

SENATE BILL REPORT

HB 2791

As Reported By Senate Committee On:
Consumer Protection & Housing, February 29, 2008

Title: An act relating to distressed property conveyances.

Brief Description: Concerning distressed property conveyances.

Sponsors: Representatives Lantz, Rodne and Kelley; by request of Attorney General.

Brief History: Passed House: 2/06/08, 96-0.

Committee Activity: Consumer Protection & Housing: 2/29/08 [DPA, w/oRec].

SENATE COMMITTEE ON CONSUMER PROTECTION & HOUSING

Majority Report: Do pass as amended.

Signed by Senators Weinstein, Chair; Kauffman, Vice Chair; Haugen, Jacobsen, Kilmer and Tom.

Minority Report: That it be referred without recommendation.

Signed by Senator Honeyford, Ranking Minority Member.

Staff: Vanessa Firnhaber-Baker (786-7471)

Background: The foreclosure process on residential property occurs when a homeowner defaults on his or her mortgage payments. The foreclosure process is determined by the type of financing the owner received, such as through a mortgage, deed of trust, or real estate contract. In Washington, deeds of trust are the most common, and they are generally foreclosed by a non-judicial sale (a sale outside the court).

If a lender forecloses on a home through a non-judicial proceeding, the lender must provide the homeowner with a notice of default, and then, at least 30 days later, provide the borrower with a Notice of Trustee's Sale and Notice of Foreclosure. Under a non-judicial foreclosure, a homeowner can avoid foreclosure by making the delinquent payments up to 11 days before the sale. The property cannot be sold until at least 190 days have passed since the homeowner fell behind in payments; and once the property is sold, the homeowner must move out within 20 days or the purchaser may file an eviction (unlawful detainer) without providing the original homeowner any additional notice.

Credit Services Organization Act. Washington has laws governing certain practices involving foreclosure of real property. The Credit Services Organization Act (CSOA) applies to any company that performs or claims it can perform certain services for a person, such as

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stopping, preventing, or delaying a foreclosure, in return for a fee or some other consideration. CSOA requires licensing and bonding of certain credit service organizations, requires a written contract with a right of cancellation, and makes a violation of the CSOA a Consumer Protection Act (CPA) violation.

Equity Skimming. Equity skimming practices are used to obtain title to properties for the purpose of either taking the equity out of the property or obtaining rents or payments on the property without satisfying any of the underlying obligations that may exist on the property. For example, a person induces a homeowner who is in financial distress to deed the property to the person with the assurance that the person will assume the underlying debt on the property. The person never assumes the debt, but instead rents or sells the property and diverts value from the property to his or her own personal use. The property is eventually foreclosed. In Washington, equity skimming is a class B felony and a violation of the CPA.

Consumer Protection Act. Under the CPA, the Attorney General may bring an action in the name of the state against any person to restrain and prevent an unlawful action. The court may order to restore to any person of interest, any personal or real property acquired by means of any act violating the CPA. The CPA also allows any person who is injured in his or her business or property by a CPA violation to bring a civil action to stop further violations and to recover actual damages, plus reasonable attorney's fees. In addition, the court may award the plaintiff treble damages (three times the actual damages sustained) not to exceed \$10,000.

Foreclosure Rescue Transactions. Homeowners who are late, or at risk of being late in their mortgage payments or have defaulted on their mortgage, may be approached with offers to assist them with their mortgage problems. Several types of assistance may be offered.

First, a person may offer to buy the homeowner's house and allow the homeowner to continue to live there as a tenant. The buyer may make representations before the sale that after a certain period of time, the homeowner will have paid enough rent to get his or her home back. This is commonly referred to as a sale-leaseback transaction.

Second, a homeowner may be approached with an offer of a foreclosure surplus sale. When a foreclosed house is auctioned off, the sale may bring more money than is due on the mortgage. That additional money is called surplus equity. In a foreclosure surplus sale, the homeowner assigns his or her right to the surplus equity to the buyer for a lump sum.

Third, other types of services may be offered to the homeowner. For instance, a person may offer to negotiate with the lender on the homeowner's behalf, or offer to arrange a sale of the home that includes an option for the homeowner to repurchase it in the future. In some circumstances, these transactions may result in the homeowner being misled or defrauded.

Summary of Bill: The bill as referred to committee was not considered.

SUMMARY OF BILL (Recommended Amendments): Regulations are imposed to govern distressed home transactions.

