



## Notice Of Default Sales N.O.D.

### Table of Contents

- I. **Introduction**
- II. **Legislative History**
- III. **Definitions**
- IV. **Legal Effects**
- V. **Exemptions from the Home Equity Sales Contract Law**
- VI. **Agency Selection and Safeguards**

### I. Introduction

A general understanding of the sale of a residence in foreclosure is essential for any real estate professional who handles residential properties.

The primary purpose of this memorandum is to assist the real estate licensee in adequately and safely representing the seller and the buyer of a residence in foreclosure, and to present the licensee with a working knowledge of general concepts for dealing with such situations. The highly technical forms, precise language, and exacting notice requirements mandated by law are not included here.

Whenever in doubt of their individual circumstances, readers should seek the advice of an attorney for legal advice in this highly technical area.

### II. Legislative History

Beginning in 1979, the California legislature enacted laws which sought to curb, under circumstances the legislature considered unscrupulous and fraudulent, business practices of certain individuals and firms (equity purchasers) who acquired homes in foreclosure from the owners (equity sellers). These laws were amended in 1990, 1997 and 2003. These transactions are entitled "Home Equity Sales Contracts," and the requirements are codified in California Civil Code Sections 1695 - 1695.17 ("Code") to strictly regulate the activities of an equity purchaser and his/her/their "representatives."

#### **Q 1. *Why did the legislature enact these laws?***

**A** These laws were enacted in response to practices that occurred in connection with sales of property in foreclosure. Although a variety of schemes were used, the results of such practices were generally the same. For example, loans, offers of services or sales contracts often involved an unsophisticated homeowner under financial duress signing complex documents with contractual terms which were financially impossible to meet. They frequently included transferring title to the equity purchaser at the same time as the contract was signed, giving the seller no opportunity to consider the transaction. Sometimes, by way of clandestine financial structuring or by hidden transfer language, the homeowner's equity and/or title was mistakenly transferred without the owner's intention to do so. The ultimate result was that the homeowner lost his/her property and/or equity to these unscrupulous individuals.

#### **Q 2. *What is the intent and purpose of Home Equity Sales Contracts law?***



**A** The intent and purpose of this law is to:

- Provide homeowners with information necessary to make informed, intelligent sales decisions;
- Require written sales agreements;
- Safeguard the public against deceit and financial hardship;
- Insure fair dealing in the sale and purchase of homes in foreclosure;
- Prohibit misleading representations;
- Restrict unfair contractual terms;
- Provide homeowners reasonable opportunity to rescind sales to equity purchasers; and
- Protect homeowners' equity.

(Cal. Civ. Code § 1695.)

### **III. Definitions**

**Q 3. *What is a Home Equity Sales Contract?***

**A** Basically, a Home Equity Sales Contract is any contract of sale between an equity purchaser and an equity seller of a residence in foreclosure. However, see the exemptions in Question 17. (Cal. Civ. Code § 1695.1(e).)

**Q 4. *In the above general definition, the word contract has been emphasized. Why is that?***

**A** The Code defines a Home Equity Sale Contract in very particular manner. This contract is defined as any contract, agreement, or arrangement, or any term thereof between an equity purchaser and equity seller incident to the sale of a residence in foreclosure. However, the Code additionally defines an equity contract as any offer incident to the sale of a residence in foreclosure between these parties. (Cal. Civ. Code § 1695.1(e).)

**Q 5. *Why would a mere offer be given the same protection as a contract?***

**A** Here again, the Code provides a far-reaching special protection to residential owners in foreclosure. Even before entering into a traditional contract, it is unlawful for any person to initiate or negotiate a sale of a residence in foreclosure to an equity purchaser if the person takes unconscionable advantage of the seller. (Cal. Civi. Code § 1695.13.)

**Q 6. *Who is an equity purchaser?***



**A** An equity purchaser is defined as any person who acquires title to any residence in foreclosure unless covered by one of the exemptions shown in Question 17 (Cal. Civ. Code § 1695.1(a)). However, the court of appeal has found this law to apply only to owners/victims who live in the residence subject to foreclosure. (*In re Phelps*, 93 Cal. App. 4th 451 (2001).)

**Q 7. Exactly what is a "residence in foreclosure"?**

**A** A residence in foreclosure means residential real property consisting of one to four family dwelling units one of which the owner (seller) occupies as his or her principal place of residence, and against which there is an outstanding notice of default properly recorded (Cal. Civ. Code § 1695.1(b)).

