

# **CALIFORNIA REAL ESTATE SPECIAL REPORT**

## **Legal Guide to Foreclosure-related Transactions**



**S**hort sales, foreclosures, home equity sales: These words were rarely uttered by REALTORS® in the not so distant past. But as subprime loans with low introductory rates adjust higher and more homeowners struggle to make their mortgage payments, these foreclosure-related transactions have become more prominent in California's real estate industry.

As C.A.R.'s Member Legal Hotline attorneys can attest, working foreclosure-related deals raises many legal questions for REALTORS®. How much time does an agent have to sell a property to save it from foreclosure? Are there any special disclosure requirements? How does a short sale differ from a trustee's sale? Read on to find the answers to these questions and more. Through this special report, you'll learn the legal underpinnings of foreclosure-related deals, practical tips for avoiding the common pitfalls of such transactions, and other legal issues you should know before working with a buyer or seller on a property in default.



**For a thorough, no-nonsense approach to learning about foreclosures and short sales, check out *Foreclosures: C.A.R.'s Comprehensive Guide*, available for \$19.95 at [www.rebs.com](http://www.rebs.com). This 30-page reference manual trains members how to best serve their clients' interests in the current market and details C.A.R. standard forms and other resources concerning foreclosure-related transactions.**

## Why Do It?

Many REALTORS® wonder: Are foreclosure-related transactions viable business opportunities? The answer depends on you. Foreclosure-related transactions are worthwhile endeavors for REALTORS® who can surmount the high learning curve necessary to master the art of closing these types of transactions. If that describes you, here are some good reasons to go for it:

- **Significant Opportunities:** In the first quarter of 2007, mortgage lenders sent out 46,760 default notices to California homeowners—the highest level in a decade—according to Data-Quick Information Systems. With so many properties in default, there’s a strong demand to hire agents who work foreclosure-related deals. Owners facing foreclosure and lenders with bank-owned real estate properties (REOs) are looking for listing agents with those specialized skills, whereas prospective buyers are zooming in on agents who can hunt down great bargains.
- **Homeowners in Need:** Unfortunately, notices of default often can work as a beacon to scam artists and predatory lenders offering fraudulent rescue loans, phony credit counseling, and other shams. Agents can use their real estate expertise to help protect homeowners from those who prey upon owners in foreclosure.
- **Compensation and Referrals:** At their core, foreclosure-related transactions are very similar to the other

### WHAT IS FORECLOSURE?

Foreclosure is the legal process of selling property to satisfy a defaulting borrower’s debt secured by that property. Most foreclosures in California are private trustee’s sales, rather than judicial foreclosures. A trustee’s sale is a public auction for selling property to the highest bidder—a quick and cost-effective process for the lender. However, if the foreclosure sales price is not enough to pay off the loan being foreclosed upon, the foreclosing lender cannot recover that shortage (also known as a deficiency judgment) from the borrower.

### FORECLOSURE SCAM

From 2003 to 2005, Martha Rodriguez and others located homeowners using computerized foreclosure lists and promised to help them refinance their loans. What Rodriguez really did, however, was arrange for straw buyers—buyers who are offered a payment, often several thousand dollars, for the use of their name and credit information to make a false purchase—to obtain new loans to pay off the loans in default, with Rodriguez pocketing the excess. By the time Rodriguez was finally caught, she had victimized more than 100 homeowners in Southern California and amassed \$12 million. On February 22, 2007, Rodriguez pleaded guilty to two counts of fraud. She faces a possible sentence of 40 years imprisonment.

transactions agents handle. Foreclosure-related transactions can generate commissions, develop your customer base, and bring you referral business from the people you help. For instance, a seller you help now may later ask you to help his parents buy a home, or a lender you work with on a short sale may later hire you to list its REO properties. Some agents even create a new niche for themselves by specializing in foreclosures, short sales, or REOs.

- **Helping the Community:** Saving a homeowner from foreclosure also can protect their community from the adverse effects of foreclosure, such as abandoned properties and vandalism. Not only do such homes become an eyesore, but they also may drive down home values in the neighborhood. A study in Philadelphia showed that for every foreclosure, the value of other homes within a block fell by 1 percent in one year.

## Listing Properties in Foreclosure

Deciding whether to list a property in foreclosure is not something to take lightly. Once you accept an agency relationship, you owe your client a fiduciary duty of utmost care, integrity, honesty, and loyalty to do what is in your client’s best interest. Moreover, the stakes are high for a homeowner in foreclosure. If you fail to sell the property, the owner may be out of time to make other arrangements, and your prospects of collecting a commission for the work you’ve done decrease.

