

HOUSE BILL REPORT

2ESHB 2057

As Passed Legislature

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

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

Sponsors: House Committee on Judiciary (originally sponsored by Representative Orwall).

Brief History:

Committee Activity:

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

Floor Activity:

Passed House: 3/6/17, 98-0.

Passed House: 1/18/18, 96-0.

Senate Amended.

Passed Senate: 3/1/18, 49-0.

House Concurred.

Passed House: 3/3/18, 96-0.

Passed Legislature.

Brief Summary of Second Engrossed Substitute Bill

- Increases the amount of the required beneficiary remittance from \$250 to \$325 into the Foreclosure Fairness Account for every recorded notice of trustee's sale on a noncommercial loan on residential real property.
- Makes several changes with respect to nonjudicial foreclosures, including changes pertaining to: access to preserve property from waste or nuisance; beneficiary declarations; notices of default; and deceased borrowers and successors in interest.
- Requires pre-foreclosure notice in the case of residential reverse mortgages.
- Provides a process that may be utilized when residential real property is determined by a local government to be abandoned, in mid-foreclosure, and a nuisance.

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.

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).

Background:

Mortgages and deeds of trust are two forms of security interests in real property used for real estate financing. A mortgage is a pledge of real property as security for a debt owed to the lender (mortgagee). A mortgage creates a lien on the real property. A deed of trust is basically 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). Most loan obligations for residential real property in Washington are secured by deeds of trust.

Judicial Foreclosure.

A mortgage may be foreclosed only through a judicial proceeding according to statutory requirements. Judicial foreclosure allows the mortgagee to obtain a deficiency judgment if the sale does not satisfy the mortgage obligation. In addition, the judicial foreclosure process allows for statutory redemption rights for the mortgage debtor and certain junior lien holders. Statutory redemption rights allow the mortgage debtor and other lien holders a certain period of time after the foreclosure sale to buy the land from the purchaser for the price paid at the sale.

Nonjudicial Foreclosure.

Deeds of trust may be foreclosed either through the judicial process or a nonjudicial trustee's sale process. The Deeds of Trust Act imposes detailed notice and process requirements for nonjudicial foreclosure. It is a requisite of nonjudicial foreclosure that no court action have been commenced by the beneficiary to seek satisfaction of an obligation secured by the deed of trust. (Seeking the appointment of a receiver is an express exception, and does not preclude nonjudicial foreclosure.) Nonjudicial foreclosure does not include the ability to obtain a deficiency judgment or statutory redemption rights.

Foreclosure Fairness Program and Account.

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.

Nuisance Abatement.

"Nuisance" is defined as unlawfully doing an act, or omitting to perform a duty that:

- annoys, injures, or endangers the comfort, repose, health, or safety of others;
- offends decency;
- unlawfully interferes with, obstructs, or renders dangerous for passage a lake, navigable river, bay, stream, canal, basin, public park, square, street, or highway; or
- in any way renders other persons insecure in life or in the use of property.

A public nuisance is a nuisance that affects equally the rights of an entire community or neighborhood. There are civil and criminal remedies and penalties for creating or allowing nuisances.

Counties, cities and towns may declare what is deemed a nuisance and abate the nuisance. Cities and towns that exercise authority to declare a nuisance, abate a nuisance, or impose fines or costs upon persons who create, continue, or maintain a nuisance are authorized to levy a special assessment on property where a nuisance is situated. The special assessment is for the purpose of reimbursing the city or town for the expense of abatement. The special assessment levied by the city or town is a lien, and after it is recorded in the county, up to \$2,000 of the recorded lien is of equal rank with state, county, and municipal taxes. Counties have the same authority granted to cities and towns, however, the amount of a county lien of equal rank with state, county, and municipal taxes is not capped.

Summary of Second Engrossed Substitute Bill:

Judicial Foreclosure.

A new section is added, requiring that before foreclosing any reverse residential mortgage the mortgagee must give written notice of such intention at least 33 days in advance. The notice must be sent:

- to the resident mortgagor; or,
- in case of the death of the last surviving mortgagor, to any known surviving spouse or to "unknown heirs" of the residential mortgagor.

The notice must be in English and Spanish, in a form to be published by the Department of Commerce, and must clearly and conspicuously set forth specified information. It is an unfair or deceptive practice in violation of the Consumer Protection Act, for any person to fail to comply with the requirements of this new section.

Nonjudicial Foreclosure.

