MARS Attacks! Oregon Realtors® Take Cover

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"We come in peace."

For those who have seen the 1996 movie, "Mars Attacks!" there is a certain metaphorical similarity between the movie and the recently enacted federal law. Both the federal law and the Martians initially seemed relatively harmless to law-abiding citizens. But alas, once again, life has imitated art….

Background. The Mortgage Assistance Relief Services Act Final Rule, 16 CFR Part 322 [aka "MARS"], effective January 1, 2011, is a meandering and somewhat "Johnny come lately" federal regulatory effort by the Federal Trade Commission ["FTC"]. When the credit and housing crisis made its first significant appearance in 2008, there also emerged a cottage industry of faux "consultants" who touted their ability to help struggling homeowners with their distressed housing choices. Many carpetbaggers came from out of state, supposedly affiliated with lawyers, real estate agents or mortgage brokers. Their business model included the payment of up-front fees coupled with the promise of assisting homeowners in securing lender consent for loan modifications and short sales. For a year or more there were anecdotal stories of distressed homeowners paying large sums of money but receiving little or no effective assistance.

For a recitation of horror stories and enforcement actions, one can read the first seven pages and 103 footnotes of the Federal Register, which appears intended to explain the immediate need for the massive rulemaking exercise that was to follow. However, nothing in the federal government occurs quickly, and now, in 2011, one must question the need for a broad federal mandate that overlaps pre-existing state laws covering the same activities.

Oregon's Legislative Approach. In its 2008 in Special Session, Oregon had enacted House Bill 3630, sometimes known as the "Foreclosure Consultant Law," although it also dealt with an illegal practice called "equity stripping," which was a scam where grifters "bought" distressed homes on unrecorded deeds, leasing them back to the distressed homeowner with a promise to resell to them at a later date. Oregon's law requires that persons offering certain foreclosure rescue services provide homeowners with a specific written contract containing certain disclosures and rights of rescission. There were several industry exclusions, including Oregon licensed lawyers and real estate brokers.

In 2009, the Oregon Legislature passed another bill, HB 2191 (the "Debt Management Law"), which appears to have been focused on the debt consolidation industry.[1] Unfortunately, it seems the drafters went a little farther than their original purpose, and added into the definition of "debt management

[1] HB 2191 replaced both the credit service organization and debt consolidating agency registrations.

services," a function that was already covered in the 2008 Foreclosure Consultant Law: *"Obtaining or attempting to obtain *** a concession from a creditor including, but not limited to, a reduction in the principal, interest, penalties or fees associated with a debt."* Even though this is precisely what real estate brokers do when they assist homeowners in their short sale discussions with lenders, HB 2191 failed to exempt brokers from this new law. Since lawyers, banks and professions similar to those exempted under the Foreclosure Consultant Law were excluded, it is inexplicable why real estate agents were not. Since there does not appear to be any express legislative history suggesting this was intentional, a *not unreasonable conclusion is that it was inadvertent*.

The Debt Management Law requires registration with the DCBS together with certain bonding requirements. Fortunately, the Oregon Department of Business and Consumer Services ("DCBS") promulgated Oregon Administrative Rule 441-910-0000 (3), which specifically excludes real estate brokers when engaged in short sale negotiations. Between this administrative rule and the Frequently Ask Questions link posted on both the DCBS and Oregon Real Estate Agency websites, real estate brokers *appear* to be permitted to engage in short sale negotiations with sellers' lenders, *without* being required to register as debt manager consultants.

However, there are two new requirements found in the FAQs, but not the administrative laws. Together, these new FAQs require - though with *no imprimatur of rulemaking*:

- *The amount charged for the short sale service cannot exceed the commission already agreed upon in the listing contract, and*
- *The service must be incidental to the transaction.*[2]

Assuming that these two new interpretive criteria are not unreasonable or burdensome, and together with the Foreclosure Consultant Law, the Debt Management law, and the laws governing Oregon real estate licensees found in ORS Chapter 696, regulate how real estate brokers are to conduct short sales in Oregon, *why do we need a federal law - e*specially now, three years after the crisis first emerged? *Is there some reason to believe that Oregon and other states have been unable to effectively deal with these issues within their own borders?*

How Does MARS Apply to Oregon Real Estate Brokers – And Should It? If one reads the congressional record in its entirety, it is clear that the legislative intent was to deal with "bad guys." That is, those folks who made their initial furtive appearance during the early stages of the foreclosure crisis, seeking to take advantage of the plight of distressed homeowners.