## PRACTICE TIP

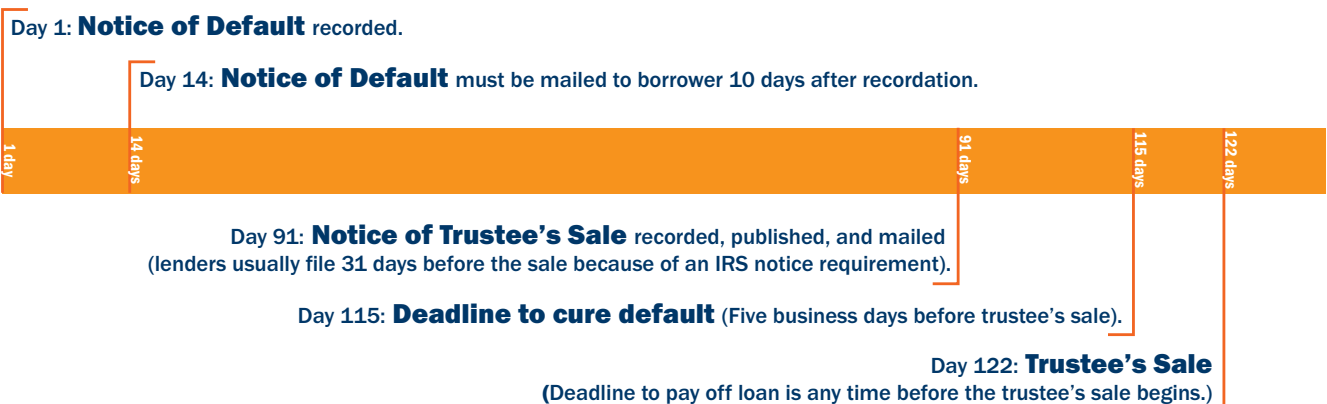
It may not be immediately apparent to you that a seller is in foreclosure. Yet, knowing about the foreclosure is an important factor in deciding whether to take the listing and under what terms. Sometimes there may be clues, like deferred maintenance to the home or a comment about financial distress. Otherwise, a notice of default is a matter of public record that you can look up in the county's records. Alternatively, an excellent practice for listing agents is to ask the owner to complete C.A.R.'s standard form *Seller Property Questionnaire* (SPQ) before entering into a listing agreement. Question 24 of the SPQ specifically inquires into the seller's knowledge of any notices of default.

Here are some factors you should consider before you agree to list a property in foreclosure:

- **Limited Time Frame:** If a borrower has only missed one mortgage payment, it may be a few more months before the lender files a notice of default. The clock, however, officially starts ticking when the notice of default is recorded. Absent an extension, the rule of thumb is that it will take about four months after the notice of default is recorded for a property to be sold at a trustee's sale (see Foreclosure Timeline below). That's four months not only to find a buyer but also to pay off the lender by closing escrow.
- **Listing Price and Terms:** A property in foreclosure must be priced high enough to satisfy existing lenders, yet low enough to attract buyers for a timely sale. Do your homework before agreeing to list. Calculate how much is needed to satisfy the existing lenders and make sure your research shows the market will bear that price. Equity in the property is a key concern. The more equity there is, the more motivated the seller will likely be to sell.
- **Assess the Client:** Emotions can run high for owners in foreclosure. In addition to financial hardships, clients may struggle with the problems that led up to foreclosure, such as job loss, illness, divorce, or mortgage fraud. While REALTORS® are familiar with distressed clients, the difference here is that owners in foreclosure can be indifferent, unrealistic, or unwilling to ask for help. After all, there are many instances of owners who aggravate their financial difficulties by failing to contact their creditors and assess the options available to them. As an agent, you should determine upfront whether your client will help or hinder the selling process.
- **Alternatives to Selling:** Carefully consider the owner's alternatives to selling, as some options may diminish your ability as the listing agent to sell the property and collect a commission. An owner might be able to work something out with the lender, such as a repayment plan, loan modification, extension, or deed in lieu of foreclosure. Other alternatives include refinancing, bankruptcy, legal action, or simply borrowing money from family or friends. Even foreclosure itself may be a viable option for some owners to get out of a losing proposition.

