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Testimony of the Department of Commerce and Consumer Affairs

**Before the
Senate Committee on Commerce and Consumer Protection
Friday, March 18, 2022
10:00 a.m.
Via Videoconference**

**On the following measure:
H.B. 2114, H.D. 1, RELATING TO MORTGAGE RESCUE FRAUD**

Chair Baker and Members of the Committee:

My name is James Evers, and I am an Enforcement Attorney with the Department of Commerce and Consumer Affairs' (Department) Office of Consumer Protection. The Department supports this administration bill.

The purposes of this bill are to: (1) delete certain exemptions to the definition of a "distressed property consultant" in the State's Mortgage Rescue Fraud Prevention Act that are not in the federal Mortgage Assistance Relief Services (MARS) Rule; and (2) correct a typographical error in the definition of "mortgage assistance relief service."

When Hawaii's Mortgage Rescue Fraud Prevention Act, Chapter 480E, Haw. Rev. Stat. (MRFA), took effect in June of 2008, the federal government had yet to enact legislation specifically designed to protect consumers from mortgage rescue scams. There was no federal counterpart to MRFA until the enactment of the Federal Trade Commission's Mortgage Assistance Relief Services Rule, 12 C.F.R. part 1015 (MARS Rule) in December 2010. While MRFA and the MARS Rule are both designed to protect

consumers from abusive mortgage relief practices, the two laws take distinctly different approaches to identify the persons from whom consumers are in need of protection. H.B. 2114, H.D. 1 takes the unique protection provisions of the MARS Rule and combines and reconciles those with the protection provisions already present in and unique to the existing MFRA. For the most part, the amendments do not represent "new" law, but a reformulation of existing law. Section 480E-2 has exemptions to the definition of "distressed property consultant" that do not exist in the federal law. The protection these exemptions offer is illusory, as anyone engaged in wrongdoing can be sued under federal law. In the absence of an amendment to section 480E-2, the State may be limited to bringing certain claims against a distressed property consultant only under federal law. H.B. 2114, H.D. 1 will help to eliminate confusion caused by existing conflicts and inconsistencies in an area where there should be none, since the MARS Rule imposes a stricter standard and the State is not at liberty to impose a lesser one.

The definition of "mortgage assistance relief service" in section 480E-2 currently refers to "deed or trust," when it should instead read "deed of trust." This typographical error should be corrected to make the Hawaii definition consistent with the federal law definition.

Cases of mortgage rescue fraud are investigated and litigated by the Office of Consumer Protection (OCP). OCP also assists with parallel investigations conducted or proceedings prosecuted by the Federal Trade Commission (FTC), the Consumer Financial Protection Bureau (CFPB), other states, the Office of Disciplinary Counsel (ODC), or federal or state criminal authorities. As a result of this experience, OCP is well-informed on the subject of mortgage rescue fraud and has proposed H.B. 2114, H.D. 1 because homeowners are in need of greater protection from scammers and fraudsters.

A quick look at the subject of advance fees will help explain the need for the proposed amendment. Advance fees are one of the major driving forces behind mortgage rescue scams. Homeowners are oftentimes required to pay advance fees for assistance in seeking a loan modification. If the desired loan modification is not obtained, however, the services paid for end up conferring no benefit upon the

homeowners, and homeowners may be left without adequate funds to pursue other options to save their homes. The collection of advance fees by mortgage assistance service providers is banned by federal law (known as the MARS Rule). Service providers collecting advance fees have been sued by OCP under the MARS Rule. A similar ban on advance fees under State law has been undermined by various exemptions in HRS 480E-2, which H.B. 2114, H.D. 1 seeks to eliminate. The payment of advance fees is no less offensive merely because the fees might be paid to a member of an exempt group since the end result is injury to consumers. The State exemptions are illusory because of the federal ban, and should therefore be eliminated.

In anticipation that testimony may be submitted in opposition to H.B. 2114, H.D. 1 like what was submitted in opposition to the Senate Companion bill, S.B. 3082, OCP wishes to address inaccuracies with the following.

1. Clarification as to the Impact of H.B. 2114, H.D. 1

Anyone is free to offer assistance to distressed property owners (i.e., owners of property either in foreclosure or at immediate risk of foreclosure). That is the case now, and that will remain the case if H.B. 2114, H.D. 1 becomes law. For the sake of protecting consumers, assistance providers (or “Consultants” as the term is defined in HRS 480E-2), are required to refrain from prohibited conduct (such as collecting advance fees), and comply with statutory safeguards (such as using written contracts containing mandatory disclosures). Anyone can serve as a Consultant, but no Consultant may charge advance fees or fail to use legally-compliant written contracts.

