

THE GIARDINELLI LAW GROUP, APC

Courtside Newsletter

Informing Real Estate Brokers, Association members, and local Businesses for over thirty years.

RECENT DEVELOPMENTS

- On July 14, 2011, John Giardinelli participated in a Legal Update on The Power Is Now Online Radio. In this teleconference, Mr. Giardinelli discusses FTC/MARS, real estate fraud, short sales, and recent cases of interest, including MERS litigation. To listen to this Legal Update, please go to <http://www.blogtalkradio.com/thepowerisnow/2011/07/14/double-your-business-without-working-twice-as-hard>.

CALENDAR

Brown Bag - Seminar

Date: September 7, 2011
Time: 11:30 a.m. – 1:00 p.m.
Location: Southwest Riverside
County Association of
REALTORS®

Please contact the Southwest Riverside
County Association of REALTORS® to
sign up!

MLS Rules & Regulations / Data Integrity (Traffic School)

Date: September 15, 2011
Time: 9:00 a.m. – 11:30 a.m.
Location: The Pacific West
Association of
REALTORS®

Please contact the Pacific West
Association of REALTORS® to sign up!

C.A.R. Expo

Date: Sept. 20-22, 2011
Location: San Jose Convention
Center

Go to www.expo.car.org for more
information and registration!

J NISWONGER
RIVERSIDE COUNTY OFFICE



There is some good news for homeowners who have to sell their properties for less than they owe (known in the industry as short sales). The California Legislature has passed Senate Bill 458, which protects sellers by prohibiting all mortgage holders from seeking to recover additional money from the seller after approving a short sale. This month's newsletter addresses the effects of Senate Bill 458 and the benefits to homeowners of this change to an existing statute.

Senate Bill 458 was signed by Governor Brown on July 11, 2011 and filed with the Secretary of State on July 15, 2011. The Bill modifies Code of Civil Procedure Section 580e and, by its terms, takes effect immediately. The most significant effect of this new law is that now any bank or other lender that holds a note secured by real property (*i.e.*, a mortgage) may not seek to recover a deficiency on that note after a short sale. That is, lenders who approve a short sale are entitled to receive only the money received through the sale of the property and may not collect any remaining balance from the seller. Previously, only the holder of the first mortgage was prohibited from recovering a deficiency. Thus, before this law recently changed, second mortgage holders (and other junior lenders) commonly approved short sales on the condition that they retain the right to recover from the seller any balance owed after the sale. This practice is now illegal.

To illustrate, assume that a seller owes \$350,000.00 on a first mortgage, and \$60,000.00 on a home equity line of credit (HELOC). Assume also that a buyer offers to purchase the property for \$200,000.00, and the first mortgage holder offers to pay the HELOC lender \$10,000.00 to approve the sale. Before the law was amended, only the first mortgage holder was prohibited from recovering additional money from the seller (*i.e.*, it could only receive the proceeds from the short sale, which, in this example would be \$200,000.00 minus \$10,000.00 to the HELOC lender minus costs and real estate commissions). A HELOC lender in this situation, however, would often include a provision in the short-sale approval that gave it the right to recover from the seller the remaining amount owed (\$50,000.00 in this example). Junior lenders, such as the HELOC lender in this example, can no longer

recover any money outside of the short sale. Like first mortgage holders, a junior lender that approves a short sale now receives only the money it agreed to receive under the terms of the short sale.

Under the law as amended, junior lenders cannot even ask sellers to contribute additional funds as a condition of approving the short sale. Thus, in the example above, the HELOC lender may not ask that the seller agree to contribute any additional funds as a condition of approving the short sale. Previously, junior lenders often negotiated with sellers to receive an additional lump sum payment to satisfy the obligation in full. For example, lenders like the HELOC lender above regularly negotiated an additional \$5,000.00 or \$10,000.00 from the seller with the promise that the loan would be treated as paid-in-full. This practice is no longer allowed.

Like the original, the modified law continues to apply only to dwellings of four units or less. Unlike the original statute, however, the new law distinguishes between loans that are secured "solely" by the property subject to the short sale and those that are secured by additional collateral (either other real property or personal property). If the loan is secured "solely" by the property subject to the short sale, the lender may not recover any deficiency. If the loan is secured by other property as well, then a lender may recover a deficiency only to the extent that a deficiency would have been available if the property had been sold through non-judicial foreclosure (see our September 2009 Courtside Newsletter for a discussion of judicial and non-judicial foreclosures).

The amended statute retains the exceptions for fraud and waste that were in the original version. This allows lenders to recover compensation from sellers who try to defraud lenders or who damage the property. An example of fraud would be if the seller received money from the buyer outside of escrow. The amended law also retains exceptions for sellers that are corporations or "political subdivisions of the state," and adds exceptions for limited liability companies and limited partnerships. The result of these exceptions is to make the law applicable only to sellers who are natural persons.

Continued...

IS THE LAW RETROACTIVE?

