

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Judiciary Committee

BILL: CS/CS/SB 992

INTRODUCER: Judiciary Committee, Banking and Insurance Committee, Senator Fasano, and others

SUBJECT: Foreclosure Fraud

DATE: April 10, 2008

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Johnson	Deffenbaugh	BI	Fav/CS
2.	Sumner	Maclure	JU	Fav/CS
3.			GA	
4.				
5.				
6.				

Please see Section VIII. for Additional Information:

- | | | |
|------------------------------|-------------------------------------|---|
| A. COMMITTEE SUBSTITUTE..... | <input checked="" type="checkbox"/> | Statement of Substantial Changes |
| B. AMENDMENTS..... | <input type="checkbox"/> | Technical amendments were recommended |
| | <input type="checkbox"/> | Amendments were recommended |
| | <input type="checkbox"/> | Significant amendments were recommended |

I. Summary:

With the increasing number of foreclosures in Florida and nationwide, a significant number of schemes have appeared that are allegedly designed to rescue or save a homeowner from foreclosure. Unscrupulous businesses have targeted and defrauded homeowners of the equity in their homes. Often the specific details of these arrangements are not explained or adequately disclosed to the homeowner.

The bill provides additional protections to such homeowners facing foreclosure. The bill defines and addresses transactions involving foreclosure-rescue consultants and equity purchasers -- two of the main players involved in foreclosure-rescue schemes.

Foreclosure-Rescue Consultants

The bill:

- Defines the term, “foreclosure-rescue consultant” as a person who directly or indirectly makes a solicitation, representation, or offer to a homeowner to provide or perform, in return

for payment of money or other valuable consideration, foreclosure related rescue services. The bill provides exceptions.

- Requires a foreclosure-rescue consultant to have a signed agreement before initiating or engaging in any services. Certain disclosures are required to be in the agreement. A homeowner is allowed one business day to review the agreement before signing, and a homeowner must receive a copy of the signed agreement within three hours of signing the agreement.
- Prohibits a foreclosure rescue-consultant from soliciting, charging, or receiving fees for such services until all services contained in the agreement have been completely performed.
- Allows the homeowner the right to cancel an agreement within three business days of signing without penalty. This right may not be waived by either party. In the event of cancellation, any payments made to a consultant are returned to the homeowner within 10 business days of cancellation notice.

Equity Purchasers

The bill:

- Defines the term “equity purchaser,” as any person who acquires title to any residential real property as a result of a foreclosure-rescue transaction.
- Requires a foreclosure-rescue transaction written agreement to contain certain disclosures. The agreement must state the specifications of any option or right to repurchase the property in foreclosure.
- Requires at the time the written agreement is signed, the purchaser must give a homeowner a notice of the homeowner’s right to cancel the transaction. A homeowner may cancel a transaction within three business days without penalty. This right to cancel may not be waived or limited by either party.
- Requires that, in the event of cancellation, any payments made by an equity purchaser to the homeowner or by the homeowner to the equity purchaser must be returned at cancellation.
- Provides that the homeowner has a 30-day right to cure any default of the contract with the purchaser, and this right may be exercised on at least three separate occasions during the life of the agreement.
- Requires that, if the homeowner has the right to repurchase the property, the purchaser must verify and demonstrate that the homeowner has a reasonable ability to make the repurchase payment. A rebuttable presumption arises that the homeowner has a reasonable ability to make the payments if the monthly payments and interest payments on other personal debt do not exceed 60 percent of the homeowner’s monthly gross income.
- Provides that price the homeowner pays may not be unconscionable. A rebuttable presumption arises that the transaction was unconscionable if the repurchase price is greater than 17 percent per annum more than the total amount paid by the equity purchaser to acquire, improve, and maintain the property.
- Provides that any foreclosure-rescue transaction involving a lease option or other repurchase agreement creates a rebuttable presumption that the transaction is a loan

- transaction and the conveyance from the homeowner to the equity purchaser is a mortgage under s. 697.01, F.S.
- Provides that a violation of any provision of this act is an unfair and deceptive trade practice. Violators are subject to the penalties and remedies provided in part II of ch. 501, F.S., including a monetary penalty not to exceed \$15,000 per violation.

