

New FTC Rule Requires Short Sale Disclosures

The Federal Trade Commission (“FTC”) has issued a final rule that may impact real estate professionals who represent clients involved in a short sale transaction. Depending on certain factors, the rules may require real estate professionals to make certain disclosures to consumers if they negotiate a short sale with a lender, advertise short sales experience, or take upfront fees from short sale sellers. The MARS rules took full effect on January 31, 2011- [click here](#) to view the MARS rule.

Background

In November 2010, the FTC published the final Mortgage Assistance Relief Services final rule (“MARS rule”). The MARS rule is primarily directed at companies that offer loan modification services to consumers. When a company is marketing these types of services to consumers, the MARS rule requires that the MARS provider make certain disclosures to consumers. In addition, the MARS rule bars advance fees paid to a MARS provider, prohibits certain representations, and imposes record keeping requirements (must retain for 2 years all MARS advertisements, sales records for covered transactions, customer communications, and customer contracts). MARS providers can only receive payment if the consumer’s loan is modified by the lender.

The FTC and state attorney generals have actively prosecuted foreclosure rescue companies, based on evidence that consumers received very little benefit for these services. The prosecutions took place under unfair trade practices laws, although some states did enact laws specifically regulating this business model. The FTC itself has brought 40 cases and FTC staff told NAR that none of these cases involved real estate professionals acting in their licensed capacity.

The FTC began its rulemaking process in 2009. NAR submitted comments and testimony during the rulemaking seeking an exemption for real estate licensees (click here to read NAR’s [first](#) and [second](#) comment letters). The FTC addressed NAR’s comments in the following footnote:

The Commission concludes that an exemption for real estate agents is not necessary. Real estate agents customarily assist consumers in selling or buying homes and perform functions such as listing homes for sale, showing homes, and finding desirable homes for consumers. The Commission is aware that real estate agents may perform these functions when properties are bought or sold through a short sale transaction, but does not consider these services to be MARS.

Final MARS Rule

The MARS rule covers short sale negotiations, and so this is the area where real estate professionals acting in their licensed capacity may need to comply with these rules. FTC staff has determined that “negotiate” will include communications with a lender about the possibility of a short sale transaction involving a consumer’s loan. A short sale is a transaction where the title to the property changes, the sales price is insufficient to pay all the liens, the seller does not provide funds to clear the liens on the property, and the lender agrees to allow the sale to occur by releasing the liens on the property. In some

cases, the lender may hold the seller liable for the shortfall, which is called a “deficiency”.

The MARS rule contains the following definitions:

“Mortgage Assistance Relief Service” is defined as a “service, plan, or program offered or provided to the consumer in exchange for consideration” that provides services in relation to a consumer’s mortgage, including negotiating a possible loan modification, directing a consumer to stop or otherwise alter the amount of his/her mortgage payment, modifying the consumer’s payment arrangements, or negotiating a short sale of a dwelling on behalf of a consumer.

“Mortgage Assistance Relief Service Provider” is someone who “provides, offers to provide, or arranges to provide, any mortgage assistance relief service.”

Based on those definitions, the MARS rule can have an impact on a real estate professional that represents clients involved in a short sale transaction or markets himself/herself as a MARS provider (i.e. short sale specialist). The focus of this article is for real estate professionals who, while acting in their licensed capacity as a real estate professional, provide services that may fall within the MARS rule. If someone is operating a full-time MARS business and not acting as a real estate licensee, they should further review these rules and consult with counsel to assure their business practices comply with MARS.

Disclosures Required by the Rules

There are three types of disclosures that a real estate professional may need to make to consumers. The rules have specific requirements on how the disclosures must be presented to consumers, depending on the communication medium. In all cases, the disclosure must be clear and prominent. For printed materials, the written disclosure must be the larger of 12-point type or one-half the size of the largest letter used to list the name of the firm providing the disclosures. Below are models that could be used in written materials; the requirements vary slightly for oral communications made to consumers.

