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## New Foreclosure Law Finds Common Ground

Legislation changes way banks undertake foreclosure process.

By **Stephen K. Lightfoot II**



**C**alifornia has seen an unprecedented rise in the number of residential foreclosures. In 2007 for example, more than 84,000 California properties were lost in foreclosure, and more than 250,000 loans on California properties went into default, the first step in the foreclosure process.

To address this extraordinary threat to California and local economies, the state Legislature started working in early 2008 on Senate Bill 1137 that was signed into law on July 8, 2008 by Gov. Arnold Schwarzenegger as emergency legislation. The new law makes major changes to non-judicial residential foreclosures in California by: (1) establishing additional, detailed procedures for lenders to follow in the foreclosure process; (2) requiring a purchaser to maintain vacant residential property purchased through foreclosure or be subject to monetary penalties; and (3) giving a renter 60 days' notice instead of 30 days' notice to vacate the property that has been foreclosed. The new law applies only to loans made between Jan. 1, 2003 and Dec. 31, 2007 for owner-occupied residential properties. Further, all provisions of the new law sunset by Jan. 1, 2013, unless a later enacted statute extends or deletes that date.

Most lenders in California use mortgages and deeds of trust that contain a power of sale clause. The lender initiates the non-judicial foreclosure process by recording and serving a notice of default, after the borrower fails to meet his loan obligations. Prior to SB 1137, lenders were not obligated to notify borrowers of their intent to commence a foreclosure. Under the new law however, a lender may not record a notice of default until 30 days after the lender contacts the borrower or 30 days after satisfying specific due diligence requirements. Furthermore, a notice of default must now include a declaration from the lender or its agent that the lender has contacted the borrower, tried with due diligence to contact the borrower or the borrower has surrendered the property.

However, as with most laws, there are exceptions. Under this senate bill, the lender is not required to contact the borrower, delay recording the notice of default, include additional contact information in the notice of sale or even exercise due diligence if the borrower has achieved a

number of steps. Those steps include surrendering his property and confirming same in writing or delivering up the keys, contracting with an organization or person whose primary business is advising people on how to extend the foreclosure process and avoiding his loan obligations or if the borrower has filed for bankruptcy, and the proceedings have not been finalized. Another section of the new law requires lenders to offer loan modifications to defaulting borrowers, if the lender's recovery under the modification exceeds its recovery through foreclosure on a net present value basis.

If, however, the default is not cured, or a loan modification is not effected, the next step in the foreclosure process is for the lender to record and serve a notice of sale. The notice of sale can be recorded three months after the notice of default is recorded. It contains the auction details, including the sale amount and the date, time and place of the sale, and it must be posted and published in specific places at least 20 days before the sale date.

If a lender had already filed a notice of default prior to the enactment of the new law and did not subsequently file a notice of rescission, then the lender must include a declaration in the notice of sale that outlines two points. The points state that the borrower was contacted so that an assessment of his financial situation is conducted and options are explored for him to avoid foreclosure or a listing of various efforts made, if any, to contact the borrower in the event no contact was made.

The new law also imposes an additional requirement for notices of sale in cases where the borrower's billing address is different than the property address. The notice must be posted at the property and also mailed to the borrower with a specifically worded, additional notice that advises him that the foreclosure process has commenced and the property may be sold. This notice will advise the tenant that he is entitled to a 60-day termination notice, which must be printed in six languages: English, Spanish, Chinese, Tagalog, Vietnamese and Korean.

In addition, the new law requires that the owner of a vacant residential

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property purchased or acquired through foreclosure maintain the subject property. At a minimum, the owner must care for the exterior of the property, prevent excessive foliage growth that diminishes the value of surrounding properties, prevent trespassers or squatters from remaining on the property and prevent mosquito larvae from growing in standing water or other conditions that may create a public nuisance. If the owner fails to maintain the property, he faces a fine of up to \$1,000 per day. This follows a 30 days' written notice that gives the owner an opportunity to abate the condition of the property or even less notice if there are potential public health and safety consequences.

Under the new law, the notice period required to terminate a tenancy at a foreclosed property is increased from 30 days to 60 days (this extended notice period does not apply if a borrower remains in the property as a tenant, subtenant or occupant). However, the new law does not affect a local just cause eviction ordinance (e.g., San Francisco, Oakland, Berkeley). For example, if the foreclosed property is located in one of those cities, the new owner (including a lender) must have just cause (one of several specific reasons) to evict the tenant from the foreclosed property. This can create numerous hurdles to an eviction process and may even prevent an eviction if just cause is not proven. It also increases the costs of maintaining and carrying the subject property to the new owner by at least one month.

The new legislation seeks to avoid unnecessary foreclosures of residential properties and thereby provide stability to California's state and local economies (and housing markets) by requiring early contact and communications between lenders and borrowers to explore options that could avoid foreclosure and by facilitating loan modification or restructuring as viable alternatives. The practical effect of the new legislation, however is that it extends the timeline for non-judicial foreclosures and extends the time under which a tenancy can be terminated in a foreclosed property. In its pursuit of protecting the borrowers and those occupying homes, the law increases costs to lenders by requiring them to take additional steps in the foreclosure process, and it increases costs to new owners by imposing maintenance obligations and extending the time for a tenancy to be terminated.

However, the new legislation may also foster additional mortgage-related litigation. Lawsuits against lenders for failing to adhere to the statutory requirements of the non-judicial foreclosure process are likely. In addition, borrowers may decide to challenge a foreclosure if the lender has not complied with the new requirements, and tenants may seek to delay evictions and/or sue for wrongful eviction in cases where new owners served improper notices of termination. While only time will tell if SB 1137 has any real impact on the California foreclosure crisis, it certainly has introduced a new path for the foreclosure process, providing potential relief to some and hopefully a better way to achieve a mutually beneficial resolution. ■



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