

Mortgage Loan Broker Compliance Evaluation Manual



Real Estate MATTERS!

State of California
Department of Real Estate

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Introduction

This Mortgage Broker Compliance Evaluation Manual was prepared primarily to assist the real estate broker who engages in mortgage loan activities to assess compliance with Department of Real Estate (“Department”) requirements. It addresses many of the questions that are asked of Department staff.

If there is any conflict between this manual and the Real Estate Law and/or Regulations of the Real Estate Commissioner, the law and regulations will take precedence. This manual was not designed to include all of a broker’s obligations and responsibilities under the Real Estate Law but rather as one of the tools to be used when reviewing business practices and record keeping procedures related specifically to a broker’s mortgage loan activity. We hope brokers will find it helpful.

Unless otherwise noted, all “Section” references are to the Business and Professions Code and “Regulation” references are to the Regulations of the Real Estate Commissioner. Applicable laws and regulations can be found in the Real Estate Law Book in the Publications menu of the Department’s Web site at www.dre.ca.gov.

Questions regarding information contained in this manual should be directed to the Department’s Mortgage Loan Activities unit at (916) 227-0770.

SECTION 1 – General Business Practices

1. Is the broker properly licensed?

Correct Procedure:

A California real estate broker license is required in order to perform mortgage loan activities in California. In addition, in order to perform residential mortgage loan origination activities, a mortgage loan originator endorsement to the real estate broker is required.

It should be noted there are other licenses that allow mortgage loan brokering under a limited set of circumstances, such as the California Finance Lenders license and the California Residential Mortgage Lending license. For information about these licenses, contact the California Department of Corporations.

Reference:

Sections 10130, 10131, 10131.1, 10132, 10166.01

2. Are the broker's salespersons properly licensed?

Correct Procedure:

All persons performing activities requiring a real estate license (which includes soliciting or negotiating loans secured by real property or a business opportunity) for compensation must hold a valid real estate license. In addition, a mortgage loan originator endorsement to the real estate license is required in order to perform residential mortgage loan origination activities.

The broker should have some procedure in place to monitor the expiration dates of the licenses of all employed salespersons. Standard broker and salesperson licenses expire four years after issuance. The broker must also retain possession of the licenses of all employed salespersons. If the broker employs broker licensees as broker associates, the broker need not retain possession of the broker licenses; however, the employing broker must monitor the license expiration dates.

Once a license has expired, the licensee can perform no licensed activity until the license has been renewed. The late renewal period simply allows the licensee to renew on a late basis without retaking the examination; it does not allow the licensee to conduct licensed activity during the late renewal period.

It is unlawful for any broker to employ or compensate, directly or indirectly, any person for performing licensed activity unless that person is a licensed broker, or a salesperson licensed to the broker. In addition, it is unlawful for any broker to employ or compensate, directly or indirectly, any licensee for engaging in any activity for which a mortgage loan originator endorsement is required if that licensee does not hold a mortgage loan originator license endorsement. A salesperson may not accept compensation for licensed activity nor pay compensation for licensed activity except through the broker under whom he/she is at the time licensed.

It is a misdemeanor, punishable by a fine of \$100 for each offense, for any person, whether obligor, escrow holder or otherwise, to pay or deliver to anyone compensation for performing any licensed acts who is not known to be or who does not present evidence that he/she is a licensed real estate broker at the time such compensation is earned.

A broker may employ non-licensed persons to assist the broker in meeting the broker's obligations to its customers in residential mortgage loan transactions as defined in Financial Code Section 50003, where the lender is an institutional lender, provided the employee does not participate in any negotiations occurring between the principals. The broker must exercise reasonable direction, control and supervision over the

activities of non-licensed persons who may only be employed at a location licensed to the broker. The broker must be obligated to withhold income taxes and provide workers compensation insurance and unemployment insurance. The non-licensed person may only perform those activities specifically described in Regulation 2841.

Reference:

Sections 10130, 10131, 10132, 10133.1(c), 10137, 10138, 10153.4, 10160, 10166.01; Regulation 2756, 2841.

3. Does the broker notify the Department of Real Estate upon the hiring and termination of salespersons?

Correct Procedure:

A broker shall notify the commissioner within five days of a real estate salesperson entering his or her employ. This notification shall be given on a form prepared by the Department which shall be signed by the broker and the salesperson, or via the Department's eLicensing system, available at www.dre.ca.gov. The notification shall provide at least the following information:

1. Name and business address of the broker.
2. Mailing address of the salesperson, if different from the business address.
3. Date the salesperson entered the employ of the broker.
4. Certification by the salesperson that he/she has complied with the provisions of Section 10161.8(d) of the Business & Professions Code.
5. Name and business address of the real estate broker to whom the salesperson was last licensed and the date of termination of that relationship.
6. Certification by the salesperson that the predecessor broker has notice of the termination of the relationship.

As an acceptable alternative to 5 and 6 above, the form may be utilized by the predecessor broker to give notice of the termination of the broker/salesperson relationship as required by Section 10161.8(b) of the Business & Professions Code, if this notice is mailed to the commissioner not more than 10 days following such termination.

Reference:

Section 10161.8; Regulation 2752.

4. Does the broker have a written broker-salesperson agreement with each employed salesperson and a broker-associate agreement with each associated broker?

Correct Procedure:

Brokers must have a written agreement with each employed salesperson, and a broker-associate agreement with each broker performing activities for the sponsoring broker. The agreement shall be dated and signed by the parties and shall cover material aspects of the relationship between the parties, including supervision of licensed activities, duties and compensation.

Reference:

Regulation 2726

5. Is the broker properly supervising?

Correct Procedure:

A broker shall exercise reasonable supervision over the activities of employed salespersons and broker-associates. Reasonable supervision includes, as appropriate, the establishment of policies, rules, procedures and systems to review, oversee, inspect and manage:

1. Transaction activities requiring a real estate license.
2. Documents which may have a material effect upon the rights or obligations of a party to the transaction.
3. Filing, storage and maintenance of such documents.
4. The handling of trust funds.
5. Advertising of any service for which a license is required.
6. Familiarizing salespersons and broker-associates with the requirements of federal and state laws relating to the prohibition of discrimination.
7. Regular and consistent reports of licensed activities by salespersons.

The form and extent of such policies, rules, procedures and systems shall take into consideration the number of salespersons employed and the number and location of branch offices.

A broker shall establish a system for monitoring compliance with such policies, rules, procedures and systems. A broker may use the services of brokers and salespersons to assist in administering the provisions of this section so long as the broker does not relinquish overall responsibility for supervision of the acts of employed salespersons and broker-associates.

Reference:

Regulation 2725

6. Does the broker retain copies of all documents?

Correct Procedure:

A licensed broker must retain for three years copies of all documents related to the loan transaction, trust account records, and other documents executed by him or her or obtained by him or her in connection with any transaction for which a broker's license is required for a period of three years. The retention period shall run from the date of the closing of the transaction or from the date of the loan application if the transaction is not consummated. After reasonable notice, the books, accounts and records shall be made available for audit, examination, inspection and copying by a Department representative during regular business hours.

Two documents require retention for four years: the investor qualification statement for a multi-lender loan (Section 10231.2(b)) and self-dealing statement (Section 10238(f)).

Electronic or digital storage of the files may be accomplished if the broker complies with the requirements

described in Regulations 2729 and 2729.5. The broker must make the files available to the Department and must be willing to provide copies of the files. The files must be stored in a “read only” mode that cannot be overwritten.

Reference:

Section 10148, 10231.2(b), 10238(f), Regulations 2729 and 2729.5

7. Does the broker have a license for each business location?

Correct Procedure:

A broker is authorized to conduct business only at the address listed on the real estate license. If the broker maintains more than one place of business within the State, the broker must apply for and procure an additional license for each branch office so maintained. The application for a branch office license must state the name of the person and the location of the place or places of business for which the license is desired. In addition, if a broker is performing residential mortgage loan origination activities from a branch office, the broker must have a branch office license endorsement.

Reference:

Section 10163, Regulation 2758.5

8. Is the broker using an unlicensed fictitious name?

Correct Procedure:

A broker shall not use a fictitious name in the conduct of any activity requiring a real estate license unless the broker first obtains a real estate license bearing the fictitious name. A fictitious business name is frequently referred to as a “dba” (doing business as).

To obtain a license bearing a fictitious name, the broker must apply to the Department and attach a certified copy of the fictitious business name statement filed with the county clerk.

The Real Estate Commissioner may refuse to issue a license bearing a fictitious name to a broker if the fictitious name:

1. Is misleading or would constitute false advertising.
2. Implies a partnership or corporation when a partnership or corporation does not exist.
3. Includes the name of a real estate salesperson.
4. Constitutes a violation of the provisions of Sections 17910, 17910.5, 17915 or 17917 of the Code. (These sections provide the procedures for issuance of a fictitious business name.)
5. Is the name formerly used by a licensee whose license has since been revoked.

Reference:

Section 10159.5; Regulation 2731

9. Is the broker conducting escrows?

Correct Procedure:

Section 17006(a)(4) of the Financial Code exempts a licensed real estate broker from the Escrow Law when the broker is conducting an escrow in the course of or incidental to a real estate transaction in which the broker is

an agent or a party to the transaction and in which the broker is performing an act for which a real estate license is required. The exemption applies to the broker and the broker shall not delegate any duties other than duties performed under the direct supervision of the broker.

The broker's exemption will not apply to any escrows performed for more than one business.

Section 17403.4 of the Financial Code requires all written escrow instructions executed by a buyer or seller to contain a statement in not less than 10-point type which shall include the licensee name and the name of the department issuing the license or authority under which the person is operating. This section does not apply to supplemental escrow instructions or modifications to escrow instructions.

Real Estate Commissioner's Regulation 2950 sets forth acts which are prohibited and may be grounds for disciplinary action:

- (a) Soliciting or accepting an escrow instruction (or amended or supplemental escrow instruction) containing any blank to be filled in after signing or initialing of such escrow instruction (or amended or supplemental escrow instruction).
- (b) Permitting any person to make any addition to, deletion from, or alteration of an escrow instruction (or amended or supplemental escrow instruction) received by such licensee, unless such addition, deletion or alteration is signed or initialed by all persons who had signed or initialed such escrow instruction (or amended or supplemental escrow instruction) prior to such addition, deletion or alteration.
- (c) Failing to deliver at the time of execution of any escrow instruction or amended or supplemental escrow instruction a copy thereof to all persons executing the same.
- (d) Failing to maintain books, records and accounts in accordance with accepted principles of accounting and good business practice.
- (e) Failing to maintain the office, place of books, records, accounts, safes, files and papers relating to such escrows freely accessible and available for audit, inspection and examination by the Commissioner.
- (f) Failing to deposit all money received as an escrow agent and as part of an escrow transaction in a bank trust account, or escrow account on or before the close of the next full working day after receipt thereof.
- (g) Withdrawing or paying out any money deposited in such trustee account or escrow account without the written instruction of the party or parties paying the money into escrow.
- (h) Failing to advise all parties in writing if he/she has knowledge that any licensee acting as such in the transaction has any interest as a stockholder, officer, partner or owner of the agency holding the escrow.
- (i) Failing upon closing of an escrow transaction to render to each principal in the transaction a written statement of all receipts and disbursements together with the name of the person to whom any such disbursement is made.
- (j) Delivering or recording any instrument which purportedly transfers a party's title or interest in or to real property without first obtaining the written consent of that party to the delivery or recording.

Reference:

Financial Code Sections 17006(a)(4) and 17403.4

Regulation 2950

10. Is the broker, or any broker-associate or salesperson in the broker's employ, performing residential mortgage loan originator activities?

