMARY OF HOUSE BILL 5446 AS INTRODUCED 2-29-12

The bill would create a new act, "the Nonrecourse Mortgage Loan Act." It contains a lengthy Enacting Section describing its intent (quoted in italics later).

The bill provides a definition of "nonrecourse loan." The term would mean a commercial loan secured by a mortgage on real property located in Michigan and evidenced by loan documents that have certain specified characteristics. (The full definition is provided later in the summary.)

[Typically under a nonrecourse mortgage loan, "the lender must look to the collateral, rather than the borrower, as the ultimate source of repayment." (Quotation from Barron's Dictionary of Banking Terms.)]

The new act would specify that a post-closing solvency covenant could not be used as a nonrecourse carveout or as the basis for any claim or action against a borrower or any guarantor or other surety on a nonrecourse loan. A provision in the documents for a nonrecourse loan that did not comply would be invalid and unenforceable.

A "nonrecourse carveout" would refer to a specific exception to the nonrecourse provisions set forth in loan documents for a nonrecourse loan that has the effect of creating personal liability of the borrower or a guarantor or other surety of the loan for all or some amounts owed to the lender, if specified events occur

A "post-closing solvency covenant" would refer to any provision of the loan documents that relates to the solvency of the borrower, including, without limitation, a provision requiring that the borrower maintain adequate capital or have the ability to pay its debts with respect to any period of time after the date the loan is initially funded. (This would apply whether the provision was expressed as a covenant, representation, warranty, or default.) The term would not include a covenant not to file a voluntary bankruptcy or other voluntary insolvency proceeding or not to collude in an involuntary proceeding.

Enacting Section 1

The bill contains a lengthy Enacting Section 1, which states:

This act applies to the enforcement and interpretation of all nonrecourse loans in existence on, or entered into on or after, the effective date of this act. The Legislature recognizes that it is inherent in a nonrecourse loan that the lender takes the risk of a borrower's insolvency, inability to pay, or lack of adequate capital after the loan is made and that the

parties do not intend that the borrower is personally liable for the payment of a nonrecourse loan if the borrower is insolvent, unable to pay, or lacks adequate capital after the loan is made. The Legislature recognizes that the use of a post closing solvency covenant as a nonrecourse carveout, or an interpretation of any provision in a loan document that results in a determination that a post closing solvency covenant is a nonrecourse carveout, is inconsistent with this act and the nature of a nonrecourse loan; is an unfair and deceptive business practice and against public policy; and should not be enforced. It is the intent of the Legislature that this act applies to any claim made or action taken to enforce a post closing solvency covenant on or after the effective date of this act; to any claim made to enforce a post closing solvency covenant that is pending on the effective date of this act, unless a judgment or final order has been entered in that action and all rights to appeal that judgment or final order have been exhausted or have expired. (Emphasis added)

The bill also says that the act does not prohibit a loan secured by a mortgage on real property located in Michigan from being fully recourse to the borrower or guarantor, including as a result of a post-closing solvency covenant, if the loan documents for that loan do not contain nonrecourse loan provisions.

Definition of Nonrecourse Loan

The bill provides a definition of "nonrecourse loan." The term would mean a commercial loan secured by a mortgage on real property located in Michigan and evidenced by loan documents that meet any of the following:

- Provide that the lender will not enforce the liability or obligation of the borrower by an action or proceeding in which a money judgment is sought against the borrower.
- Provide that any judgment in any action or proceeding on the loan is enforceable against the borrower only to the extent of the borrower's interest in the mortgaged property and other collateral security given for the loan.
- Provide that the lender will not seek a deficiency judgment against the borrower.
- Provide that there is no recourse against the borrower personally for the loan.
- Include any combination of the paragraphs above or any other provisions to the effect that the loan is without personal liability to the borrower beyond the borrower's interest in the mortgage property and other collateral security given for the loan.

FISCAL IMPACT:

House Bill 5446, and the similar Senate Bill 992, would not have a significant fiscal impact on state or local budgets as the bills pertain to permissible provisions of private (contract) law.

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