This bill creates section 501.1377, Florida Statutes, and repeals section 501.2078, Florida Statutes.

II. Present Situation:

Background

Prime loans are typically made to creditworthy borrowers, while subprime loans are generally made to borrowers with impaired or limited credit. Foreclosure can begin after a borrower defaults on the mortgage loan. Default is generally defined as being 90 days delinquent, although some lenders may use another definition. Once in default, a lender must determine whether a workout solution is viable, or whether to proceed with foreclosure.

The average foreclosure rate for all subprime loans during 2006-2007 was 4.35 percent nationwide, while the average prime loan foreclosure rate was 0.48 percent.¹ Borrowers with financial or cash flow problems are likely to find it difficult to avoid foreclosure when they cannot quickly sell their homes for prices that would cover most or all of their mortgage. Due to the high costs associated with a foreclosure proceeding, lenders may want to try a loss-mitigation or workout solution with defaulted borrowers. The cost of foreclosure for a lender was estimated at \$58,759 per loan.²

The National Delinquency Survey, issued by the Mortgage Bankers Association, provides two measures of foreclosures: (1) foreclosure starts, which are loans that entered the foreclosure process during the quarter and (2) foreclosure inventory, which represents the aggregate number of loans that were in the foreclosure process during the quarter (regardless of when they entered the process).³ A review of the fourth quarter data, as of December 31, 2007, indicated the following:

- The delinquency rate (past due rate) for mortgage loans nationwide (on one-to-unit residential properties) was 6.31 percent of all outstanding loans. In Florida, 7.47 percent of the loans were delinquent.
- In Florida, 3.22 percent of loans were in foreclosure. The national average was 2.04 percent. Florida ranks fourth, behind Michigan, Ohio, and Indiana.
- The percent of Florida loans that started the foreclosure process during the period was 1.46 percent. In contrast, the national average was 0.88 percent.

¹ Congressional Research Service, *Understanding Mortgage Foreclosure: Recent Events, the Process, and Costs*, November 7, 2007.

² Amy Crews Cutts and Richard K. Green, *Innovative Servicing Technology: Smart Enough to Keep People in Their House?* Freddie Mac Working Paper #04-03 (July 2004).

³ Mortgage Bankers Association, National Delinquency Survey, Fourth Quarter 2007, Data as of December 31, 2007.

- The rate of foreclosure starts in Florida more than tripled between the fourth quarter of 2006 and the fourth quarter of 2007.

With the increasing number of foreclosures in Florida and nationwide, schemes have appeared that are allegedly designed to rescue or save a homeowner from foreclosure. According to the National Consumer Law Center, a significant number of these scams involve fraud.⁴ Generally, homeowners who are seriously delinquent on the payment of mortgage payments are targeted by foreclosure consultants. These consultants find distressed homeowners through public foreclosure notices via government offices or commercial websites. The scheme is usually initiated by a telephone call from the consultant to the homeowner in which a resolution is offered. Absent the homeowner submitting documentation for the consultant to conduct a complete financial analysis, the homeowner is “qualified” over the phone for services, provided a fee is paid first. Moreover, during the telephone call, the fee is collected via debit or credit card, or check. Generally, the contractual terms and conditions are not discussed in detail. However, the written contract the homeowner ultimately receives from the consultant may contain numerous limitations to the services and to the homeowner’s refund and cancellation rights. In actuality, the foreclosure consultant may perform little or no services on behalf of the homeowner.⁵

In exchange for the fee, the consultant, for example, makes inquiries to the lender regarding a plan for repayment that the lender will accept. Often, these negotiations are done by the consultant without knowledge of the homeowner’s financial condition or ability to meet any repayment plan. The resulting repayment plan represents the consultant fulfilling his service obligations. Consequently, the homeowner could be further burdened with a predatory or unrealistic repayment plan. The consultant has collected his fee, with no contractual obligation to return any portion of it, despite the homeowner’s inability to comply with the new repayment plan.⁶