Correct Procedure:

All licensees performing residential mortgage loan originator activities (taking an application, offering, or negotiating loan terms) for compensation or gain must obtain and maintain a mortgage loan originator license endorsement.

The broker should have some procedures in place to monitor the status of the license endorsements of all licensees performing residential mortgage loan origination activities on behalf of the broker. In addition, the broker's Nationwide Mortgage Licensing System & Registry (NMLS) record must reflect all branch offices and fictitious business names used to conduct residential mortgage loan origination activities.

Reference:

Section 10166.01, 10166.04, Regulation 2758.5

11. Do independent contractor processors and underwriters of residential mortgage loan transactions have a mortgage loan originator license endorsement?

Correct Procedure:

All independent contractor loan processors and loan underwriters must have a mortgage loan originator license endorsement in conjunction with their real estate broker license.

Reference:

Section 10166.03

SECTION 2 - Trust Fund Handling

Typically the broker will only collect an appraisal and/or credit report fee from the prospective borrower. These must be treated as trust funds unless the broker is being reimbursed for advancing payment of the fee(s) to the vendor(s). Under those circumstances, the following rules will apply:

1. The funds must be strictly for the purposes of reimbursing the broker for fees that he or she has advanced for an appraisal or credit report on behalf of the borrower. If the broker has not advanced the funds, and is receiving a check from escrow on behalf of the borrower to pay an appraiser or a credit-reporting agency, the funds must be deposited to a trust account for payment to the vendor.
2. There can be no markups of any sort of the fees. Example: If an appraisal costs \$250.00 and that is the amount advanced by the broker, a "reimbursement" for \$300.00 must be deposited to the trust account and the additional \$50.00 must be identified as an actual cost or expense of the loan.
3. The broker must keep clear general account records of the funds expended on behalf of the borrower and paid to the vendor, subject to Department examination, so that it may be clearly established that the broker advanced funds to an appraiser or credit reporting agency for a specific borrower.
4. There must be clear instructions from the beneficiary (borrower) to the broker authorizing the reimbursement to his or her general account. This may be contained in the escrow instructions signed by the borrower.

The following questionnaire applies to brokers who collect appraisal and/or credit report fees in advance where the funds are negotiable by the broker. No other fees may be collected in advance without an approved advance fee agreement (see Section 6 - Advance Fees).

Trust Fund Handling Questionnaire

Does the broker collect trust funds from prospective borrowers?

1. Is the bank account used for trust fund handling in the name of the broker as trustee?
2. Are control records complete and accurate?
3. Are the separate transaction records complete and accurate?
4. Is monthly reconciliation of the control records and separate records performed and documented?
5. Are trust funds deposited in a timely manner?
6. Are authorized signatories either employed by the broker and licensed or unlicensed but bonded?
7. Are broker's funds commingled with trust funds?

1. Is the bank account used for trust fund handling in the name of the broker as trustee?

Correct Procedure:

1. If the broker is a sole proprietor broker, the account should be set up in his or her name (or in the name of a fictitious business name if the broker is a holder of a license bearing such a fictitious name) and should be designated as a trust account.

For example:

John Doe Trust Account

or

Jane Doe Trust Account

or, assuming broker has registered dba of 25th Century Realty,

25th Century Realty Trust Account

2. If the broker is a corporate broker licensee, the account should be set up in the corporation's name (or in the name of a fictitious business name if the corporate broker is the holder of a license bearing such fictitious name) and should be designated a trust account.

For example:

ABC, Inc. Trust Account

or, assuming corporate broker has registered dba of ABC Realty,

ABC Realty Trust Account

Reference:

Regulation 2832

2. Are control records complete and accurate?

Correct Procedure:

Every broker shall keep a record of all trust funds received, including uncashed checks.

1. If a broker does not maintain a trust account or maintains a trust account but forwards all trust funds received to either the escrow or to the owner of the funds, then he or she must maintain a Record of Trust Funds Received but not Deposited to the Trust Fund Bank Account (for example, Department Form RE 4524). This record should show the following in chronological sequence:

- a. Date funds received.
- b. Form of payment.
- c. Amount received and from whom.
- d. Description of property or other identification.
- e. Identity of person to whom funds were forwarded.
- f. Date of disposition.

A broker is not required to keep the above records of checks made payable to service providers (e.g., escrow, credit and appraisal services) when the total of such checks from any one principal for any transaction does not exceed \$1,000. Upon request of the Department or the maker of such checks, a broker shall account for the receipt and distribution of such checks. A broker shall retain for three years copies of receipts issued or obtained in connection with the receipt and distribution of such checks.

2. If a broker maintains a trust account, he/she must maintain a Columnar Record of all Trust Funds Received and Paid Out of the Trust Fund Bank Account (for example, Department Form RE 4522). This record should show the following in chronological sequence:

- a. Date funds received.
- b. From whom funds received.
- c. Amount received.
- d. Date of deposit.
- e. Check number and date of related disbursement.
- f. Daily balance of trust bank account.

Reference:

Section 10145; Regulation 2831

3. Are the separate transaction records complete and accurate?

Correct Procedure:

Brokers must maintain a Separate Record for Each Beneficiary or Transaction (for example, Department Form RE 4523). This record accounts for the funds received from, or for the account of, each beneficiary or each transaction and deposited to the trust fund bank account. These records are necessary for the broker to ascertain the total owed to each of the beneficiaries. The record should show in chronological sequence the following:

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1. Date of deposit.
 2. Amount of deposit.
 3. Date of each related disbursement.
 4. Check number of each related disbursement.
 5. Amount of each related disbursement.
 6. If applicable, dates and amounts of interest earned and credited to the account.
 7. Balance after posting transactions on any date.

Reference:

Section 10145; Regulation 2831.1

4. Is monthly reconciliation of the control records and separate records performed and documented?

Correct Procedure:

The balance of all separate beneficiary or transaction records (for example, Department Form RE 4523) must be reconciled with the record of all trust funds received and disbursed (for example, Department Form RE 4522) at least once a month. A record of reconciliation must be maintained and it must identify the following:

1. Bank account name.
2. Account number.
3. Date of reconciliation.
4. Name of beneficiaries.
5. Trust fund liabilities of the broker to each beneficiary.

For example:

ABC Realty, Inc. Trust Account
0339-000011
5/31/99
Balances per Separate Beneficiary Records:
 Jones \$500.00
 Smith \$250.00
 Thompson \$100.00
Total of Separate Records: \$850.00
Balance per Record of All Trust Funds Received: \$850.00
Difference (if any, should be fully explained): \$0.00

Reference:

Regulation 2831.2

5. Are trust funds deposited in a timely manner?

Correct Procedure:

Unless otherwise specified in writing by the beneficiary of the funds, a broker is required to do one of the following three things with trust funds no later than three business days following receipt of the funds by the broker or the broker's salesperson:

1. Deposit the funds into a neutral escrow depository.
2. Place funds accepted on behalf of the owner into the hands of the owner of the funds.
3. Deposit the funds into a trust fund bank account maintained by the broker.

When broker is handling escrow funds:

A real estate broker who is not licensed under the Escrow Law (Section 17000 et seq. of the Financial Code), when acting in the capacity of an escrow holder in a real estate transaction in which the broker is performing acts for which a real estate license is required, shall place all funds accepted on behalf of another into one of the three places listed above not later than the next business day following receipt of the funds by the broker or the broker's salesperson.

Reference:

Section 10145; Regulation 2832

6. Are authorized signatories either employed by the broker and licensed or unlicensed but bonded?

Correct Procedure:

Withdrawals may be made from the trust account only upon the signature of the broker or by one or more of the following persons with written authorization from the broker:

1. A salesperson licensed to the broker.
2. A person licensed as a broker who has entered into a written agreement with the employing broker.
3. An unlicensed employee of the broker with fidelity bond coverage at least equal to the maximum amount of trust funds to which the employee would have access.

Withdrawals may be made from the trust account of a corporate broker only upon the signature of an officer through whom the corporation is licensed or one of the persons detailed above. The corporate broker should always be a signatory on the trust account.

Concerning an unlicensed employee with fidelity bond coverage, it is recommended that the fidelity bond specifically identify the trust account which is being covered. The fidelity bond must not include a deductible clause.

Reference:

Regulation 2834

7. Are broker's funds commingled with trust funds?

Correct Procedure:

Funds belonging to a broker should not be commingled with trust funds. Common examples of commingling are:

- personal or company funds deposited into the trust fund bank account;
- trust funds deposited into the general or personal bank account; and
- funds collected on real property wholly owned by the broker handled through the trust account.

A broker, however, is allowed to maintain up to \$200 of personal funds in a trust account to cover checking account service fees and other bank charges.

Commissions, fees, other income earned by a broker, and funds belonging in part to the broker's principal and in part to the broker when it is not reasonably practicable to separate such funds, must be withdrawn from the trust account within 25 days from the date of deposit.

Reference:

Section 10176(e); Regulation 2835

SECTION 3 - Borrower Disclosures

1. Does the broker provide the required borrower disclosures in every transaction?

Correct Procedure:

1. In a transaction in which a broker is arranging a loan, a Mortgage Loan Disclosure Statement, Traditional (RE 882) or a Mortgage Loan Disclosure Statement (RE 883) must be provided within three days of receiving a completed written loan application from a prospective borrower(s). A copy of the disclosure statement signed by the borrower(s) and the broker, or the broker's representative, must be retained by the broker for three years. (There is an informational sheet with instructions for completing each form.)

2. When a transaction involves a nontraditional loan product, a Mortgage Loan Disclosure Statement, Nontraditional Mortgage Loan Product - One to Four Residential Units (RE 885) must be given according to the same rules as in #1. A nontraditional loan product is defined in Regulation 2842. See also Section 15 for additional compliance information on nontraditional loan products. (There is an informational sheet with instructions for completing the form and an instructional guide for completing the comparison of sample mortgage features on page 4 of the form.)

3. In the alternative, in a federally-related loan transaction where the principal loan amount for a senior lien is \$30,000 or more or for a junior lien is \$20,000 or more, a broker may provide a "good faith estimate" that complies with RESPA and meets the following conditions: the disclosure sets forth the broker's real estate license number, contains a clear and conspicuous statement on its face that the "good faith estimate" is not a loan commitment, all applicable disclosures required by the Truth in Lending Act are provided, and, if the loan contains a balloon payment, an acceptable disclosure of the balloon payment is provided. Prior to becoming obligated to the loan, the borrower(s) must acknowledge receipt of the "good faith estimate" and disclosures in writing. The broker must retain a true and correct copy of the "good faith estimate" and disclosures as acknowledged by the borrower(s) for three years.

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4. The disclosures must include the real estate broker's license identification number and NMLS unique identifier number if an individual broker or the corporation's license identification number and NMLS unique identifier number if a licensed corporation.
 5. The disclosures must contain the amount of all compensation to be earned by the broker including the actual amount of any yield/spread premium, if known, or an estimate of any anticipated yield/spread premium or other rebates from the lender. The disclosures must also contain the Department's licensing information telephone number. Disclosure of any material changes to the costs, expenses, or terms of the loan must be made to the borrower(s) in a timely manner.
 6. The broker must advise the borrower(s) whether or not the loan will be made with "broker-controlled funds," as defined.
 7. At the time of application, the broker must provide a Fair Lending Notice (RE 867A) to the prospective borrower(s). The notice must also be posted in a conspicuous place for public inspection. A signed acknowledgement of receipt of the notice (RE 867) should be retained by the broker for three years.
 8. If the broker is making or arranging a "covered loan," the "Consumer Caution and Home Ownership Counseling Notice" is provided to the prospective borrower(s) no later than three business days prior to signing the loan documents. (See also Section 10 – Covered Loans).
 9. If the broker negotiates a loan primarily in Spanish, Chinese, Tagalog, Vietnamese or Korean, a translated Mortgage Loan Disclosure Statement must be provided to the borrower(s) in one of the appropriate languages in order to comply with Civil Code Section 1632. Translated forms are available on the Department's Web site.