#### IV. Legal Effects

**Q 8. How do these laws impact the equity purchaser?**

**A** These laws require precise and exact conduct of the equity purchaser and various detailed written provisions. Briefly, the time period in which the seller must be allowed to rescind with no penalty and acts required by the equity purchaser before the right of cancellation has fully lapsed, are as follows:

- Allow equity seller up to five full business days after signing any equity contract or up to 8:00 a.m. of the trustee sale day, whichever occurs first, to cancel (Cal. Civ. Code § 1695.4);
- Do not make any untrue or misleading statements regarding value, proceeds, contract terms, seller's rights, or obligations;
- Do not induce equity seller to execute or accept any executed instrument of conveyance;
- Do not record any instrument of conveyance signed by the seller;
- Do not transfer or encumber or purport to transfer or encumber any interest in such property to any third party;
- Do not pay equity seller any consideration;
- Return any documents signed by equity seller within 10 days following receipt of notice of cancellation, without any conditions. (Cal. Civ. Code § 1695.6.)

**Q 9. What are the legal rights of an equity seller in the event these laws are violated?**

**A** An equity seller has been provided a multitude of legal rights under these laws in addition to the traditional legal rights of a party to a contract. If the equity purchaser violates any requirements in Question 8 or takes unconscionable advantage of the owner in foreclosure, the seller may file a court action for recovery of all damages, injunction, other equitable relief, or a combination of these remedies (Cal. Civ. Code § 1695.7). Furthermore, fraud or deceit upon the equity seller may result in criminal penalties up to \$10,000 (\$25,000 beginning on January 1, 2004) or one year in jail (Cal. Civ. Code § 1695.8).



**Q 10. What are the damages that an equity seller can recover?**

**A** In an action for damages for the above violation, the equity seller can recover:

- Actual damages;
- Attorney's fees and costs; and
- Mandatory exemplary damages in an amount not less than three times the seller's actual damages or a civil penalty of up to \$2500 if no exemplary damages are awarded. (Cal. Civ. Code § 1695.7.)

**Q 11. Is the equity seller provided other legal rights under the Code?**

**A** Yes. In addition to the right of cancellation after signing any contract with the equity purchaser, for five full business days or up to 8:00 a.m. of the trustee sale day, the seller has the following legal rights:

- Rescission of any transaction found to be unconscionable within two years of recordation of the conveyance (Cal. Civ. Code § 1695.14);
- Court protection from seller's waiver of any provision of these laws as being void (Cal. Civ. Code § 1695.10); and
- A declaration by the legislature that any contract provision which attempts or purports to limit the liability of the equity purchaser from damages resulting from the statement or conduct of his/her representative is void (Cal. Civ. Code § 1695.16).

**Q 12. Who is a "representative" of the equity purchaser?**

**A** Under the Code, a representative is a person who in any manner solicits, induces, or causes any property owner in foreclosure to transfer title to the equity purchaser (Cal. Civ. Code § 1695.15(b)).

**Q 13. How far-reaching is the definition of a "representative"?**

**A** A representative of an equity purchaser is also a person who solicits any member of the property owner's family or household to induce or cause the equity seller to transfer title to an equity purchaser. Thus, solicitation of a member of the equity seller's family, or even of mere household members, presumably regardless of blood relationship, is prohibited. (Cal. Civ. Code § 1695.15(b).)

**Q 14. What does the Code require of a representative of the equity purchaser?**

**A** A representative of the equity purchaser must:



1. Provide written proof to the equity seller that the representative has:
  - a valid, current California Real Estate Sales License (broker or salesperson); and
  - a bond from an admitted surety insurer in an amount equal to twice the fair market value of the property.
2. Provide a written statement, under penalty of perjury, that the agent:
  - has the above license;
  - has the above bond; and
  - has complied with the above by providing written proof to the equity seller.

The written statement under penalty of perjury shall be provided to both the equity seller and equity purchaser prior to transfer of any interest in the subject real property.

Should these requirements not be fulfilled, the equity seller may choose to render the purchase contract void. Even if the seller cancels, the equity purchaser is liable for all damages caused by the failure to comply with these requirements.

(Cal. Civ. Code § 1695.17.)

**Q 15. *Are such bonds by an admitted surety insurer available in California?***

**A** Such bonds are not currently available.

**Q 16. *Why was this apparently impossible bonding requirement placed on licensees?***

**A** The answer to this is somewhat unclear. The bonding requirement may have found roots in a section of the Code concerning the liability of equity purchasers. Under this section, an equity purchaser is liable for all damages resulting from any statement or act committed by his/her representative. Even though the equity purchaser may not always directly control every act of the representative, the law as written places indirect legal responsibility for such conduct on the purchaser of a residence in foreclosure -- a form of strict liability. The equity purchaser is also liable for his/her/their representative's conduct in any manner connected with the acquisition, receipt of any consideration from or on behalf of the equity seller, or the performance or non performance of any act prohibited or required by the Code.

