Rescuing the Rescued: Stemming the Tide of Foreclosure Rescue Scams in Washington

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I. INTRODUCTION

As interest rates rise, adjustable-rate mortgage payments swell, and consumer debt grows, many Washington homeowners find themselves being pushed toward the brink of foreclosure.[1] At the same time, however, the booming housing market of recent years has led to home price appreciation that has greatly outpaced inflation.[2] Financially distressed homeowners may not realize that the spike in home values has created substantial home equity in their properties.[3] This confluence of financial distress and rising home values has created a nationwide epidemic of a type of mortgage fraud known as the foreclosure rescue scam (FRS).[4] A typical FRS involves the conveyance of a homeowner's property to a "rescuer" who promises to save the home from foreclosure, coupled with a lease-option agreement that makes the homeowner a tenant in the home he or she previously owned. This purported transactional "rescue" is soon followed by the former homeowner's eviction by the "rescuer." The former homeowner is left homeless; the "rescuer" walks away with

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1. Phuong Cat Le, *Homeowners Warned About Foreclosure 'Rescue' Scams*, SEATTLE POST-INTELLIGENCER, Sept. 21, 2006, at A1; *see also* Greg Griffin, *Foreclosing on the American Dream*, DENVER POST, Nov. 19, 2006, at K1.

2. STEVE TRIPOLI & ELIZABETH RENUART, NAT'L CONSUMER LAW CTR., DREAMS FORECLOSED: THE RAMPANT THEFT OF AMERICANS' HOMES THROUGH EQUITY-STRIPPING FORECLOSURE "RESCUE" SCAMS 7 (2005).

3. *Id.*

4. Editorial, *Preventing Mortgage Fraud*, 30 NAT'L MORTGAGE NEWS 44 (2006).

the property's equity.[5] "Rescuers," or foreclosure rescue scam artists (FRSAs),[6] target stressed homeowners who are on the brink of losing their homes.[7] Moreover, they focus on those who can least afford to be scammed: elderly and low-income homeowners.[8]

FRSAs easily identify distressed homeowners by monitoring recorded notices of default on government websites[9] or by subscribing to a private service that compiles lists of such notices.[10] Homeowners in default soon find themselves inundated by offers of help from FRSAs,[11] who try to create a personal connection with homeowners through phone calls and personal visits.[12] They promise a chance to start over but warn the homeowner that he or she must act quickly to save his or her home and must not contact a lawyer or the mortgage lender.[13] FRSAs promise to pay off the amount owed by the homeowner in return for the conveyance of the property; they then structure a lease-buyback arrangement that sets the scam victim up to fail.[14] At some point, the former owner inevitably misses an unaffordable rent payment and is unceremoniously evicted from the home he or she once owned.[15] Thus, the scam is complete: The FRSA keeps the home and its equity.[16] Part II of this Comment will further explore the intricacies of how this scam is accomplished.

While FRS victims have many remedies under existing statutes, these remedies are inadequate because they fail to holistically address the FRS problem. A successful statutory approach to combating the spread of this insidious scam must rest on three legs: education, enforcement, and litigation. First, homeowners facing foreclosure need timely warnings regarding the existence and prevalence of the FRS before the onslaught of FRSA solicitations begins. Next, in addition to education,

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5. TRIPOLI & RENUART, *supra* note 2, at 8.

6. FRSAs may also be referred to as "foreclosure consultants" or "foreclosure rescue specialists."

7. TRIPOLI & RENUART, *supra* note 2, at 5.

8. Nathaniel C. Nichols, *Home Alone: Home Mortgage Foreclosure Rescue Scams and the Theft of Equity*, 11 J. AFFORDABLE HOUS. & CMTY. DEV. L. 280, 280–81 (2002).

9. *See, e.g.*, King County Recorder's Office Official Public Records, http://www.metrokc.gov/recelec/records/ (last visited Mar. 18, 2007).

10. *See, e.g.*, foreclosure.com, http://www.foreclosure.com/ (last visited Oct. 18, 2006).

11. Le, *supra* note 1, at A1.

12. TRIPOLI & RENUART, *supra* note 2, at 9.

13. *Id.*

14. Le, *supra* note 1. In a lease-buyback arrangement, the homeowner surrenders title to the house but continues living there as a tenant, with the right to repurchase the property within the next few years. TRIPOLI & RENUART, *supra* note 2, at 8.

15. TRIPOLI & RENUART, *supra* note 2, at 9.

16. *Id.*

homeowners need effective enforcement of the statutes that are supposed to protect them. Finally, homeowners wronged by FRSAs need to be able to seek civil relief that both adequately compensates them for their losses and provides incentives to attorneys willing to represent them in these complex, time-consuming cases.

By making only minor amendments to existing statutes, the Washington legislature could accomplish all three goals, thereby significantly strengthening protections for financially distressed homeowners. Therefore, focusing on the State of Washington,[17] this Comment recommends amendments to the Equity Skimming Act (ESA),[18] Deeds of Trust Act,[19] Mortgage Lending Fraud Prosecution Account Act,[20] and the Consumer Protection Act (CPA).[21]

To fully illustrate the problem, Part II will examine the structure of a typical FRS and provide a case study of an actual FRS that took place in King County. Part III will then survey the range of statutory, common law, and equitable remedies available to FRS victims in Washington. Finally, Part IV recommends four state statutory amendments that will eliminate loopholes, strengthen enforcement, and educate potential victims.

II. BACKGROUND

A. Structure of a Foreclosure Rescue Scam

Homeowners become potential FRS victims when they default on their mortgage payments, leading to foreclosure under the Deeds of Trust Act.[22] This Act requires that a notice of the forthcoming foreclosure sale be sent to the homeowner.[23] Currently, only a notice of the foreclosure sale is required by the statute, even though this early contact with distressed homeowners offers a valuable opportunity to educate them about the existence and danger of FRSAs.[24]

Upon learning of the pending foreclosure sale, the FRSAs begin to circle. Their aim is to obtain a substantial portion of a defaulting

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17. Statutes regulating "foreclosure consultants" have been enacted in California, Colorado, Georgia, Illinois, Maryland, Minnesota, and Missouri. An analysis of such legislation lies outside of the scope of this Comment.

18. WASH. REV. CODE § 61.34 (2006).

19. *Id.* § 61.24.

20. *Id.* § 36.22.18.

21. *Id.* § 19.86.

22. *Id.* § 61.24.

23. *See id.* § 61.24.040(1)(b)(i).

24. *See infra* Part IV.B.

homeowner's equity without providing a material benefit in return.[25] To accomplish this, an FRSA first convinces the homeowner that he or she will prevent the foreclosure for a reasonable fee.[26] After obtaining the homeowner's trust by paying repeated visits and establishing a personal relationship, the FRSA purchases the house from the homeowner for a very low price, pays off the homeowner's mortgage debt, leases the home back to the homeowner for a year or two at an unaffordable rate, and gives the homeowner a repurchase option that he or she will be unable to exercise.[27] To complete the scam and abscond with the homeowner's equity, the FRSA simply sells the property for its fair market value after evicting the homeowner either for nonpayment of rent or because the lease has expired.[28]

Often, the FRS is complicated by the presence of a third-party "investor," who is commonly an accomplice of the FRSA.[29] In this version of the scam, FRSAs act as middlemen between the homeowner and the investor.[30] In return for their "services," FRSAs may collect fees from the homeowner for handling the transaction, split the homeowner's equity with the investor after the property has been resold, or both.[31]

An FRS necessarily involves a substantial amount of deceit, trickery, and exploitation,[32] making the elderly and those with cognitive disabilities especially susceptible.[33] FRSAs commonly use the following tactics to defraud their victims: (1) making promises to the homeowner but subsequently omitting them in the final documents; (2) having the homeowner sign incomplete documents and subsequently filling in the terms; (3) delaying the signing until the last moment before the foreclosure sale, thereby depriving the homeowner of better options and forcing him or her to sign whatever documents the FRSA presents; (4) charging excessive fees; and/or (5) failing to disclose material information about the proposed transactions.[34] In addition, some FRSAs employ a method known as "affinity marketing," in which they attempt to gain the victim's trust by demonstrating commonalities with the victim and persuading

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25. Steve Fredrickson & Eric Dunn, King County Bar Association Foreclosure Rescue Scams Continuing Legal Education Materials 2 (July 14, 2006) (unpublished manuscript, on file with the author).

26. *Id.*

27. *Id.* at 3.

28. *Id.*

29. *Id.* at 5.

30. *Id.*

31. *See id.*

32. *See id.* at 4.

33. *See id.*

34. *Id.*

him or her that they are on the same side.[35] A Spanish-speaking FRSA, for example, might exclusively target Spanish-speaking homeowners.[36]

The case study presented next provides an excellent example of a FRSA gaining the trust of the victim by demonstrating a commonality of personal issues.

B. Case Study

Amy Jones was a single woman in her fifties, living solely on disability income and acting as the sole caregiver for her adult son, who was severely mentally ill.[37] In the spring of 2001, Amy was unemployed and fell behind in the mortgage payments for the home she shared with her son. In March, a notice of trustee's sale was issued, stating that the house would be sold at public auction in June unless $6,290, the amount in arrears, was paid by June 18.

