

HOUSE BILL REPORT

HB 2057

As Reported by House Committee On:
Judiciary

Title: An act relating to the services and processes available when residential real property is abandoned or in foreclosure.

Brief Description: Concerning services and processes available when residential real property is abandoned or in foreclosure.

Sponsors: Representative Orwall.

Brief History:

Committee Activity:

Judiciary: 2/14/17, 2/16/17 [DPS].

Brief Summary of Substitute Bill

- Puts in place a multi-level process by which a servicer may enter abandoned residential real property to make repairs or remediate problems.
- Authorizes the Housing Finance Commission (HFC) to issue certificates of abandonment for a fee, and requires the HFC to notify the appropriate city, town, or county.
- Makes changes to the method and amount of beneficiary remittances into the Foreclosure Fairness Account.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 10 members: Representatives Jinkins, Chair; Kilduff, Vice Chair; Muri, Assistant Ranking Minority Member; Frame, Goodman, Graves, Hansen, Kirby, Klippert and Orwall.

Minority Report: Do not pass. Signed by 3 members: Representatives Rodne, Ranking Minority Member; Haler and Shea.

Staff: Cece Clynch (786-7195).

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.

Background:

Foreclosure Fairness Program and Account.

Most loan obligations for residential real property in Washington are secured by deeds of trust. In 2011 the Foreclosure Fairness Act was enacted, making changes to the process related to the nonjudicial foreclosure of deeds of trust. As part of those changes, the Foreclosure Fairness Program (Program) was established.

A variety of agencies are involved with the Program. Their roles and responsibilities, and the services they provide, are set forth below:

- The Department of Commerce (Department) is charged with the overall development and management of the Program. The Department is also responsible for training, approving, and maintaining a list of approved foreclosure mediators and assigning them to mediation cases. The Director of the Department authorizes expenditures from the Foreclosure Fairness Account (the Account).
- The Housing Finance Commission administers the homeowner counseling program and oversees a toll-free hotline where homeowners in need of foreclosure prevention assistance can call and receive free foreclosure prevention counseling.
- The Office of the Attorney General Consumer Protection Division investigates consumer protection complaints and enforces deed of trust foreclosure laws.
- The Office of Civil Legal Aid contracts with qualified legal aid programs to provide free legal assistance to low-income and moderate-income homeowners in matters related to foreclosure.

Certain beneficiaries must remit \$250 to the Department for every notice of trustee's sale recorded on residential real property, excluding the recording of an amended notice of trustee's sale. For purposes of this section:

- "Residential real property" includes residential real property with up to four dwelling units, whether or not the property or any part thereof is owner-occupied.
- The remittance requirement does not apply to: any beneficiary or loan servicer that is a federally insured depository institution and that certifies under penalty of perjury that fewer than 50 notices of trustee's sale were recorded on its behalf in the preceding year; or, any homeowners' or condominium association beneficiaries.

Monies in the Account pay for the Program, including mediation, counseling, consumer protection, and legal representation.

Jordan v. Nationstar.

In 2016 a majority of the Washington Supreme Court held in *Jordan v. Nationstar* that under Washington's lien theory of mortgages and statutory provisions a borrower and a lender cannot, prior to default, enter into a contractual agreement that allows the lender to enter, maintain, and secure the property prior to foreclosure. The majority recognized that, absent post-default consent, a lender may use a statutory receivership to gain access to the property prior to foreclosure, and that this is not the exclusive avenue, but it did not indicate what particular other remedies might be available. The dissent, on the other hand, would have held that a lender may, pursuant to a pre-default agreement, enter, maintain, and secure seemingly abandoned property before foreclosure.

Summary of Substitute Bill:

Foreclosure Fairness Program and Account.