As the legislative history indicates, because some equity purchasers turned to thinly-veiled corporations and independent contractors whom they controlled to circumvent the 1979 law, the legislature in 1990 imposed these requirements on all buyer's representatives.

#### **V. Exemptions from the Home Equity Sales Contract Law**

**Q 17. *Do these laws ever allow a buyer to purchase a residence in foreclosure without placing impossible restrictions on the buyer's representative?***

**A** Yes, when a buyer acquires title in the manner as follows:



- For the purpose of using the property as a personal residence;
- By a deed in lieu of foreclosure of any voluntary lien or encumbrance of record;
- By a deed from a trustee acting under the power of sale contained in a deed of trust or mortgage at a foreclosure sale;
- At any sale of property authorized by statute (such as a tax sale);
- By order or judgment of any court (such as probate or family law court); or
- From a spouse, blood relative, or blood relative of a spouse.

(Cal. Civ. Code § 1695.1(a).)

The Code has specifically excluded these buyers from the definition of an equity purchaser. Stated otherwise, these types of buyers are "non-equity" purchasers.

**Q 18. *Could you provide examples of these exceptions?***

**A** For example, an equity purchaser is normally not a purchaser at a trustee sale, a foreclosing holder of a trust deed or mortgage (beneficiary) who receives a deed in lieu of foreclosure, a transferee at a sale authorized by statute such as under a probate proceeding, or a transferee under a court-ordered sale such as in a marital dissolution proceeding.

In addition, persons who acquire title from their spouse, a blood relative, or a blood relative of their spouse are not equity purchasers under the Code. The exemption that applies to more situations than any other is that a person acquiring title to a residence in foreclosure for the purpose of making it a personal residence is not an equity purchaser.

**Q 19. *What is the impact upon a real estate licensee when s/he represents an exempt person?***

**A** A real estate licensee representing any of the above "non-equity" purchasers is exempted from the requirements of a surety bond and is also not subject to the liabilities imposed on an agent of an equity purchaser.

**Q 20. *Is a real estate licensee subject to the surety bond and other liabilities imposed by the Code when representing only the equity seller?***

**A** No. The Code does not impose these restrictions upon a representative of the equity seller only.

## **VI. Agency Selection and Safeguards**

**Q 21. *As a listing agent without an exempt buyer, what agency should I select?***



**A** The safest practice is to represent the seller exclusively. This agency relationship must be maintained unless a buyer of a residence in foreclosure fits clearly within one of the exemptions noted in Questions 17 and 18.

**Q 22.** *My buyer claims to be purchasing for purpose of using the property as a personal residence. However, I don't feel comfortable about that statement. What should I do?*

**A** Normally a licensee is not responsible for the hidden undisclosed true intent of a buyer. However, be aware of possible red flags that may arise. For example, the conduct and actions of the buyer may raise questions about his/her veracity when the loan application indicates non-occupier status or title vesting in another person.

**Q 23.** *What is the bottom line for licensees?*

**A** The real estate licensee must be fully aware of the special requirements and risks imposed when representing an equity purchaser of a residence in foreclosure. Unless the buyer is clearly within the noted exceptions and is therefore a "non-equity" purchaser, licensees cannot represent any other residential purchaser and still legally comply with bonding requirements because the bonds do not exist. Liabilities of an equity purchaser are specific, exceedingly broad, and potentially very costly. The same thing applies to real estate licensees acting as agents in a transaction.

Licensees should take care to handle home equity sales contracts in a manner that fully complies with California law, such as by acting as the agent of the equity seller only.

Another possible solution is for the purchaser to bring the property out of foreclosure by paying current the loan and then purchasing the property. Clearly this solution is not totally risk free.

**Q 24.** *Does C.A.R. have the applicable forms as required by this law?*

**A** Yes. A package of three forms are available for purchase through [www.rebs.com](http://www.rebs.com) or through WinFORMS®: the Notice of Default Purchase Agreement (C.A.R. Form NODPA), the Home Equity Explanation and Agency Agreement (C.A.R. Form HEAA), and the Notice of Cancellation of the Notice of Default Purchase Agreement (C.A.R. Form HENC). This tri-partite package of forms is for use only when an owner-occupant of residential property, against which a Notice of Default has been recorded, is selling the property to an investor purchaser. The HEAA describes the law regarding this particular type of transaction, the consequences for violating the law, and the withdrawal of the buyer's agent from the transaction. The NODPA is the actual purchase agreement printed in the statutorily required format. The HENC is the form the seller uses if the seller desires to rescind the sale within the statutory period.

**Q 25.** *Where may I get more information on the subject?*



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