Reference:

Sections 10176(a),(c),(g), 10236.4(b), 10240, 10240.3, 10241; Regulations 2840, 2840.1, 2842, 2842.5; Health and Safety Code Section 35830; Civil Code Section 1632

2. Is the broker representing a buyer or seller in a real estate transaction and also being compensated for obtaining the loan for the buyer?

Correct Procedure:

If a broker, or his or her agent, will represent a buyer or seller in a real estate transaction and will also be compensated for obtaining the loan for the buyer, the broker, or his or her agent, must make a written disclosure of the broker or agent's roles pertaining to the transaction. In addition, the broker must disclose to all parties in the transaction the form, amount, and source of the compensation received or expected for the loan.

The broker may wish to consult with the U.S. Department of Housing and Urban Development (HUD) to determine their rules regarding real estate sales and the arranging of Federal Housing Administration (FHA) loans and federally related loans.

Reference;

Section 10177.6; Regulation 2904

SECTION 4 – Advertising

Does the broker’s mortgage loan advertising comply with the Department’s advertising criteria?

Correct Procedure:

1. No real estate licensee shall advertise, or cause to be advertised in any manner, any statement or representation with regard to rates, terms or conditions for making, purchasing or negotiating loans secured by real property which are false, misleading or deceptive. The advertisement cannot contain any claims or representations that are misleading or cannot be supported with satisfactory evidence to the Department.
2. Every advertisement disseminated primarily in California for a loan must include a disclosure within the printed text or oral text (radio or television) of the license under which the loan will be made or arranged and the NMLS unique identifier number.

The following are the approved license disclosures: “Real Estate Broker, California Department of Real Estate” or “California Department of Real Estate, Real Estate Broker.” “California” may be abbreviated as “CA,” “CAL” or “Calif” and “Department” can be abbreviated as “Dept.” A dash may be used instead of the comma.

The type size of the license disclosure must be at least as large as the smallest size type in the advertisement.

3. Advertisements to prospective lenders or note purchasers must include the broker license identification number.
4. When an advertisement contains a representation of an interest rate, the annual percentage rate must be disclosed in equally prominent type and font.
5. When an advertisement contains a representation of a payment, all of the following must be included in equally prominent type and font: term of the loan, principal loan amount, interest rate, and annual percentage rate. When the loan is an adjustable rate loan, there must also be equally prominent disclosure of how long the initial interest rate is in effect, how often and how much the interest rate and/or payments can change, and, if there is the potential for negative amortization (deferred interest), a statement to that effect. If the loan contains a provision for a balloon payment, the amount of the balloon payment must be disclosed in equally prominent type and font. There are additional rules for advertising payments on adjustable rate, interest-only or payment-option loans.
6. When advertising a “low doc/no doc,” “stated income,” or similar loan product, there must be a statement that the product may have a higher interest rate, more points or more fees than other products requiring documentation.
7. When an advertisement offers a gift, premium or rebate (inducement) to prospective borrowers, there must be a disclosure of all of the conditions that must be met in order to receive the gift, premium or rebate. These inducements may not be offered to a prospective lender or note purchaser.
8. When advertising the sale of a note to prospective note purchasers, no specific yield may be indicated or implied without disclosure of the note interest rate and the discount from the remaining principal balance at which it is being offered for sale.
9. Commissioner’s Regulation 2848 requires the Department to take such action as is appropriate to prevent or halt the publication of advertising that is false, misleading or deceptive in and of itself or through the omission of information that would prevent it from being false, misleading or deceptive. In addition to the actual text,

consideration is given to such factors as format, pictorial display and emphasis in determining whether an advertisement is likely to create a false impression. Real estate licensees must ensure that their advertising complies with all of the criteria established in Commissioner's Regulation 2848.

10. Brokers may submit their proposed mortgage loan advertisements to the Department for approval on a voluntary basis. The submission must include a Mortgage Loan Advertising Submittal (RE 884) signed by the broker or, if a corporate broker, the designated officer, a fee of \$40.00 and the proposed advertisement in triplicate. The submission may be made in person or by mail.

Reference:

Sections 10140.6, 10235, 10235.5, 10236.1, 10236.4, 10240.3; Regulations 2770.1, 2773, 2847.3, 2848

SECTION 5 – Fees

Does the broker fully disclose all fees, costs and compensation?

Correct Procedure:

1. No costs and expenses of making a loan may be charged to a borrower which have not been paid, incurred or reasonably earned by the broker. No fee may be charged as part of the costs and expenses of making a loan which exceeds the fee customarily charged for the same service or comparable service in the community where the service was rendered. If an escrow is conducted by a licensed escrow agent, title insurance company, bank or trust company, or a savings institution and a fee is charged to the borrower by the escrow depository for the service, no additional fee can be charged to the borrower by the broker, a salesperson licensed to the broker or any entity controlled by the broker for services related to the escrow.
2. A broker must disclose to the prospective borrower(s) all anticipated compensation being paid from all sources, including from the borrower and the lender. The broker must disclose to the prospective borrower(s) all yield/spread premiums, rebates and other compensation that he or she will earn.
3. A real estate licensee who acts as the agent for either party in a transaction for the sale, lease or exchange of real property, a business opportunity or a mobilehome, and receives or anticipates receiving compensation for securing a loan to finance the transaction, must disclose to both parties to the transaction, prior to closing, the form, amount and source of compensation received or expected.

Reference:

Sections 10176(g), 10240; Regulations 2843, 2904.

SECTION 6 – Advance Fees

Does the broker collect any fees from prospective borrowers, other than for appraisals and/or credit reports, for any services that will be provided by the broker or others?

Correct Procedure:

1. An advance fee is defined as “a fee, regardless of the form, that is claimed, demanded, charged, received, or collected by a licensee for services requiring a real estate license, or for a listing, as that term is defined in Section 10027, before fully completing the service the licensee contracted to perform or represented would be performed.” In a mortgage loan transaction it is unlawful for a broker to collect a fee in advance for services to

be rendered to a principal (client) without first submitting, and obtaining approval of, an advance fee agreement and related materials from the Department. This includes loan modification activities performed by a broker. As stated in Section 2, Trust Fund Handling, a broker may collect a fee for an appraisal report and/or credit report in advance without having an advance fee agreement.

2. When a broker collects an advance fee pursuant to qualified agreement, the fee must be held in a trust account and the funds remain the property of the principal (client) until the service or services are completed. An accounting must be provided to the principal at the end of each calendar quarter and when the contract has been completed.

3. If a broker is providing loan modification or other similar foreclosure consulting services to a homeowner where a Notice of Default has been recorded against the property, the broker may not claim, demand, charge, receive or contract for an advance fee.

4. Effective October 11, 2009, brokers are prohibited from collecting advance fees for residential loan modification activities pursuant to Senate Bill 94 (Section 10085.6). Brokers may not separate services for the purpose of collecting fees in advance of the loan modification service being completed.

Reference:

Sections 10026, 10027, 10085, 10085.5, 10085.6, 10131.2, 10146; Civil Code Section 2945; Regulations 2970 and 2972.

SECTION 7 – Article 7 - Regulated Loans

With the exception of the disclosure statement requirement and rules regarding late charges and prepayment penalties, Article 7 only applies to bona fide senior liens under \$30,000 and bona fide junior liens under \$20,000, so called “regulated loans.” NOTE: These rules may also apply to a “covered loan” discussed in Section 11.

Does the broker make or arrange loans secured directly or collaterally by liens on real property where the principal amount on a senior lien is less than \$30,000 and on a junior lien is less than \$20,000.

Correct Procedure:

1. With the exception of the disclosure statement requirement (see Section 3 – Borrower Disclosures), Article 7 applies only to loans secured by a dwelling which is defined as a single dwelling in a condominium or cooperative or any parcel containing four or fewer residential buildings.

2. The broker must provide the Mortgage Loan Disclosure Statement, Traditional (RE 882), Mortgage Loan Disclosure Statement (RE 883), Mortgage Loan Disclosure Statement, Nontraditional Mortgage Loan Product - One to Four Residential Units (RE885) or alternative disclosure statements to the borrower(s). (See Section 3 – Borrower Disclosures.)

3. The maximum amount of all costs and expenses for obtaining the loan, not counting actual charges for title insurance and recording fees, cannot exceed 5% of the principal amount of the loan or \$390 if the 5% amount is less than \$390. In no event can the fees exceed \$700. Only costs and expenses that have actually been paid, incurred or reasonably earned by the broker can be charged to the borrower.

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4. The maximum commissions that can be charged to the borrower are determined by the lien priority (senior lien or junior lien) and the term of the loan as follows:
 - For a senior lien, 5% of the principal amount of the loan if the term is less than three years and 10% where the term is for three years or more,
 - For a junior lien, 5% of the principal amount of the loan if the term is less than two years, 10% if the term is two years but less than three years and 15% if the term is three years or more.
 5. The purchase of credit life or credit disability insurance cannot be a condition of making the loan.
 6. If the property securing the loan, either directly or collaterally, is an owner-occupied dwelling of three units or less and is not a note given back to the seller by the purchaser, then no payment that is more than twice the amount of the smallest payment, can be due in less than 73 months; therefore, in the first six years of the loan, the installment payments must be substantially equal..
 7. If the property securing the loan, either directly or collaterally, other than a note given back to the seller by the purchaser, and is not an owner-occupied dwelling, then no payment that is more than twice the amount of the smallest payment can be due in less than three years.
 8. A late charge cannot be more than 10% of the principal and interest installment due except that a minimum of \$5 can be charged if the late charge would be less than \$5. No late charge can be charged more than once for the same late payment and cannot be charged if the payment is made within 10 days of its scheduled payment date. For a balloon payment, the late charge cannot be more than the late charge assessed for the largest single monthly payment other than the balloon payment. A late charge for a balloon payment can be charged for each month that the balloon payment is past due.
 9. A prepayment penalty on a loan secured by a single-family, owner-occupied dwelling can be charged only if the prepayment is made within seven years of the date the loan was executed. A prepayment not exceeding 20% of the unpaid balance of the loan can be made without penalty in any 12-month period and any prepayment made in excess of that amount can be subject to a charge of not more than six months advance interest.

Reference:

Sections 10240, 10240.1, 10240.2, 10240.3, 10241, 10241.1, 10242, 10242.5, 10242.6, 10244, 10244.1, 10245; Regulations 2840, 2840.1, 2843

SECTION 8 – Article 5 - Private Money Transactions

Article 5 does not apply to the negotiation or sale of notes that were created for the purpose of financing the sale or exchange of real property (seller carry-backs) where the broker acted as an agent, was not a party to the transaction and where the required disclosures were given to each party to the transaction. (The provisions of Article 5 dealing with “threshold” reporting, loan servicing agreements and the delivery of property appraisals do not pertain to transactions where the lenders or note purchasers are primarily institutional lenders or investors, or where the note or sale is negotiated or the loan is being serviced pursuant to a permit issued by the Department of Corporations pursuant to the Corporate Securities Law of 1968.)

Does the broker arrange loans for, sell existing notes to, or service loans for, private individual, non-institutional lenders or note-purchasers?