The June deadline passed. Shortly before the home was to be auctioned off, Rick Coburn, a broker at a well-known real estate company, appeared unsolicited at Amy's doorstep. Coburn told her that he knew her property was going to be auctioned. He gave her his business card and told her that he and his friend, the president of a mortgage company, were experienced in foreclosure matters and could help save her home. Coburn emphasized that he had helped many people in her situation. Amy declined his help, stating that she planned on delaying the sale by filing for bankruptcy the next day. Coburn departed, but not before ominously warning her that bankruptcy would not save her house or the equity she had accumulated.[38]

The very next day, Coburn's accomplice came to Amy's house. He introduced himself as Jim Rogers, the president of Coburn's mortgage company, and gave her his business card, which contained the slogan, "Providing Financial Solutions for a Brighter Tomorrow." Rogers reiterated that he could help save Amy's home, and he asked if he could come inside to discuss the matter. She declined, stating that she had just filed for bankruptcy that morning. Not one to be rebuffed, Rogers remained on the porch and began confiding to her about his personal life.

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35. TRIPOLI & RENUART, *supra* note 2, at 10.

36. *Id.*

37. Although names have been changed to protect the privacy of those involved, this case study is based on facts alleged in a complaint recently filed in King County Superior Court.

38. A bankruptcy petition would probably have only delayed Amy's loss of her house for a few months, as her income was insufficient to allow her to reorganize her debts, preserve her important assets, such as the house, and remain solvent. A sale of the home at fair market value, however, would likely have enabled her to both pay off her debt and retain her accumulated equity. *See* Fredrickson & Dunn, *supra* note 25, at 3.

Specifically, he discussed his difficult childhood and alcoholic father. Amy, in turn, opened up and told Rogers about her son's mental illness and her own struggles with depression.

Amy's bankruptcy petition caused the foreclosure sale to be postponed for four months, until October. In the months leading up to the sale, Coburn and Rogers visited or called her at least twenty times, pleading with her to let them help save her house. Coburn and Rogers never specifically explained how they would accomplish this. Amy assumed, however, that because Rogers ran a mortgage company, the assistance would involve refinancing her existing mortgage. Believing that Coburn and Rogers were truly interested in helping her, Amy divulged additional personal information to them during this period. Specifically, she confided that she continued to be severely depressed and that she could not afford to pay a lawyer to complete her bankruptcy action.

In October, Amy realized that time was running out. Her bankruptcy petition would soon be dismissed, and she would lose her home. Believing there was no alternative, she finally agreed to accept Coburn and Rogers's help. She filled out a loan application and sent it to Rogers. Shortly before the foreclosure sale, Coburn summoned her to his real estate company and asked her to sign four documents. Coburn was careful to keep Amy engaged in conversation as she signed the documents without reading them. Although she was not given copies of what she had signed, it later became apparent that she had executed: (1) a purchase-and-sale agreement describing a sale of her home to Coburn and Rogers for $160,000; (2) a statutory warranty deed conveying her home to Coburn and Rogers; (3) an option to repurchase the property within two years at seventy-five percent of its assessed value; and (4) a one-year lease stating that she would rent the property back from Coburn and Rogers at $1,400 per month.

After the mortgage loan, property taxes, and closing costs were paid off by Coburn and Rogers, Amy was left with $7,350. The amount of the loan at the time it was repaid was $148,250, and the home's value was assessed that year at $310,000, which meant that her equity was conservatively valued at $161,750. She had conveyed her equity to Coburn and Rogers for *less than five cents on the dollar*. Moreover, to repurchase her property before the option expired in two years, Amy would need to pay the duo approximately $242,250 (seventy-five percent of the 2003 assessed value), in addition to the monthly rent payments. In the unlikely event Amy was to somehow accomplish this feat, Coburn and Rogers would receive a $79,250 return on their $163,450 investment. A more likely outcome, of course, would be the expiration of the repurchase option and Amy's subsequent eviction, after which Coburn and

Rogers would sell the house for its full market value and pocket an even greater return.

Amy continued to live in her former home for the next two and a half years, until 2004. Although her monthly rent payment was initially $1,400 per month, Coburn and Rogers later raised it to $1,550 per month. As they were well aware, Amy had originally defaulted on her mortgage because she was unable to make regular payments of $1,480 per month on that loan. Knowing that they could not complete the scam while Amy was in the house, Coburn and Rogers, her purported rescuers, had set her up to fail.

But she didn't fail—somehow Amy managed to keep current with the payments. Coburn and Rogers, however, had a backup plan. In the summer of 2004, after the repurchase option had lapsed, they notified Amy that they would not renew her lease. In September, they evicted her, and she and her mentally ill son joined the ranks of the homeless. She was forced to move back in with her father, while her son resorted to sleeping in her car. In October, distraught over her situation, Amy attempted suicide by overdosing on sleeping pills.

Next, Part III of this Comment will examine existing remedies that Amy might pursue in attempting to regain her home and/or equity.

III. EXISTING REMEDIES IN WASHINGTON

A. State Remedies

The following sections of this Comment survey the various state bases of recovery for FRS victims. Many of the theories applicable in FRS litigation arise under state law.[39] First, statutory remedies under acts such as the CPA are examined. Second, remedies under common law theories such as fraud are discussed. Finally, equitable remedies such as the theories of equitable mortgage and unconscionability are considered. This Comment contends that the Washington legislature can

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39. *See* Equity Skimming Act, WASH. REV. CODE § 61.34 (2006); Mortgage Broker Practices Act, WASH. REV. CODE § 19.146 (2007); Credit Services Organization Act, WASH. REV. CODE § 19.134 (2006); Consumer Protection Act, WASH. REV. CODE § 19.86 (2006). The remedies discussed throughout Part III might also apply vicariously to a company employing an FRSA in certain circumstances. Fredrickson & Dunn, *supra* note 25, at 25–27. Vicarious liability aids FRS victims in obtaining relief because, while an individual FRSA may be judgment-proof, the employer company presumably will have deeper pockets. Establishing vicarious liability can be difficult for an FRS victim, however, because he or she must convince a fact-finder that the company has either given the FRSA actual authority to act on its behalf or manifested to a third party, based on a reasonable and objective interpretation, that the FRSA has apparent authority to act on its behalf. *See* Udall v. T.D. Escrow Svcs., Inc., 132 Wash. App. 290, 300, 130 P.3d 908, 913 (2006).

best protect vulnerable homeowners from FRSAs by taking action that recognizes and strengthens the three legs (education, enforcement, and litigation) of a holistic approach to preventing equity theft. Specifically, as recommended in Part IV, the legislature can best effectuate such protection by making minor amendments to the ESA,[40] Deeds of Trust Act,[41] Mortgage Lending Fraud Prosecution Account Act,[42] and the CPA.[43]

1. Statutory Remedies

a. Consumer Protection Act

The CPA, which prohibits unfair, deceptive, or fraudulent business practices,[44] can provide an FRS victim relief either standing alone or in conjunction with other statutes, but it offers an inadequate remedy because of a low damages cap. It assumes great significance in FRS litigation because it can provide the remedy for violations of other consumer protection statutes commonly violated by FRSAs.[45] The CPA fails to protect victimized homeowners, however, because its $10,000 cap on exemplary damages has not been raised since being established in 1971.[46] This paltry limit reduces the number of attorneys willing to represent FRS victims, discourages the victims themselves from vindicating their rights, decreases governmental efficiency, and fails to deter both actual and potential FRSAs.[47]

A plaintiff bringing a claim under the CPA must establish five elements: (1) the defendant committed an unfair or deceptive act or practice; (2) the act or practice occurred in trade or commerce; (3) the act or practice impacts the public interest; (4) the plaintiff suffered injury; and (5) the act or practice caused the injury.[48]

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40. WASH. REV. CODE § 61.34 (2006).

41. *Id.* § 61.24.

42. *Id.* § 36.22.181.

43. *Id.* § 19.86.

44. *Id.* § 19.86.920.

45. *See* Fredrickson & Dunn, *supra* note 25, at 28–29; *infra* Parts III.A.1.b–d, III.B.1–2.

46. 25 DAVID K. DEWOLF ET AL., WASHINGTON PRACTICE: CONTRACT LAW AND PRACTICE § 18-310.00 (2006).

47. *See infra* Part IV.D.

48. Westview Invs., Ltd. v. U.S. Bank Nat'l Ass'n, 133 Wash. App. 835, 854, 138 P.3d 638, 647 (2006). FRS victims pursuing a CPA claim may establish one or more of these elements by showing that the FRSA violated other statutes. For example, a violation of the Credit Services Organization Act establishes the first CPA element, *see* WASH. REV. CODE § 19.134.070(5) (2006); *infra* Part III.A.1.d, while a violation of the Mortgage Brokers Practices Act establishes the first three CPA elements, *see* WASH. REV. CODE § 19.146.100 (2006); *infra* Part III.A.1.c.

