

HOUSE BILL REPORT

ESHB 2614

As Amended by the Senate

Title: An act relating to residual debts following short sales of owner-occupied residential property secured by deeds of trust.

Brief Description: Limiting deficiency judgments pertaining to residual debts following short sales of owner-occupied residential property secured by deeds of trust.

Sponsors: House Committee on Judiciary (originally sponsored by Representatives Kenney, Ryu, Hasegawa and Santos).

Brief History:

Committee Activity:

Judiciary: 1/26/12, 1/30/12 [DPS].

Floor Activity:

Passed House: 2/13/12, 69-29.

Senate Amended.

Passed Senate: 2/29/12, 48-1.

House Refused to Concur.

Senate Amended.

Passed Senate: 3/5/12, 47-1.

Brief Summary of Engrossed Substitute Bill

- Prohibits a beneficiary from obtaining a deficiency judgment, under certain circumstances, when there has been a short sale of residential real property secured by a deed of trust.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 12 members: Representatives Pedersen, Chair; Goodman, Vice Chair; Rodne, Ranking Minority Member; Shea, Assistant Ranking Minority Member; Eddy, Hansen, Kirby, Klippert, Nealey, Orwall, Rivers and Roberts.

Staff: Trudes Tango (786-7384).

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:

In Washington, most loan obligations for residential real property are secured by deeds of trust. Under the Deeds of Trust Act, a beneficiary may use the non-judicial foreclosure process when a borrower defaults on the loan obligation. When there is a non-judicial foreclosure sale of residential real property under the Deeds of Trust Act, the beneficiary may not obtain a deficiency judgment.

A "short sale" is a real estate transaction in which the proceeds of the sale are insufficient to pay the debts encumbering the property and the borrower is unable to pay the difference. Selling the property in a short sale can be one option for the borrower to avoid foreclosure. Generally, a beneficiary with a security interest in the property must consent to receiving less than the beneficiary is owed in return for releasing its lien on the property. Depending on the terms of the agreement between the borrower and the beneficiary, the borrower may or may not be liable for the remaining amounts owed that are not covered by the sale.

Summary of Engrossed Substitute Bill:

A beneficiary may not obtain a deficiency judgment on the obligations secured by a deed of trust against a borrower in any case when, as a consequence of or in conjunction with a sale of owner-occupied residential real property resulting in proceeds that were insufficient to pay the obligation in full, the beneficiary reports to the Internal Revenue Service that the beneficiary has canceled all or a portion of the borrower's debt. This provision does not apply: (1) to a deed of trust securing a commercial loan; (2) to an obligation secured by owner-occupied residential real property when the funds were used to finance a commercial venture; or (3) when the property sold was not occupied by the borrower as the borrower's principal residence at the time of the sale.

EFFECT OF SENATE AMENDMENT(S):

1. Regarding short sales, the Senate amendment is the same as the previously adopted Senate amendment, which requires notice to the seller stating whether a beneficiary intends to waive or reserve its right to collect full payment of the debt. If the beneficiary does not initiate a court action to collect the outstanding debt within three years of the date it released its security interest, the right to collect is forfeited. Real estate licensees must also notify a seller that a short sale does not relieve the seller of the obligation to pay other costs, such as the real estate licensee's commission.
2. Regarding the Foreclosure Fairness Act, the Senate amendment incorporates all the provisions of Substitute House Bill 2421, which provides:
 - The meet and confer process may be by telephone and applies to borrowers who have filed for bankruptcy.
 - A borrower may be referred to mediation after a notice of default has been issued but no later than 20 days after a notice of sale has been recorded.
 - The foreclosure mediation process is amended to, among other things, provide more time for scheduling a mediation, specify how and when documents and information must be provided by beneficiaries and borrowers, specify when

- the mediator's fee must be paid, and provide immunity to all foreclosure mediators.
 - The time period between the trustee sale and the notice of sale for owner occupied residential real property is expanded from 90 days to 120 days for certain borrowers.
 - The quarterly reporting by beneficiaries must include updated contact information and reports are due within 45 days of the end of each quarter.
 - The allocation of funds from the beneficiaries' quarterly remittance is changed for housing counselors and the Department of Commerce. This section has an emergency clause.
3. Regarding the rescission of foreclosure sales, the Senate amendment incorporates all the provisions of SSB 6515, which provides:
- Up to 11 days following a trustee's sale, the trustee, beneficiary, or authorized agent for the beneficiary may declare the sale and trustee's deed void if: (a) the trustee, beneficiary, or authorized agent asserts that there was an error with the foreclosure sale process including, but not limited to, an erroneous opening bid; (b) the beneficiary and borrower, prior to the sale, agreed to a loan modification or loss mitigation plan to postpone or discontinue the sale; or (c) the beneficiary or authorized agent accepted funds that fully reinstated or satisfied the loan. The trustee must refund the bid amount to the purchaser. The trustee must send a notice of rescission to parties no later than 15 days following the sale. If the rescission is based on an error in the sale process or on the borrower and beneficiary previously agreeing to a loan modification or to postpone the sale, the trustee may set a new sale date within a certain time and must comply with certain notice requirements.
 - A domestic limited liability corporation may be a trustee.
4. The Senate amended the title to "An Act relating to assisting homeowners in crisis by providing alternatives, remedies, and assistance."

Appropriation: None.

Fiscal Note: Not requested.

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) Homeowners think they have extinguished their debt after a short sale, but they find out that the lender intends to collect the rest of the debt. The lender generates the Internal Revenue Service (IRS) form, then "double collects" by getting the benefit of the loss in its accounting but collecting the rest of the debt.

(With concerns) This is a good concept, but the specific language needs to be changed to provide more certainty and clarity for homeowners. The bill must be clarified so that it only applies to single family owner occupied residential real property and not to sales when the

home was used as collateral for a commercial loan. The bill should allow lenders to review the circumstances in its totality and allow lenders to say no to a short sale.

(Opposed) The second part of the bill regarding the lender consenting to the short sale is most problematic. If the bill is enacted as written, lenders will veto these sales because they will lose all ability to pursue a deficiency judgment. Community banks fund small business activities which are often funded with home equity lines of credit. The decision to release collateral for the short sale is separate from the decision to relieve the debt. The bank's ability to collect on a debt extends far beyond the single transaction. The notion of "double dipping" is not accurate. The bank would have to issue a revised IRS form and show it as income if the bank is still pursuing the debt. Short sales are complicated transactions. All parties who have a lien must agree to the sale and this type of legislation will make the process more complicated.

Persons Testifying: (In support) Representative Kenney, prime sponsor.

(With concerns) Bob Mitchell, Washington Association of Realtors; Stacy Augustine, Northwest Credit Union Association; and Denny Eliason, Washington Bankers Association.

(Opposed) Brad Tower, Community Bankers of Washington.

Persons Signed In To Testify But Not Testifying: None.