Correct Procedure:

1. Pooling of loan funds – Except as authorized by a permit from the Department of Corporations pursuant to the Corporate Securities Law of 1968, funds accepted by the broker from a lender/purchaser, or caused to be deposited into an escrow from a lender/purchaser, must be for a specific loan transaction. Payments of loan funds payable according to the terms of a note secured by real property or by a real property sales contract, including payoffs, cannot be retained by a broker for more than 25 days without a written agreement with the lender/purchaser.
2. Self-dealing - When a broker, or a salesperson acting on behalf of a broker, solicits funds from a prospective lender or note purchaser for a purchase or loan transaction that will directly or indirectly benefit the broker, so-called self-dealing, certain rules must be followed. Prior to making the solicitation or presenting the investor with the Lender/Purchaser Disclosure Statement, the broker must first submit a complete copy of the disclosure statement, without the investor's signature, to the Department. The completed disclosure is sent along with a statement that it is being submitted pursuant to Business and Professions Code Section 10231.2. (Self-dealing does not include transactions where the broker is benefiting only from the commissions, costs or expenses of making or arranging a loan.) The broker must then provide the investor with the completed Lender/Purchaser Disclosure Statement not less than 24 hours before receiving any funds from the investor, or the execution of any agreement obligating the investor to make the loan or purchase the note. The disclosure statement must be signed by the prospective lender/purchaser and an exact copy must be retained by the broker for four years.
3. Threshold Reporting – Brokers who meet the “threshold” reporting criteria are required to submit specified quarterly and annual reports to the Department. There are several ways for a broker to meet the reporting criteria as follows:
 - Negotiation of 10 or more loans secured directly or collaterally by liens on real property of business opportunities in an aggregate amount of more than \$1 million as an agent of another or others, in a successive 12-month period or
 - Negotiation of 10 or more sales or exchanges of real property sales contracts or notes secured directly or collaterally by liens on real property or business opportunities in an aggregate amount of more than \$1 million as an agent of another or others, in a successive 12-month period or
 - Negotiation of 10 or more sales or exchanges of real property sales contracts or notes secured directly or collaterally by liens on real property or business opportunities in an aggregate amount of more than \$1 million as the owner of those notes or contracts, in a successive 12-month period or
 - Making collections of payments in an aggregate amount of \$250,000 or more on behalf of owners (beneficiaries) of notes secured directly or collaterally by real property or real property sales contracts or both, in a successive 12-month period or
 - Making collections of payments in an aggregate amount of \$250,000 or more on behalf of obligors (borrowers) of notes secured directly or collaterally by real property, lenders of real property sales contracts or both in a successive 12-month period.
 - The negotiation of a combination of two or more new loans and sales in an aggregate amount of more than \$250,000 in any successive three months or a combination of five or more new loans and sales in an aggregate amount of more than \$500,000 in any successive six months will create a rebuttable presumption

that the broker will meet the threshold.

- Within 30 days of meeting any of the above criteria, the broker must submit a Threshold Notification (RE 853) to the Department. The “threshold” reporting criteria apply only to transactions where the prospective lender/purchaser is a private individual investor or trustees of a pension, profit-sharing or welfare fund with a net worth of less than \$15 million and where the loan or sale is not negotiated or the note is not serviced, under the authority of a permit issued by the Department of Corporations pursuant to the Corporate Securities Law of 1968.
- If a broker who meets the threshold reporting criteria fails to notify the Department in writing of that fact within 30 days of meeting the criteria, the broker shall be assessed a penalty of \$50 per day for each additional day the notification is not received for the first 30 days and then a penalty of \$100 per day not to exceed \$10,000 until the Department receives written notification. The notification must also be submitted when a broker will no longer meet the above reporting criteria.

4. “Threshold” Reports – Brokers who meet the above criteria must submit quarterly and annual reports to the Department based on their fiscal year as follows:

- Within 90 days after the end of the broker’s fiscal year, an independent accountant’s report of a review of trust funds (Trust Account Review). If a broker did not collect trust funds during the entire fiscal year, the broker may submit a Trust Fund Non-Accountability Report (RE 854), signed before a notary. If the broker’s fiscal year ends between November 30 and the last day of February, then the report shall be due no later than May 31 of each calendar year.
- Within 90 days after the end of the broker’s fiscal year, a Mortgage Loan/Trust Deed Annual Report (RE 881) that reports the broker’s business activities during the fiscal year.
- Within 30 days after the end of each of the first three of the broker’s fiscal quarters, a Trust Fund Status Report (RE 855), a Trust Fund Bank Account Reconciliation (RE 856) and the bank statement for the last month of the fiscal quarter. If the broker did not collect trust funds during a fiscal quarter, the broker shall submit a Trust Fund Non-Accountability Report (RE 854) for that fiscal quarter.
- If the broker fails to submit any of the above reports by the established due date or within any additional time as the Department may allow for good cause, the Department may conduct an audit of the brokers books and records and prepare the reports at a cost to the broker of one and a half times the cost of conducting the audit and preparing the reports.

5. Disclosure Statements – When soliciting or negotiating the arrangement of a loan or sale of a note, a broker must provide the prospective investor with a Lender/Purchaser Disclosure Statement (LPDS) (RE 851) as early as practicable and before the receipt of funds by or on behalf of the investor. The LPDS must be signed by the lender/purchaser and by the broker, or a salesperson licensed to the broker, and must be retained for a period of three years. There are separate versions of the LPDS for the arrangement of a loan, the sale of a note or the collateral assignment of a note. Each must be fully completed with the required information in order for the lender/purchaser to be able to make an informed decision whether or not to make the loan or purchase the note. Each disclosure must contain the real estate broker’s license identification number if an individual broker or the corporation’s license identification number if a licensed corporation. The prospective lender/purchaser is entitled to a copy of a written, independent appraisal. On a case-by-case basis, the investor may waive his or her right to the appraisal in writing. In that case, the broker must provide the investor with a written estimate of the fair market value of the property securing the loan supported by objective data.

The LPDS is not required with respect to the following persons:

- The prospective purchaser of a security offered under the authority of a permit issued by the Department of Corporations pursuant to the Corporate Securities Law of 1968 which requires that each prospective purchaser be given a prospectus or other approved disclosure statement,
- The seller of real property carrying back all or part of the purchase price,
- The prospective purchaser of a security offered pursuant to a Department of Corporations regulation granting an exemption from qualification of the offering if one of the conditions is that each prospective purchaser be given a prescribed disclosure statement before becoming obligated to purchase the security,
- The prospective lender or purchaser is a bank, savings institution, finance lender or other institutional lender or investor or is a licensed residential mortgage lender,
- A licensed real estate broker selling all or part of the note to a person that is not required to receive a LPDS.

6. Servicing Agreements – A real estate broker who undertakes to service a promissory note secured directly or collaterally by a lien on real property or a real property sales contract must have the written authorization of the borrower, lender or note owner that complies with the following:

- The terms of the servicing agreement must satisfy all of the requirements of Business and Professions Code Section 10238(k)(1), (2), (4) and (5).
- The licensee must provide the lender with the following accountings:
 1. an accounting of the unpaid principal balance at the end of the year.
 2. an accounting of collections and disbursements received and made during each year
 3. each accounting must identify the person who holds the original note or contract and deed of trust
- The licensee must provide the lender or note owner written notification within 15 days of any of the following events:
 1. the recording of a notice of default
 2. the recording of a notice of trustee sale
 3. the receipt of any payment constituting an amount greater than or equal to five monthly payments, together with a request for partial or total reconveyance of the real property, in which case the notice shall also indicate any further transfer or delivery instructions.
 4. the delinquency of any installment or other obligation under the note or contract for over 30 days.

7. Advancing Funds – If a broker is servicing a note secured by real property on behalf of a mortgagee, beneficiary or note owner and causes funds, other than funds received from the obligor (borrower), to be applied toward a payment to protect the security of the note being serviced, including a payment on a senior lien, the broker shall give written notice to the mortgagee, beneficiary, or note owner of the following: the date and amount of the payment, the name of the person to whom the payment was made, the source of the funds and the reason for making the payment. The notice must be made no later than 10 days after making the payment.

8. Loan Servicing – For the purposes of the California Commercial Code, if a broker arranges or sells a note secured by real property, or any interest therein, and then undertakes to service the note on behalf of the lender or purchaser, delivery, transfer and perfection shall be deemed complete even if the broker retains possession of the note or collateral instruments as long as the deed of trust or assignment of deed of trust in favor of the

lender or purchaser is recorded in the office of the county recorder in the county in which the securing property is located and the note is made payable to the lender or is endorsed or assigned to the purchaser.

9. Recordation of Trust Deeds and Assignments

- When a licensee negotiates a loan secured by a deed of trust, the licensee must cause the deed of trust to be recorded in the name of the beneficiary or the beneficiary's nominee. The deed of trust cannot be recorded in the name of the licensee or licensee's nominee (so-called table funding). The deed of trust must be recorded with the county recorder in the county in which the securing property is located before funds are disbursed unless the lender has given written authorization for prior release.
- If funds are released on the lender's written authorization prior to recording, the deed of trust must be recorded or delivered to the lender or beneficiary with a written recommendation that it be recorded within 10 days following release of the funds.
- When a licensee sells, exchanges or negotiates the sale or exchange of a real property sales contract or note secured by a deed of trust, the licensee must cause a proper assignment of the real property sales contract or deed of trust to be executed and cause the assignment to be recorded in the name of the purchaser or purchaser's nominee (who shall not be the licensee or licensee's nominee). The assignment must be recorded in the office of the county recorder in the county in which the secured property is located within 10 working days after the licensee or seller receives funds from the buyer or after close of escrow, or the real property sales contract or deed of trust must be delivered to the purchaser with a written recommendation that the assignment thereof be recorded forthwith.
- The above requirements do not apply if the lender or purchaser is any person or entity listed in Section 10232(c)(1), the deed of trust is recorded with the county recorder in the county in which the property is located and, the real property is not a single dwelling unit in a condominium or cooperative or any parcel containing only one to four residential units.

10. Delivery of copies of deed of trust – In addition to the above requirements, a broker must deliver or cause to be delivered conformed copies of any deed of trust to both the investor or lender and the borrower in a reasonable amount of time from the date of recording.

11. A real estate licensee cannot advertise to give or offer to give to a prospective note purchaser or lender, any premium, gift, or any other object of value as an inducement to make or purchase a promissory note secured directly or collaterally by a lien on real property or a real property sales contract.

- A real estate licensee may offer an inducement to a prospective borrower, however any advertisement or offer must include all of the conditions required to receive the offer and no fees, costs or expenses may be increased by the licensee in order to offset to cost of giving the inducement.

Reference:

Sections 10230, 10231, 10231.1, 10231.2, 10232, 10232.2, 10232.25, 10232.4(b), 10232.5, 10236.4(b), 10236.5, 10233, 10233.1, 10233.2, 10234, 10234.5, 10235, 10236.1; Regulations 2846, 2846.5, 2846.7, 2846.8, 2849.01, 2849.1.

SECTION 9 – Article 6 - Private Money Transactions with Multiple Beneficiaries (Fractionalized Loans)

Article 6 applies only to the exemption from securities qualification claimed under Section 25102.5 of the

Corporations Code. Article 6 does not apply to transactions conducted pursuant to a permit issued by the Department of Corporations to qualify the offer and sale of securities under the Corporate Securities Law of 1968 or to any other exemption from securities qualification which may be claimed without complying with Article 6. Transactions conducted pursuant to the exemption from securities qualification provided by Article 6 must comply with each and every provision of Article 6. Section 10237 states, “Any transaction that involves the sale of or offer to sell a series of notes secured directly by interests in a note secured directly by one or more parcels of real property equivalent to a series transaction, shall comply with all of the provisions of this article.”