## FORECLOSURE TIMELINE

Approximate minimum timeframe for the foreclosure process.



## WHAT IS A DEED IN LIEU OF FORECLOSURE?

It's a transfer of title from a borrower to the lender, which the lender accepts in full satisfaction of a mortgage debt.

## Subprime Loans

In recent months, the subprime loan crisis has taken center stage in the real estate market. Subprime loans are generally loans made available to borrowers who do not qualify for conventional, mainstream financing because they have low credit scores and a history of payment delinquencies, charge-offs, or bankruptcy. A subprime loan also tends to involve loose underwriting requirements, such as a minimal down payment and the option to provide a "stated income" without documentation. Because subprime loans are highly risky, lenders expect a lot in return: They typically charge higher interest rates, points, and fees, and institute prepayment penalties. A common subprime loan is the 2/28 "exploding" adjustable-rate mortgage loan (or option ARM). This loan starts off with a discounted "teaser" rate for two years, after which the interest rate may rise sharply and cause financial hardship for some borrowers.

Delinquencies and defaults are more common among subprime borrowers than among homeowners who have more traditional financing. Yet, during the first half of this decade, California's real estate market was robust

and subprime borrowers experiencing financial difficulty could simply refinance their loans to cash out their built-up equity, or sell their homes at a profit. Absent that robust market, however, subprime borrowers may not have any home equity available as a safety cushion. Without the options of refinancing or selling, subprime borrowers in financial trouble are falling into default. Because the number of subprime loans funded peaked in 2006, and the interest rates of these loans are not scheduled to be reset for a few more years, certain aspects of the subprime fallout—including an increased rate of foreclosures—may continue through 2008.

### Impact of Subprime Loans on REALTORS®

The most palpable impact the subprime loan crisis has on REALTORS® is the increase in foreclosure-related transactions on the market. Whether you've now listed your first property in foreclosure or you've considered writing an offer for a short sale, chances are you've experienced the subprime fallout firsthand in one way or another.

REALTORS® also need to adjust to changes in the mortgage business resulting from the subprime fallout. Some subprime lenders have gone out of business or stopped offering subprime loans, while other subprime and prime lenders have changed their loan products and tightened their underwriting guidelines. Marginal borrowers who previously

could only buy a home using subprime financing may be shut out of the real estate market for now.

## WHAT IS BANKRUPTCY?

It is a federal court procedure for people who are unable to pay their debts to settle those debts with their creditors under a judge's supervision. The filing of a bankruptcy case temporarily stops foreclosure proceedings. Under a Chapter 7 bankruptcy case, if the lender's interests are not adequately protected, the court may allow the lender to resume its foreclosure proceedings. Under a Chapter 13 case, the debtor can keep the property by paying the amount overdue over a three-to-five year plan (along with the regular mortgage payments).

### Learn about Foreclosures at CALIFORNIA REALTOR® EXPO 2007

At this year's EXPO, REALTORS® can attend "Foreclosure Opportunities for Buyers/Clients" to learn more about foreclosure-related transactions. Taking place on Thursday, October 11 from 8:30 a.m. to 4:30 p.m., this one-day elective for the ABR designation provides you with valuable tips for working with clients in financial distress. The cost is \$165 and lunch will be provided. To register, visit [www.realtorexpo.org](http://www.realtorexpo.org).

## CONTRACT TIP

C.A.R.'s *California Residential Purchase Agreement* (RPA-CA) and other purchase agreements require the buyer, within seven days after acceptance, to provide the seller with a prequalification or preapproval letter, as well as written verification of the buyer's down payment and closing costs.

Keeping this lending climate in mind, REALTORS® should be aware of the following contractual concerns:

*Listing Agents:* Listing agents and sellers may wish to closely scrutinize a buyer's ability to obtain a loan and consummate a sales transaction.

Here are some negotiable terms in a sales contract that may concern the listing agent and seller:

- Whether the buyer's offer is contingent upon obtaining financing.
- The loan-to-value ratio.
- The buyer's initial good faith deposit.
- Proof of the buyer's down payment and closing costs.
- A prequalification or preapproval letter from a reputable lender.
- Whether the buyer provides other documentation demonstrating financial ability and creditworthiness, such as a FICO score, credit report, paycheck stubs, loan application, or authorization for the seller to verify the loan process and approval directly with the lender.