Unless established through the violation of another statute,[49] whether the first three elements are met are questions of fact.[50] If necessary, an FRS victim could meet the first CPA element by arguing, for example, that the FRSA committed unfair and deceptive acts either by delaying the closing date until immediately before the foreclosure sale or by arranging less favorable terms in a written transaction than were described orally.[51] To meet the second element, the homeowner could argue that the FRSA's conduct occurred in trade or commerce because the FRSA sought a fee for providing a commercial service.[52] To meet the third element, an FRS victim might argue that an FRSA's unfair or deceptive conduct implicates the public interest for four reasons: (1) the conduct usually takes place in the course of the FRSA's business; (2) most FRSAs advertise to the general public; (3) FRSAs generally actively solicit their victims; and (4) FRSAs typically occupy a superior bargaining position to the homeowner.[53]

Even if the first three elements are established, in order to prevail on his or her CPA claim, an FRS victim must establish the fourth and fifth elements without the assistance of the auxiliary statutes.[54] To meet the fourth element, the homeowner must establish that he or she was injured through the loss of his or her home and/or equity.[55] Finally, to meet the fifth element, the homeowner must prove that, but for the FRSA's unfair or deceptive conduct, the homeowner would have retained the home or equity he or she lost.[56]

If an FRS victim can meet all five elements, the CPA is a valuable weapon because it allows injunctive relief, the awarding of attorney's fees and court costs, and a discretionary award of exemplary damages, not to exceed $10,000, of up to three times the amount of actual damages.[57] As previously mentioned, the $10,000 cap has not been raised since it was first instituted in 1971.[58] Adjusted for inflation, $10,000 in 1971 is equivalent to roughly $50,000 today.[59]

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49. *See infra* Parts III.A.1.b–d, III.B.1–2.

50. *See* Fredrickson & Dunn, *supra* note 25, at 29.

51. *See* WASH. REV. CODE § 19.86.020 (2006).

52. *See id.* § 19.86.010(2).

53. *See* Svendsen v. Stock, 143 Wash. 2d 546, 559, 23 P.3d 455, 461 (2001).

54. *See infra* Parts III.A.1.b–d, III.B.1–2.

55. *See* Hangman Ridge Training Stables v. Safeco Title Ins. Co., 105 Wash. 2d 778, 792, 719 P.2d 531, 539 (1986).

56. *See id.* at 792–93, 719 P.2d at 539.

57. *See* WASH. REV. CODE § 19.86.090 (2006).

58. DEWOLF ET AL., *supra* note 46.

59. The Inflation Calculator, http://www.westegg.com/inflation/infl.cgi (last visited Nov. 25, 2006).

The legislature can brace the litigation leg of the holistic statutory approach by raising the cap on exemplary damages under the CPA from $10,000 to $50,000. While many homeowners in today's market hold equity exceeding $50,000, and an even higher cap would provide greater protection, it would be pragmatic for the legislature to approach this problem incrementally. An amendment that merely raises the cap to account for inflation should be easier to enact than one that doubles or triples the limit. Under the anachronistically low cap in place today, an FRS victim who loses $15,000 in equity (a relatively small amount in today's market) is barred from recovering any exemplary damages under the CPA. That same victim would be more willing to vindicate his or her rights if he or she could potentially recover $45,000 in exemplary damages. He or she would also benefit from a wider selection of experienced attorneys willing to take on the likely complex and time-consuming case. The filing of a lawsuit in which a larger award of exemplary damages is sought would give the FRSA a strong incentive to quickly agree to a settlement, thereby not only fairly compensating the victim but also lightening the court's docket. In addition, the increased liability for exemplary damages would provide a greater deterrent to other FRSAs contemplating preying upon a Washington homeowner.

As stated above, the CPA can afford an FRS victim relief either standing alone or by operating in conjunction with other statutes.[60] This Comment next examines these other statutes, together with common law and equitable remedies, that an aggrieved homeowner can utilize in attempting to regain his or her home and/or equity.

b. Equity Skimming Act

The ESA was enacted for the purpose of forbidding "equity skimming," but defines that practice so narrowly that it almost never applies in the FRS context.[61] Moreover, the ESA was enacted to address the problem of "persons . . . defrauding innocent homeowners of their equity interest . . . in residential dwellings under the guise of a purchase of the owner's residence."[62]

An FRSA commits an "act of equity skimming" under the ESA only if all of the following conditions are met: (1) an investor purchases a residential property from a homeowner; (2) the homeowner finances all or part of the purchase price; (3) the homeowner's right to receive the

60. *See infra* Parts III.A.1.b–d, Parts III.B.1–2.
61. *See* WASH. REV. CODE § 61.34.020(4) (2006).
62. *Id.* § 61.34.010.

balance of the purchase price is either not secured by a lien on the home or is secured by a lien inferior to a mortgage taken out by the investor; (4) the investor encumbers the property with a mortgage superior to any lien of the homeowner to recover the balance of the purchase price; (5) the investor uses proceeds from the mortgage for his or her own benefit rather than for the property; and (6) the investor defaults on the mortgage within two years.[63]

Although at first blush the ESA would appear to be directly applicable in FRS cases, most FRS scenarios actually fall outside its narrow definition of equity skimming.[64] The typical FRS does not qualify as an "act of equity skimming" for two reasons. First, the transactions are structured so that the homeowner does not finance any part of the purchase price. Second, the FRSA keeps the new mortgage current until he or she sells the property at fair market value, rather than defaulting on a home equity loan and absconding with its proceeds.[65]

The ESA provides for civil liability under the CPA if an FRSA happens to be sloppy enough to commit "an act of equity skimming" under the statute's constricted definition. An "act of equity skimming" establishes the first three of the five elements needed to prove a CPA violation.[66] Moreover, the commission of at least three such acts within a three-year period is defined by the statute as a "pattern of equity skimming."[67] Any person who willfully engages in a "pattern of equity skimming" is guilty of a class B felony,[68] and every "act of equity skimming" committed is considered a separate current offense for purposes of determining the sentencing range.[69]

While the ESA adequately provides for criminal and civil liability if its provisions are triggered, it fails to sufficiently protect Washington homeowners because its definition of equity skimming is unjustifiably narrow. The legislature could vastly improve the statute's efficacy by expanding this limited definition. The ESA was enacted to protect homeowners from people intent on defrauding them of their equity under the guise of a purchase of the homeowner's property.[70] Its constricted language, however, fails to protect homeowners from FRSAs. In the

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63. *See id.* § 61.34.020(4).

64. *See* Fredrickson & Dunn, *supra* note 25, at 37.

65. *Id.* at 39.

66. *See* WASH. REV. CODE § 61.34.040 (2006); *supra* Part III.A.1.a.

67. WASH. REV. CODE § 61.34.020(1).

68. *Id.* § 61.34.030. A class B felony is punishable by a maximum of ten years in prison, a fine of $20,000, or both. *Id.* § 9A.20.021(1)(b).

69. *Id.* § 61.34.030.

70. *Id.* § 61.34.010.

typical Washington scam, the FRSA obtains new financing that allows him to pay off the homeowner's loan in default; he or she subsequently sells the property at fair market value and pockets the homeowner's equity.[71] The mechanics of the scam put it outside the scope of the ESA, which requires either that the purchaser assume the existing mortgage[72] or that the seller finance some or the entire purchase price.[73]

Simply by amending the ESA slightly, the legislature could significantly bolster the enforcement and litigation legs of the holistic approach to fighting foreclosure rescue abuses. Specifically, it could create a new category within the definition of "act of equity skimming,"[74] which would broaden the ESA by bringing FRSAs within its scope. For example, an effective addition to the definition might state that a person commits an "act of equity skimming" if he or she: (1) purchases a dwelling from a seller who has a mortgage or deed of trust in default; (2) enters into a leaseback/repurchase transaction with the seller; (3) fails to reconvey the property to the seller at the end of the term specified in the transaction; and (4) commits a violation of the CPA[75] in the course of his or her dealings with the seller. Such an amendment would supply strength and relevance to a statute that has been rendered essentially useless by its overly narrow ambit.

c. Mortgage Broker Practices Act

The Washington legislature enacted the Mortgage Broker Practices Act (MBPA) to promote honesty and fair dealing in that industry, as well as to preserve public confidence in the lending and real estate community.[76] The statute is relevant in FRS litigation because some FRSAs are, or present themselves to the public as, mortgage brokers.[77] Any person who makes, or assists in obtaining, residential mortgage loans (or holds him- or herself out as being able to do so) for financial gain is a mortgage broker under the statute.[78] All mortgage brokers are required to be

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71. *See* Fredrickson & Dunn, *supra* note 25, at 39.

72. WASH. REV. CODE § 61.34.020(4)(a)(i) (2006).

73. *Id.* § 61.34.020(4)(b)(i).

74. *Id.* § 61.34.020(4).

75. *Id.* § 19.86. The typical FRSA regularly violates the CPA by committing a multitude of "unfair or deceptive" acts. For example, a FRSA might pressure the homeowner to enter the transaction by delaying the closing until immediately before the foreclosure sale; the FRSA might then draft transaction documents that are far less favorable than the oral description of the transaction. *See id.* § 19.86.020; Fredrickson & Dunn, *supra* note 25, at 30–31.

76. WASH. REV. CODE § 19.146.005 (2006).

77. *See* Fredrickson & Dunn, *supra* note 25, at 32.

78. WASH. REV. CODE § 19.146.010(12) (2006).

licensed.[79] As described below, the MBPA specifically prohibits a number of practices commonly engaged in by FRSAs.