2. Clarification as to the Scope of H.B. 2114, H.D. 1

When Hawaii enacted HRS Chapter 480E in 2008, it was full of exemptions. When the federal government enacted the MARS Rule in 2010, there were no such exemptions in the MARS Rule except for limited exemptions for the distressed property owners’ attorney, lender and servicer. To the extent that 480E sets forth broader protections, the exemptions are illusory because they offer no protection to anyone accused of violating the MARS Rule. Under H.B. 2114, OCP is seeking no greater enforcement powers than OCP currently possesses in its enforcement of the MARS

Rule. Removing illusory exemptions will better enable Consultants to comply with those laws designed to protect homeowners from mortgage rescue fraud.

3. Continued Exemption of the Homeowners' Lender and Servicer

Some opponents to this proposal assert that removing the blanket exemption for banks will do away with the current protection now enjoyed by the homeowners' lender and servicer. That is simply not true. H.B. 2114, H.D. 1 expressly provides that the term "distressed property consultant" shall not include (1) attorneys licensed in the State of Hawaii engaged in the practice of law; (2) the residential loan holder, or any agent or contractor of such individual or entity; and (3) the servicer of a residential loan, or any agent or contractor of such individual or entity. Under H.B. 2114, H.D. 1, just as is the case under the MARS Rule, the homeowners' lender and servicer may do what they can to remedy a default and spare homeowners from losing their home in foreclosure, without having to comply with the safeguards imposed upon Consultants. The continued exemption of the homeowners' lender and servicer dispenses with opponents' objections.

4. Reconciling the MARS Rule with HRS Chapters 480 and 480E

HRS Chapter 480 protects consumers by making unlawful unfair or deceptive acts or practices (or UDAPs). The statute does not attempt to list all of the possible UDAPs, because the United States Supreme Court has recognized that there is no limit to human inventiveness, and attempting to list all UDAPs would be an endless task. Some of the more common UDAPs constituting mortgage rescue fraud have been identified and described in the MARS Rule and in HRS Chapter 480E. Under HRS 480E-11 (a) and (b), violations of the MARS Rule or HRS Chapter 480E are per se UDAPs and violations of HRS Chapter 480. Because there is no limit to human inventiveness, neither the MARS Rule nor HRS Chapter 480E describe all of the UDAPs in the area of mortgage assistance offered to distressed property owners. Independent of the MARS Rule or HRS Chapter 480E, relief from any such other conduct believed to constitute a UDAP may be sought under HRS Chapter 480, and most telling is the fact that under HRS Chapter 480, there are no exemptions for anyone – not attorneys, not banks, not realtors, nor anyone else. In fact, in April of 2019, the

Supreme Court of Hawai'i held that the practice of law constitutes conduct in "trade or commerce" within the meaning of HRS § 480-2(a) and thus attorneys were not categorically exempt from its operation. In its opinion the Court relied in part upon a case brought by the CFPB, and noted that what constitutes an "unfair, deceptive, or abusive act or practice" (or UDAAP) in violation of the Consumer Financial Protection Act is determined by the same standard applied to UDAPs under the Federal Trade Commission Act.

Financial institutions engaged in unfair or deceptive acts or practices in the conduct of any trade or commerce are subject to State enforcement. The fact that financial institutions may not be prosecuted by the FTC under the MARS Rule does not mean that they can't still be held accountable for violating HRS Chapter 480.

5. Clarification as to the Attorney Exemption under 480E

Under the MARS Rule, qualifying attorneys may be exempt from the definition of "Provider," which is the term used for those providing mortgage assistance relief services. Satisfying one set of criteria enables attorneys to enjoy a limited exemption, and satisfying a second set of criteria enables attorneys to enjoy a broader exemption. Failure to satisfy either set of criteria means the attorney would be treated like any other Provider. One of the problems associated with the federal exemption having been set up in this fashion is the lack of transparency. Consumers have no way of knowing whether attorneys have satisfied the criteria to be fully exempt, and the case law serves to prove that those issues may be litigated for years after the fact.