The record is devoid of anecdotal reports of Realtor® abuses. If so, why is there any belief that this law was intended to even apply to them in the first place? My belief is that MARS was never intended to apply to real estate brokerage practices. There certainly was no mystery that short sales were comprising an ever increasing portion of total sales across the country. However, following a sort of Wikipedia logic that if a belief is repeated often enough, it takes on the appearance of unassailable fact.

[2] To say that the service is "free" or that it is "incidental" to the rest of the transaction (as explained in the FAQs) ignores today's realities: (a) 40% to 50% of *all* Oregon transactions are short sales, and (b) Negotiations with the lenders and servicers are the most time consuming and labor intensive part of the entire short sale transaction. Realistically, these negotiations are neither "incidental" or "free." "Professional real estate activity" as described in ORS 696.010 (15), easily includes within its broad definition, negotiations with sellers' lenders – it is an essential part of all short sales and serves a seller's best interest. It is unrealistic and unnecessary to treat these activities as a form of "permitted exception" to professional real estate activity, in light of the frequency and magnitude of this essential component of so many transactions today.

In short, it is "knowledge by repetition." However, this is a conclusion reached without taking the time to read the federal record, which, after all, is the actual source of the law.

During the rulemaking stages, when MARS was being formulated, the National Association of REALTORS® sought a specific exemption. It should have been granted. However, in a counterintuitive response, the FTC felt it was not necessary, because real estate transactions were precisely what real estate agents did, so there was no need to specifically exclude them from coverage. Following that logic, one might conclude that licensed attorneys, who are typically permitted under state law to perform the equivalent of "professional real estate activity" without meeting the brokers' licensing requirements, would also not need to be excluded. However, MARS goes to great lengths to grant them a broad exclusion, so long as they are acting on behalf of their clients and conform to state Bar ethical rules.

At footnote No. 126 of the Federal Register, the MARS law notes as follows:

> As a general matter, the Final Rule **is not intended to apply to the marketing of services to assist consumers in selling their properties to third parties**. *** One commenter *[i.e. the National Association of REALTORS® ("NAR") – PCQ]* urged the Commission to exempt licensed real estate professionals from the Final Rule. *** The commenter argued the Rule would restrict real estate agents in helping consumers with the process of selling their homes through short sales. Id. **The Commission concludes that an exemption for real estate agents is not necessary. Real estate agents customarily assist consumers in selling or buying homes and perform functions such as listing homes for sale, showing homes, and finding desirable homes for consumers. The Commission is aware that real estate agents may perform these functions when properties are bought or sold through a short sale transaction, but does not consider these services to be MARS.** *[Emphasis and comments mine. - PCQ]*

Unfortunately, in the same footnote, the FTC included the following observation:

> The Final Rule, however, does specifically cover the marketing of services involving the sale of properties to third parties if those services are designed or intended to assist consumers in averting foreclosure, e.g., through a short sale or deed-in-lieu of foreclosure.

As a standard – and logical – rule of legal interpretation, we must ask, "How can these two statements be reconciled?" If they were included together in the same footnote, we must assume they were not intended to be mutually exclusive.

It is my belief that the statements should be read together, and doing so, permits the following interpretation:

- If a real estate agent is performing a short sale in the ordinary course of their standard real estate practice, the MARS law should not be applied to their activity.

- However, if the real estate agent is holding themselves out as someone who can do a short sale to "avert a foreclosure" – or words to that effect - then MARS applies since it appears that the short sale service is "designed or intended" to avert foreclosure. This

seems to be the same interpretation taken by the Federal Trade Commission found at this link.