*Buyer's Agents:* Given the tightening of loan underwriting requirements, buyer's agents also should verify a prospective buyer's ability to obtain financing as soon as possible. It also may be helpful to encourage prospective buyers to obtain preapproval from a reputable lender.

When writing an offer, also be aware that buyers may wish to include a loan contingency that allows the buyer to back out and keep the escrow deposit if they cannot obtain a loan. The buyer also may want a loan contingency that provides ample time to get a loan processed, or to even have the loan contingency remain in effect until funding, in case the lender goes out of business before close of escrow.

## Short Sales

A short sale is a sales transaction in which the seller's mortgage lender agrees to accept a payoff of less than the balance due on the loan. A short sale may or may not involve a property in foreclosure.

Properties are more likely to become short sales when the market is soft and the rate of home price appreciation is low. However, the loan is generally the main instigator for a short sale. The loan in a short sale is often subprime, highly leveraged, negatively amortizing, includes a prepayment penalty, or all of the above.

Taking a listing for a short sale raises similar concerns as those previously discussed for listing properties in foreclosure.

However, for short sales, REALTORS® also should consider the amount of loan forgiveness the seller is seeking. The greater that amount, the less likely the lender will agree. Another consideration is the actual lender(s) involved in the short sale. Some

lenders are more amenable to short sale requests. Finally, also take into account whether you are willing to make what may be a significant time investment to handle the paperwork and negotiations with the lender.

Why would a lender agree to a short sale? Lenders make their own business judgments when accepting or rejecting short sales. For agents negotiating short sales, knowing a lender's concerns improves your ability to get the short sale approved. The bottom line is that lenders are in the business of making and servicing loans, not taking properties back through foreclosure and reselling them. Some of the things lenders want to avoid are:

## CONTRACT TIP

C.A.R.'s *California Residential Purchase Agreement* (RPA-CA) gives a buyer 17 days after acceptance to remove the loan contingency or cancel the agreement. However, a buyer may insert more days if needed, or even keep the loan contingency in effect until the designated loans are funded.

## PRACTICE TIP

Like foreclosures, it may not be apparent to an agent taking a listing that there may be a short sale. Obtaining a property profile upfront will usually alert you to the possibility of a short sale before you agree to take a listing.

- Spending time and money to foreclose, evict borrowers, and resell properties.
- Adding a bad loan and REO to their portfolio.
- Paying property taxes, insurance, maintenance, and repairs for REO properties.
- Risking theft and vandalism to the property, either by the borrower before they vacate the premises or by others when the REO property is vacant.

## FAST FACT

C.A.R.'s Standard Forms Advisory Committee currently is considering the release of an addendum to the *Residential Listing Agreement* (RLA) for short sale transactions.

Here are additional insights: Junior lien holders (those who are not in first position) who are more likely to get wiped out through foreclosure than senior lien holders, also are more likely to agree to a short sale. Other things that improve your chances of getting a lender's approval include submitting a sales contract from a well qualified buyer, submitting properly packaged paperwork, and knowing who to talk to at the bank. It's also a good idea to make sure upfront that the lender approving the short sale will agree to release the buyer from any further obligation on the debt.

## DISCLOSURE REQUIREMENTS FOR FORECLOSURE-RELATED TRANSACTIONS

Short sales and home equity sales are treated just like any other sales transaction in terms of disclosures, and require, for example, the *Transfer Disclosure Statement* (TDS), *Natural Hazard Disclosure Statement*, and so forth. However, short sales and home equity sales give rise to certain contractual concerns as discussed next. Also, there are special disclosure requirements for properties sold at a foreclosure sale or by an REO lender that has taken back a property through foreclosure. For more information, C.A.R. has published a *Sales Disclosure Chart for REALTORS®*, available online at <http://qa.car.org>.

## Listing Short Sales in the MLS

The California Model Multiple Listing Service (MLS) Rules include special guidelines for handling the unique situation posed by short sales. In a short sale, the lender considering a reduction in its loan payoff may request that the real estate agents also reduce their commissions. A listing broker need not oblige but may nevertheless choose to do so to achieve the sale.

A listing broker who chooses to accept a reduced commission still is obligated to pay the cooperating broker the compensation published in the MLS, unless the listing broker also has included all of the following information in the MLS listing:

- The fact that the sale and gross commission are subject to lender approval.
- The method by which the compensation offered through the MLS will be reduced if the lender reduces the gross commission.

As an example, a conditional offer of compensation for short sales may be placed in the "Remarks" section of the MLS as follows:

"Short sale and gross commission subject to lender approval. Any commission reduction to be split 50/50."