This ambiguity was exploited in Hawaii by individuals each claiming to be acting as a private attorney general. After a four week jury trial in federal court, the mastermind behind this scheme, who had no law license, was convicted of 32 counts of wire fraud and mail fraud, and sentenced to 240 months' imprisonment. Many victims in Hawaii experienced hardship as a result of this scam, and several lost their homes.

For the sake of greater transparency, the attorney exemption is now set up differently under HRS Chapter 480E. "Attorneys licensed in the State of Hawaii and engaged in the practice of law" are exempt from the definition of distressed property consultant (or Consultant) (the State equivalent of a Provider under the MARS Rule).

This fact is easily verifiable, but that does not end the analysis. Even attorneys exempt from the definition of Consultant must still comply with HRS § 480E-15 entitled “Requirements for attorneys licensed in Hawaii.” This section requires the use of written contracts, and the use of client trust accounts for the retention of all monies received by the attorney until the attorney has fully performed all of the services covered by the written contract, as well as any such additional services the attorney represented would be performed.

No profession can claim that its members are free from corruption, and that includes attorneys. In 2013, OCP was investigating an attorney who technically fell within the attorney exemption under HRS Chapter 480E, even though the attorney was acting in violation of the MARS Rule and in a manner entirely inconsistent with the norms for the legal profession. The matter was referred to the ODC, and the attorney was eventually disbarred in 2015. Despite his disbarment, the attorney continued to engage in mortgage rescue fraud and regularly received illegal advance fees from consumers. In 2019, OCP filed suit in federal court under both the MARS Rule and HRS Chapter 480, and prevailed. Even after having been enjoined from engaging in mortgage rescue fraud, the disbarred attorney persisted with his illegal conduct, and in 2021 was held in contempt of court. While attorneys remain outside the definition of Consultants, the enactment of HRS § 480E-15 should curtail the abuses seen in the legal profession.

6. Clarification of the Exemption for Nonprofits

Aside from the three exemptions set forth in H.B. 2114, H.D. 1, there are no other exemptions, and as shown, this is due in part to the fact that there are no exemptions set forth in HRS Chapter 480.

The cases investigated or litigated by OCP over the past eight years have shown that blanket exemptions are based upon a faulty premise that there is some correlation between a certain profession and the risk of harm to consumers.

In January of 2020, after a jury convicted a woman of five counts of wire fraud and three counts of aggravated identity theft of approximately \$207,000, United States District Judge J. Michael Seabright sentenced the woman to 66 months of

imprisonment. The woman was a former employee of the U.S. Department of Housing and Urban Development (HUD), and used her position to perpetrate the fraud, which she attempted to conceal using aliases and forged signatures.

OCP does not anticipate that any legitimate nonprofit will be adversely impacted by the passage of H.B. 2114, H.D. 1. In advance of drafting the bill, OCP contacted the nonprofits most involved with distressed property owners to inquire as to their retention arrangements, and it does not appear as though the nonprofits would satisfy the definition of Consultant. Legitimate nonprofits do not request or require compensation for their services, and typically fall outside the definition of distressed property consultant because their services typically fall outside the definition of mortgage assistance relief service.

Realtors are not exempt from compliance with the MARS Rule, and the state exemption is providing a false sense of security. If H.B. 2114, H.D. 1 passes, realtors will not be precluded from selling distressed properties or even from acquiring distressed properties, provided that they comply with HRS 480E. For example, if a realtor is going to purchase distressed property, a legally compliant distressed property conveyance contract is required. Failure to do so constitutes violations of the MARS Rule. OCP anticipates that the removal of the illusory State exemption would prompt realtors to comply with both State law and the MARS Rule. The risks associated with such conveyances are just too great to ignore.

In 2020, OCP prosecuted a real estate broker licensed since 1989. Her license and years of experience did not prevent her from engaging in mortgage rescue fraud in collaboration with others, including a former real estate salesperson and two former mortgage solicitors. Their backgrounds gave them credibility, making them more dangerous to consumers. Hundreds of bogus documents were recorded in Hawaii's Bureau of Conveyances, and hundreds of thousands of dollars were lost. Two of the collaborators have since pled guilty to criminal charges in federal court. This is why no such exemptions appear in HRS Chapter 480.