- Since MARS deals not only with specific [one-on-one] communications, but general non-specific communications as well, it is reasonable to conclude that whenever a real estate broker (or brokerage) advertises their services, they may be subject to the MARS rules if they attempt to combine their short sale services together with the goal of averting foreclosure.

If one reads the NAR pronouncements about MARS, they are tentative. They do not definitively say that MARS applies to *all Realtors®* in *all cases when they are engaged in short sales as a regular part of their professional real estate activity.* My take is that in advising Realtors® about the new law, NAR is suggesting compliance out of an abundance of caution – at least until they can convince the FTC to be more specific as to the sale of homes with negative equity, that of necessity, include a short sale. *[Footnotes are a nice "tip of the hat" acknowledgment to NAR's legitimate concern, but it would be much more helpful to have an explicit exception – like the one given to lawyers. – PCQ]*

My primary concern with the "Wikipedia approach" to the application of MARS to *all* real estate agents, is that compliance with an ambiguous law creates the "appearance" that one believes the law applies to them. Pretty soon, someone will actually assert a MARS violation against a Realtor®. The alleged violator (or their attorney) will argue that the law doesn't really apply to them, so there is no violation. But the complainant (or their attorney) will undoubtedly ask: *"So why did you deliver those MARS disclosures and disclaimers to my clients? You apparently thought it applied to you at that time. Were you wrong then, but right now?"* Touché.

The Take Away. What is the risk of non-compliance with MARS? I believe it is much greater for those Realtors® whose business model depends upon touting their skills as a "short sale specialist" or words to the effect. This is the unfortunate consequence of the FAQs, discussed above, focusing on a broker's marketing efforts rather than the substance of a broker's service.

It is important to know and appreciate that besides MARS, the DCBS also seems to make this distinction – i.e. if your business model focuses on short sales, it is not, by definition, "incidental." My difficulty with this logic is that short sales are almost the rule today – not the exception. How does one tout their real estate skills without mentioning "short sales" which comprise almost half the market in some areas of Oregon? That would be like telling lawyers they can advertise that they "practice law," but prohibiting them from saying they're really great in court. How is the consumer to make an informed decision as to which lawyer to select?

Moreover, almost all homeowners I have spoken with – and there have been many - who are considering short sales, do so because they foresee a possible foreclosure in their future. They believe – correctly – that a short sale may result in less of a negative credit impact than foreclosure. Accordingly, they need to get more information from their Realtor® about the process. In my opinion, an overly restrictive state or federal regulatory scheme based on how Realtors® promote their own skills, *potentially* constitutes a restraint of commercial free speech. Ah, but I digress….

What will we do in Oregon? Out of an abundance of caution, we will issue MARS-compliant forms. Oregon Real Estate Forms, LLC is drafting them now, and final approval should occur shortly. For those concerned about the application of the law to their short sale transaction, they will be available . *But remember that if you deliver them to your seller client, you will likely be held to the rules they are based upon.*

The MARS Landscape. So with the above discussion out of the way, what follows is a summary of MARS as it potentially[3] relates to real estate brokers and others:

- **"Mortgage Assistance Relief Service" ["MARS"].** Includes ''…any service, plan, or program, offered or provided to the consumer in exchange for consideration, that is represented, expressly or by implication, to assist or attempt to assist the consumer'' in negotiating a modification of a dwelling loan that reduces the amount of interest, principal balance, monthly payments, or fees; stopping, preventing, or postponing a foreclosure or repossession; or obtaining one of several other types of relief to avoid delinquency or foreclosure. These additional types of relief include obtaining:
  - A forbearance or repayment plan;
  - An extension of time to cure default, reinstate a loan, or redeem a property;
  - A waiver of an acceleration clause or balloon payment; and
  - A short sale, deed-in-lieu of foreclosure, or any other disposition of the property except a sale to a third party that is not the lien holder.
- **''Mortgage Assistance Relief Service Provider''.** A person *[I shall resist the temptation to call them "MARTIANS". - PCQ]* who provides, offers to provide, or arranges for others to provide, any "mortgage assistance relief service." It is intended to apply only to *for-profit* MARS providers.
- ***Deceptive Practices.*** MARS prohibits unfair and deceptive acts and practices in connection with mortgage assistance relief services. A MARS provider's claim is ''deceptive'' if there is ''a representation or omission of fact that is likely to mislead consumers acting reasonably under the circumstances, and that representation or omission is material.'' A representation is material if it is likely to influence consumers' decisions or conduct. It includes the following provisions:
  - Prohibits providers from instructing consumers to cease communication with their lenders or servicers;
  - Bars MARS providers from misrepresenting any material aspect of their services, including but not limited to the following non-exhaustive list:
    - The likelihood of negotiating, obtaining, or arranging a specific form of mortgage relief;

[3] I say "potentially," because to me, there is still an open question whether MARS even applies to real estate brokers who, in the ordinary course of their traditional real estate practice, also engage in short sales that include negotiations with sellers' lenders. The only real risk is if brokers advertise their short sale services as a "tool" in averting foreclosure.

- The amount of time needed to obtain the promised mortgage relief;
- The affiliation of the provider with the government, public programs, or consumers' lenders or servicers;
- Consumers' payment obligations under their mortgage loans;
- The terms or conditions of consumers' mortgage loans;
- The provider's refund and cancellation policies; and
- That the provider has performed the promised services or has the right to demand payment.

- The MARS rules give five examples of prohibited misrepresentations:
  - Misrepresentations about whether consumers will receive legal services;
  - Misrepresentations of the benefits and costs of using alternatives to for-profit MARS to obtain relief, such as working with the consumer's lender or servicer directly or consulting with a nonprofit housing counselor;
  - Misrepresentations regarding the amount or percentage of debts that consumers may save by purchasing MARS;
  - Misrepresentations regarding the total costs consumers must pay to purchase MARS; and
  - Misrepresentations regarding the terms, conditions, or limitations of any offer of MARS the provider obtains from the consumer's lender or servicer, including the amount of time the consumer has to accept or reject the offer.

- ***Liability for Providing "Substantial Assistance".*** MARS applies to *those who provide substantial assistance or support* to another whom they know or consciously avoid knowing is engaged in a violation of the MARS rules. This is more than casual or incidental assistance. Substantial assistance could include such critical support functions as lead generation, telemarketing and other marketing support, payment processing, back-end handling of consumer files, and customer referrals. Lead generators then sell the consumer information to MARS providers. If those who provide substantial assistance or support to MARS providers receive or become aware of information that reasonably calls into question the legality of the MARS provider's practices, they will be liable if they continue to assist and support that provider. In general, the determination of whether a person had the requisite knowledge will depend on a variety of factors such as the person's relationship to the MARS provider, the nature and extent of the person's degree of involvement in the operations of the MARS provider, and the nature of the provider's violations.

- ***Actions by States.*** States have authority to file actions against those who violate the MARS rules.

- ***Waiver Not Permitted***. It is a violation of the MARS rules for any person to obtain, or attempt to obtain, a waiver from any consumer.

- ***Record Keeping.*** Requires that providers maintain records for a period of two years. It requires that MARS providers keep:

  - All contracts or other agreements between the provider and any consumer for any MARS;
  - Copies of all written communications between the provider and any consumer occurring prior to the date on which the consumer enters into an agreement with the provider for any MARS;
  - Copies of all documents or telephone recordings;
  - All consumer files containing the names, phone numbers, dollar amounts paid, quantity of items or services purchased, and descriptions of items or services purchased, to the extent MARS providers obtain such information in the ordinary course of business;
  - Copies of all materially different sales scripts, training materials, commercial communications, or other marketing materials, including websites and weblogs; and
  - Copies of the documentation provided to the consumer in order to comply with the advance fee ban.