Does the broker arrange loans for, sell existing notes to, or service loans for, private individual, non-institutional lenders or note-purchasers where there are multiple (fractional) beneficial interests?

Correct Procedure:

1. The Notice

A broker must submit the Multi-Lender Transaction Notice (RE 860) to the Department within 30 days of:

- The broker’s first transaction
- Any material change to the information required in the notice
- Becoming the servicing agent for notes upon which the payments due in any consecutive three-month period exceeds \$125,000 or the number of persons entitled to payments exceeds 120.

2. Advertising

All advertising must show the name of the broker and comply with Section 10235, Section 2848 of the Commissioner’s Regulations and Section 260.302 of Title 10, California Code of Regulations. Making reference to Article 6 in any advertising may be considered misleading or deceptive if the representation may be reasonably construed by the investor as an implication of merit or approval of the transaction.

3. The Security

Loans must be directly secured by real property located in California. No collateral assignments are permitted. Loans cannot be, by their terms, subject to subordination to any subsequently created deed of trust. The notes cannot be promotional notes as defined in Section 10238(d).

4. No Self-Dealing

The notes or interests must be sold by or through a broker, as principal or agent. At the time the interests are originally sold or assigned neither the broker nor any affiliate of the broker can have an interest as an owner, lessor, or developer of the securing property, or any contractual right to acquire, lease or develop the securing property. The two exceptions to this rule are when:

- The broker or an affiliate of the broker is acquiring property pursuant to a foreclosure under, or sale pursuant to, a deed of trust securing the note for which the broker is the servicing agent,
- The broker or an affiliate of the broker is reselling from inventory property acquired by the broker pursuant to a foreclosure under, or sale pursuant to, a deed of trust securing a note for which the broker is the servicing agent.

5. Maximum Number of Investors and Investor Qualification Statements

The notes or interests cannot be sold to more than 10 persons who meet one or both of the qualifications based on income or net worth. The person must sign a specified statement which must be retained by the broker for a

period of four years.

For the purposes of counting the number of investors:

- A husband and wife and their dependents, and an individual and his or her dependents are counted as one person
- A retirement plan, trust, business trust, corporation, or other entity that is wholly-owned by an individual and the individual's spouse or the individual's dependents are not counted separately from the individual. The investments of these entities are aggregated with those of the individual for the purposes of meeting the income and/or net worth requirements.
- "Institutional investors" enumerated in Sections 25102(i) or 25104(c), or a rule adopted pursuant thereto, are not counted.
- A partnership, limited liability company, corporation or other organization that was not specifically formed for the purpose of purchasing the security offered pursuant to Article 6 is counted as one person.

6. Identical Interests

The notes or interests must be identical in their underlying terms, including the right to direct or require foreclosure, rights to and rate of interest, and other incidents of being a lender. The sale to each purchaser must be upon the same terms, subject to adjustment for the face or principal amount or percentage interest purchased and for interest earned or accrued. There can be different selling prices for interests to the extent that the differences are reasonably related to changes in the market value of the loan occurring between the sales of the interests. The interest of each purchaser must be recorded pursuant to the requirements of Section 10234.

7. Maximum LTV's, Construction Loans, Multiple Properties

The aggregate principal amounts of the notes or interests sold, including the balance of any senior encumbrances, are subject to maximum loan to value percentages. The percentages based on the current market value of the securing property as determined by the broker or appraiser as required by Section 10232.6. This amount can be exceeded if mortgage insurance is obtained through a licensed insurer for the benefit of the holders of the notes or interests. The maximum loans to value percentages are:

- Single-family, owner-occupied - 80%
- Single-family, not owner-occupied - 75%
- Commercial and income-producing properties - 65%
- Single-family residentially zoned lot or parcel which as installed offsite improvements including drainage, gutters, sidewalks, paved roads, and utilities as required - 65%
- Land that has been zoned (and if required, approved for subdivision as) commercial or residential development - 50%
- Other real property - 35%

The percentages above can be exceeded when and to the extent that the broker determines that exceeding the percentages is reasonable and prudent considering all relevant factors pertaining to the real property. However, in no event can the aggregate principal amounts of the notes or interests sold, including any senior encumbrances, exceed 80% of the current market value of improved real property or 50% of the current market value of unimproved real property, except in the case of a single-family zoned lot or parcel as described above

which cannot exceed 65% of the current market value, plus any insured amount as described above. A written statement by the broker setting forth the material considerations and facts that he or she relied upon for the determination must be retained in the broker's transaction file. Either a copy of the statement or the information contained in the statement must be included in the Lender/Purchaser Disclosure Statement. A copy of the appraisal or broker's evaluation for each parcel or real property securing the note must be delivered to each purchaser, and the broker must advise each purchaser of their right to receive a copy.

For construction and rehabilitation loans, the term "current market value" may be deemed to be the value of the completed project if all of the following safeguards are met:

- An independent neutral third-party escrow holder is used for all deposits and disbursements,
- The loan is fully funded, with the entire amount to be deposited in escrow prior to recording the deed of trust,
- A comprehensive, detailed draw schedule is used to ensure proper and timely disbursement to allow for completion of the project,
- The disbursement draws from the escrow account are based on verification from an independent qualified person, as defined pursuant to Section 10238(h)(4)(D), who certifies that the work completed to date meets the related codes and standards and that draws were made in accordance with the construction contract and draw schedule.
- An appraisal is completed by a qualified and licensed appraiser in accordance with USPAP.
- In addition to the transaction documentation required pursuant to Section 10238(i), the documentation must include a detailed description of actions that may be taken in the event of a failure to complete the project, whether the failure is due to default, insufficiency of funds or other causes.
- The entire amount of the loan does not exceed \$2,500,000.
- If a note or interest is secured by more than one parcel of real property, for the purpose of determining the maximum amount of the loan, each property securing the loan must be assigned a portion of the loan that does not exceed the percentage of current market value described above.

8. Loan Documentation for Defaults

The documentation of a loan transaction must require that:

- A default upon any interest or note is a default upon all of the interests or notes and
- The holders of more than 50% of the recorded beneficial interests of the notes or interests may govern the actions to be taken on behalf of all holders in accordance with Civil Code Section 2941.9 in the event of default or foreclosure for matters that require direction or approval of the holders, including designation of the broker, servicing agent, or other person acting on their behalf, and the sale, encumbrance or lease of real property owned by the holders resulting from foreclosure or receipt of a deed in lieu of foreclosure.

The required terms may be included in the deed of trust, in the assignment of interests, or in any other documentation as is necessary or appropriate to make them binding on the parties.

9. Receipt of Funds, Trust Accounts and CPA-prepared Reports

- No funds can be collected, or caused to be collected, from prospective lenders or note purchasers except as to a specific loan or note secured by a deed of trust that the broker owns, is authorized to negotiate or is

unconditionally obligated to buy.

- All funds must be handled pursuant to Section 10145 for disbursement to the persons entitled to the funds upon recordation of their interests.
- The books and records of the broker or servicing agent, or both, must be maintained in a manner that clearly identifies transactions conducted pursuant to Article 6 and the receipt and disbursement of funds in connection with these transactions.
- If a broker or affiliate of the broker is the servicing agent for notes or interests sold pursuant to Article 6 that have payments due in any consecutive 3-month period which exceed \$125,000, or the number of persons entitled to the payments exceeds 120, the trust account(s) of the broker must be inspected by a CPA and a specified report must be submitted to the Department. The CPA will select at random a specified number of “sales” and “payments” as defined in Section 10238(j)(4) and (5) for inspection. The report, Trust Account Report (Multi-Lender Transactions) (RE 852), must be submitted by the accountant to the broker or servicing agent and to the Department and is due to the Department within 30 days after the end of the broker’s fiscal quarter (the same schedule and “threshold reports”). NOTE: The criteria for the CPA-prepared reports required under Article 6 is based on payments due in any three-month period as opposed to the reporting criteria for “threshold brokers” described in Section 8 above which is based on payments collected in any 12-month period.

10. Sale of the Notes or Interests, Requirements of the Servicing Agreement

The notes or interests must be sold subject to a written agreement that obligates a licensed real estate broker, or a person exempted from the licensing requirement, to act as servicing agent for the purchasers or lenders. A copy of the servicing agreement must be delivered to each purchaser. The broker must offer his or her services, or the services of an affiliate of the broker, as the servicing agent for each transaction. The agreement must contain the requirements specified in Section 10238(k)(1)(2)(4) and (5).

11. Lender/Purchaser Disclosure Statement

- The Lender/Purchaser Disclosure Statement (RE 851A or RE 851B as appropriate) must be provided to each prospective lender or note purchaser in the same manner as described in Section 8 (Private Money Transactions) item #5.
- Any interest of the broker or affiliate of the broker in the transaction as permitted by Section 10238(e) must be included in the disclosure statement.
- Whenever the broker knows information regarding the transaction that is not specified in the disclosure statement and the information is material or essential to keep the information provided in the form from being misleading, the information must be provided by the broker to the prospective lenders or note purchasers.
- If more than one parcel of real property will secure the note or interests, the Lender/Purchaser Disclosure Statement (RE 851D) must be provided to each prospective lender or note purchaser.

12. Identity of the Purchasers

The broker or servicing agent must provide any purchaser of a note or interest, upon request, with the names and addressers of the purchasers of other persons with interests in the note.

13. Option to Purchase

The broker cannot have the option or election to acquire the interests of the lenders or purchasers or to acquire the real property securing the interests. There is no prohibition to the broker or affiliate from acquiring the interests with the consent of the purchasers or lenders whose interests are being purchased, or the property with the consent of the purchasers or lenders, if the consent is given at the time of acquisition.

14. Annual Trust Account Report

The broker or servicing agent that meets the reporting criteria described in #9 above must also submit an annual report of a review of its trust accounts (Trust Account Review). If the broker submits reports as a “threshold broker” (see Section 8 – Article 5 – Private Money Transactions, 4. “Threshold” Reports) then that annual report will satisfy this requirement. The broker’s transactions conducted under Article 6 must be included in that report.

15. Annual Business Activities Report

The broker or servicing agent that meets the reporting criteria described in #9 above must also submit the annual report of business activities, Mortgage Loan/Trust Deed Annual Report (RE 881). If the broker submits reports as a “threshold broker” (see Section 8 – Article 5 – Private Money Transactions, 4. “Threshold” Reports) then that annual report will also satisfy this requirement. The broker’s transactions conducted under Article 6 must be included in the report.

16. Identifying the Transaction

The broker must indicate in the transaction file whether the transaction was conducted pursuant to a permit issued by the Department of Corporations, or any exemption from the requirement for a permit, including the exemption provided by Article 6. The broker must also provide a copy of this information to each investor. The broker must retain the information for three years.

Reference:

Sections 10236.7, 10237, 10238 (a) through (p), 10239, 10239.1, 10239.2, 10239.3; Regulations 2846.1, 2846.7, 2849.01

SECTION 10 – Business Activity and Mortgage Call Reports

Business Activity Reports will be submitted online to the Department by brokers who are performing residential mortgage loan activities. Part A of the form will include the activities performed by the broker and the residential mortgage loan originators sponsored by the broker. This report will be due within 90 days following the end of the broker’s fiscal year.

Brokers who meet the threshold and/or multi-lender reporting criteria will submit Part B of the online submission form.

Brokers will submit online quarterly Mortgage Call Reports to the NMLS system. These reports will be due 30 days following the end of each of the broker’s quarters and will include the activities performed by the mortgage loan originators sponsored by the broker. In addition, brokers will submit financial condition reports to the NMLS system.

Reference:

Sections 10166.07 and 10166.13

SECTION 11 – Covered Loans (Financial Code Section 4970 et seq.)

