

SENATE BILL REPORT

2SHB 1362

As Reported by Senate Committee On:
Financial Institutions, Housing & Insurance, March 16, 2011

Title: An act relating to protecting and assisting homeowners from unnecessary foreclosures.

Brief Description: Protecting and assisting homeowners from unnecessary foreclosures.

Sponsors: House Committee on Ways & Means (originally sponsored by Representatives Orwall, Hope, Rolfes, Moeller, Liias, Probst, Green, Darneille, Frockt, Kirby, Miloscia, Roberts, Hunt, Dickerson, Upthegrove, Fitzgibbon, Kagi, Eddy, Hasegawa, Pettigrew, Ormsby, Sells, Kenney, Cody, Hudgins, Lytton, Moscoso, Ryu, Appleton, Reykdal, Van De Wege, Carlyle, Dunshee, Santos, McCoy, Tharinger, Haigh, Goodman, Jinkins, Jacks, Takko, Sullivan, Blake, Seaquist, Billig, Stanford, Ladenburg, Finn and Pedersen).

Brief History: Passed House: 3/02/11, 83-13.

Committee Activity: Financial Institutions, Housing & Insurance: 3/16/11 [DPA].

SENATE COMMITTEE ON FINANCIAL INSTITUTIONS, HOUSING & INSURANCE

Majority Report: Do pass as amended.

Signed by Senators Hobbs, Chair; Prentice, Vice Chair; Benton, Ranking Minority Member; Fain, Keiser and Litzow.

Staff: Alison Mendiola (786-7483)

Background: Deeds of Trust. A deed of trust is a type of security interest in real property. A deed of trust is essentially a three-party mortgage. The borrower (grantor) grants a deed creating a lien on the real property to a third party (the trustee) who holds the deed in trust as security for an obligation due to the lender (the beneficiary).

The major difference between a deed of trust and a mortgage is that the deed of trust may be nonjudicially foreclosed, whereas a mortgage may only be foreclosed judicially. If the grantor defaults on the loan obligation, the trustee may foreclose on the real property as long as certain procedural and notice requirements are met.

The trustee of a deed of trust may be a domestic corporation, a title insurance company, an attorney, a professional corporation whose shareholders are licensed attorneys, an agency of

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the United States government, a bank, or a savings and loan association. A trustee must resign at the request of a beneficiary, and the beneficiary may designate a successor trustee.

In order for a deed of trust to be nonjudicially foreclosed, the following requirements must be met: (1) the deed contains a power of sale and provides that the real property is not used principally for agricultural purposes; (2) a default has occurred which makes the power of sale operative; (3) the deed has been recorded; (4) a notice of default is sent at least 30 days before a notice of sale is recorded; and (5) no other action is pending to seek satisfaction of an obligation secured by the deed of trust.

To initiate foreclosure procedures the trustee must (1) file a notice of trustee's sale 90 days before the sale; (2) send notice of the sale to the grantor, beneficiary, and any other person with a recorded interest in the land; (3) post the notice on the property or personally serve any occupants; and (4) publish the notice of sale in a newspaper at specified dates.

The sale may not take place less than 190 days from the date of default. Any person other than the trustee may bid on the sale.

The proceeds of the foreclosure sale are distributed first to the expenses of sale and the obligation secured by the deed of trust, and the surplus is deposited with the clerk of the court. Any interests or liens on the real property that are eliminated by the sale are attached to the surplus proceeds.

Notice of trustee's sale must be given to occupants of property consisting of a single-family residence, condominium, cooperative, and dwelling with less than five units; the notice must identify personal property that may be sold and any other action that is pending to foreclose on another security; the notice must specify the potential effects of foreclosure on the occupants of the property, and there are two eight-day time periods during which the trustee must publish the notice of sale in a legal newspaper.

The trustee has a duty of good faith to the beneficiary, grantor, and others with an interest in the property.

Certain claims, such as the trustee's failure materially to comply with the deed of trust law, are not waived by the borrower's failure to bring a lawsuit to prohibit a foreclosure sale of an owner-occupied one- to four-unit residence, but these claims must be asserted within two years of the foreclosure sale.

There must be proof that the beneficiary is the actual holder of the obligation secured by the deed of trust.

Meet and Confer Requirements. In 2009 ESB 5810 placed into law an additional step in the foreclosure process for deeds of trust made from January 1, 2003, to December 31, 2007, for owner-occupied, residential property. For such properties, a 30-day extension is made to the current timeline for foreclosure. Thirty days must pass before the notice of default can be filed. The 30 days are measured from the time the lender contacts the borrower, or satisfies due diligence requirements to contact the borrower, to work out a way to avoid foreclosure.