- ***Proof of MARS Results.*** MARS providers must provide consumers with documentary proof of the results they achieved before requesting or receiving payment. The rules require providers to give consumers a written offer—for the consumer to accept or reject—from the lender or servicer setting forth the mortgage relief they have obtained for the consumer, such as a forbearance agreement, short sale, or deed-in-lieu of foreclosure transaction; waiver of an acceleration clause; opportunity to cure default or reinstate a loan; or repayment plan. The documentation required is a comprehensive written instrument that memorializes a lender's or servicer's agreement to offer the concession.

- ***Attorney Exclusion***. Those providing MARS as part of the practice of law are exempted from most provisions subject to the following requirements:

  - They must be licensed in the state where the consumer *or* the dwelling is located;
  - They must comply with relevant state licensing and Bar requirements; and
  - They are exempt from the rules' advance fee ban if they set aside MARS fees in a client trust account and withdraw them only as they are earned.

  Here are some examples of activities that may be in violation of state laws and regulations, and thus would render attorneys ineligible for the exemption:

    - Failing to work diligently and competently on behalf of clients, *i.e.,* not taking reasonable efforts to obtain mortgage assistance relief;
    - Neglecting to keep clients reasonably informed as to the status of their matters, including the potential for adverse outcomes;

- Misrepresenting any material aspect of the legal services, including the likelihood they will achieve a favorable result, an affiliation with a government agency, or the cost of their services;
- Sharing legal fees for MARS-related services with non-attorneys;
- Forming partnerships with non-attorneys in connection with offering MARS; and
- Aiding MARS providers in engaging in the unauthorized practice of law, i.e., providing legal services without a license to do so.

➢ ***Lenders and Servicers.*** There is no blanket exemption based solely on their status. The exemption only applies to the actual loan holder or servicer of the loan. The exemption rules encompass both agents and authorized contractors acting on behalf of the actual lenders and servicers.

➢ ***Residential Dwelling Limitation.*** The MARS rules are limited to services that are offered to consumers who are obligated under loans secured by a ''dwelling'' or residence. A ''dwelling'' is defined as "…a residential structure containing four or fewer units, regardless of whether it is attached to real property." The term dwelling includes ''an individual condominium unit, cooperative unit, mobile home, manufactured home, or trailer.'' Finally, the definition of ''dwelling'' applies only to residences that are ''primarily for personal, family, or household purposes.'' The definition of ''dwelling'' includes second homes and rental properties of consumers, because it was believed that consumers who own such properties may seek help to avoid foreclosure on these properties. However, ''dwelling'' does not cover MARS offered in connection with commercial properties.

➢ ***MARS Disclosures.*** There are three main categories of disclosures:

- **<u>Disclosures in All "General" Commercial Communications</u>:**
  - The MARS provider ''is not associated with the government";
  - The MARS "is not approved by the government or your lender.''
  - "Even if you agree to use our service, your lender may not agree to change your loan.''
  - If the MARS provider advises, expressly or by implication, to stop making their mortgage payments, they must warn consumers: ''If you stop paying your mortgage, you could lose your home and damage your credit rating.''
- **<u>Disclosures in All "Consumer-Specific" Commercial Communications</u>:**
  - Include warnings for All General Commercial Communications above, plus the following:
  - The total amount the consumer will have to pay to purchase, receive, and use the service;
  - They may withdraw from the service at any time;

- They have the right to reject any offer of mortgage relief that the provider obtains from the servicer or lender; and

- If they withdraw they owe nothing to the provider.

- **Disclosures in All General Commercial Communications, Consumer-Specific Commercial Communications, and Other Communications:**

  - The MARS provider ''is not associated with the government''; and

  - The MARS "is not approved by the government or your lender.''

  - "Even if you agree to use our service, your lender may not agree to change your loan.''

  - If the MARS provider advises, expressly or by implication, to stop making their mortgage payments, they must warn consumers: ''If you stop paying your mortgage, you could lose your home and damage your credit rating.''