The statute's efficacy in the fight against FRSs, however, is hampered by three factors. First, FRS victims must prove that their purported conveyances were, in fact, residential mortgage loans.[80] Second, the statute provides no protection if the FRSA is not a mortgage broker and does not hold him- or herself out to the public as one.[81] Finally, an FRSA who violates the MBPA can be convicted of only a misdemeanor.[82]

The MBPA prohibits a variety of conduct commonly engaged in by FRSAs. For example, mortgage brokers may not employ any "scheme, device, or artifice" to defraud someone; nor may they engage in any unfair or deceptive practices toward any person or obtain property by fraud or misrepresentation.[83] Likewise, a broker who fails to comply with any requirement of the Truth-in-Lending Act (TILA)[84] or the Real Estate Settlement Procedures Act (RESPA)[85] has also committed a violation of the MBPA.[86] In addition, the MBPA requires mortgage brokers, within three days of receiving an application or payment, to provide borrowers with a complete itemization and explanation of all fees and costs associated with the proposed loan, including a specification of all fees charged by the brokers themselves.[87] Moreover, under the MBPA, every contract between a mortgage broker and a borrower must be in writing and must contain the entire agreement.[88]

An FRSA who violates the MPBA may not face stiff sanctions. An MBPA violation is an "unfair or deceptive act or practice and unfair method of competition in the conduct of trade or commerce" that "vitally affect[s] the public interest"; it thus establishes the first three elements of the CPA, and a remedy may be sought under that statute.[89] A violation of the MBPA, or any rule or order of the director of the Department of

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79. *Id.* § 19.146.200.

80. *See id.* § 19.146.0201(7).

81. *See id.* § 19.146.010(12).

82. *Id.* § 19.146.110. Congress has recognized that the designation of fraudulent conduct as a misdemeanor can fail to provide "adequate deterrents" against such behavior. H.R. REP. NO. 95-393(II), at 53 (1977), *as reprinted in* 1977 U.S.C.C.A.N. 3039, 3055.

83. WASH. REV. CODE § 19.146.0201(1–3) (2006).

84. *See infra* Part III.B.1.

85. *See infra* Part III.B.2.

86. WASH. REV. CODE § 19.146.0201(11) (2006).

87. *Id.* § 19.146.030(1).

88. *Id.* § 19.146.040.

89. *Id.* § 19.146.100; *see supra* Part III.A.1.a.

Financial Institutions (DFI), is a misdemeanor.[90] Mortgage brokers (or those presenting themselves to the public as such) who run afoul of the MBPA may be fined or ordered to pay restitution by the director of the DFI.[91] The DFI investigates alleged violations of the MBPA by FRSAs, but takes a reactive approach to enforcement, acting only upon the receipt of a complaint.[92]

While the MBPA may be applicable in certain FRS cases, it is designed for standard mortgage lending situations and is intended to protect *borrowers* from commercial lenders.[93] To invoke the statute, an FRS victim must convince the court that the sale-leaseback transaction he or she executed was, in substance, an attempt to obtain a residential mortgage loan.[94] In addition, an FRS victim is not protected by the statute if the FRSA is not a mortgage broker and does not hold him- or herself out to the public as such.[95] Moreover, because a violation of the MPBA constitutes only a misdemeanor,[96] the strength of the statute is undermined and rendered a less effective tool in the fight against foreclosure rescue abuses.

d. Credit Services Organization Act

The Credit Services Organization Act (CSOA) regulates persons who claim that they can stop, prevent, or delay the foreclosure of a mortgage in return for financial gain.[97] A person offering such a service is faced with several restrictions under the CSOA: He or she must (1) obtain a $10,000 surety bond issued on the condition of compliance with the CSOA; (2) refrain from charging for mere referrals to other credit-repair retailers; (3) refrain from advising customers to make untrue or misleading statements to a credit reporting agency or potential lender;

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90. WASH. REV. CODE. § 19.146.110 (2006). A misdemeanor is punishable by a maximum of ninety days imprisonment, a fine of $1000, or both. *Id.* § 9A.20.021(3).

91. *Id.* § 19.146.220(2).

92. *See* E-mail from Steven C. Sherman, Financial Legal Examiner, Department of Financial Institutions, to the author (Feb. 7, 2007, 14:50 PST) (on file with author). In 2003, the Washington Legislature enacted the Mortgage Lending Fraud Prosecution Account Act, which established, for a term of three years, a one-dollar surcharge on the recording of each deed of trust, to be used by the DFI to pursue criminal prosecution of fraudulent activities relating to mortgage lending. S.H.B. 1081, 58th Leg., Reg. Sess. (Wash. 2003) (codified at WASH. REV. CODE § 36.22.181 (2006)). The legislature subsequently extended the surcharge until 2011. H.B. 2338, 59th Leg., Reg. Sess. (Wash. 2006).

93. WASH. REV. CODE § 19.146.005 (2006).

94. *See id.* § 19.146.0201(7).

95. *See id.* § 19.146.010(12).

96. *Id.* § 19.146.110.

97. *Id.* § 19.134.010(2)(a)(iii).

and (4) refrain from personally making untrue or misleading statements or engaging in fraudulent or deceptive conduct in connection with his or her business activities.[98]

Under this statute, an FRSA must provide a complete and detailed description of the services to be performed, along with the total amount that will be charged for those services.[99] He or she must also provide the homeowner with a statement that explains the homeowner's right to proceed against the surety bond and gives the name and address of the company that issued it.[100] The CSOA requires that a written contract be signed by the homeowner; the contract must contain essential terms of the agreement and a conspicuous statement of the homeowner's five-day right to cancel.[101] Furthermore, an FRSA violates the CSOA if he or she attempts to persuade the homeowner to waive any of the rights it provides.[102] In any event, a homeowner's attempted waiver of a CSOA right is void.[103]

FRSAs are likely to violate the CSOA in a number of ways.[104] For example, the typical FRSA might do any of the following: fail to obtain the required surety bond, make untrue or misleading statements to the homeowner, engage in fraudulent or deceptive conduct, fail to make the required disclosures, or disregard the five-day cancellation period.[105] A violation of the CSOA can lead to criminal penalties and civil liability.[106] A violator is guilty of a gross misdemeanor, and district courts are given equitable jurisdiction to restrain and enjoin ongoing violations.[107] In addition, a CSOA violation serves to establish the first of five elements needed by an FRS victim to prevail on a CPA claim.[108] Persons injured by violations of the CSOA may sue to recover actual and punitive damages, reasonable attorney's fees, and court costs.[109]

On its face, the CSOA appears to be a fairly well-crafted statute. Its provisions for both criminal and civil liability, as well as injunctive relief, apparently make it a useful tool for those victimized by FRSAs.

98. *Id.* § 19.134.020.

99. *Id.* § 19.134.050(3).

100. *Id.* § 19.134.050(4)–(5).

101. *Id.* § 19.134.060.

102. *Id.* § 19.134.070(1).

103. *Id.*

104. Fredrickson & Dunn, *supra* note 25, at 36.

105. *Id.* at 36–37.

106. WASH. REV. CODE § 19.134.070–.080 (2006).

107. *Id.* § 19.134.070(3). A gross misdemeanor is punishable by a maximum of imprisonment for one year, a fine of $5000, or both *Id.* § 9A.20.021(2).

108. *See id.* § 19.134.070(5); *supra* Part III.A.1.a.

109. WASH. REV. CODE § 19.134.080(1) (2006).

Because there is a lack of case law interpreting and applying the CSOA, however, the statute's true value to FRS victims has yet to be established.

In addition to statutory remedies, a victimized homeowner may also seek to be made whole under a number of common law theories. This Comment next explores, from the perspective of an FRS victim, the strengths and weaknesses of these potential avenues of relief.

2. Common Law Remedies

a. Fraud

Virtually any FRS will contain elements of fraudulent conduct.[110] Three types of fraud are prevalent in these scams: intentional misrepresentations, material omissions, and bad-faith promises.[111] An FRSA typically uses numerous forms of deception over the course of the scam in order to gain the homeowner's trust and confidence and to prevent the homeowner from pursuing logical methods of avoiding foreclosure, such as refinancing or selling the property.[112]

To establish a claim of intentional misrepresentation in Washington, a plaintiff must prove nine elements by "clear, cogent, and convincing evidence."[113] Although an FRSA's conduct may fairly be characterized as fraudulent, an FRS victim bringing an intentional-misrepresentation claim may often be vulnerable to a motion to dismiss, due to the large number of elements that must be established and the heavy evidentiary burden that must be carried.

The second type of fraud often seen in FRSs is characterized by the material omission, i.e., the failure to reveal a material fact within one's knowledge when one has a duty to speak.[114] For example, a homeowner in default might receive a solicitation from an FRSA claiming expertise in saving homes from foreclosure. The homeowner might then ask the FRSA what the homeowner can do to save the house. If the FRSA suggests that the homeowner sell the property to the FRSA and then

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110. Fredrickson & Dunn, *supra* note 25, at 13.