How the reduction is allocated in a short sale (e.g., 50/50 in the above example) is at the listing broker's sole discretion, as long as the cooperating broker is given notice of such allocation.

## CONTRACT TIP

Paragraph 5 of C.A.R.'s *Purchase Agreement Addendum* (PAA) pertaining to short payoffs addresses these concerns. A listing agent who receives an offer that should be made subject to the lender's approval may use the *Counter Offer* (CO) form and incorporate paragraph 5 of the PAA.

## Short Sale Contracts

An important contractual issue for a seller entering into a short sale contract is to include a contingency allowing the seller to back out in the event the lender does not approve the short sale. Other contractual issues to address include

whether the seller may present other offers to the lender, and whether the buyer may cancel the contract during the short sale process.

### **Credit and Tax Issues for Short Sales**

A short sale implicates possible credit and tax issues for the owner. As such, an owner considering a short sale should be encouraged to discuss these issues with an attorney, accountant, or other appropriate professional. For instance, a short sale may adversely affect a borrower's credit rating because a lender can report for seven years that a loan has been "settled" for less than its balance. Although a lender is unlikely to change what it reports to credit bureaus, a borrower may attempt to negotiate this issue when arranging the short sale or request a letter from the lender detailing any extenuating circumstances surrounding the short sale.

The tax implications of a short sale also may be so significant that it is not in the owner's best interest to proceed. The debt forgiven by a lender is generally taxable to the borrower as "debt discharge income." When a taxpayer receives proceeds from a new loan, those proceeds are not taxable income because there is an offsetting obligation to repay. However, if the debt is cancelled, there may be debt discharge income.

Discharges through the following situations are not taxable as income:

- Bankruptcy.
- When the owner is otherwise insolvent (i.e., current liabilities exceed assets, but this exemption only applies to the extent that the liabilities exceed assets).
- For purchase-money seller financing (but the discharged debt is treated as a reduction in the owner's tax basis).
- For qualified real property business indebtedness (but the discharged debt will be treated as a reduction in tax basis).
- For qualified farm indebtedness.

## **SHORT SALE VERSUS TRUSTEE'S SALE**

Like short sales, properties sold through foreclosure at a trustee's sale also have tax, credit, and other legal implications. A trustee's sale may adversely affect a borrower's credit. If the borrower is not personally liable for the debt (a "non recourse" loan), such as a purchase-money loan for a personal residence, there is no taxable income at foreclosure for discharged debt. Nevertheless, foreclosure is a sale for capital gain purposes. The amount realized on the sale is generally the principal balance of the loan at the time of foreclosure.

The tax on debt discharge income in a short sale is in addition to any income tax from capital gains the seller may owe. Even if a seller nets nothing from selling a property in a short sale, the seller may nevertheless owe taxes on both debt discharge income and capital gains.

## **Home Equity Sales Contracts**

The sale of certain properties in foreclosure requires special handling under the Home Equity Sales Contracts Act, which was enacted in 1979. The purpose of this law is to protect homeowners in foreclosure and their equity from unscrupulous people. Homeowners experiencing the financial hardship of foreclosure

may be induced to sell their homes for a small fraction of the fair market value through fraud, deceit, or unfair dealings.

Not all properties in foreclosure fall under the home equity sales law. The requirements of the home equity sales law only apply when all four of the following conditions are met:

- The property is one-to-four family dwelling units.
- The owner occupies one of the units as a principal residence.
- There is an outstanding notice of default recorded.
- The buyer will not use the property as a personal residence. (The buyer in this situation is called an "equity purchaser.")

All four of the above conditions must be met to trigger the home equity sales law. In the typical situation where a buyer of a property in foreclosure will be occupying the property as a personal residence, the home equity sales law does not apply.

**Want more legal information?**

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**<http://legal.car.org>**



The following transfers also are exempt from the home equity sales law:

- By deed in lieu of foreclosure
- By trustee's sale
- By tax sale or other sale authorized by statute
- By court order
- By spouse, blood relative, or blood relative of spouse

## CONTRACT TIP

To help REALTORS® comply with the legal requirements for home equity sales contracts, C.A.R. offers a standard form, *Notice of Default Purchase Agreement (NODPA)*, and two attachments: the *Home Equity Explanation and Agency Agreement (HEAA)* and the *Notice of Cancellation of Notice of Default Purchase Agreement (HENC)*.