Exemptions are particularly inappropriate in connection with the sale of distressed property. Desperate homeowners need more protection, not less, and that is

what OCP sees in the real world. In 2021, OCP prevailed in a case where the homeowners, believing they were using a proven strategy designed to save their house from a foreclosure filed in 2011, signed a deed conveying title to their Consultant, a former mortgage solicitor with a criminal record for fraud. The Consultant proceeded to charge them rent, none of which was used by the Consultant to pay the mortgagee, as the Consultant had promised. The property was once again in foreclosure in 2019, only now the Consultant was included as a Defendant. OCP investigated and sued in 2019 to void the conveyance and void the attachment of the liens of the Consultant's judgment creditors. This fraudulent conveyance scheme enabled the Consultant to steal 73 monthly mortgage payments made between 2013 and 2019, for which the consumers were awarded restitution and the Consultant was fined in excess of 1.5 million dollars.

8. Clarification of Subject Matter Jurisdiction in Federal Court

OCP is authorized to enforce the MARS Rule. Since the MARS Rule is federal legislation, the federal court will always have subject-matter jurisdiction over any case in which claims under the MARS Rule have been pled, and the court is then free to exercise supplemental jurisdiction of OCP's claims brought under State law. OCP has a successful track record for pleading cases in federal court precisely this way.

In OCP's case against the disbarred attorney filed in 2019, OCP filed suit in federal court under both the MARS Rule and HRS Chapter 480, and prevailed. The violations of the MARS Rule constitute per se violations under State law, and the Court exercised supplemental jurisdiction in awarding monetary fines and penalties in excess of \$450,000 under State law.

Thank you for the opportunity to testify in support of this bill.

March 18, 2022

The Honorable Rosalyn H. Baker, Chair

Senate Committee on Commerce and Consumer Protection
Via Videoconference

RE: House Bill 2114, HD1, Relating to Mortgage Rescue Fraud

HEARING: Friday, March 18, 2022, at 10:00 a.m.

Aloha Chair Baker, Vice Chair Chang, and Members of the Committee,

I am Mihoko Ito, testifying on behalf of the Hawai'i Association of REALTORS® ("HAR"), the voice of real estate in Hawai'i, and its over 11,000 members. HAR **opposes** House Bill 2114, HD1, which amends the definitions of a "distressed property consultant" and "mortgage assistance relief service" in section 480E-2, Hawaii Revised Statutes.

Federal Law

To protect homeowners from mortgage relief scams during the last financial crisis, the Federal Trade Commission ("FTC") published the Mortgage Assistance Relief Services ("MARS") final rule on December 1, 2010. While the intent of the MARS rule was to protect distressed homeowners from mortgage relief scams, it was written so broadly that it also required real estate brokers and agents acting in their licensed capacity to comply when they negotiate with the lender on the terms of a short sale.

The National Association of REALTORS® and the FTC discussed the difficulty real estate brokers and agents have in complying with the literal requirements of the MARS rule since it was not drafted with a real estate sales transaction in mind.

On July 15, 2011, the FTC announced it has decided not to enforce most provisions of its MARS Rule against real estate professionals who are acting in their licensed capacity while assisting sellers to obtain a short sale for their residence. The FTC will still enforce the Rule against real estate professionals who make fraudulent misrepresentations during the course of obtaining a short sale for their clients.¹

As such, a fraudulent misrepresentation claim can already be pursued against a licensee. Moreover, if the intent of this measure is to mirror federal law, it would then reflect the FTC's announcement that it will not enforce most provisions of the MARS rule against real estate professionals acting in their licensed capacity.²

¹ <https://www.nar.realtor/mortgage-assistance-relief-services-mars-rule>

² <https://www.ftc.gov/news-events/news/press-releases/2011/07/ftc-will-not-enforce-provisions-mars-rule-against-real-estate-professionals-helping-consumers-obtain>

State Law

In 2008, the Mortgage Rescue Fraud Prevention Act (Act 137) was passed to protect financially strapped homeowners from equity skimming and foreclosure rescue scams. At the time, there was no real estate licensee exemption which placed a chilling effect on real estate licensees trying to help their clients that have a distressed property.

Real estate licensees help homeowners by negotiating with lenders, sometimes multiple lenders, to avoid foreclosure. In turn, they negotiate on behalf of their client to the lender to pursue better options, such as short sales, which puts more control on the part of the homeowner and is better on their credit than a foreclosure.

The following year, [Act 66](#) amended Act 137, to add the real estate broker salesperson exemption. Act 66 also amended HRS 467-14, to provide that a licensee may have their license revoked, suspended or be fined, if they acquire an "ownership interest, ownership interest, directly or indirectly, or by means of a subsidiary or affiliate, in any distressed property that is listed with the licensee or within three hundred sixty-five days after the licensee's listing agreement for the distressed property has expired or is terminated."