Sometimes, the homeowner will deed the property over to an unscrupulous equity purchaser and rent or lease the property back in anticipation the homeowner will be able to repurchase the residence in a few years. However, the provisions of these buyback agreements may not be financially viable for the homeowner. A lease/buy back is a foreclosure rescue scam in which the homeowner (usually unknowingly) deeds the house to the rescuer and leases it back with an option to repurchase, normally after a year. The rescuer pays arrearages (usually nothing more) in exchange for the deed. The buyback price is normally at fair market value, which usually nets the rescuer many times his initial or only investment. However, the homeowner may not be able to afford the rent, which exceeds the initial mortgage payment, and is evicted, forfeiting the right to repurchase. The rescuer then simply sells the house and keeps the equity.⁷

According to the Attorney General’s staff, presently there are approximately 20 active investigations, and litigation is under way involving foreclosure-rescue consultants and equity

⁴ National Consumer Law Center, *Dreams Foreclosed: The Rampant Theft of American’s Homes Through Equity-Stripping Foreclosure Rescue Scams*, June 2005, <http://www.consumerlaw.org/>.

⁵ *Id.*

⁶ *Id.*

⁷ *Id.*

purchasers. In recent months, the Office of the Attorney General has initiated actions related to foreclosure rescues under part II of ch. 501, the Florida Deceptive and Unfair Trade Practices Act (FDUTPA). This act provides a civil penalty of up to \$10,000 for each violation under s. 501.2075, F.S. Section 501.211, F.S., authorizes any person who has suffered a loss under this act to bring an action to recover actual damages, plus attorney's fees and court costs. In addition, the Office of the Attorney General has prosecuted these types of fraudulent schemes under chs. 812 (theft, robbery, and related crimes), 817 (fraudulent practices), and 895 (offenses concerning racketeering and illegal debts), F.S.

Section 501.2078, F.S., which is also in part II of ch. 501, F.S., addresses violations involving homeowners during residential foreclosure proceedings. According to the Attorney General's office, this law is not generally used for prosecuting foreclosure fraud due to its limited scope.

Currently, there are 12 states that have enacted laws that regulate foreclosure consultants. They are: California, Colorado, Georgia, Illinois, Indiana, Maryland, Minnesota, Missouri, Nevada, New Hampshire, New York, and Rhode Island.⁸

Judicial Sales Procedure

Under current law, a lienholder or creditor must serve a complaint, a notice of *lis pendens*,⁹ and a summons on the debtor in order to initiate foreclosure proceedings. The procedure for the sale of real or personal property, otherwise known as a judicial sale, is provided for in s. 45.031, F.S. This section provides that a final judgment from a foreclosure proceeding must include a statement notifying the property owner and subordinate lienholders, if any, that there may be additional money from the foreclosure sale and notifying the property owner that he or she may claim such additional funds without representation by a lawyer or other person, if the subject property qualified for a homestead exemption in the most recent tax year.¹⁰ The sale must be conducted at public auction at the time and place set forth in the final judgment.¹¹

Expedited Show-Cause Foreclosure Procedure

Section 702.10, F.S., provides a fast track foreclosure process through an order to show cause, whereby a lender can obtain an *in rem* judgment. Upon filing a foreclosure complaint, the mortgagee can request an order to show cause for the entry of a final judgment. The judge must then read the complaint and verify that it states a cause of action.¹² If the complaint is verified, the judge will issue an order to the defendant to show cause why a final judgment should not be entered.¹³ If a defendant waives the right to be heard, the judge shall promptly enter a final

⁸ National Conference of State Legislatures, *State Foreclosure Solutions*, January 2008, <http://ncsl.org/>.

⁹ The definition of "lis pendens," as appropriate for this analysis, is "[a] notice, recorded in the chain of title to real property, required or permitted in some jurisdictions to warn all persons that certain property is the subject matter of litigation, and that any interests acquired during the pendency of the suit are subject to its outcome." BLACK'S LAW DICTIONARY (8th ed. 2004). Essentially, "[t]he purpose of a notice of lis pendens is to alert creditors, prospective purchasers and others to the fact that the title to a particular piece of property is involved in litigation." 35 FLA. JUR. 2D *Lis Pendens* § 3 (2008).

¹⁰ Section 45.031(1)(a) and (b), F.S.

¹¹ Section 45.031(3), F.S.

¹² Section 702.10(1), F.S.