## Requirements of the Home Equity Sales Law

Transactions falling within the scope of the home equity sales law must meet certain requirements. The contract itself must be in 10-point bold font and in the same language principally used by the parties to negotiate the sale. It also must contain certain contractual provisions. Most notably, the seller must be given a notice of the right to cancel within five business days after signing the contract (or by 8 a.m. of the day of the trustee's sale, if sooner).

Under the home equity sales law, a buyer's agent generally cannot represent an equity purchaser. A "representative" for purposes of this law is anyone who solicits, induces, or causes an owner (or a member of the owner's family or household) to transfer title to the equity purchaser. Among other things, the representative of the equity purchaser must provide proof of a valid California real

## LEGAL TIP

A listing agent disavowing any agency relationship with an equity purchaser may use C.A.R.'s standard form *Buyer Non Agency Agreement (BNA)*, whereas a buyer's agent may use the *Termination of Buyer's Agency (TBA)* form. Both agents also should conduct themselves accordingly by not acting as an equity purchaser's agent.

estate license and be bonded by an admitted surety insurer for twice the value of the property. Yet, such bond is difficult, if not impossible, to find. This bonding requirement applies to a buyer's agent or dual agent but not a listing agent representing the seller exclusively.

## Violations

A violation of the home equity sales law can be very serious. Equity purchasers who violate the home equity sales law may be convicted of a crime punishable by one year imprisonment, plus a \$25,000 fine, for each violation. Furthermore, in a civil court, the seller can recover actual damages, exemplary damages of at least three times the actual damages (or a \$2,500 civil penalty), attorneys' fees, and costs. The seller also may recover equitable relief, including the rescission of an unconscionable contract up to two years after conveyance of the property.

## PRACTICE TIP

For more information, C.A.R.'s Legal Department published a legal article entitled "Home Equity Sales Contracts," available online at <http://qa.car.org>.

## Foreclosure Consultants

The foreclosure consultant law was enacted in 1979 in conjunction with the Home Equity Sales Contracts Act. It sets forth stringent rules regulating the activities of foreclosure consultants to prevent unfair dealings. These requirements only pertain to transactions involving one-to-four family dwelling units, one of which the owner occupies as a principal residence, and against which an outstanding notice of default is recorded.

The foreclosure consultant law generally applies to anyone who, for compensation, performs or offers to perform foreclosure-related services, such as stopping or postponing a foreclosure sale, providing financial counseling, or contacting an owner's creditors. Real estate licensees are exempt from the foreclosure consultant law to a limited extent as discussed below. Also exempt are attorneys, licensed accountants, and others.

REALTORS® should have an understanding of the foreclosure consultant law to make sure they comply with the law in their dealings with homeowners in foreclosure.

Also, knowledge of the foreclosure consultant law helps homeowners and their listing agents distinguish between legitimate foreclosure consultants and scam artists. The foreclosure consultant law is fully set forth in the California Civil Code beginning with section 2945.

### Applicability to Real Estate Agents

The foreclosure consultant law is a complicated body of law. As a general rule, agents dealing with homeowners in foreclosure and engaging in “normal” agent activities are exempt from the foreclosure consultant law. More specifically, for owner-occupied one-to-four residential units in foreclosure, agents may fall within the foreclosure consultant rules if they engage in any of the following activities:

- Acquire an interest in a residence in foreclosure (other than a “direct loan” as described below);
- Receive any compensation before performing their real estate services; or
- Assist an owner to obtain the remaining proceeds from the foreclosure sale of the owner’s residence.

A real estate broker may make a “direct loan” without having to meet the requirements of the foreclosure consultant law. A “direct loan” must satisfy all of the following requirements:

- A loan of the real estate broker’s own funds;
- A loan secured by a deed of trust on the residence in foreclosure; and
- The real estate broker makes a good faith attempt to assign the note and deed of trust to a lender for an amount at least sufficient to cure the default on a recorded notice of default.

### Foreclosure Consultant Requirements

If an exemption does not apply, a foreclosure consultant must meet certain requirements. The foreclosure consultant must enter into a written contract with the owner as prescribed by law (standard form not currently available through C.A.R.), and the contract must provide, among other things, the owner’s right to cancel within three business days.