Sometimes called “Cal-32,” this statute applies to certain high-cost, high-fee loans. Real estate brokers licensed by the Department of Real Estate, or licensees under the California Department of Corporations or California Department of Financial Institutions who conduct these transactions should pay careful attention to all of the provisions of this law. Note: Additional rules will apply if the transaction also falls under Article 7 (see Section 7 – Article 7 – Regulated Loans). Loans that fall within the requirements of this statute are:

- A “consumer loan” secured by real property located in California that is, or is intended to be, used as the principal dwelling of the consumer that is improved by a one to four residential unit (Note: “Consumer loan” does not include a reverse mortgage, an open line of credit defined in Part 226 of Regulation Z, or a bridge loan as defined in Financial Code Section 4970(d). A “consumer loan” also does not include a consumer credit transaction that is secured by a rental property or second home.), and
- The original principal balance does not exceed the most current conforming loan limit for a single-family first mortgage loan established by the Federal National Mortgage Association (FNMA) for a mortgage or deed of trust, and
- The annual percentage rate at consummation of the transaction will exceed by more than eight percentage points the yield on Treasury Securities having comparable periods of maturity on the 15th day of the month immediately preceding the month in which the application is received by the creditor, or
- The total points and fees payable by the consumer at or before closing will exceed six percent of the total loan amount.
- Points and fees include the following:
 - All items required to be disclosed as finance charges under Sections 226.4(a) and 226.4(b) of Regulation Z, including the Official Staff Commentary, except interest,
 - All compensation and fees paid to mortgage brokers in connection with the loan transaction,
 - All items listed in Section 226.4(c) of Regulation Z, only if the person originating the covered loan receives direct compensation in connection with the charge. Does the broker arrange or make certain “high-cost, high-fee” loans for borrowers that are covered loans?

Correct Procedure:

The following are prohibited acts and limitations for covered loans:

1. A covered loan cannot include a prepayment penalty after the first 36 months after the consummation of the loan.
 2. A covered loan may include a prepayment penalty only if the person who originates a covered loan:
 - Has also offered the consumer a choice of another product without a prepayment penalty and
 - Has disclosed in writing to the consumer at least three days prior to loan consummation the terms of the prepayment penalty for accepting a covered loan with the prepayment penalty and the rates, points and fees that would be available to the consumer for accepting a covered loan without a prepayment penalty and,
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- Has limited the amount of the prepayment penalty to an amount not to exceed the payment of six months advance interest at the contract interest rate then in effect, on the amount prepaid in any 12-month period in excess of 20 percent of the original principal amount.
 - A covered loan cannot impose a prepayment penalty if the covered loan is accelerated as a result of default.
 - Will not finance a prepayment penalty through a new loan that is originated by the same person.
3. A covered loan with a term of five years or less may not provide at origination for a payment schedule with regular periodic payments that do not fully amortize the principal balance as of the maturity date of the loan.
- For a payment schedule that is adjusted for the seasonal or irregular income of the consumer, the total installments in any year cannot exceed the amount of one year's worth of payments on the loan. This requirement does not apply to a bridge loan as defined in Financial Code Section 4973(b)(2). Note: The definition of "bridge loan" for the purpose of this requirement is different than the definition of "bridge loan" when determining if a loan is a covered loan. (See Financial Code Section 4970(d)).
4. A covered loan cannot contain a provision for negative amortization such that the payment schedule for regular monthly payments causes the principal balance to increase, unless the covered loan is a first mortgage and the person who originates the loan discloses to the consumer that the loan contains a provision for negative amortization that may add principal to the balance of the loan.
5. A covered loan cannot include terms under which periodic payments required under the loan are consolidated and paid in advance from the loan proceeds.
6. A covered loan cannot contain a provision that increases the interest rate as a result of a default.
- This provision does not apply to interest rate changes in a variable (adjustable) rate loan that are otherwise consistent with the provisions of the loan documents, provided that the change in interest rate is not triggered by a default or the acceleration for the indebtedness.
7. A person who originates a covered loan cannot make or arrange a covered loan unless at the time the loan is consummated the person reasonably believes the consumer(s) will be able to make the scheduled payments based on their current or expected income, current obligations, employment status, and other financial resources, other than the equity in the dwelling that secures the loan.
- In a covered loan that is structured to increase to a specific designated rate at a specific designated date not exceeding 37 months from the date of application, the evaluation of the consumer's ability to repay the loan must be based on the fully indexed rate calculated at the time of application.
 - The consumer shall be presumed to be able to make the scheduled payments if, at the time the loan is consummated, the consumer's total debt to income ratio does not exceed 55% of their current gross income as verified.
 - No presumption of inability to make the scheduled payment will arise solely from the fact that, at the time the loan is consummated, the consumer's total debt to income ratio including the covered loan, exceeds 55%.
 - In the case of a stated income loan, the reasonable belief can be based on the income stated by the consumer and other information that the person originating the loan customarily obtains in connection with loans of this type. A person cannot knowingly or willingly originate a covered loan as a stated income loan with the intent or effect of evading this law.
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8. A person who originates a covered loan cannot pay a contractor under a home-improvement contract from the proceeds of the loan other than by an instrument that is payable to the consumer, or jointly payable to the consumer and the contractor, or at the election of the consumer, to a third party escrow agent for the benefit of the contractor in accordance with the terms and conditions in a written escrow agreement signed by the consumer, the person that originates the loan and the contractor prior to the disbursement of funds.
- No payments, other than progress payments for home-improvement work that the consumer certifies is completed, can be made to a escrow account or jointly to the consumer and contractor unless the person who originates the loan is presented with a signed and dated completion certificate by the consumer showing that the home-improvement contract was completed to the satisfaction of the consumer.
9. It is unlawful for a person who originates a covered loan to recommend or encourage a consumer to default on an existing consumer loan or other debt in connection with the solicitation or making of a covered loan that refinances all or any portion of the existing consumer loan or debt.
10. A covered loan cannot contain a call provision that permits the lender, in its sole discretion, to accelerate the indebtedness. This prohibition does not apply if the repayment of the loan has been accelerated in accordance with the terms of the loan documents (1) as a result of the consumer's default, (2) pursuant to a due-on-sale provision, or (3) due to fraud or material misrepresentation by a consumer in connection with the loan or the value of the security for the loan.
11. A person who originates a covered loan cannot refinance or arrange the financing of a consumer loan where the new loan is a covered loan that is made for the purpose of refinancing, debt consolidation or cash out, that does not result in an identifiable benefit to the consumer, considering the consumer's stated purpose for seeking the loan, fees, interest rates, finance charges and points.
12. A covered loan cannot be made unless the "Consumer Caution and Home Ownership Counseling Notice" specified in Financial Code Section 4973(k) is provided to the consumer no later than 3 business days prior to signing the loan documents.
- It shall be a rebuttable presumption that the licensed person has met his or her obligation to provide the disclosure if the consumer provides the licensed person with a signed acknowledgement of receipt of a copy of the notice.
13. A person who originates a covered loan cannot steer, counsel, or direct any prospective consumer to accept a loan product with a risk grade less favorable than the risk grade that the consumer would qualify for based on that person's current underwriting guidelines, prudently applied, considering the information available to that person, including the information provided by the consumer.
- A person will not be deemed to have violated this prohibition if the risk grade determination applied to a consumer is reasonably based on the person's underwriting guidelines if it is an appropriate risk grade category for which the customer qualifies with the person.
 - If a broker originates a covered loan, the broker cannot steer, counsel, or direct any prospective consumer to accept a loan product at a higher cost than that for which the consumer could qualify based on the loan products offered by the persons with whom the broker regularly does business.
14. A person who originates a covered loan cannot avoid, or attempt to avoid, this law by:
- Structuring a loan transaction as an open-end credit plan for the purpose of evading the provisions of this law when the loan would have been a covered loan if the loan had been structured as a closed-end loan,
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- Dividing any loan transaction into separate parts for the purpose of evading the provisions of this law.

15. A person who originates a covered loan cannot act in any manner that constitutes fraud.

16. A person who originates a covered loan must inform any employee who originates covered loans on behalf of the person, of the administrative or civil penalties for a violation of this law.

17. Upon request, a person who originates a covered loan must provide the Department or the consumer, at no cost, documentation that clearly demonstrates whether any loan is a covered loan. The documentation must include, but not be limited to, a full disclosure of the original principal balance, the APR, and the total points and fees, as defined in Financial Code Section 4970.

18. A person who provides brokerage services to a borrower in a covered loan transaction by soliciting lenders or otherwise negotiating a consumer loan secured by real property is the fiduciary of the consumer, and any violation of the person's fiduciary duties is a violation of this law.

- A broker who arranges a covered loan owes this fiduciary duty to the consumer regardless of whom else the broker may be acting as an agent for in the course of the loan transaction.

19. A person who originates a consumer loan cannot make a covered loan that finances points and fees in excess of \$1,000 or 6% of the original principal balance, exclusive of points and fees, whichever is greater.

20. A person who originates a covered loan cannot finance, directly or indirectly, into a consumer loan or finance to the same borrower within 30 days of a consumer loan any credit life, credit disability, credit property, or credit unemployment insurance premiums, or debt cancellation or suspension agreement fees.

- It is not a prohibition for these premiums to be calculated and paid on a monthly basis.
- "Credit insurance" does not include a contract issued by a government agency or private mortgage insurance company to insure the lender against loss caused by the mortgage's default.

Reference:

Financial Code Sections 4970(a) through (i), 4973(a) through (n), 4978.6, 4979, 4979.5, 4979.6, 4979.7.

SECTION 12 – Higher-Priced Mortgage Loans (Financial Code Section 4995 et seq.)

See definition of Higher-Priced Mortgage Loan in Financial Code (FC) Section 4995 for loans originated on or after 7/1/2010 for a principal dwelling.

- If the loan was a first lien, was the interest rate charged 1.5% higher than the average rate?
- If the loan was a second lien, was the interest rate charged 3.5% higher than the average rate?

Were terms of the loan within legal limits per FC Section 4995.1?

Prepayment penalty maximum in first 12 months was 2% of the prepaid balance

Prepayment penalty maximum in second 12 months was 1% of the prepaid balance

Were terms of the loan within legal limits per FC Section 4995.2? Violations of this section include "yes" answers to the following:

- Was the loan divided to avoid applying this section?
 - Was there any other subterfuge?
 - Was there any false, deceptive, or misleading statement or representation?
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- Did the broker disclose if only higher-priced mortgages are made or offered?
- Was there steering to a loan at a higher cost than the borrower would qualify for?
- Was there compensation for a prepayment penalty loan that exceeds the amount of compensation that would have been paid for a loan without a prepay penalty?
- Was the compensation fee different for the borrower, lender or third party?
- Did the broker recommend defaulting on the borrower's current loan when refinancing?
- Was there negative amortization?

Reference:

Financial Code Sections 4995, 4995.1, 4995.2, 4995.3, 4995.4, 4995.5, 4995.6

SECTION 13 – Residential Mortgage Loan Report (RE 857)

This section applies only to Department-licensed brokers who act as direct lenders. This section does not apply to Department-licensed brokers who do not make loans.

Does the broker act in the capacity of a direct lender?