For each notice of trustee's sale (NOTS) on noncommercial loans on residential real property, a beneficiary must remit \$300 to the county auditor at the time of recording. The auditor may retain 3 percent for purposes of operations and maintenance and must remit the remaining funds to the Department of Commerce (Department) for deposit into the Foreclosure Fairness Account. Beneficiaries or loan servicers that are federally insured depository institutions that record fewer than 50 NOTS in a year must make the remittance at the time of recording, but may subsequently request a refund from the Department on either a quarterly or an annual basis.

Every NOTS must include a cover sheet on which it is clearly indicated the name of the beneficiary and whether the loan is commercial or noncommercial. The auditor is required to index the NOTS by beneficiary.

Multi-Level Process for Entry or Maintenance.

The Housing Finance Commission (HFN) is authorized to issue a Certificate of Abandonment (Certificate) for a fee, not to exceed \$100. The HFC is required to notify the appropriate city, town, or county upon issuance. These certificates are part of the following multi-level process, pursuant to which a servicer may enter abandoned residential real property to make repairs or remediate problems:

1. With the borrower's written permission, a servicer may enter the premises and inspect, secure, repair, or maintain the premises in accordance with the scope of the permission granted.
2. Absent permission but after default and a reasonable inspection that provides reasonable cause to believe property is abandoned, a servicer may enter premises and perform reasonable external maintenance such as maintaining landscaping, collecting and disposing of trash, painting over graffiti, and removing hazardous property. Such work can only be done after providing the requisite three-day notice that includes information about the borrower's right to possession, a 24-hour phone number to call with questions or concerns, the phone number of a housing counseling agency, and information about the Foreclosure Fairness Act. "Reasonable cause to believe the property is abandoned", for this level, means that the property bears some or all of the following indicia:
 - a. overgrown or dead vegetation;
 - b. an accumulation of newspapers, circulars, fliers, or mail;
 - c. past due utility notices, or some or all of the utilities have been disconnected;
 - d. an accumulation of trash, junk, or debris;
 - e. a lack of evidence of occupancy, such as cars, toys, pets, or activity.
3. Absent permission but after default, issuance of a Certificate, provision of appropriate notice, and expiration of a 30-day waiting period, a servicer may enter a dwelling to take reasonable steps to secure the property. To be considered abandoned for purposes of issuance of a Certificate, the property must be open and unprotected and in reasonable danger of significant damage resulting from exposure to the elements or vandalism *or* the local police, fire department, or code enforcement has requested that

- the borrower, owner, or any other interested party secure the property because it has been declared an imminent danger *and* at least three of the following must be met:
- a. the absence of furnishings and personal items consistent with residential habitation;
 - b. the gas, electric, and water utility services have been disconnected;
 - c. statements by neighbors, passersby, delivery agents, or government employees that the property is vacant;
 - d. multiple windows on the property are boarded up or closed off or are smashed through;
 - e. doors are smashed through, broken off, or continuously unlocked;
 - f. the property has been stripped of copper or other materials, or interior fixtures have been removed;
 - g. law enforcement have received at least one report of trespassing or vandalism or other illegal activities within the immediately preceding six months;
 - h. the property has been declared unfit for occupancy or ordered to remain vacant.
4. Finally, if the requirements of the third level have been met and there is a threat of imminent danger of harm, a servicer need not wait 30 days but may enter immediately and, simultaneous with entry, post the required notice. "Imminent danger of harm" means:
- a. active flooding, including damage to the roof such that water is entering the structure;
 - b. extreme weather conditions exist and immediate and extensive property damage is likely; or
 - c. notification by the police, fire department, or code enforcement that there is immediate danger to health, safety, and welfare of the public.

Certificates are not required for the first or second levels, but the HFC must be informed so that it may notify the appropriate city, town, or county.

Servicers and Agents.

The authority of an agent, such as a property preservation entity, to enter abandoned property and to perform any sort of work derives solely from the servicer's authority. A servicer has a duty to supervise and monitor its agents and to make sure that its agents possess the appropriate permit, license, certificate, or registration, and are properly bonded and insured if so required. The servicer must also require that the agent implement stringent background check requirements for all of its employees.