111. *Id.*

112. *Id.*

113. Guarino v. Interactive Objects, Inc., 122 Wash. App. 95, 126, 86 P.3d 1175, 1191 (2004) (citing Williams v. Joslin, 65 Wash. 2d 696, 697, 399 P.2d 308, 308–09 (1965)). The elements of intentional misrepresentation are (1) representation of an existing fact; (2) its materiality; (3) its falsity; (4) the speaker's knowledge of the truth; (5) the speaker's intent that the recipient will rely upon the fact; (6) ignorance on the part of the recipient; (7) reliance on the part of the recipient; (8) the recipient's right to rely; and (9) the recipient's resulting damage as a result of his or her reliance. *Id.*

114. Favors v. Matzke, 53 Wash. App. 789, 796, 770 P.2d 686, 690 (1989).

lease it back, but fails to disclose viable alternatives such as selling the property at fair market value or refinancing, the FRSA likely has breached a duty to disclose the material fact of the homeowner's alternatives.[115]

The third type of fraud relevant in FRS litigation is the bad-faith promise, which occurs when a person makes a promise that he or she does not, at that time, intend to keep.[116] An FRSA, for example, might promise a homeowner assistance in obtaining a loan in order to reacquire the property at the end of the lease period, with full knowledge that the homeowner will almost certainly lack the income necessary to acquire a loan for the buyback amount.[117]

If a court determines that fraud has occurred, one remedy at its disposal is the constructive trust. A court will impress a constructive trust on property when it finds that the property was acquired under circumstances indicating that the holder of legal title has been unjustly enriched at the expense of another interested party.[118] An FRS victim can use the constructive trust doctrine to seek recovery of either the victim's home or its equity.[119] He or she will be barred from recovering the property under this doctrine, however, if the FRSA has subsequently conveyed the property to a bona fide purchaser for value.[120]

In sum, the pursuit of a fraud claim may not provide as much protection as might be thought at first glance, due to the many elements that must often be established, the high evidentiary burden imposed, and the inability to recover the home from a bona fide purchaser. Implementing the holistic approach advocated for in this Comment, however, would help fill the gaps inherent in this theory of recovery.

b. Breach of Contract/Promissory Estoppel

Occasionally, the terms of an FRS transaction are fair or even advantageous to the homeowner facing foreclosure; FRSAs in such cases victimize the homeowner by failing to honor the agreed-to terms.[121] For

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115. *See id.*

116. *In re* Marriage of Lutz, 74 Wash. App. 356, 367–68, 873 P.2d 566, 572 (1994).

117. Fredrickson & Dunn, *supra* note 25, at 15.

118. Imagineering, Inc. v. Kiewit Pac. Co., 976 F.2d 1303, 1313 (9th Cir. 1992). An imposition of a constructive trust amounts to a holding that the wrongdoer is to be treated as if he had been a trustee for the victim of the fraud from the time he acquired title. Huber v. Coast Inv. Co., 30 Wash. App. 804, 810, 638 P.2d 609, 612 (1981) (citing G. BOGERT, TRUSTS AND TRUSTEES § 471 (2d rev. ed. 1978)).

119. Fredrickson & Dunn, *supra* note 25, at 16.

120. *See In re* Seaway Express Corp., 912 F.2d 1125, 1128 (9th Cir. 1990).

121. *See* Fredrickson & Dunn, *supra* note 25, at 22.

example, a homeowner might contract for an option to repurchase his or her home for a reasonable price after leasing for a year, only to see the FRSA double the price of the option when he or she tries to exercise it.[122] In this situation, the FRS victim can pursue a claim for breach of contract or, if a contract was never formed, the quasi-contractual theory of promissory estoppel.[123] Possible remedies for breach of contract and promissory estoppel include specific performance, compensatory damages, and expectation damages.[124]

An FRS victim should consider pursuing a breach of contract claim only in those rare cases where the terms of the contract favor him or her. In addition, aggrieved homeowners will likely find it difficult to prevail on a promissory estoppel claim because FRSAs are generally careful not to leave a paper trail of their many false promises.

c. Breach of Fiduciary Duty

Homeowners facing foreclosure often place heightened trust in the skill and expertise of an FRSA who is, or poses as, a real estate agent or mortgage broker.[125] Under these circumstances, an FRSA can become a fiduciary of the homeowner, which allows the homeowner to justifiably relax his or her guard and repose trust in the FRSA.[126] When such a relationship is exploited by an FRSA, the victim may possess a viable tort claim for breach of fiduciary duty.[127]

In Washington, real estate brokers owe fiduciary duties to their clients as a matter of law,[128] as do mortgage brokers.[129] Therefore, if an FRSA is neither a real estate broker nor a mortgage broker, an FRS victim will need to establish a fiduciary duty by implication. To establish such an implied duty, victims must show two things. First, they must

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122. *Id.* at 23.

123. *Id.* at 22–24.

124. *Id.* at 24.

125. *See id.* at 16.

126. *See* Liebergesell v. Evans, 93 Wash. 2d 881, 889–90, 613 P.2d 1170, 1175 (1980) (stating that a fiduciary relationship can arise *in fact* between parties regardless of their relationship *in law*).

127. *See id.*

128. Koller v. Belote, 12 Wash. App. 194, 195–96, 528 P.2d 1000, 1001–02 (1974) (quoting Mersky v. Multiple Listing Bureau of Olympia, Inc., 73 Wash. 2d 225, 437 P.2d 897 (1968)) (holding that real estate broker forfeited commission by failing to make a clear and express disclosure of his dual agency).

129. *See* Rushing v. Stephanus, 64 Wash. 2d 607, 612, 393 P.2d 281, 284 (1964) (quoting Mattieligh v. Poe, 57 Wash. 2d 203, 356 P.2d 328 (1960)) (holding that mortgage broker forfeited commission and was liable for clients' expenses due to his breach of fiduciary duty). *But see* Brazier v. Sec. Pac. Mortgage, Inc., 245 F. Supp. 2d 1136, 1143 (W.D. Wash. 2003) (finding no factual basis for an implied-in-law fiduciary duty between mortgage broker and client when contract specifically provided that broker was not client's agent).

demonstrate both that they placed their trust and confidence in an FRSA and that there was a resulting superiority and influence on the FRSA's part.[130] Second, they must demonstrate the existence of an agency relationship between themselves and the FRSA.[131]

Because FRS victims have lost their homes and equity, it should not be difficult for them to establish that they were injured by the breach of fiduciary duty. To prevail under this theory, however, victims must also establish that *but for the breach*, they would not have suffered the loss.[132] Homeowners have the burden of finding and proving specific fiduciary breaches that directly caused them to make decisions or take actions that led to the loss of their homes and equity.[133] FRS victims pursuing a breach of fiduciary duty theory will likely find this causation element the most difficult to establish.[134]

3. Equitable Remedies

a. Equitable Mortgage

Under the equitable mortgage doctrine, a court has the equitable power to declare that a deed purporting to convey title is in fact merely a mortgage conveying a security interest to the grantee.[135] This doctrine is critical in FRS litigation because an essential component of the scam involves the homeowner conveying his or her property title to the FRSA or a confederate.[136] FRS victims who prevail on an equitable mortgage claim may be able to recover and keep their homes if they are able to repay the amount that the FRSA spent to pay off the defaulted mortgage

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130. *See* Hood v. Cline, 35 Wash. 2d 192, 205, 212 P.2d 110, 118 (1949) (quoting Wheeler v. Yoakam, 136 Wash. 216, 219, 239 P. 557, 558 (1925)) (finding no fiduciary relationship between parties to land transaction where one neither reposed any particular confidence in the other nor relied upon any information he conveyed).

131. *See* Mullen v. N. Pac. Bank, 25 Wash. App. 864, 877, 610 P.2d 949, 957 (1980) (citing Moss v. Vadman, 77 Wash. 2d 396, 404, 463 P.2d 159, 164 (1969)) (holding that lender had no fiduciary duty to borrower to insure borrower's interest in vehicle that was collateral for loan). An agency relationship results from the manifestation of consent by one person that another shall act on his behalf and subject to his control, with a correlative manifestation of consent by the other party to act on his behalf and subject to his control. Skagit State Bank v. Rasmussen, 109 Wash. 2d 377, 388, 745 P.2d 37, 43 (1987) (quoting Moss v. Vadman, 77 Wash. 2d 396, 402–03, 463 P.2d 159, 164 (1969)).

132. *See* Miller v. U.S. Bank of Wash., N.A., 72 Wash. App. 416, 426, 865 P.2d 536, 543 (1994) (quoting Hansen v. Friend, 118 Wash. 2d 476, 479, 824 P.2d 483, 485 (1992)).

133. *See* Fredrickson & Dunn, *supra* note 25, at 19–20.

134. *See id.* at 19.

135. *See* Plummer v. Ilse, 41 Wash. 5, 9, 82 P. 1009, 1011 (1905).

136. Fredrickson & Dunn, *supra* note 25, at 8.

loan.[137] If they cannot repay the FRSA, they can at least sell their property at fair market value, repay the FRSA, and recover their equity.[138] On one hand, the evidence needed to prevail under an equitable mortgage cause of action will ordinarily be accessible; on the other, FRS victims must prove their cases under the daunting "clear, cogent, and convincing" evidentiary standard,[139] which can make it quite difficult for them to succeed.[140]

b. Unconscionability

Because the facts and circumstances of a typical FRS affront the sense of decency, a scam victim will often be able to assert a viable claim for relief on the ground that the transactions he or she entered into were unconscionable.[141] Parties to a contract are generally bound by its terms, but a court that finds a term unconscionable may either sever that term from the contract, leaving the contract otherwise intact, or declare the entire agreement void and unenforceable.[142] In Washington, a contract, or a term therein, may be invalid based on either procedural or substantive unconscionability.[143]

A court will find procedural unconscionability in the formation of a contract if a party lacked meaningful choice when entering into it.[144] An aggrieved homeowner might effectively demonstrate a lack of meaningful choice by establishing that he or she lacked sufficient knowledge to exercise other alternatives, such as refinancing or selling the property at fair market value; the homeowner could also show that actions by the FRSA rendered other alternatives infeasible.[145] To make the first showing, an FRS victim might demonstrate a lack of sufficient knowledge by introducing evidence of a lack of financial sophistication, cognitive

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137. *Id.* at 10.