Correct Procedure:

1. If the broker files reports at the federal level pursuant to the Home Mortgage Disclosure Act (HMDA) for a calendar year, no reports must be filed with the Department.
 - Lenders should determine if they meet the HMDA reporting criteria through the HMDA Web site at www.ffiec.gov/hmda under "About HMDA." Check the criteria for "Nondepository institutions."
 - Lenders who meet the reporting criteria of Regulation C, Home Mortgage Disclosure Act must file specified reports at the federal level and are exempt from filing the Residential Mortgage Loan Report (RE 857) with the Department.
2. If a broker who acts as a direct lender does not meet the reporting criteria under HMDA then the broker may be required to file the Residential Mortgage Loan Report (RE 857) with the Department.
 - If the broker has assets that total \$10 million or less, who regularly fund real estate purchase and/or home improvement loans, and who originate less than 100 home purchase loans per year. "Regularly" is defined as 12 or more transactions annually during the immediately preceding calendar year, that in the aggregate total more than \$500,000.
 - Only lenders making 10% or more in qualified loans must report.
3. Licensed brokers who are required to report to the Department must file the Residential Mortgage Loan Report (RE 857) no later than March 31 of the next calendar year (e.g. 2010 calendar year loan data would be due no later than March 31, 2011). Reports must be filed in duplicate.
4. The Residential Mortgage Loan Report (RE 857) is available on the Department's Web site www.dre.ca.gov under "Forms" in the Publications menu.

Reference:

SECTION 14 – Licensees Acting as Lenders

Does the broker act in the capacity of a direct lender?

Correct Procedure

1. Any person who makes eight or more loans to the public in a calendar year from the person's own funds when they are held or resold and are secured by one to four unit residential dwelling must be a licensed real estate broker. Transactions negotiated through a real estate broker who qualifies as a "threshold broker" (see Section 8 #3) are not counted. See also "own funds" as in Section 12 #1.

2. Licensees who meet this requirement must comply with all of the lending practices for nontraditional and subprime mortgage products as set out in Regulation 2844 in regards to:

- Risk Management Practices
- Underwriting Standards
- Control Systems
- Consumer Protection

Reference:

Section 10131.1, Regulation 2844

SECTION 15 – Nontraditional Mortgage Loan Products

Does the broker arrange nontraditional loans secured by one-to four-unit residential properties?

A nontraditional loan product is defined as one that allows the borrower to defer repayment of principal or interest. These products include, but are not limited to, interest-only loans where a borrower pays no principal for a period of time and payment-option loans where one or more of the payment options may result in negative amortization. A nontraditional loan is secured by a one- to four-unit residential property whether owner or non-owner occupied. Reverse mortgages and Home Equity Lines of Credit (HELOC) - other than simultaneously recorded second liens (piggybacks) - are not nontraditional loans. Balloon loans where the monthly payments require full payment of principal and interest until maturity (e.g. 30 due in 15, 30 due in 5) are not nontraditional loans.

Correct Procedure

1. In a transaction where the broker is arranging a nontraditional loan, a fully completed "Mortgage Loan Disclosure Statement, Nontraditional Mortgage Loan Product - One to Four Residential Units), RE885, must be provided within three days of receiving a completed, written loan application. A copy of the disclosure statement, signed by the borrower(s) and the broker or the broker's representative, must be retained by the broker for three years.

2. The broker must complete each column of the Comparison of Sample Mortgage Features on Page 4 of the RE885 or sign the certification on Page 3.

3. All of the rules specified in Section 3 – Borrower Disclosures – will apply.

4. The broker has adopted all of the policies and procedures of the Interagency Guidance on Nontraditional Mortgage Product Risks and the Statement on Subprime Mortgage Lending. The documents can be found on the Department's Web site under "DRE Publications & Resources" in the Industry menu.

5. The broker's advertising of nontraditional loans must comply with Section 10235 and Regulation 2848, specifically subsection (a)(17) and (a)(18).

Reference:

Sections 10176(a), (c), (g), 10236.4(b), 10240, 10240.3, 10241; Regulations 2840, 2840.1, 2842, 2842.5; Health and Safety Code Section 35830; Civil Code Section 1632

Mortgage Loan Broker Compliance Checklist

(RE 7A)

This checklist is designed as a guide to be used in conjunction with the Mortgage Broker Compliance Evaluation Manual (RE 7) and should not be relied upon to be all-inclusive of the broker's duties and responsibilities under the Real Estate Law and related Regulations. All references are to the Business and Professions Code or Regulations of the Real Estate Commissioner unless otherwise stated.

GENERAL BUSINESS PRACTICES:

- ❑ All salespersons are properly licensed and employed by the broker pursuant to a broker-salesperson agreement. The broker has possession of all salespersons' license certificates. (Sections 10130, 10131(d), 10132, 10137, 10138, 10139, 1053.4, 10160; Regulation 2726)
- ❑ The broker notifies the Department of Real Estate of the employment and termination of all salesperson licensees within five days. (Section 10161.8; Regulation 2752)
- ❑ The broker is exercising reasonable supervision over the activities of licensees or, as a designated officer of a corporate broker, is exercising reasonable supervision over the licensed activities of the corporation. (Section 10176(h); Regulation 2725)
- ❑ All salespersons and broker-associates who perform residential mortgage loan origination activities have a mortgage loan originator license endorsement, and all real estate brokers and corporations who hire mortgage loan originators have also obtained and maintain a mortgage loan originator license endorsement. (Section 10166.01)
- ❑ All documents executed or obtained by the broker in connection with the loan transaction are in file and will be maintained for three years (Section 10148; Regulation 2729)
- ❑ The broker has a license for each business location. (Sections 10162, 10163)
- ❑ The broker's license bears the name of all fictitious business names (dba's). (Section 10159.5; Regulation 2731)
- ❑ If the broker employs unlicensed assistants pursuant to the licensing exemption under Section 10133.1(c), their employment and duties fully comply with Regulation 2841.

GENERAL TRUST FUND HANDLING (Section 10145):

** See also the Trust Funds publication (RE 13) publication, available on the Department's Web site*

- ❑ The bank account used for trust fund handling is in the name of the broker, or a fictitious name on the broker's license, as trustee. (Regulation 2832)
- ❑ The trust account control records are complete and accurate. (Regulation 2831)
- ❑ The trust account separate beneficiary records are complete and accurate. (Regulation 2831.1).
- ❑ A monthly reconciliation of the control records and separate beneficiary records is performed. (Regulation 2831.2)
- ❑ Trust funds are deposited to the trust account within three days of receipt. (Regulation 2832)

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- ❑ Authorized signatories are either licensed or unlicensed but bonded. (Regulation 2834)
 - ❑ The trust account contains no more than \$200.00 of the broker's funds. (Section 10176(e); Regulation 2835)
 - ❑ Appraisal/credit report fees received from an escrow are deposited to the trust account for payment to the vendor(s). (Section 10145)

BORROWER DISCLOSURES:

- ❑ A Mortgage Loan Disclosure Statement (MLDS) (RE 882, RE 883 or RE 885) is provided to the borrower(s) within three days of receiving the completed, written loan application (Section 10240(a), 10240.3; Regulations 2840, 2840.1, 2842 and 2842.5), or
- ❑ An alternative disclosure is provided to the borrower(s) that fully complies with Business and Professions Code Section 10240(c).
- ❑ A copy of the signed MLDS (10240(a)) or acknowledgement (10240(c)) is in all files and retained for three years.
- ❑ The disclosures contain the amount of all compensation including any anticipated rebates from the lender. (Section 10176(g))
- ❑ Disclosure of any material changes to the costs, expenses or terms of the loan is made to the borrower(s) in a timely manner. (Sections 10176(a), 10176(c))
- ❑ The disclosures contain the broker license identification number, NMLS unique identifier number, and DRE licensing information telephone number. (Section 10236.4(b))
- ❑ A Fair Lending Notice (RE 867A) is posted in a conspicuous location for public inspection and a copy is given to the borrower(s). (Health & Safety Code Section 35830)
- ❑ A Fair Lending Notice acknowledgement of receipt (RE867) signed by the borrower(s) is in each file and retained for three years.
- ❑ If the broker elects to make the loan from "broker-controlled funds," disclosure is made to the borrower(s). (Sections 10241(j), 10241.2)
- ❑ If the broker is conducting the escrow pursuant to Financial Code Section 17006(a)(4), the broker has disclosed in all written escrow instructions and all escrow instructions transmitted electronically, in not less than 10-point type, that the escrow is being conducted under its real estate broker license and with a disclosure of the broker's license identification number.
- ❑ Translated Mortgage Loan Disclosure Statements for loans negotiated in Spanish, Tagalog, Vietnamese, or Korean are provided to the borrower(s). (Civil Code Section 1632)
- ❑ Disclosure of roles when arranging financing. (Section 10177.6)

ADVERTISING:

- ❑ Advertising contains the proper license disclosures (Sections 10140.6 and 10235.5; Regulation 2847.3)
- ❑ Advertising also contains the broker license identification number. (Section 10236.4(a)).
- ❑ Advertising complies with all of the provisions of Regulation 2848.

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- ❑ Advertising does not contain any claims that are misleading or cannot be supported by the broker (Section 10235)
 - ❑ Advertising a payment or payments for a loan contains an equally prominent disclosure of the loan term, principal loan amount, interest rate, and annual percentage rate. (Regulation 2848(5))
 - ❑ Advertising a payment or payments for an adjustable rate loan, interest-only loan, or payment-option loan additionally contains an equally prominent disclosure of the initial interest rate, number or months the initial interest rate will be in effect, fully-indexed rate, maximum rate, an explanation of the difference between the payment rate, initial interest rate and fully-indexed rate if different, how often the interest rate and payments can change, maximum periodic change in the interest rate and payments (caps), number of months and percentage 30 of original loan amount after which minimum payments will not be accepted and the loan re-amortizes, the monthly payment based on the maximum interest rate and the loan balance after all negative amortization is included assuming minimum payments are made, if the loan contains a prepayment penalty, a statement to that effect, and if the loan contains a balloon payment, a statement to that effect. (Regulation 2848(17))
 - ❑ Advertising a “low doc/no doc”, “no income/no asset”, “stated income”, “stated asset”, “no ratio” or similar loan product contains a statement that those products may have a higher interest rate, more points or more fees than other products requirement documentation. (Regulation 2848(18))
 - ❑ Advertising a payment or payments for a balloon payment loan additionally contains an equally prominent disclosure of the amount of the balloon payment. (Regulation 2848(5)).
 - ❑ Advertising a gift, premium or rebate to prospective borrowers contains all conditions that must be met in order to receive the gift, premium or rebate. (Section 10235)
 - ❑ When advertising the sale of a note where a specific yield is indicated or implied, the actual note rate and discount from the principal balance being offered is also included. (Section 10235)

FEES AND COMPENSATION:

- ❑ No commissions, fees or costs are charged to the borrower(s) that have not been incurred, paid or reasonably earned by the broker. (Regulation 2843)
- ❑ Compensation that the broker anticipates being paid from all sources, including all lender rebates, is disclosed to the borrower(s) in writing on the appropriate disclosure form. (Sections 10176(g), 10240(a), 10240(c))
- ❑ If the broker, or licensees of the broker, represent either party in a sales transaction and receive compensation in connection with the loan, a disclosure was given to both parties prior to escrow. (Regulation 2904)

ADVANCE FEES:

- ❑ The broker collects only appraisal report and/or credit report fees in advance unless an advance fee agreement has been submitted to, and approved by, the Department. (Sections 10026, 10085, 10085.5; Regulation 2972)
 - ❑ The broker has submitted to the Department, and received Department approval of, all advance fee materials including contracts, advertising and accounting formats, for any fees (other than for appraisal reports and credit reports) collected in advance of providing licensed services. (Sections 10026, 10085, 10085.5; Regulations 2970 , 2972)
 - ❑ The broker deposits all advance fees collected into the trust account to be disbursed after the service(s) are completed. (Section 10146)
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- ❑ The broker provides a quarterly and final verified accounting to the principal. (Section 10146; Regulation 2970)
 - ❑ The broker does not collect an advance fee in connection with a residential loan modification and does not collect any advance fee for a loan modification, loss mitigation or similar services if a Notice of Default has been recorded against the property. (Civil Code Section 2945)

ARTICLE 7 – REGULATED LOANS (Senior liens under \$30,000, junior liens under \$20,000 and secured by a one- to four-unit dwelling. Note: Additional rules apply if the loan is a “covered loan.” See the section on covered loans):

- ❑ The commissions, fees and costs charged on loans do not exceed the legal maximums. (Section 10242)
- ❑ The purchase of credit life insurance or credit disability insurance is not a condition of making a loan. (Section 10241.1)
- ❑ The balloon payments on loans secured by an owner-occupied dwelling have due dates of more than six years. (Section 10244.1)
- ❑ The balloon payments secured by a dwelling other than owner-occupied have due dates of three years or more. (Section 10244)
- ❑ If loans contain a prepayment penalty, the terms comply with Section 10242.6.