Obligations of the lender to the borrower are to advise the borrower of his or her right to request a subsequent meeting, to schedule that meeting to occur within 14 days, and to give the borrower a toll-free telephone number for contacting a HUD-certified housing counselor.

The notice of default must include a declaration from the lender that it contacted the borrower or used due diligence in attempting to do so. Actions by the lender to contact the borrower and the times at which these actions are to be taken are specified in detail.

Under certain circumstances the 30-day delay in filing the notice of default and the due diligence requirements need not be met. This meet and confer requirement expires on December 31, 2012.

Tenants. Tenants in non-owner-occupied one- to four-unit residences must be notified of the impending foreclosure sale; the potential consequences to them; and their option to contact a lawyer, legal aid, or a housing counselor about their rights. Tenants living in foreclosed property must be given written notice 60 days before they are removed from the property by an unlawful detainer action.

Mediation. Mediation, a form of alternative dispute resolution, is a way of resolving disputes between two or more parties. A third party, the mediator, assists the parties to negotiate their own settlement.

Summary of Bill (Recommended Amendments): Numerous changes are made to the deeds of trust foreclosure process.

Meet and Confer. The meet and confer process is amended to allow for an additional 60 days before the notice of default may be issued, if the borrower responds within 30 days of the initial contact. The beneficiary makes initial contact by sending a form letter, which must contain model language developed by the Department of Commerce (COM). The letter must contain statements urging the borrower to contact a housing counselor or attorney as soon as possible. If the borrower, or the borrower's housing counselor or attorney, requests a meeting with the beneficiary, the meeting must be in person unless waived by the borrower. However, a person authorized to make decisions for the beneficiary may participate by phone. The meet and confer requirement is made applicable to all deeds of trust and the expiration date is repealed.

Housing Counselors. A housing counselor who is contacted by a borrower has a duty to act in good faith to attempt to reach a resolution within the time frame of the meet and confer process. A resolution may include, but is not limited to a loan modification, an agreement to conduct a short sale, a deed in lieu of foreclosure, or some other plan. Housing counselors are not liable for civil damages resulting from acts or omissions in providing assistance to borrowers, unless the acts or omissions constitute gross negligence or willful or wanton misconduct.

Mediation. A foreclosure mediation program is established that applies only to borrowers of deeds of trust on owner-occupied residential property who have been referred to mediation by a housing counselor or attorney. The housing counselor or attorney may refer a borrower to mediation if mediation is appropriate based on the individual circumstances and a notice of

sale has not yet been recorded. A referral to mediation does not preclude a trustee from issuing a notice of default. The mediation provision does not apply to financial institutions that have fewer than 250 foreclosure sales in a calendar year.

A housing counselor or attorney referring a borrower to mediation must send a notice form to the COM. Within ten days of receiving the notice, the COM must select a mediator and notify the parties. The mediator must convene an in-person mediation session within 45 days after being selected, unless the parties agree in writing to extend the time. Provisions are established to address when the mediator must send the parties notice of the mediation session, what documents and information the parties must provide to the mediator, and what factors the parties must consider during mediation. The parties must mediate in person, but a decision-maker on behalf of the beneficiary may participate by phone.

Parties in mediation have a duty to act in good faith. A violation of the duty to act in good faith may include the failure to timely participate in mediation without good cause, the failure of either party to provide certain information to the other party, the failure of a party to pay its portion of the mediator's fees, and other conduct set forth.

Within seven days of the conclusion of the mediation, the mediator must certify to the COM the outcome of mediation and whether the parties acted in good faith. A certification that the beneficiary violated the duty to act in good faith constitutes a defense to the foreclosure, but not to any future foreclosure action. A certification that the borrower violated the duty to act in good faith authorizes the beneficiary to proceed with the foreclosure.

If an agreement was not reached and the mediator's certification shows that the net present value of a modified loan exceeds the anticipated net recovery, the showing constitutes a basis for the borrower to enjoin the foreclosure.

The mediator's fees must not exceed \$400 for a three-hour session and must be paid for equally by the borrower and beneficiary. The COM must maintain a list of approved foreclosure mediators and may establish a training program for mediators. The COM must make annual reports to the Legislature on the results of the mediation program.

Funding. Beginning October 1, 2011, and every quarter after, beneficiaries must (1) report to the COM the number of owner-occupied residential real properties for which the beneficiary has issued notices of default during the previous quarter; and (2) remit to the COM a lump-sum payment of \$250 per property. No later than 30 days after the effective date of this provision, the beneficiaries must remit to the COM a lump-sum payment of \$250 per owner-occupied residential real property for which the beneficiary has issued a notice of default during the three months prior to the effective date of this provision. This reporting and remitting requirement does not apply to financial institutions that have issued fewer than 250 notices of default in the preceding year.