138. *Id.*

139. *See* Pearson v. Gray, 90 Wash. App. 911, 916, 954 P.2d 343, 346 (1998).

140. Proving the existence of an equitable mortgage under this evidentiary standard is more difficult than it would be under the typical civil "preponderance" standard but easier than it would be under the criminal "beyond a reasonable doubt" standard. *See* Bland v. Mentor, 63 Wash. 2d 150, 154, 385 P.2d 727, 730 (1963). In establishing the creation of an equitable mortgage, the FRS victim's burden of proof may approach that of the criminal prosecutor's. *See* 5 KARL B. TEGLAND, WASHINGTON PRACTICE: EVIDENCE LAW AND PRACTICE § 301.3 (5th ed. 2007) (stating that the "clear, cogent, and convincing" standard requires *something* less than proof "beyond a reasonable doubt").

141. *See* Fredrickson & Dunn, *supra* note 25, at 11.

142. *See* Zuver v. Airtouch Commc'ns, Inc., 153 Wash. 2d 293, 320, 103 P.3d 753, 768 (2004).

143. *See* Al-Safin v. Circuit City Stores, Inc., 394 F.3d 1254, 1259 (9th Cir. 2005).

144. Adler v. Fred Lind Manor, 153 Wash. 2d 331, 348–49, 103 P.3d 773, 783 (2004).

145. Fredrickson & Dunn, *supra* note 25, at 12.

disabilities, limited English proficiency, illiteracy, or similar traits.[146] To make the second showing, an FRS victim could prove that the FRSA took steps to ensure that other alternatives were infeasible, including (1) delaying the FRS transaction until immediately before the foreclosure sale, so that it was too late to exercise other options; (2) amending the transactions terms at the last minute; (3) clouding the property's title with documents such as purchase-and-sale agreements in order to obstruct a sale to anyone other than the FRSA; or (4) initiating improvements to the property, so as to obstruct refinancing or sale to another party.[147]

FRS transactions often raise issues of substantive unconscionability as well. A court finds substantive unconscionability if a term or clause of a contract is excessively one-sided.[148] In making this determination, the court evaluates whether the term is "shocking to the conscience," "monstrously harsh," or "exceedingly calloused."[149] Many transactions executed in the course of an FRS will exhibit some of these one-sided aspects of substantive unconscionability, because these scams ultimately result in the homeowner losing most or all of his or her equity and the FRSA reaping a windfall.[150] In claims of substantive unconscionability, the party attacking a contract or term thereof bears the burden of proof.[151] The aggrieved homeowner might do this successfully by contrasting the typical home sale with the FRS transaction he or she actually entered into. Demonstrating this contrast will often be straightforward for the homeowner. A typical home sale results in the seller retaining accumulated equity, less reasonable fees and commissions. An FRS, on the other hand, leads to the homeowner keeping little or none of his or her equity.[152]

Despite the potential relief afforded by the doctrine of unconscionability, the most glaring danger for an FRS victim pursuing this type of claim is that he or she will simply not be able to persuade a court that there was unconscionability in the formation or substance of the instruments executed. In spite of the inequitable facts in the record, many

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146. *Id.*

147. *Id.*

148. *Adler*, 153 Wash. 2d at 344, 103 P.3d at 781 (quoting Schroeder v. Fageol Motors, Inc., 86 Wash. 2d 256, 260, 544 P.2d 20, 23 (1975)).

149. *See id.* at 344–45, 103 P.3d at 781 (quoting Nelson v. McGoldrick, 127 Wash. 2d 124, 131, 896 P.2d 1258, 1262 (1995)).

150. *See* Fredrickson & Dunn, *supra* note 25, at 12.

151. Tjart v. Smith Barney, Inc., 107 Wash. App. 885, 898, 28 P.3d 823, 830 (2001) (citing Schroeder v. Fageol Motors, Inc., 86 Wash. 2d 256, 262–63, 544 P.2d 20, 25 (1975)).

152. Fredrickson & Dunn, *supra* note 25, at 12.

courts will have little sympathy for homeowners who sign contracts and then subsequently claim to have not read or understood them before signing.[153] The education leg of this Comment's holistic approach is implicated here. Informing financially distressed homeowners about the existence and danger of the FRS, as early as possible, can help eliminate the possibility that they will later need to rely on an unsympathetic judge in order to regain their stolen equity.

In addition to state remedies, an FRS victim may choose to pursue remedies created by federal statute. The next Section surveys these potential avenues of relief.

B. Federal Remedies

While both the statutes and common law of Washington offer possible remedies for FRS victims, limited federal relief may also be available. Federal consumer protection statutes have been applied in FRS litigation.[154] Unfortunately, none of these federal forms of relief squarely addresses the needs of FRS victims. This section will briefly discuss TILA,[155] RESPA,[156] and the Racketeer Influenced and Corrupt Organizations Act (RICO).[157]

1. Truth-in-Lending Act

Congress enacted TILA so that potential borrowers could more easily compare the loan terms offered by potential lenders.[158] TILA requires that lenders disclose certain material terms on a model disclosure form prescribed by the Federal Reserve Board.[159] By requiring standardized disclosure of these material terms, Congress reasoned, potential borrowers will find it easier to compare the terms offered by various sources, thus enabling them to choose the best deal available.[160]

Not all FRSs fall under TILA, but it does offer significant advantages to FRS victims who can establish that their sale-leaseback

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153. *See* Larry A. DiMatteo & Bruce Louis Rich, *A Consent Theory of Unconscionability: An Empirical Study of Law in Action*, 33 FLA. ST. U. L. REV. 1067, 1092–1100 (2006) (analyzing 148 federal cases from 1968 to 2003 involving unconscionability and finding that the contract was held to be unconscionable in only 37.8% of the cases).

154. Fredrickson & Dunn, *supra* note 25, at 40–49. FRS victims litigating in state court should keep in mind that bringing claims under these statutes could result in the removal of the action to federal court under federal question jurisdiction. *Id.* at 40.

155. 15 U.S.C. §§ 1601–1667f (2006).

156. 12 U.S.C. §§ 2601–2617 (2006).

157. 18 U.S.C. §§ 1961–1968 (2006).

158. *See* 15 U.S.C. § 1601(a) (2006).

159. *Id.* § 1604(b).

160. *See* Fredrickson & Dunn, *supra* note 25, at 43.

transaction was, in substance, a loan from the FRSA to the victim.[161] If the plaintiff homeowner can both establish this and prove that he or she did not receive accurate material disclosures, then he or she has standing to bring a TILA complaint and may recover actual and statutory damages, attorney's fees, costs, and injunctive relief.[162] Most importantly, the homeowner may also rescind the transaction.[163] In addition, a homeowner who proves a TILA violation need not establish a causal relation between the violation and his or her damages in order to obtain relief.[164]

TILA violations can also trigger certain state law provisions. For example, a proven TILA violation not only constitutes a violation of the state MBPA but also establishes the first three elements needed to prevail on a state CPA claim.[165] Moreover, prevailing on a TILA claim can be relatively straightforward for a victim.[166] Indeed, victims can usually prove a violation by merely introducing into evidence the transaction documents they signed with the perpetrators of the scam.[167]

To pursue a TILA claim, however, an FRS victim must hurdle three significant obstacles. First, for the statute to apply, the victim must convince the court that the sale-leaseback transaction was actually a loan in substance.[168] Second, the FRS victim must demonstrate that the FRSA meets TILA's narrow definition of "creditor," i.e., a lender who "regularly extends" credit.[169] Finally, some FRS victims will be unable to recover their homes under the TILA rescission remedy because that remedy usually expires when the FRSA resells the property.[170] Thus, under TILA, an FRS victim whose home has been sold to a bona fide purchaser may be limited to seeking damages, fees, and costs.[171]

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161. *See In re* Hanley, 111 B.R. 709, 713 (Bankr. C.D. Ill. 1990) (whether a purported rental agreement-purchase option is a credit agreement for TILA purposes is a question of fact).

162. 15 U.S.C. § 1640 (2006).

163. *Id.* § 1635.

164. *See, e.g.*, Huff v. Stewart-Gwinn Furniture Co., 713 F.2d 67, 69 (4th Cir. 1983) (minor violations of TILA impose liability even if consumer was not misled).

165. Brazier v. Sec. Pac. Mortgage, Inc., 245 F. Supp. 2d 1136, 1142 (W.D. Wash. 2003); *see supra* Parts III.A.1.a, III.A.1.c.

166. Fredrickson & Dunn, *supra* note 25, at 48.

167. *Id.*

168. *See In re* Hanley, 111 B.R. 709, 713 (Bankr. C.D. Ill. 1990).