➢ ***Presentation of Disclosures.*** All MARS disclosures are subject to the following rules:

- ***Written Disclosures -*** MARS specifies that written disclosures must be easily readable; in a high degree of contrast from the immediate background on which it appears, and distinct from other text, such as inside a border; and in a distinct type style, such as **bold**. The disclosure must be communicated in the same languages that are substantially used in the commercial communication. They must "…appear parallel to the base of the communication and, unless otherwise specified, each letter of the disclosure text shall be, at a minimum, the larger of 12-point type or one-half the size of the largest character used in the name of the advertised website or telephone number to which consumers are referred for information on any MARS."

- ***Audio Disclosures –*** [Such as broadcast radio or streaming radio.] These rules say that MARS providers must deliver their required disclosures ''in a slow and deliberate manner and in a reasonably understandable volume and pitch.''

- ***Video Disclosures -*** Video communications include those that appear on television or are streamed over the Internet. The disclosures must be made simultaneously in both audio and video, the latter of which must be displayed for at least the duration of the audio disclosure and comprise at least four percent of the vertical picture height of the screen.

- ***Interactive Media -*** [Such as software, the Internet, or mobile media.] The disclosures must conform with the requirements for written, audio, and video disclosures. They must meet the ''clear and prominent'' rule. In addition, the disclosures must be provided in a way that the consumer cannot avoid the information, *i.e.*, it must be visible without the need to scroll down a Web page. The disclosures must be made on or immediately prior to the page on which the consumer takes any action or incurs a financial obligation. Finally, the rules require that the disclosures appear in text at least the same size as the largest character of the advertisement.

- ***Program-Length Media -*** Requires that disclosures in program-length television, radio, and Internet-based advertisements for MARS be presented at the beginning, near the middle,

and at the end of the advertisement. The disclosures must be delivered at different stages of the broadcast to make it more likely that consumers who join a broadcast in progress will receive them.

- ***Payment of Advance Fees.*** MARS prohibits the collection of fees until the provider has:
  - Secured a written and executed agreement *between the consumer and the lender or servicer* for mortgage assistance. The offer from the lender or servicer (e.g. consenting to short sale, deed-in-lieu, or modification) must be accompanied by the following:
    - "The notice must be made in a clear and prominent manner, on a separate written page, and preceded by the heading: ''**IMPORTANT INFORMATION FROM YOUR [name of lender or servicer] ABOUT THIS OFFER.**'' The heading must be in **bold** face font that is two-point-type larger than the font size of the required disclosure. "You may accept or reject the offer. If you reject the offer, you do not have to pay us. If you accept the offer, you will have to pay us [same amount as disclosed pursuant in written agreement with MARS provider] for our services.''
    - The MARS provider must also furnish the consumer with a *written notice from the consumer's lender or servicer* describing all "material differences'' between the terms, conditions, and limitations of the consumer's mortgage loan and those associated with the offer for mortgage relief. It must be preceded with the following disclosure: ''**IMPORTANT INFORMATION FROM YOUR [name of lender or servicer] ABOUT THIS OFFER**.'' The heading must be in **bold** face font that is two-point-type larger than the font size of the required disclosure and including but not limited to the following:
      - Principal balance; Contract interest rate, including the maximum rate and any adjustable rates, if applicable; Amount and number of the consumer's scheduled periodic payments on the loan; Monthly amounts owed for principal, interest, taxes, and any mortgage insurance on the loan; Amount of any delinquent payments owing or outstanding; Assessed fees or penalties; and Term

- ***Fines for Violation.*** $11,000 per day.

Conclusion. It seems that most Realtors® will voluntarily comply with the MARS rules by distributing the OREF forms to their seller-clients. That is fine - out of an abundance of caution. *Better to be safe, than sorry.* However, perhaps with a little help from the National Association of REALTORS®, the FTC can be persuaded to make a specific exclusion for licensed brokers conducting legitimate short sale transactions- so long as they are not promoted as a "foreclosure prevention technique". The existing state statutes and administrative rules are perfectly adequate to protect Oregon consumers.