The funds are to be deposited into the newly created Foreclosure Fairness Account, which is a non-appropriated account administered by the COM. The funds must be distributed as follows: no less than 80 percent to fund housing counselors; the greater of up to 6 percent, or \$655,000 per biennium, to the Consumer Protection Division of the Office of the Attorney General (AGO); up to 2 percent to the Office of Civil Legal Aid for purposes of contracting

with legal aid programs for representation of homeowners in matters relating to foreclosure; the greater of up to 9 percent, or \$451,000 per biennium, to the COM to implement the Foreclosure Fairness Act; and up to 3 percent to the Department of Financial Institutions to conduct homeowner outreach and education programs. The amount specified to fund housing counselors may be less than 80 percent if necessary to meet the level of funding specified for the AGO and the COM.

Consumer Protection Act. It is a Consumer Protection Act violation for any person or entity to (1) violate the duty of good faith in the mediation requirement; (2) fail to initiate contact with the borrower and exercise due diligence under the meet and confer requirement; and (3) fail to comply with the reporting and remitting requirements to COM.

Servicer's Duty. A servicer's duty to maximize net present value under a pooling and servicing agreement is a duty that is owed to all parties in a deed of trust pool, not to a particular party, and the servicer acts in the best interests of all parties if it agrees to a modification where default on the loan is reasonably imminent and anticipated recovery under a modification is more than the anticipated recovery through foreclosure.

Real Estate Excise Tax. If a deed in lieu for foreclosure transaction includes providing the transferor with a nominal sum of funds to assist the transferor with relocating, the transfer is not considered a sale for the purposes of the real estate excise tax.

EFFECT OF CHANGES MADE BY FINANCIAL INSTITUTIONS, HOUSING & INSURANCE COMMITTEE (Recommended Amendments): The department is to include additional information in its annual report regarding the mediation program. Community association beneficiaries are not subject to the mediation requirements or the \$250 Notice of Default fee under this act. Financial institutions who are not subject to the mediation requirements are to report their exemption to the department by January 31 (vs. January 10) annually. Housing counselors are to be approved by HUD or the Washington State Housing Finance Commission. It is clarified as to who is eligible to be a foreclosure mediator. Any loan servicer who is a federally insured depository institution that issues less than 250 notices of default in the preceding year are not subject to the \$250 Notice of Default fee. Technical changes are made.

Appropriation: None.

Fiscal Note: Available.

[OFM requested ten-year cost projection pursuant to I-960.]

Committee/Commission/Task Force Created: No.

Effective Date: This bill takes effect 90 days after adjournment of the session in which the bill is passed, except for section 11, relating to creating an account, section 12, relating to requiring beneficiaries to remit funds, and section 16, relating to requiring the Department of Commerce to create forms and authorizing rule-making, which contain an emergency clause and take effect immediately.

Staff Summary of Public Testimony on Recommended Amendments: PRO: Washington's foreclosure rate is rapidly increasing which is why this bill is so important. The bill is a result of the work of a diverse group of stakeholders who spent over 30 hours alone in drafting meetings. This bill provides an opportunity for a borrower to talk to their lender and try and workout an alternative to foreclosure when possible and provides increased access to housing counselors and mediation if necessary. This bill doesn't stop someone from going to court to assert any rights they may otherwise have, including questions about the title.

If this bill passes – it is no insignificant piece of legislation as Washington would become the third non-judicial state to offer foreclosure mediation. There is lots of fraud against homeowners (robo-signing, perjury of documents, securities fraud, homes sold with a clouded title) so while this bill is supported more should be done to stop these fraudulent practices and protect homeowners. This bill takes advantage of existing resources such as housing counselors and the Dispute Resolution Centers which will be helpful as the bill is implemented.

CON: Having processed over 600 applications for clients, 98 percent of homes that were reviewed in foreclosure, are in foreclosure due to fraud. The bill shouldn't die but it should be postponed, and we should hold people accountable for false documentation after closing.

Persons Testifying: PRO: Representative Orwall, prime sponsor; Denny Eliason, Washington Bankers Association; Bruce Neas, Columbia Legal Services; Holly Chisa, United Trustees Association; Karen Pooley, Nancy Gibson, citizens; Dan McConnon, Department of Commerce.

CON: Steve Neuenschwander, Mortgage Investigation Services.