Senate Bill 458 officially became law on July 15, 2011 when it was filed with the Secretary of State, and applies to all short sales after that date. Questions arise regarding whether the amended statute provides any protection for sellers who completed short sales before July 15, 2011, or for sellers who entered into short-sale agreements before July 15, 2011 with escrow closing after that date. The analysis of whether a law is retroactive is complex, and involves a number of considerations beyond the scope of this newsletter. It appears, however, that the revised law will protect many sellers who closed escrow before July 15, 2011 or who entered into contracts before that date.

The precise wording of the amended statute states, "No deficiency shall be owed or collected, and no deficiency judgment shall be requested or rendered for any deficiency. . . ." Based upon this wording, a reasonable argument may be made that a lender who has not yet obtained a deficiency judgment will be prohibited from recovering any deficiency from a seller. This analysis is consistent with current California court determinations regarding whether and to what extent a statute is retroactive. It is possible that the words "no deficiency shall be owed or collected," may even prevent lenders from collecting existing deficiency judgments. How the courts will determine these issues, however, remains to be seen. The legislative history of this amendment strongly suggests that the lawmakers intended immediate protection for all sellers, including those who do not yet have judgments against them. The Giardinelli Law Group is currently vigorously defending deficiency claims based on the interpretation that such claims are absolutely barred as of July 15, 2011.

A LIKELY REPERCUSSION OF THE NEW LAW

Nothing in the amended law requires junior

likely be more difficult in the future to convince junior lenders to approve a short-sale offer. Instead of accepting a fraction of the amount owed by approving a short sale, junior lenders may prefer to allow the property to go into foreclosure and pursue a deficiency judgment after the foreclosure sale (see our September 2009 Courtside Newsletter for a discussion of when a junior lender may seek a deficiency after a foreclosure sale).

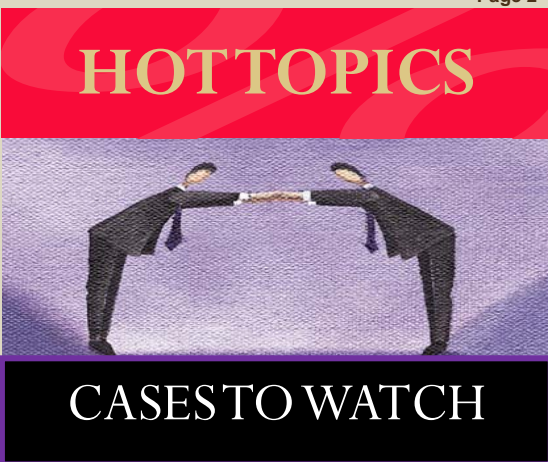
Also, junior lenders may initially withhold approval of a short sale in the hope that the seller may offer additional compensation as an incentive for the lender to sign the short-sale approval. While the law specifically states that junior lenders "shall not require" the seller to pay additional compensation, nothing in the law prohibits sellers from voluntarily offering additional compensation. Whether such a tactic is permissible will likely be the subject of future court decisions.

Senate Bill 458 closed a large loophole in short-sale law, but while it provides important protections for sellers, it creates a likely cost that fewer short sales will be approved by junior lenders. Only time will tell whether this law will have a positive impact on the current mortgage crisis.

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Biography

J Niswonger is the senior litigation attorney at The Giardinelli Law Group, APC. Mr. Niswonger has been a general civil litigator for more than 18 years, and has litigated real estate matters for more than 16 years. In addition to his litigation experience, Mr. Niswonger has successfully mediated a significant number of real estate cases. Mr. Niswonger may be reached at jniswonger@glawgroupapc.com or (951) 244.1856.



LegalZoom is currently being sued in Missouri District Court in a class action alleging that LegalZoom engaged in the unauthorized practice of law. LegalZoom tried to get the matter dismissed on the argument that providing legal documents does not constitute the unauthorized practice of law. The Court denied the motion on the grounds that LegalZoom provided more than documents. Some of the services provided by LegalZoom include software assistance in drafting documents and assistance in filing the document. The court did not determine the issue regarding whether LegalZoom engaged in the unauthorized practice of law, stating that the issue is a question of fact for a jury to decide. If the case is not settled before trial, it will be interesting to see what a jury will do with it.

Don't let LegalZoom steer you in the wrong direction. Contact us today to ensure accurate legal assistance.

www.glawgroupapc.com / (951) 244-1856

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Update on Enforcement of Mars Rule

The California Association of REALTORS® recently revised its Q & A on the MARS rule to reflect the FTC's current position regarding enforcing the rule against REALTORS®. As of July 15, 2011, the FTC is generally not enforcing the MARS rule with respect to REALTORS® who are simply trying to help their clients complete a short sale. Agents who are short sale negotiators, or who promote themselves as helping homeowners avoid foreclosure, however, must still comply with the MARS rule. Of course, the FTC will enforce the MARS rule against any REALTOR® who engages in unfair or deceptive practices in the handling of a short sale. For the complete MARS rule Q & A, contact the California Association of REALTORS®, or visit their website at www.car.org. For in depth legal advice regarding the MARS rule or other real estate matters, feel free to contact The Giardinelli Law Group, APC.

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