General Commercial Communications Disclosures

A real estate professional that advertises MARS services which is not directed at a specific consumer will need to include in all advertisements a clear and prominent disclosure with the following:

IMPORTANT NOTICE *(in two point-type larger than the font size of the disclosure): (Name of company)* is not associated with the government, and our service is not approved by the government or your lender. Even if you accept this offer and use our service, your lender may not agree to change your loan. If you stop paying your mortgage, you could lose your home and damage your credit rating.

Consumer-Specific Commercial Communications

The second disclosure is required in all communications that the MARS provider directs to specific “prospective” clients, and so these disclosures may need to be made by a real estate professional that represents a seller in a short sale transaction. These communications must be provided by the MARS provider before the provider begins mortgage-assistance services on behalf of the consumer. As discussed in this article, the time when the real estate professional needs to provide this disclosure will vary, as a listing broker may not be aware that the transaction will need to be a short sale until far into the listing process.

In order to comply with this disclosure requirement, a listing broker should provide this disclosure to the client in a letter or memo once he/she is aware the transaction may be a short sale, highlighting this fact in the document and prominently displaying the below disclosure statement. The real estate professional should work with their attorney in drafting this document. NAR has also provided a model disclosure form- [click here](#) to view. The disclosure must provide the following:

IMPORTANT NOTICE (*in two point-type larger than the font size of the disclosure*): You may stop doing business with us at any time. You may accept or reject the offer of mortgage assistance we obtain from your lender [or servicer]. If you reject the offer, you do not have to pay us. If you accept the offer, you will have to pay us (*insert amount or method for calculating the amount*) for our services. (*Name of company*) is not associated with the government, and our service is not approved by the government or your lender. Even if you accept this offer and use our service, your lender may not agree to change your loan. If you stop paying your mortgage, you could lose your home and damage your credit rating.

Disclosure When Providing an Offer of Mortgage Relief

The third disclosure needs to be provided, in a clear and prominent manner, at the time the real estate professional presents its client with the lender’s short sale approval letter. The disclosure must be provided on a separate page and state:

IMPORTANT NOTICE: Before buying this service, consider the following information (*in two point-type larger than the font size of the disclosure*): This is an offer of mortgage assistance we obtained from your lender [or servicer]. You may accept or reject the offer. If you reject the offer, you do not have to pay us. If you accept the offer, you will have to pay us [*same amount as disclosed previously*] for our services. If you stop paying your mortgage, you could lose your home and damage your credit rating.

The real estate professional must also provide a notice from the lender or servicer that describes all material differences between the seller’s current loan and the lender’s

proposal to modify the loan if the seller accepts the short sale offer, which may include the lender holding the seller liable for the deficiency amount. This information will likely be contained in the lender's short sale approval letter.

MARS Scenarios

Real Estate Professionals with Possible Short Sale Listings

Negotiating a short sale with a lender will cause the real estate professional to fall within the definition of a MARS provider and so would be subject to the MARS rule. As stated above, negotiation will include communications with a lender about a short sale transaction on behalf of a client. How the broker will need to comply with MARS will depend on the facts and circumstances of the broker's business and how the broker has conducted the negotiations. A brokerage which promotes itself as a MARS provider will need to fully comply with MARS.

A broker that becomes involved in a short sale transaction listing during the normal course of his/her real estate brokerage operations and doesn't otherwise promote himself/herself as a MARS provider will need to comply with the MARS rule for the specific transactions involving a short sale if the broker will negotiate the loan with the lender or otherwise arranges for such negotiations. The broker will provide the Consumer-Specific Commercial Communications disclosure to consumers as soon as he/she is aware of the need for a short sale transaction.

The time when these disclosures need to be made will depend on the facts of each transaction. If the broker learns that a short sale will be required during its initial meeting with the seller, the broker will need to make the required disclosures at that time. A broker who doesn't learn that a short sale is required until the first offer is received will not need to make disclosures until that time.

The time for disclosure is similar to the requirement that many MLSs impose upon participants. Under those rules, a participant has a duty to let other MLS participants know about the possibility for a short sale when it is "reasonably known" by the listing broker. Real estate professionals should follow a similar process in making MARS disclosures to their clients.