169. *See* Eby v. Reb Realty, Inc., 495 F.2d 646, 649–50 (9th Cir. 1974). For example, under TILA, a person who has extended credit more than 25 times in the current or preceding calendar year, or one who has extended credit secured by a dwelling more than five times in the current or preceding calendar year is considered a lender who "regularly extends" credit. 12 C.F.R. § 226.2(a)(17) (2006).

170. *See* 15 U.S.C. § 1635(f) (2006).

171. *See id.* § 1640.

In sum, TILA can play an important role in FRS litigation, but its usefulness is hampered by the hurdles and limitations described above. Rather than forcing FRS victims to rely on this frayed federal safety net, the Washington legislature could better protect its constituents by strengthening the three legs of the holistic statutory approach proposed in this Comment.

2. Real Estate Settlement Procedures Act

RESPA governs certain aspects of residential real estate closings.[172] Two aspects of RESPA are important in FRS cases. First, it applies in almost all residential real estate transactions involving mortgage loans and requires the closing agent to prepare a "HUD-1 Settlement Statement" (HUD-1) and distribute it to the borrower, seller, and lender at or before the closing.[173] Second, RESPA prohibits giving or receiving unearned fees or kickbacks relating to a closing involving a federally regulated mortgage loan.[174]

The HUD-1 is a standard form developed by the United States Department of Housing and Urban and Development (HUD).[175] The agent conducting the closing must use the form to clearly itemize all charges imposed on both the borrower and the seller if a federally related mortgage loan is involved.[176] Because the HUD-1 mandates disclosure of material information about a transaction, such as the sale price of the property, the funding source, the parties paid, and fees and charges, not only is this form key to understanding the details of an FRS, but it is also a critical piece of evidence in litigation.[177] Unfortunately for an FRS victim, RESPA's HUD-1 requirement is enforceable only through HUD administrative action.[178]

The RESPA prohibition of unearned fees and kickbacks enables a scam victim to challenge the various fees and charges that FRSAs commonly pile on transactions in order to maximize their equity theft.[179] For example, an FRS victim might successfully challenge an escrow agent's charge for an "account processing fee." A court may find this charge to

172. 12 U.S.C. § 2601 (2006).

173. *See* 24 C.F.R. § 3500.8(a) (2006). FRSAs often rely on mortgage loans to finance their acquisition of properties, which subjects them to RESPA requirements. *See* Fredrickson & Dunn, *supra* note 25, at 39.

174. 12 U.S.C. § 2607 (2006).

175. *Id.* § 2603(a).

176. *Id.*

177. *See* Fredrickson & Dunn, *supra* note 25, at 41.

178. *Id.* at 42.

179. *Id.* at 41.

be an unearned fee for RESPA purposes if the fee is duplicative or correlates to a nonexistent or nominal service on the part of the escrow agent.[180] Like a HUD-1 violation, a violation of this provision triggers administrative enforcement; in addition, however, this type of transgression also creates a private right of action.[181] Under RESPA, an FRS victim charged an unlawful fee in a closing may recover three times the amount charged through a civil action, as well as court costs and attorney's fees.[182] Moreover, a RESPA violation both constitutes a per se violation of the state MBPA and establishes the first three elements needed to prevail on a state CPA claim.[183] While undoubtedly useful to an FRS victim for recouping bogus closing costs, RESPA's efficacy as a bar to equity theft is marginal.

3. Racketeer Influenced and Corrupt Organization Act

The final federal statute discussed here that may possibly be of use to FRS victims is RICO. The statute is applicable in the FRS context due to its prohibition against collecting "unlawful debts."[184] The statute's definition of an "unlawful debt" encompasses any loan with an interest rate at least twice that of the maximum allowed under a state's usury law.[185] In cases involving most legitimate residential mortgage loans issued by lenders regulated by federal agencies, federal regulations preempt state usury laws, thus allowing higher interest rates than would otherwise be permitted.[186] Because FRSAs are not federally regulated lenders, however, they *are* subject to state usury laws.[187] As a result, FRSAs frequently violate RICO by lending money, under the guise of a conveyance, to homeowners at an interest rate exceeding twice that allowed under Washington law.[188]

RICO provides several forms of relief for an FRS victim. For example, anyone who is injured "in his person or property" by a RICO violation may seek a remedy of treble damages, costs, and attorney's fees in federal court.[189] Additionally, district courts possess authority to order

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180. *See* 24 C.F.R. § 3500.14(c) (2006).

181. 12 U.S.C. § 2607(d)(2) (2006).

182. *Id.* § 2607(d)(2).

183. Brazier v. Sec. Pac. Mortgage, Inc., 245 F. Supp. 2d 1136, 1142 (W.D. Wash. 2003); *see supra* Part III.A.1.a; III.A.1.c.

184. 18 U.S.C. § 1962 (2006).

185. *Id.* § 1961(6). At present, the maximum interest rate under Washington's usury law is approximately twelve percent. *See* WASH. REV. CODE § 19.52.020 (2006).

186. *See* 12 U.S.C. §§ 1735f, 3801–3806 (2006).

187. *See* Fredrickson & Dunn, *supra* note 25, at 49.

188. *Id.*

189. 18 U.S.C. § 1964(c) (2006).

injunctive relief under the statute.[190] Finally, RICO also has conspiracy provisions that may come into play in the FRS context; they assist in attaching liability to the multiple actors, both individual and corporate, commonly involved in these swindles.[191]

Unfortunately, there are two limitations under RICO that may put an FRS victim at a significant disadvantage in court. First, the victim will need to establish that the apparent conveyance of the property to the FRSA was, in fact, a loan subject to Washington's usury law.[192] Second, a victim whose strategic interests would best be served by litigating in state court must nevertheless file a RICO claim in federal court.[193] While RICO is a valuable tool in the FRS victim's arsenal, it plainly will not stem the tide of foreclosure rescue abuses on its own.

TILA,[194] RESPA,[195] and RICO[196] are the federal statutes most likely to be invoked by FRS victims attempting to recover their stolen homes and equity. Aggrieved homeowners may, of course, concurrently pursue the state remedies previously discussed.[197]

IV. RECOMMENDATIONS

As discussed previously in Part III, FRS victims have a variety of potential remedies available to them. For example, an aggrieved homeowner could pursue a state statutory remedy under the CPA, a federal statutory remedy created by TILA, a remedy under a common law theory such as breach of fiduciary duty, or an equitable remedy based upon the doctrine of unconscionability. In an appropriate case, the homeowner might pursue all four claims.

Existing remedies, however, are each inadequate to some extent, as evidenced by the growing prevalence of FRSs. This Comment recommends the adoption of a holistic approach to combating this type of insidious scheme, one that emphasizes each of the three crucial legs of this strategy: education, enforcement, and litigation. The Washington legislature can implement this approach, thus greatly strengthening the protections afforded vulnerable homeowners, simply by making minor amendments to existing statutes. Specifically, the legislature should

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190. *Id.* § 1964(a).

191. Fredrickson & Dunn, *supra* note 25, at 49.

192. Similar "substance-over-form" arguments are of use to FRS victims pursuing equitable mortgage or TILA claims. *See supra* Parts III.A.3.a, III.B.1.

193. *See* 18 U.S.C. § 1964(a) (2006).

194. 15 U.S.C. §§ 1601–1667f (2006).

195. 12 U.S.C. §§ 2601–2617 (2006).

196. 18 U.S.C. §§ 1961–1968 (2006).

197. *See supra* Part III.A.

amend the ESA,[198] the Deeds of Trust Act,[199] the Mortgage Lending Fraud Prosecution Account Act,[200] and the CPA.[201]

A. Make the Equity Skimming Act Applicable to Foreclosure Rescue Scams

As explained above, the ESA fails to protect homeowners from FRSAs because it is too narrowly drawn.[202] Thus, the typical Washington FRS falls outside of the scope of the ESA. The legislature, however, can easily strengthen the enforcement and litigation legs of a holistic approach to fighting these scams by slightly amending the ESA. The amendment should create a new category within the definition of "act of equity skimming"[203] that describes the operation of an actual FRS. An effective addition to the definition might state that a person commits an "act of equity skimming" if he or she: (1) purchases a dwelling from a seller who has a mortgage or deed of trust in default; (2) enters into a leaseback/repurchase transaction with the seller; (3) fails to reconvey the property to the seller at the end of the term specified in the transaction; and (4) commits a violation of the CPA at some point in the course of his or her dealings with the seller.

In its battle against FRSAs, the State of Washington would be well served by a broader ESA that actually accomplishes what it currently only purports to do. The legislature enacted the ESA in order to put a stop to equity skimming;[204] without a broadening of its scope, this intent will be thwarted and the statute will remain a dead letter.

B. Amend the Deeds of Trust Act to Require Lenders to Send Defaulting Homeowners Notice Describing Foreclosure Rescue Scams and Listing Counseling Opportunities

While this Comment has discussed a variety of post-FRS remedies, many of these scams could be prevented outright if homeowners facing foreclosure were warned of the danger FRSAs pose and were apprised of the various alternatives available to persons in their situation. A potential victim needs early notice of the existence and prevalence of this type

198. WASH. REV. CODE § 61.34 (2006).

199. *Id.* § 61.24.