ARTICLE 5 – PRIVATE MONEY TRANSACTIONS:

- ❑ Funds received from the lender/purchaser are for a specific loan transaction. (Section 10231)
- ❑ Funds received on behalf of the lender/purchaser in repayment of a loan serviced by the broker are not held more than 25 days except pursuant to a written agreement. (Section 10231.1)
- ❑ If the broker receives direct or indirect benefit from borrowed funds (self-dealing), a copy of the Lender/Purchaser Disclosure Statement (LPDS) and the required notice is forwarded to the Department before making any solicitation for the funds (Section 10231.2(a))
- ❑ If the broker receives direct or indirect benefit from borrowed funds (self-dealing), the Lender/Purchaser Disclosure Statement (LPDS) is provided to the prospective lender or purchaser at least 24 hours before the lender or purchaser signs the LPDS or gives the broker funds. (Section 10231(b))
- ❑ If the broker receives direct or indirect benefit from borrowed funds (self-dealing), the Lender/Purchaser Disclosure Statement (LPDS) is retained for four years. (Section 10231.2(b))
- ❑ The broker provides an approved Lender/Purchaser Disclosure Statement (LPDS) to each prospective lender or purchaser before the person solicited becomes obligated to make or purchase a loan. (Sections 10232.4, 10232.5; Regulation 2846)
- ❑ The broker provides the lender or purchaser with an independent appraisal of the securing property. (Section 10232.5(a)(b))
- ❑ If the lender or purchaser waives the right to an independent appraisal in writing (case-by-case basis only), the broker provides a written estimate of fair market value which includes the objective data on which the estimate is based. (Section 10232.5(a)(b))

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- ❑ The broker has a servicing agreement for each loan serviced that complies with Section 10233.
 - ❑ The broker causes each deed of trust, or assignment of deed of trust, to be recorded in the name of the lender or purchaser, in the appropriate county within 10 days after close of escrow. (Section 10234)
 - ❑ The broker delivers, or causes to be delivered, a conformed copy of each deed of trust to the investor or lender and the borrower within a reasonable time after recording. (Section 10234.5)
 - ❑ If the broker has met the criteria for filing quarterly and annual “threshold” reports with the Department, a Threshold Notification (RE 853), has been submitted. (Section 10232)
 - ❑ If the broker has met the reporting criteria, quarterly and annual reports are being submitted to the Department (Sections 10232.2, 10232.25; Regulations 2846.5, 2846.6, 2846.7, 2849.01, 2849.1)
 - ❑ If the broker has been filing reports with the Department pursuant to Section 10232 and no longer meets the reporting criteria, a Threshold Notification (RE 853) to end the broker’s reporting status and any reports that are, or will be due, is submitted. (Section 10236.5)

ARTICLE 6 – PRIVATE MONEY TRANSACTIONS WITH MULTIPLE BENEFICIARIES:

- ❑ The broker has filed the Multi-lender Transaction Notice (RE 860) with the Department within 30 days after the first multi-lender loan transaction and within 30 days of any material change to the information in the Notice. (Section 10238(a); Regulation 2846.1)
 - ❑ The broker has filed the Multi-lender Transaction Notice (RE 860) with the Department within 30 days of becoming the servicing agent on multi-lender loans, where payments due or the number of persons entitled to payments exceed the levels stated in Section 10238(b).
 - ❑ The broker’s advertising for multi-lender loan transactions complies with Section 10235, Regulation 2848 and Title 10, California Code of Regulations Section 260.302.
 - ❑ Each loan is secured directly by real property located in California and is not subject to subordination. (Section 10238(d))
 - ❑ The broker, or affiliate of the broker, does not have any interest, or any contractual right to acquire an interest, in property securing the loans (self-dealing). (Section 10238(e))
 - ❑ The broker has, and retains for four years, the required investor qualification statements. (Section 10238(f))
 - ❑ The interests of all investors are identical except for different selling prices that allow for changes in market value when interests are sold. (Section 10238(g))
 - ❑ All loans comply with the loan to value limitations of Section 10238(h).
 - ❑ For construction or rehabilitation loans, when the value of the completed project is used as the “current fair market value”, all of the requirements of Section 10238(h) are met.
 - ❑ When more than one parcel of real property secures a loan, the loan to value limitations for each property are met. (Section 10238(h)(5))
 - ❑ Transaction documentation complies with Section 10238(i).
 - ❑ Funds received from the lender or purchaser are for a specific transaction. (Section 10238(j))
 - ❑ If the broker is the servicing agent and has met the reporting criteria, quarterly CPA-prepared reports are submitted to the Department. (Sections 10238(j)(4)(5)(6), 10238(k)(3))
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- ❑ The broker, or an exempt entity, services the loans subject to servicing agreements. (Section 10238(k))
 - ❑ If the broker is the servicing agent, payments received are transmitted to the note-owners pro-rata according to their interests within 25 days of receipt. (Section 10238(k)(2))
 - ❑ If the broker is the servicing agent, a Request for Notice of Default upon any prior encumbrances is filed for each loan and the note-owners are promptly notified of any default. (Section 10238(k)(4)(5))
 - ❑ The broker provides each prospective investor with a Lender/Purchaser Disclosure Statement (LPDS) (RE 851A or RE 851B). (Section 10238(l))
 - ❑ When more than one parcel of real property secures a loan, the broker provides the Lender/Purchaser Disclosure Statement – Multi-Property Addendum (RE 851D). (Section 10238(l)(5))
 - ❑ The broker provides any investor, upon request, the names and addresses of the owners of the other interests (Section 10238(m))
 - ❑ The broker has no option or election to acquire the interests of any of the investors or the securing properties. (Section 10238(n))
 - ❑ The broker clearly indicates in the transaction file the provision of the Corporate Securities Law of 1968, or exemption, under which transactions are conducted, and submits a copy of this information to each investor. (Section 10236.7)

COVERED LOANS (FINANCIAL CODE SECTIONS 4970 TO 4979.8):

(See FC §4970 for the definition of a covered loan. Note: Additional rules apply if the loan falls under Article 7. See the Section on Article 7 loan compliance.)

- ❑ If the loan contains a prepayment penalty, the borrower was offered another product without a prepayment penalty and was given a written disclosure at least three days before consummation of the loan stating the amount of the prepayment penalty and stating the rate, points and fees available for a loan without a prepayment penalty. (Section 4973(a)(2)(A)(B))
 - ❑ If the loan contains a prepayment penalty, the borrower may pay up to 20 percent of the original loan amount in any 12-month period without penalty. (Section 4973(a)(2)(C))
 - ❑ If the loan contains a prepayment penalty, the amount of the penalty does not exceed six months advance interest at the rate of interest then in effect. (Section 4973(a)(2)(C))
 - ❑ If the loan contains a prepayment penalty, it does not exceed 36 months from the date of consummation of the loan. (Section 4973(a)(1))
 - ❑ The loan does not provide for a prepayment penalty if the loan is accelerated due to a default. (Section 4973(a)(2)(D))
 - ❑ No prepayment penalty was financed through a new loan originated by the same broker. (Section 4973(a)(2)(E))
 - ❑ If the loan is not fully amortized, the maturity date is for more than five years. (Section 4973(b)(1))
 - ❑ If the loan provides for negative amortization, it is a first mortgage, and disclosure was made to the borrower that the negative amortization may add principal to the balance. (Section 4973(c))
 - ❑ No advance payments have been collected from the borrower. (Section 4973(d))
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- ❑ There is no provision for an interest rate increase due to default. (Section 4973(e))
 - ❑ The loan was not made solely on the equity in the securing property, and the broker has a reasonable belief that the borrower can repay the loan from current or expected income or other financial resources. (Section 4973(f))
 - ❑ If the loan was for a home-improvement contract, proceeds were paid directly to the consumer, jointly payable to the consumer and contractor, or, at the election of the consumer, to a third party escrow agent. The consumer has also provided a signed and dated completion certificate that the work was completed to the consumer's satisfaction. (Section 4973(g))
 - ❑ No recommendation or encouragement was given to the consumer to default on an existing consumer loan or debt. (Section 4973(h))
 - ❑ The loan does not contain a call provision to accelerate repayment of the loan at the lender's sole discretion. (Section 4973(I))
 - ❑ If for a refinance, the loan results in an identifiable benefit to the consumer. (Section 4973(j)).
 - ❑ The borrower(s) were given the "Consumer Caution and Home Ownership Counseling Notice" no later than three business days prior to signing the loan documents and the consumer has provided an acknowledgement of receipt of the notice to the person originating the loan.
 - ❑ The consumer was not steered, counseled or directed to accept a loan product less favorable than that for which the consumer qualifies. (Section 4973(l))
 - ❑ The loan was not structured as an open-end credit plan or divided in separate parts for the purpose of evading the covered loan law. (Section 4973(m))
 - ❑ No points or fees were financed in excess of \$1,000 or 6% of the original principal balance (exclusive of points and fees), whichever is greater. (Section 4979.6)
 - ❑ No credit life, credit disability, credit property, credit unemployment or credit debt cancellation premiums were financed into the loan or financed to the borrower within 30 days of the loan. (Section 4979.7)

RESIDENTIAL MORTGAGE LOAN REPORT (RE 857):

- ❑ The Residential Mortgage Loan Report (RE 857) is submitted to the Department no later than March 31 of each year if the broker acts in the capacity of a direct lender, meets the reporting criteria and does not file reports at the federal level pursuant to the Home Mortgage Disclosure Act (HMDA). (Health and Safety Code Sections 35815, 35816)

LICENSEES ACTING AS LENDERS:

- ❑ The broker complies with all of the lending practices for nontraditional and subprime mortgage products in regard to risk management practices, underwriting standards, control systems and consumer protection (Section 10131.1(b)(1)(C); Regulation 2844)

NONTRADITIONAL MORTGAGE LOAN PRODUCTS

- ❑ A fully completed "Mortgage Loan Disclosure Statement– Nontraditional Mortgage Loan Product (One

to Four Residential Units), RE885, is provided within three days of receiving a completed, written loan application. (Section 10240(a); Regulation 2842)

- ❑ A copy of the disclosure statement, signed by the borrower(s) and the broker or broker's representative, is retained by the broker for three years. (Section 10240(a))
- ❑ The Comparison of Sample Mortgage Features on page 4 of the RE885 is fully completed or the broker signs the certification on page 3. (Regulation 2842)
- ❑ The broker has adopted all of the policies and procedures of the Interagency Guidance on Nontraditional Mortgage Product Risks and the Statement on Subprime Mortgage Lending (Section 10240.3; Regulation 2842)
- ❑ The broker's advertising of nontraditional mortgage loan products complies with Section 10235 and Regulation 2848, specifically subsections (a)(17) and (a)(18).