Substitute Bill Compared to Original Bill:

The contents of the original bill are removed and replaced with all of the elements described above.

Appropriation: None.

Fiscal Note: Available.

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

Staff Summary of Public Testimony:

(In support) Over the years, the stakeholder group has spent countless hours negotiating the Foreclosure Fairness Act (FFA). The funding formula for the FFA services was changed last year. It is not bringing in the amount of money that was anticipated. Some of this is due to a decrease in foreclosures, as well as the manner of collection, and this issue must be dealt with this year. In addition, there is a new partnership between local communities, banks, and homeowners to deal with the problem of abandoned properties. There will be ongoing work on these issues and this bill.

The lead attorney in the *Jordan* case has six years of experience and insight on the issue that was at the heart of *Jordan*. There were numerous forcible entries based on uniform contractual provisions in deeds of trust. In *Jordan*, the court said this violated a Washington statute that has been on the books since territorial days that grants exclusive right of possession to the borrower until foreclosure is complete. This bill provides a framework for preforeclosure entry when a house is truly abandoned and truly suffering waste. It contains important definitions. It also assists municipalities that truly suffer when homes are abandoned. Support is still contingent on not changing protections found in the bill. In addition, the bill needs some additions, such as express requirements regarding the licensing of businesses that actually enter the homes. Typically, loans are securitized and held in trust. Servicers administer the loans and handle the default process, too. Servicers, in turn, contract with property preservation companies. National property preservation companies contract with regionals, and then the regionals contract with a local contractor. These are not necessarily licensed contractors, but people found on Craigslist. There have been entries into homes that are not abandoned, and removal of personal property. This is why it is important that there be a licensing component. Also, there needs to be more direct language that servicers cannot disavow their agency relationship as they have been known to do. Do not include a retroactivity provision. It is unclear that such a provision would even be constitutional.

The bankers want to support this. It is very important for the industry. Inclusion of a retroactivity provision should also be considered. Consideration should be given to clarifying that servicers should not be sued for what has gone before and measures that were taken that were in accord with requirements imposed by Fannie Mae and Freddie Mac and were pursuant to contracts that they had with homeowners. The bankers do not represent government-sponsored entities such as Fannie Mae and Freddie Mac, but banking representatives have spoken to them about this issue because it has the potential to impact them. Retroactivity is not a request made for those who acted in bad faith, but for the others who did not. Also, a provision should be included with respect to successors in interest. There is a need for certainty when the borrower is deceased. The bankers will continue to negotiate in good faith.

A bipartisan group of legislators created the FFA. It isn't perfect, but it is considered a model in the nation. Two important fixes need to be made. First, *Jordan* has led to uncertainty. Second, funding changes are needed so as to ensure counseling and mediation services.

Jordan invalidated a key provision that has been included in deeds of trust for decades. As a result, banks cannot maintain abandoned properties and cannot preserve the value of the property. The bill will protect homeowners and will regulate property preservation companies. It will allow servicers and agents access to maintain the properties, and it will create a duty to maintain properties, both in foreclosure and post-foreclosure. This effort is complicated, but there is confidence that it will get done. A further change is needed to the funding to make sure that those who should pay are paying. Financial institutions have agreed to raise the fee and pay up front. The smallest will be able to apply for a refund for fees paid upfront. This will allow full funding of the program and tracking.

Cities such as Tacoma, SeaTac, and Spokane Valley have seen increased numbers of vacant and abandoned homes. Cities support the bill. The sponsor's leadership on the issue, and the inclusion of cities as partners in this effort is appreciated. When neighbors notice crime and graffiti, they contact their local city and the city looks into it. Under current law, cities have limited options. Cities try to contact the owner, but who that is can be unclear. One element of the bill increases communication with the locals. This allows the city to know the status of the property. Cities do have nuisance abatement authority, but ideally they would like the lenders and owners to do the work and not impose this cost on taxpayers. There should be a provision added that requires financial institutions to continue to maintain homes that are in mid-foreclosure as well as post-foreclosure. It is recommended that the Oregon model be examined. Cities like Bremerton must keep neighborhoods healthy and fight blight and want to see this move forward.