200. *Id.* § 36.22.18.

201. *Id.* § 19.86.

202. *See supra* Part III.A.1.b.

203. WASH. REV. CODE § 61.34.020(4) (2006).

204. *Id.* § 61.34 (finding "this form of real estate fraud and abuse" to be "contrary to the public policy of this state").

of scam before the first seemingly friendly face appears at his or her door. Homeowners who have had notices of default filed against them are often bombarded with FRS offers; FRSAs would find far fewer homeowners willing to deal with them if homeowners in default were informed of the availability of low-cost financial counseling services.[205]

Giving consumers the information they need to protect themselves at the time of default supports the education leg of the holistic statutory approach advocated in this Comment. Potential FRS victims need timely information that helps them understand that it is almost always better to sell or refinance their home at the outset of the foreclosure process than to attempt rescue measures, such as the FRS, that inevitably lead to a total loss of equity.[206]

To best effectuate this educational goal, the legislature should amend the Deeds of Trust Act[207] to assure that homeowners in default are warned of the existence of foreclosure rescue abuses and notified of the availability of low-cost homeownership counseling.[208] The statute does not currently require the lender, at the time of default, to take affirmative steps that would help prevent FRSs. Instead, it requires only that a trustee foreclosing a deed of trust transmit a copy of the notice of trustee's sale and the notice of foreclosure to the homeowner.[209] In addition to these two notices, the statute should require that the beneficiary also include a conspicuous notice (perhaps printed on brightly colored paper) both warning of and describing the FRS and including a listing of free or low-cost homeowner counseling services.[210]

Of course, some potential FRS victims would undoubtedly overlook such a notice, due not only to the stress inherent in their situation but also to the oppressive volume of rescue offers such homeowners commonly receive in the mail once a notice of default is filed. Many others, however, are likely to be helped by such a notice—an educated potential victim is a non-victim. Moreover, the cost to mortgage lenders and other beneficiaries of deeds of trust would be minimal: merely the

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205. *See* NORMA PAZ GARCIA, CONSUMERS UNION, DIRTY DEEDS: ABUSES AND FRAUDULENT PRACTICES IN CALIFORNIA'S HOME EQUITY MARKET pt. 4 (1995) *available at* http://www.consumersunion.org/pub/core_newmoney/001968.html.

206. *See id.*

207. WASH. REV. CODE § 61.24 (2006).

208. *See* TRIPOLI & RENUART, *supra* note 2, at 50.

209. WASH. REV. CODE § 61.24.040 (2006).

210. *See* TRIPOLI & RENUART, *supra* note 2, at 50. Free or low-cost counseling on the topic of foreclosure avoidance currently exists. *See, e.g.*, Solid Ground Housing Counseling, http://www.solid-ground.org/Programs/Housing/Counseling/Pages/default.aspx (last visited Nov. 12, 2007).

price of one or two sheets of paper. While the costs of this proposal are negligible, the potential benefits are staggering. Washington homeowners can no longer afford to be ignorant of the growing threat the FRS poses to their equity.

C. Amend the Mortgage Lending Fraud Prosecution Account Act to Raise the Mortgage Recording Fee Surcharge that Funds Foreclosure Rescue Scam Investigations by the Department of Financial Institutions

In 2003, the Washington legislature enacted the Mortgage Lending Fraud Prosecution Account Act, which established, for a term of three years, a one-dollar surcharge on the recording of each deed of trust, to be used by the DFI to pursue criminal prosecution of fraudulent activities within the mortgage lending process.[211] In 2006, the legislature extended the surcharge until 2011.[212] The surcharge allows the DFI, which enforces the MBPA, to hire its own prosecutors, rather than having to persuade overworked local prosecutors to take on its cases.[213] As of mid-2006, the DFI had hired three enforcement attorneys and two criminal attorneys and was prosecuting six FRS cases using surcharge funds.[214]

The legislature can strengthen the enforcement leg of the holistic statutory approach recommended in this Comment by boosting the DFI's enforcement capabilities against FRSAs through an increase in the statutory recording surcharge. A fivefold increase, for example, would result in a nominal recording fee of only five dollars, but would allow the DFI to substantially expand its roster of prosecutors. Currently, the DFI investigates violations of the MBPA by FRSAs only upon receiving a complaint.[215] An influx of funding from a surcharge increase would empower the DFI to investigate FRSAs in a more aggressive and proactive fashion. Ramping up enforcement via this simple and painless method would significantly enhance the State's ability to protect the most vulnerable segment of its homeowning population.

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211. S.H.B. 1081, 58th Leg., Reg. Sess. (Wash. 2003) (codified at WASH. REV. CODE § 36.22.181 (2006)).

212. H.B. 2338, 59th Leg., Reg. Sess. (Wash. 2006).

213. Editorial, *Preventing Mortgage Fraud*, 30 NAT'L MORTGAGE NEWS 44 (2006).

214. *Id.*

215. *See* E-mail from Steven C. Sherman, Financial Legal Examiner, Department of Financial Institutions, to the author (Feb. 7, 2007, 14:50 PST) (on file with author).

D. Raise the Consumer Protection Act's Cap on Exemplary Damages

As previously mentioned, the CPA's cap on exemplary damages has not budged since 1971 and is in dire need of an upward revision.[216] The CPA authorizes exemplary damages in order to give citizens an incentive to act as private attorney generals.[217] Because the Office of the Attorney General lacks the resources to fully enforce the CPA, private suits benefit the public by supplementing public enforcement.[218] A low cap on exemplary damages discourages citizens from bringing suit against violators and thus weakens the deterrent effect of the statute.[219]

The legislature should strengthen the litigation leg of the holistic approach to fighting FRSAs by raising the CPA's cap on exemplary damages from $10,000 to $50,000. An increased limit on this type of liability would have several benefits. First, a raised cap would increase the number of attorneys willing to represent FRS victims. Second, it would encourage victims to fight back against those who would rob them of their homes and their equity. Third, an increased limit on exemplary damages would increase judicial efficiency by promoting settlements between FRSAs and their victims. Fourth, a higher cap would encourage more private suits against CPA violators, which would, in turn, lighten the Attorneys General enforcement burden. Finally, greater liability in this area would deter both actual and potential FRSAs from committing future scams. A hike of the CPA's cap on exemplary damages is long overdue. By implementing an increase from $10,000 to $50,000, which merely tracks inflation, the legislature can significantly strengthen the enforcement and litigation legs of the holistic statutory approach to preventing equity theft.

V. CONCLUSION

Amy Jones's plight, as previously recounted, demonstrated how easily an FRSA can turn a bad situation into a disastrous one.[220] Homeowners in Amy's situation desperately want to believe that the FRSA will allow them to start over and wipe the slate clean. As illustrated by Amy's typical experience, however, the duped homeowner inevitably conveys the property for a pittance and is then abruptly removed from

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216. *See supra* Part III.A.1.a.
217. S. 60-5815, 1st Reg. Sess., at 2 (Wash. 2007).
218. *Id.*
219. *See id.*
220. *See supra* Part II.B.

the home he or she once owned. The FRSA sells the home for fair market value, pockets its equity, and moves on to seek his or her next victim.

If this Comment's recommendations had been in place when Amy ran into financial difficulties, her story would likely not have been so tragic. If her lender had been required to send her a notice that described the danger of FRSs and contained information on homeownership counseling, Amy would have been aware of her viable options, such as selling her home at fair market value or refinancing. She probably would have recognized Coburn and Rogers's pitch as an FRS, thus allowing her to dismiss their duplicitous offer out of hand. Because the increase in the recording surcharge would have bolstered the DFI's enforcement of the MBPA, Coburn and Rogers's operation might even have been shut down before they had the opportunity to approach Amy.

Even if she ignored the notice and fell victim to the scam, Amy's alternatives for pursuing the return of her equity would have been strengthened under the approach this Comment recommends. The amended ESA would have properly treated Coburn and Rogers's conduct as an "act of equity skimming," which would have greatly eased Amy's pursuit of a CPA claim; the ESA violation would have established three of the five elements needed to recover under that statute. Prevailing under the CPA would have entitled Amy to actual damages, court costs, attorney's fees, and exemplary damages of up to $50,000. In addition, if it could be shown that Coburn and Rogers had committed two other "acts of equity skimming" within a three-year period, they each would have faced ten years in prison and a $20,000 fine.

As the number of Washingtonians facing foreclosure increases,[221] one may expect a concomitant increase in the volume of FRSs targeting this vulnerable segment of our population. Any attempt to stem this rising tide of fraud and deception must rest on three legs: education, enforcement, and litigation. Homeowners in default must be made aware of their options, any of which are doubtless preferable to transacting with an FRSA. Enforcement of existing laws proscribing the conduct inherent in the typical scam must be ramped up in order to keep pace with the rising foreclosure rate. Homeowners unlucky enough to fall victim to a FRS must have access to tenacious attorneys who are able and willing to recover the homes and equity stolen from their clients.

A home is often the most valuable asset a person will ever own. By fine-tuning the laws implicated in foreclosure rescue abuses, the

221. Aubrey Cohen, *Walls Closing in on Homeowners*, SEATTLE POST-INTELLIGENCER, Mar. 17, 2007, at A1.

Washington legislature can and should enhance the protection extended to such a vital part of its constituents' lives.