¹³ *Id.*

judgment of foreclosure.¹⁴ Upon receipt of a final judgment, the procedures set out in s. 45.031, F.S., for a judicial sale should be followed.

III. Effect of Proposed Changes:

Foreclosure-Rescue Consultants

Definition

The term, “foreclosure-rescue consultant” is defined as a person who directly or indirectly makes a solicitation, representation, or offer to a homeowner to provide or perform, in return for payment of money or other valuable consideration, foreclosure-related rescue services.

Exemptions

The following persons are exempted from the definition of “foreclosure-rescue consultant”:

- a person exempted under the Florida Deceptive and Unfair Trade Practices Act (FDUTPA) (s. 501.212, F.S.);
- a person acting under the express authority of the U.S. Department of Housing and Urban Development to provide foreclosure-related rescue services;
- a charitable, not-for-profit agency that offers consumer counseling;
- a person who holds or is owed an obligation secured by a lien any residential real property in foreclosure if the person performs the foreclosure-related rescue services in connection with the obligation or lien;
- a financial institution as defined in s. 655.005, F.S., and any parent or subsidiary of the financial institution or of the parent or subsidiary; and
- a licensed mortgage broker, mortgage lender, or correspondent mortgage lender that provides mortgage counseling or advice regarding residential real property in foreclosure.

Prohibitions

In the course of offering or providing foreclosure-related rescue services, a foreclosure-rescue consultant may not:

1. Engage in or initiate foreclosure-related rescue services prior to executing a written agreement for foreclosure-related rescue services; or
2. Solicit charge, receive, or attempt to collect or secure payment, directly or indirectly, for foreclosure-related rescue services before successfully completing or performing all services contained in the agreement for foreclosure-related rescue services.

¹⁴ Section 702.10(1)(d), F.S.

Notice

The bill requires several disclosures be incorporated into an agreement as a means to enhance consumer protections. The agreement must be printed in a minimum 12-point type, and the homeowner has at least one business day to review the agreement prior to signing. Among the many disclosures is a recommendation disclosure. A recommendation disclosure must direct the homeowner to contact the mortgage lender or servicer prior to signing the agreement, because an opportunity may exist to negotiate a payment plan free of charge through the lender.

The agreement must describe in detail the procedure for notifying the consultant of cancellation. The agreement must be signed by both parties, and the homeowner must receive a copy within three hours of signing the agreement. Additionally, the agreement must allow a homeowner at least three business days after the signing date to cancel without penalty. If an agreement is cancelled, any payments are to be returned within 10 days. Moreover, the right to cancel may not be waived by the homeowner or limited in any manner by the foreclosure-rescue consultant.

Equity Purchasers

Definition

The term “equity purchaser”, is defined as “any person who acquires a legal, equitable, or beneficial ownership interest in any residential real property as a result of a foreclosure-rescue transaction.”

Exemptions

The term “equity purchaser” does not apply to persons who acquire legal, equitable, or beneficial interest in property:

- By a certificate of title from a foreclosure sale;
- At a sale of property authorized by statute;
- By order or judgment of any court;
- From a spouse, parent, grandparent, child, grandchild, or sibling of the person or the person’s spouse; or
- As a deed in lieu of foreclosure, a workout agreement, a bankruptcy plan or any other agreement between a foreclosing lender and a homeowner.

The bill also includes additional definitions for the terms: foreclosure-rescue transaction, homeowner, residential real property, and residential real property in foreclosure.

Disclosure

The bill requires several disclosures to be included in the equity purchasers’ agreements. The bill requires at least a 12-point uppercase type written agreement signed by the homeowner and equity purchaser prior to executing any instrument quitclaiming, assigning, transferring, conveying, or encumbering an interest in the foreclosure property. The bill requires that among those disclosures there be an option or right to repurchase the property that list such things as the

total consideration to be paid by the equity purchaser, the terms of payment, any services that the equity purchaser must perform, and the date and time when possession of the property is to be transferred to the equity purchaser. Specific disclosures, pursuant to the federal Truth in Lending Act, must be in the agreement that describe all the material terms of the transaction.