A final note, Act 137 was not patterned after the Federal MARS statute; differs significantly in its provisions; and has proven effective in prosecuting mortgage fraud scam artists in the State of Hawai'i. In point of fact, the suggestion that this measure is necessary to conform Act 137 to Federal law is not true and is inconsistent with the past fourteen years of enforcement experience.

As such, real estate licensees are highly regulated to ensure the consumer is protected. Moreover, those found in violation can already be prosecuted under a fraudulent misrepresentation claim. **For the foregoing reasons, we respectfully request that real estate brokers and salesperson continue to be exempt under this measure.**

Mahalo for the opportunity to testify.

Presentation to The
Committee On Commerce and Consumer Protection
Friday, March 18, 2022, 10:00 AM
State Capitol Conference Room 229 & Videoconference

Testimony on HB 2114, HD1 In Opposition

TO: The Honorable Rosalyn H. Baker, Chair
The Honorable Stanley Chang, Vice Chair
Members of the Committee

My name is Neal K. Okabayashi, Executive Director of the Hawaii Bankers Association (HBA). HBA represents seven Hawai'i banks and three banks from the continent with branches in Hawai'i.

HBA does not object to the purpose of the Mortgage Assistance Relief Services Rule (Rule), as republished in 12 CFR section 1015.7 (Rule) as a Consumer Financial Protection Bureau (CFPB) Rule, and in fact HBA supports the Chapter 480E, Hawai'i's version of the Rule.

Our objection to the proposed amendment is that it is unnecessary and does not add to consumer protection from borrowers in default, and in fact, detracts from consumer protection. The proposed amendment is not aligned with the justification sheet claiming that certain exemptions are not in the Rule although the substance of the Chapter 480E exemptions is consistent with the Rule and meets the spirit of the Rule. The OCP seeks to mirror certain language of what was the Federal Trade Commission (FTC) rule but the OCP's interpretation of some exemptions is contrary to the FTC compliance guidelines which specifically states that "The Rule doesn't cover **lenders** and servicers that offer mortgage assistance relief services in connection with loans they own or service." Despite the FTC guidance, OCP seeks to eliminate lenders from the exemption.

Last year, the Office of Consumer Protection (OCP) sent HBA a letter lauding one local bank that spotted a potential mortgage rescue fraud and assisted OCP in its investigation of the matter. Under the proposed amendment to the law, that bank would not be exempt from Chapter 480E unless it was a server. Banks that may spot a potential consumer fraud because of a depository issue on a mortgage would not be exempt.

Section 480E-2 includes as an exemption: "Banks, savings banks, savings and loan associations, credit unions, trust companies, depository and nondepository financial service loan companies, . . ." There is no reason to delete that exemption since the FTC, which then interpreted the Rule, said lenders were exempt.

It has long been the case that local banks have taken the lead in attempting to help borrowers with loan mortgage issues by engaging in negotiation on loan forbearance and loan mitigation.

Despite the justification sheet claiming the amendments are to mirror federal law, that is not correct. The amendment would retain the full exemption for attorneys but the Rule itself only has a partial exemption for attorneys and thus does not mirror federal law.

The proposed amendments would also delete the exemption for certified public accountants. The FTC compliance guide states that accountants are exempt as long as they do not claim that their services will help a homeowner get a loan modification.

The proposed amendment also deletes the exemption for nonprofits contrary to the FTC compliance guidelines that says the Rule does not apply to bona fide non-profit organizations. This proposed amendment prevents HUD approved housing counselors and foreclosure avoidance counselor, such as Hawaii Homeownership Center, Legal Aid Society, Hawaiian Community Assets, and the Consumer Credit Counseling Services of Hawaii from being exempt and thus may shy away from advising consumers on loan forbearance and mitigation efforts.

In the justification sheet, the OCP claims that the amendments will allow the state to file in either state or federal court. Generally, one can file in federal court only if there is a federal case, meaning a violation of federal law or there is diversity of citizenship, meaning the opposing parties are in different states. Since the lawsuit will be based on state law, it appears that the federal court will have no jurisdiction over the OCP lawsuit, regardless of whether state law mimics federal law in certain sections.

Thank you for the opportunity to submit this testimony in opposition on HB 2114, HD1. Please let us know if we can provide further information.

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