Example #1: Real estate broker A has a residential real estate brokerage business and is paid by commission. He does not advertise as a MARS provider. A takes a listing from a seller, but the property does not sell during the first six months and prices in the local market have dropped during that time. A then receives an offer that is substantially below the listing price, but consistent with the recent sales in the market. The seller informs A that his mortgage exceeds the offer price but the seller will accept the offer if the lender would be willing to accept the offered price. If A decides to continue working with his client during the short sale and will negotiate with the lender or will arrange for a MARS provider to negotiate with the lender, A should now make the Consumer-Specific Commercial Communications disclosure and may also need to update the listing in his local MLS.

Example #2: Real estate salesperson B has a prospect walk into her office, inquiring about possibly selling his home. The prospect tells B that he has lost his job and so needs

to sell his home because he cannot afford to continue making mortgage payments. Based on the amount remaining on his loan and current market conditions, B may need a short sale in order to sell his home. B will need to provide the client with the Consumer-Specific Commercial Communications if she decides to pursue this listing.

MARS & Marketing Materials

The MARS rule requires an entity who specifically markets MARS to consumers to make certain general disclosures in all advertisements promoting MARS services. So, any brokerage that specifically solicits business from short sale sellers will need to include these disclosures in all of its advertisements, including telephone solicitations.

A real estate brokerage that isn't specifically seeking to be a MARS provider yet wants to mention its short sale experience/qualifications in its marketing materials may or may not need to provide the general MARS disclosures. The FTC's practice is to review ads on a case-by-case basis, and determine the impression that a particular ad would make upon a "reasonable" consumer.

So, an advertisement listing the accomplishments of a licensee and the types of services that the licensee provides to his/her clients which mentions experience with short sale transactions, among other services, may not need to comply with the MARS advertising rules. Similarly, an advertisement identifying a licensee as having the SFR designation, without more, is also likely outside of the MARS advertising rules. However, an advertisement promoting a real estate professional's short sales brokerage business will likely need to comply with the rules, since the average consumer would have the impression that these advertisements are from a MARS provider.

Licensees Accepting Upfront Fees

As stated above, the MARS rule bars the receipt of upfront fees. Therefore, brokers whose business model involves upfront fees need to be aware that if they take an upfront fee from a client and then later help the client negotiate a short sale, they will be in violation of MARS.

Buyer's Representatives

Buyer's representatives may need to make the Consumer-Specific Commercial Communication to sellers if they negotiate a modification of the seller's loan with a lender while representing a potential buyer. Despite the fact that the buyer's representative does not otherwise represent the seller in the transaction, the buyer's representative will be seen as a MARS provider once he/she begins negotiating the terms of the short sale with the lender(s). Additionally, the buyer's representative cannot charge a separate fee to the seller for this service, unless the buyer's representative has entered into a separate agreement with the seller and this agreement meets the other conditions of the MARS rule (no upfront fee, can only receive payment if the loan is modified, and the other relevant provisions of the regulation).

Referrals

The MARS rule also includes in the definition of MARS provider “any person that...arranges for others to provide any mortgage assistance relief service.” Therefore, any licensee referring a client to a MARS provider in exchange for a referral fee will need to be careful that it is not “arranging” the mortgage relief services for its client; otherwise, it will need to comply with the MARS disclosure requirements.

If a real estate professional does have clients in need of short sales but the real estate professional would rather refer the short sale negotiations with the lender(s) to a MARS provider, a possible solution is to offer the client a list of providers and allow the client to choose the MARS provider. Whether the real estate professional is seen as arranging the transaction will again be a factual determination, but allowing the client to choose the provider and making it clear that the client is not required to use the MARS providers offered by the real estate professional should remove the real estate professional from the need to comply with the MARS rule. The real estate professional should also disclose upfront any referral fee arrangements with the MARS provider to the client.

The real estate professional also needs to take steps to assure that any MARS provider to whom it refers customers is complying with the MARS rule, as it is a violation if “substantial assistance” is provided to someone that he/she knows or should have known is not complying with the MARS rule.

Conclusion

If a real estate professional represents clients in short sales, takes an upfront fee for his/her services, or promotes himself/herself to potential short sale sellers, the real estate professional needs to be aware of the MARS rule and the disclosure requirements.