Notice

An equity purchaser must give the homeowner, at the time the written agreement is signed, a notice stating that the homeowner may cancel the transaction without penalty within three business days. Any money paid by the purchaser or equity purchaser must be returned at cancellation.

Right to Repurchase

If the homeowner has the right to repurchase the property, the purchaser must verify and demonstrate that the homeowner has a reasonable ability to make the repurchase payment. A rebuttable presumption arises that the homeowner has a reasonable ability to make the payments if the monthly payments and interest payments on other personal debt do not exceed 60 percent of the homeowner's monthly gross income.

Unconscionability – Rebuttable Presumption

The bill provides that the price the homeowner pays may not be unconscionable. A rebuttable presumption arises that the transaction was unconscionable if the repurchase price is greater than 17 percent per annum more than the total amount paid by the equity purchaser to acquire, improve, and maintain the property.

Lease Option – Rebuttable Presumption

In addition, any foreclosure-rescue transaction involving a lease option or other repurchase agreement creates a rebuttable presumption that the transaction is a loan transaction and the conveyance from the homeowner to the equity purchaser is a mortgage under s. 697.01, F.S. This rebuttable presumption does not apply unless the lease option or other repurchase agreement, or a memorandum of the lease option or other repurchase agreement, is recorded in accordance with s. 695.01, F.S.

Violations

The bill establishes penalties for violating the act. A person who violates any provision of this act commits an unfair and deceptive trade practice as defined in part II of ch. 501, F.S. Violators are subject to the penalties and remedies provided in part II of ch. 501, F.S., including a monetary penalty not to exceed \$15,000 per violation. The Attorney General may bring an action on behalf of one or more consumers for actual damages (s. 501.207, F.S.). In any civil litigation resulting from a violation, the prevailing party may receive reasonable attorney's fees and costs from the non-prevailing party (s. 501.2105, F.S.).

Repeal of Section 501.2078, F.S.

The bill repeals s. 501.2078, F.S., which currently prohibits persons, subject to exemptions, from willfully using a method or practice that victimizes or attempts to victimize homeowners during the course of a residential-foreclosure proceeding and who knew or should have known that such conduct was unfair or deceptive.

Effective Date

The act takes effect October 1, 2008.

IV. Constitutional Issues:**A. Municipality/County Mandates Restrictions:**

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

The bill will provide additional rights and protections for consumers facing foreclosures and establishes civil penalties for persons engaging in foreclosure consultant and equity purchaser schemes.

C. Government Sector Impact:

The bill provides additional enforcement authority to prosecute persons engaged in fraudulent foreclosure rescues or equity purchaser's schemes and allows fines for up to \$15,000 per violation.

The amount of potential revenues the state will receive for penalties and remedies as provided in part II of ch. 501, F.S. is indeterminate at this time.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS/CS by Judiciary on April 8, 2008:

The committee substitute changes the time within which the foreclosure-rescue consultant must give the homeowner a copy of the signed “Foreclosure-Related Rescue Services” agreement and the “Foreclosure-Rescue Transaction” agreement from one business day to three hours after the homeowner signs the agreement.

CS by Banking and Insurance on March 18, 2008:

The committee substitute:

- Expands the definition of “equity purchaser” to include persons who acquire a legal, equitable, or beneficial ownership interest in any real estate property, as a result of a foreclosure through other means (i.e., trust purchases).
- Revises the exemptions for entities that are considered a “foreclosure-rescue consultant” by incorporating the exemptions under s. 501.212, eliminating attorneys, and expanding the exemption for financial institution to include a parent and a subsidiary of a financial institution.
- Clarifies the term “foreclosure-rescue transaction” to include a “lease option interest” as a form of conveyance.
- Considers unconscionable a repurchase price that is greater than 17 percent per annum more than the total amount paid by the purchaser to acquire, improve, maintain, and hold the property.
- Changes five-day right of cancellation to three days for homeowners who sign a contract for foreclosure rescue services. Provides in event of cancellation, any moneys paid by the purchaser to the homeowner or by the homeowner to the equity purchaser must be returned at that time.
- Requires that the lease option documents be recorded in accordance with s. 695.01, F.S., in order for the loan to be presumed valid.
- Provides an effective date of October 1, 2008, rather than July 1, 2008.

B. Amendments:

None.