A foreclosure consultant also is prohibited from engaging in certain activities, including, but not limited to, the following:

- Acquiring an interest in a residence in foreclosure.
- Claiming compensation exceeding 10 percent per annum of any loan made by the foreclosure consultant.
- Claiming compensation before services are fully performed.
- Taking a power of attorney from the owner for any purpose, other than to inspect documents as provided by law.
- Failing, as the foreclosure consultant’s agent or employee, to provide written proof of a current real estate sales license and a bond from an admitted surety insurer for twice the fair market value of the property.

### Violations

A violation of the foreclosure consultant law can be a crime punishable by one year imprisonment, plus a \$10,000 fine. An owner also may sue in civil court to recover actual damages, exemplary damages, reasonable attorneys’ fees and costs, and equitable relief.

### PRACTICE TIP

If you are contemplating developing a marketing plan that targets homeowners in foreclosure, be mindful of the foreclosure consultant law. As an example, if a salesperson considers using personal funds to make a secured loan to a homeowner in foreclosure in exchange for a listing, the foreclosure consultant law is triggered. Alternatively, an agent offering to list a home in foreclosure and promising to personally buy the property before the foreclosure sale, if necessary, falls within the scope of the foreclosure consultant law.

# 2007 New Laws Quick Reference Guide

Failing to learn and understand the laws affecting your real estate practice can be disastrous to your business. That's why **C.A.R. Legal Services** publishes periodic legal updates each year to keep your knowledge about licensing, fair housing, and other legal issues up-to-date. Below you'll find brief summaries of a handful of laws that became effective earlier this year. For a complete listing, visit **C.A.R. Legal Online** at <http://legal.car.org>.

**60-Day Notice to Terminate Lease:** Starting this year, residential landlords are required to give any month-to-month tenant a 60-day eviction notice if that tenant has lived on the property for more than one year. However, a 30-day notice to terminate is allowed if the tenant has lived on the property for less than one year or when all of the following conditions are present: the dwelling is a single-family home; an escrow has been established with a bona fide buyer who is a natural person and intends to use the property as a principal residence for at least one year; the notice is given within 120 days after escrow is opened; and the tenant did not previously receive a notice to terminate from the landlord. The 60-day notice does not apply to fixed-term (e.g., one-year) leases.

**Advertising Faxes:** Before you send an advertising fax to a prospective or current client, take note: Pursuant to federal law, you must obtain the recipient's oral or written permission to send a fax, and you must include an opt-out notice on the first page of the fax that discloses your contact information. This opt-out clause must be separate and distinguishable from the advertising portion of the fax.

**California Capital Gains Taxes:** In most real estate transactions, escrow companies were previously required to withhold 3 1/3 percent of the sales price. Common exceptions to this requirement include transactions involving a principal residence and 1031 exchanges. Beginning this year, non-exempt sellers can now choose to have escrow withhold a sum of money equal to the maximum California personal or corporate tax rate multiplied by the anticipated recognized gain on the transferred property instead of 3 1/3 percent of the sales price. This means that even if the seller is not exempt from withholding, the seller can choose to have escrow withhold the actual California capital gains tax owed, rather than an arbitrary 3 1/3 percent of the sales price.

**Conditional Licenses:** Currently, nearly 85 percent of new licensees obtain what is called a "conditional salesperson's license," which allows them to conduct licensed activities upon completing one of three required classes, passing the exam, and promising to complete the additional two classes within 18 months. Beginning in October 2007, this "conditional salesperson license" will be eliminated, and all applicants will be required to complete the three mandatory courses before receiving a new salesperson's license.

**Registered Sex Offenders:** California's Megan's Law prohibits people from using information obtained from the Megan's Law Web site for purposes related to housing and accommodations. However, the Attorney General recently stated this does not mean that registered sex offenders, as a class, are protected from housing discrimination. In other words, registered sex offenders may be subject to housing discrimination in order to protect persons at risk.

**Reverse Mortgages:** Lenders can no longer accept an application for a reverse mortgage—a transaction where the homeowner uses his/her home equity as a source of income—until the borrower certifies that he/she has received financial counseling. Prior to this year, lenders only had to provide a disclosure notice advising applicants to seek such financial counseling. The new law also prohibits lenders from requiring borrowers to obtain an annuity as a condition for obtaining a reverse mortgage; requires lenders to refer the borrower to a housing counseling agency and to provide a list of independent counselors; and requires mortgage documents to be translated into the language in which the mortgage was negotiated.

For a complete listing of new laws taking effect in 2007, visit **C.A.R. Legal Online** at <http://legal.car.org>.



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