Distressed Home Transactions. A distressed home consultant (consultant) is a person who offers to provide mortgage, credit, or other debt assistance to an owner of a home that is in danger of foreclosure, or is in the process of being foreclosed.

In addition to any applicable disclosure or related requirements in the CSOA and the mortgage brokers practices act, a transaction between a consultant and homeowner is voidable by the homeowner at any time unless the following requirements are met.

First, distressed home consulting transactions must: (1) be in writing and in the language that the consultant used to describe his or her services; (2) fully disclose the exact nature of the services to be provided; (3) be dated and signed by the homeowner; and (4) contain the consultant's full contact information.

Second, the transaction contract required must also include a conspicuous notice warning the homeowner that the transaction could result in the loss of his or her home and advising the homeowner to consult with an attorney before entering into the contract.

Third, the consultant must provide the homeowner with a copy of the contract, and must also keep a copy of the contract on file for at least five years.

Consultants owe fiduciary duties to homeowners. These duties specifically include: acting in good faith and in the best interests of the homeowner, disclosure of all material facts to the homeowner, using reasonable care, and providing an accounting to the homeowner for all money received from the homeowner.

Licensed attorneys, financial institutions that a homeowner is a customer of, and nonprofit licensed credit counseling organizations are not distressed home consultants and are not subject to the above restrictions.

The provisions of the act may not be waived by the homeowner.

Distressed Home Conveyances. A distressed home conveyance is a transaction in which: (1) a foreclosed homeowner transfers an interest in the distressed home to a distressed home purchaser (DHP); (2) the DHP allows the foreclosed homeowner to occupy the home; and (3) the DHP or a person acting in participation with the DHP conveys, or promises to convey, the home to the foreclosed homeowner, or provides the foreclosed homeowner with an option to purchase the home at a later date, or promises the foreclosed homeowner an interest in, or portion of, the proceeds of any resale of the home. Terms of a distressed home conveyance include:

- a written contract is required with clearly disclosed terms completed that is signed and dated by the homeowner and purchaser prior to the home's transfer;
- the foreclosed homeowner has a right to cancel the terms of the contract within five business days;
- the purchaser must demonstrate that the foreclosed homeowner is able to meet the terms of the contract including making interest and lease payments and is capable of purchasing the home within the allowable period; and
- the homeowner must receive at least 82 percent of the difference between the home's fair market value and the underlying mortgage in the event of a sale to a third party.

A violation of the distressed home consulting and distressed home conveyance provisions are a per se violation of the Consumer Protection Act (CPA). In a private right of action under the CPA, the court may double or triple the damages award, subject to the statutory limit. However, if the court determines that the defendant acted in bad faith, the limit for doubling or tripling the damages award may be increased up to \$100,000. A claim for damages must be

filed within four years of the date of the alleged violation. The act neither limits nor supersedes any other remedy or legal theory otherwise available to a homeowner.

Unlawful Detainer Actions Involving Distressed Homes. In an unlawful detainer action involving a distressed home, the plaintiff (purchaser) must disclose to the court whether the defendant previously held title to the distressed home and explain how the purchaser came to acquire title.

A defendant who previously held title to the distressed home may not be required to escrow any money pending trial when a material question of fact exists as to whether the plaintiff (purchaser) acquired title from the defendant through a distressed home conveyance.

All other related actions are stayed pending the outcome of the unlawful detainer action.

Appropriation: None.

Fiscal Note: Available.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: The original bill was a simple and effective bill; however, it only regulated sale-leasebacks. This striker is even better and provides greater consumer protections. There is a lot of anxiety out there about subprime loans and foreclosures. This piece of legislation will really address these anxieties. The real problem that this bill addresses effectively is that people are being convinced to sell their homes for no money. There is no reason for a homeowner to do a sale leaseback unless it gives the homeowner a chance to get the person's house back. The addition of the unlawful detainer provision is great because if the judge in the eviction proceeding knows that the eviction is related to the sale-leaseback transaction, the person will be able to stay the action and consider equitable remedies.

CON: There are some honest investors and realtors out there who do sale-leasebacks and oppose this bill. The 82 percent figure is problematic because the value of a home is difficult to determine. It is also problematic because it means that it will never make sense to do a sale-leaseback.

Persons Testifying: PRO: Representative Pat Lantz, prime sponsor; Jim Sugarman, Attorney General's Office, Consumer Protection Division; Fred Corbit, Northwest Justice Project.

CON: Jack Burns, Estate Rescue Limited Liability Corporation.