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**Business & Financial Services Committee**

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**HB 1558**

**Brief Description:** Addressing the foreclosure crisis in Washington state through the creation of alternative mortgage financing based on shared appreciation.

**Sponsors:** Representatives Hudgins, Orwall, Fitzgibbon, Darneille and Moscoso.

**Brief Summary of Bill**

- Requires a beneficiary to inform the borrower of the option for a shared appreciation loan modification in certain circumstances.
- Makes the failure of a beneficiary to contact a borrower who requested a shared appreciation loan modification a defense to a foreclosure.
- Exempts shared appreciation loan modifications from the state real estate excise tax.

**Hearing Date:** 2/15/11

**Staff:** Jon Hedegard (786-7127).

**Background:**

Shared Appreciation.

The concept of shared appreciation mortgages is that the lender and borrower may agree that to lower the interest rate on a mortgage or reduce the amount that will be owed by the borrower in exchange for a percentage of the appreciation of the value of the property over time. For example, a lender might reduce the interest rate or might accept \$250,000 in a down payment and a mortgage on the purchase of a \$300,000 home in return for 50% of the appreciation in the home. If the home is sold 10 years later for \$400,000, the borrower and lender would split the \$100,000 of increased value. With an existing mortgage, the lender and borrower might agree to a shared appreciation loan modification to reduce the contracted interest rate or the amount that is currently owed on the mortgage.

State Regulation.

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

The Department of Financial Institutions (DFI) regulates a variety of persons and entities involved in mortgage lending, including consumer loan companies. While there is no definition for a shared appreciation mortgage in state law, the concept is discussed in statute in relation to reverse mortgages made by consumer loan companies. The DFI also adopted a rule requiring consumer loan companies to provide additional disclosures for shared appreciation mortgages or mortgages with a shared appreciation provision.

#### Federal Study.

The federal Dodd-Frank Wall Street Reform and Consumer Protection Act (House Resolution 4173) included a provision requiring the Secretary of Housing and Urban Development (HUD) to conduct a comprehensive study to determine prudent statutory and regulatory requirements that would provide for the widespread use of shared appreciation mortgages:

- to strengthen local housing markets;
- provide new opportunities for affordable homeownership; and
- enable homeowners at risk of foreclosure to refinance or modify their mortgages.

A report on the results of the study is due to Congress six months after the enactment of federal law. The report must include recommendations for regulatory and legislative requirements. The federal law was signed on July 21, 2010.

#### Foreclosure Process for Deeds of Trust.

Unlike a mortgage, which requires judicial foreclosure, a deed of trust may be nonjudicially foreclosed on if the borrower defaults on the loan obligation. The deeds of trust act establishes procedures for foreclosure and imposes certain requirements on beneficiaries and trustees. To foreclose on a deed of trust, the beneficiary or trustee must send a notice of default to the borrower. After 30 days from when the notice of default is sent, the trustee may record a notice of foreclosure sale. The notice of sale is recorded in the county auditor's office. The foreclosure sale may not occur until after 90 days from the time the notice of foreclosure sale is recorded, and may not occur until at least 190 days from the date of default. Within that time frame, the borrower may cure the default and discontinue the sale. The trustee's sale is automatically stayed if the borrower files for bankruptcy. The trustee also has authority to continue a sale for up to 120 days for any cause the trustee deems advantageous.

#### Real Estate Excise Tax.

The sale of real estate is subject to the state real estate excise tax (REET). The tax is measured by the full selling price, including the amount of any liens, mortgages, or other debts multiplied by the rate of 1.28 percent. State law also authorizes several local REETs. The REET also applies to transfers of controlling interests in entities that own property in the state. In order for the REET to apply to the sale of a controlling interest in an entity that owns real property, the following must have occurred: (1) the transfer or acquisition of the controlling interest occurred within a 12-month period; (2) the controlling interest was transferred in a single transaction or series of transactions by a single person or acquired by a single person or a group of persons acting in concert; (3) the entity has an interest in real property located in this state; (4) the transfer is not otherwise exempt from tax under state law; and (5) the transfer was made for valuable consideration. The REET is a legal obligation of the seller. Additionally, a statutory lien is placed on the property until the tax is paid. If REET is not properly paid, the Department of Revenue (DOR) may enforce the obligation in an action of debt against the seller, enforce the lien in the same manner as a mortgage foreclosure, or some combination of the two. A buyer

may also be liable for the REET unless the buyer notifies the DOR in writing within 30 days following the sale.

Federal taxation.

There are federal tax implications regarding the interest and the contingent appreciation provisions under a shared appreciation mortgage or a shared appreciation loan modification.

**Summary of Bill:**

A beneficiary and homeowner may renegotiate a home loan to reflect the market value of the home in exchange for the beneficiary receiving up to 50 percent of the future appreciation of the home. The future appreciation of the home is determined by the actual sale price of the home. The amount of appreciation to be shared is the amount of the actual sale price that exceeds the modified loan, minus the borrower's original down payment and closing costs paid by the borrower when the borrower purchased the home. The beneficiary may not add any fees or charges.

At least 30 days before the recording of a notice of a nonjudicial foreclosure sale, a beneficiary must inform the borrower of the option for a shared appreciation loan modification if:

- the debt under the borrower's current deed of trust is greater than the property's market value as estimated by a certified appraiser; and
- the deed of trust is secured by the residential real property.

If the borrower does not request a shared appreciation loan modification within 30 days of being notified of option, the beneficiary may record the notice of sale and proceed with the foreclosure.

If the borrower requests a shared appreciation loan modification, the beneficiary must contact the borrower within 30 days of the request and review with the borrower the decision whether or not to enter into a shared appreciation loan modification.

Failure of the beneficiary to contact the borrower if the borrower requests a shared appreciation loan modification is a defense to any foreclosure.

Real Estate Excise Tax.

For the purpose of the REET, a shared appreciation loan modification is not a sale or transfer when the borrower on the shared appreciation loan modification is the same borrower on the previous loan being modified.

**Appropriation:** None.

**Fiscal Note:** Requested on 2/11/11.

**Effective Date:** The bill takes effect 90 days after adjournment of the session in which the bill is passed.