Several amendments and additions are made to the Deeds of Trust Act, as follows:

- It is expressly provided that filing a civil case to obtain court approval to access, secure, maintain, and preserve property from waste or nuisance (similar to seeking the appointment of a receiver) does not constitute an action for determining whether the requisites for nonjudicial foreclosure are met.
- A trustee is required to have proof, in the form of a declaration, that the beneficiary is the holder, rather than the owner, of any promissory note secured by the deed of trust (DOT). This declaration must be transmitted to the borrower and the grantor.
- The Notice of Default must include on the top of the first page:
 - the current beneficiary;
 - the current mortgage servicer; and
 - the current trustee.
- Procedures are put in place with respect to deceased borrowers and successors in interest.
- A Notice of Trustee's Sale must include additional indexing requirements.
- A new section expressly governs cases in which a trustee is named as a defendant in an action or proceeding in which the DOT is the subject. A trustee is authorized to file a declaration of nonmonetary status if there are no substantive allegations that seek damages from the trustee or seek to enjoin the foreclosure based on any alleged unlawful actions or omissions by the trustee. Other parties to the action may file objections to the declaration. Timelines and procedures are specified.

References in the Foreclosure Fairness Act to the expired federal Home Affordable Modification Program are Stricken.

Foreclosure Fairness Program and Account.

For each notice of trustee's sale (NOTS) on noncommercial loans on residential real property, a beneficiary must remit \$325 to the Department for deposit into the Foreclosure Fairness Account. The Department is authorized to adjust the fee via rulemaking, however, the fee may not exceed \$325.

Additional Nuisance Abatement Process.

A new chapter is created, providing a process that may be utilized when residential real property is determined by a county, city, or town, to be abandoned, in mid-foreclosure, and a nuisance. This authority is expressly in addition to, and not in limitation of, any other authority provided by law.

The local government may commence the process on its own initiative, or a mortgage servicer may request that a local government visit a property and make a determination. For purposes of this chapter, property is:

- "Abandoned" when there are no signs of occupancy and at least three of 13 specified indications of abandonment are visible from the exterior.
- In "mid-foreclosure" when, pursuant to the Deeds of Trust Act, a notice of default or notice of pre-foreclosure options has been issued or a notice of trustee's sale has been recorded.
- A "nuisance" when so determined by a county, city, or town, pursuant to its authority under existing statutory law.

A county, city, or town may notify a mortgage servicer, via certified mail, that a property has been determined to be abandoned, in mid-foreclosure, and a nuisance. Such a notice must be accompanied by an affidavit or a declaration made under penalty of perjury by a local governmental official that a property is abandoned, in mid-foreclosure, and a nuisance. The affidavit or declaration must outline at least three indicators of abandonment and be supported with time and date stamped photographs, a finding that the property is a nuisance, and a copy of the notice of default, notice of pre-foreclosure options, or notice of trustee's sale.

Alternatively, a mortgage servicer may contact the local government regarding a property it believes to be abandoned, and a nuisance and request that such a determination be made. When making such a request, the mortgage servicer must furnish a copy of a notice of default, notice of pre-foreclosure options, or notice of trustee's sale applicable to the property. The local government must respond to the request within 15 calendar days and notify the mortgage servicer:

- that a visit has been made to the property and a determination made that the property is not abandoned or not a nuisance;
- that a visit has been made, as well as a determination that the property is abandoned, in mid-foreclosure, and a nuisance. In this case, the notice shall be accompanied by an affidavit or a declaration that meets the requisites set forth above; or
- that the local government does not have adequate resources or is otherwise unable to make the requested determination.

Upon receipt of such an affidavit or declaration, a mortgage servicer or its designee may enter the property for the purposes of abating the identified nuisance, preserving property, or preventing waste and may take certain steps, such as replacing missing windows and performing pest control services, to secure the property. The mortgage servicer or designee must; make a record of entry by means of dated and time-stamped photographs; not remove personal items unless the items are hazardous or perishable; ensure that the required statutory notice is posted on the front door; and keep records of entry for at least four years. If, upon entry, the property is found to be occupied, the mortgage servicer or designee must leave the property immediately and notify the local government. Thereafter, entry is not permitted regardless of whether the property constitutes a nuisance or complies with local code enforcement standards. Similarly, if the borrower notifies the mortgage servicer that the property is not abandoned, the mortgage servicer must notify the local government and not enter the property.

Except in instances when the mortgage servicer has found the property occupied or received notice from the borrower that the property is not abandoned, if a mortgage servicer receives notice from a county, city, or town that a property is abandoned, in mid-foreclosure, and a nuisance, or a grantee of a trustee's deed or a sheriff's deed receives notice from the local governmental entity that a property is a nuisance, and fails to abate the nuisance within the time prescribed, the county, city, or town may exercise its authority to abate the nuisance and recover associated costs by levying an assessment on the property to reimburse the local government for the costs of abatement, excluding any associated fines or penalties. This assessment constitutes a lien against the property and is of equal rank with state, county, and municipal taxes.

A local government is not liable for any damages caused by any act or omission of the mortgage servicer or its designee.

Appropriation: None.

Fiscal Note: Available.

Effective Date: 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.