Much work has been done over the last few years to protect homeowners and make sure there is a fair process. The impetus to work on the issue of abandoned properties comes from an economic justice perspective. Homes that are abandoned and crime-ridden become a problem for the municipalities and the neighbors. For this reason, there is interest in seeing a narrow exception to the longstanding law that says the homeowner has possession until foreclosure is complete. But, homeowner rights must be protected. There are numerous stories of what clients have faced at the hands of property preservationists who have taken property and replaced locks on doors. Many times in these situations the homeowners think that they cannot come back, and they leave long before they have to. In this state, they have the right to occupy until 20 days after the foreclosure is complete. Columbia Legal Services' support is limited to fixing the funding and providing for prescribed, limited entry into abandoned property.

Although there have been about 12,000 recorded notice of trustee's sales (NOTS), only about 7,000 NOTS' worth of funds have been paid into the account. It is recognized that it is a big, bold request to require that the fee be paid upfront at the time of recording, but it is necessary. The funding problem may be due to exemptions. Some of those on the list that the Department of Commerce kept were not entitled to exemptions. After pushing on this issue, those not entitled to be on the list were removed from the list. This new method will work better.

An attorney in private practice representing a wide range of clients, not just lower income clients, has seen that these issues affect people of all different income levels. Property preservationists have a perverse incentive to break into a house because, if a house is not abandoned, and they don't break in, they don't get paid. There have been instances when: a

condo unit was broken into for the purported purpose to winterize, but this condo unit was inside a condo building, and such action, therefore, makes no sense; and a new lock box was put on a home where there was a real estate sales sign up. Retroactivity is a no-go and would be unconstitutional. Homeowners will never agree to it. Homeowners and their representatives want to stop blight but a lot of responsibility falls on banks who are letting properties become blighted.

The trustees support this and hope that all can be resolved. Trustees are third parties in the process. There are other updates that should be included in addition to the *Jordan* fix. One issue is around a beneficiary declaration and when it is provided. Perhaps, this will be provided at the notice of default stage. Another issue being looked at concerns trustees being able to get out of a dispute by saying they have no financial interest. The last component is funding. Trustees float fees during the foreclosure process and don't get paid until the end. This can be a very long wait. Trustees have been asked what they think about paying this fee on NOTS at the time of recording, and they should be responding in the near future.

(Opposed) None.

(Other) Representative Orwall deserves thanks for working on this. The City of Spokane is concerned with over 500 abandoned homes. This weekend there was a fire in a home that had been in foreclosure for two years. A squatter set the house on fire. This bill needs more work. The major item for Spokane is that the city already has in place a registry and fees with respect to abandoned homes and wants to make sure the city can continue to do what it is doing, or that the legislation does at least as good a job. The *Jordan* fix is important to community banks. A standard part of these contracts allows the lender to maintain the property. As to the funding issue, the actions that precipitated the foreclosure crisis were not the actions of community banks. Community banks are not comfortable yet with the way this is structured for payment, but are willing to continue to work on this going forward.

Persons Testifying: (In support) Representative Orwall, prime sponsor; Clay Gatens; Jessica Fortescue, Washington Mortgage Bankers Association; Briahna Murray, Cities of Tacoma, Spokane Valley, and SeaTac; Denny Eliason, Washington Bankers Association; Lili Sotelo, Columbia Legal Services; Melissa Huelsman, Law Offices of Melissa A. Huelsman PS; Holly Chisa, United Trustees Association; and Dino Davis, City of Bremerton.

(Other) Brad Tower, Community Bankers of Washington; and Nick Federici, City of Spokane.

Persons Signed In To Testify But Not Testifying: None.