



# MORTGAGE LOAN BULLETIN

Arnold Schwarzenegger, Governor  
Sunne Wright McPeak, Secretary, Business, Transportation and Housing Agency  
Jeff Davi, Real Estate Commissioner

Spring 2006

## RESPA's Anti-Kickback and Unearned Fee Provisions

*from the U.S. Department of Housing and Urban Development, Office of RESPA and Interstate Land Sales*

As you know, buying a home and obtaining a mortgage is complicated and many consumers rely on real estate agents and mortgage brokers to help them through this process. Consumers trust their real estate agent or mortgage broker to assist them in getting the best and most cost effective settlement services available to meet their needs. Unfortunately, this does not always happen and consumers are often steered to higher priced settlement services.

More than 30 years ago, Congress realized this problem and enacted a consumer protection statute — The Real Estate Settlement Procedures Act (RESPA). With few exceptions, RESPA covers all single-family residential mortgage loans, including home purchases, refinances, and equity lines of credit. Most industry professionals and consumers are familiar with the statute's disclosures like the Good Faith Estimate (GFE) and the HUD-1 Settlement Statement. However, not all industry professionals, and fewer consumers, are aware of certain prohibitions under the statute.

Section 8(a) of RESPA, 12 U.S.C. § 2607(a), and its implementing regulations at 24 C.F.R. § 3500.14, prohibits giving and receiving any fee, kickback, or thing of value for the referral of settlement service business. Things of value are broadly defined under RESPA's rules and include monies, trips, an opportunity to win a prize, free advertising, stock in a company,

etc. Some examples of prohibited practices are:

- Title companies, mortgage brokers, lenders offering real estate agents a free chance to win a contest or prize, such as trips, money, coupons and discount certificates.
- Mortgage brokers, lenders, title companies offering to assist real estate agents promote themselves or their property listings, by providing such things as postcards, virtual tours, and marketing materials.
- Mortgage brokers, lenders, title companies offering to pay or defray any costs that real estate brokers or agents would otherwise have to incur, such as providing continuing education or paying disproportionate costs for joint advertising.
- Mortgage brokers, lenders, title companies providing "thank you" gifts to real estate agents for referring business.
- Mortgage brokers or lenders paying real estate brokers or agents a commission for referring a loan.
- Real estate agents or mortgage brokers paying "finders fees" to friends and past customers for referring new business.

The provisions under Section 8 of RESPA do not prohibit compensation for providing actual goods, facilities,

or services. However, compensation must be reasonably related to the market value of such goods, services, or facilities. HUD may consider any excess payment as compensation for referring business. Here are some situations to avoid involving compensation for goods, facilities, and services:

- Mortgage brokers paying commissions to lenders or other mortgage brokers for their turndowns or so-called "leads." It's okay to purchase lead lists as they are considered "goods." However, compensation based on the outcome of the lead is not permissible.
- Title companies paying real estate agents for performing duplicate or unnecessary work.
- Mortgage brokers or lenders at-

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Governor

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DRE's Internet address is:  
<http://www.dre.ca.gov>



## Legislative Update

The following bills of interest to the mortgage loan industry were signed into law and became effective on January 1, 2006, unless otherwise specified:



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### *Assembly Bill 901 (Ridley-Thomas)*

Amended Financial Code 4970 to increase the maximum loan amount for a covered loan from \$250,000 to the most current Federal National Mortgage Association (FNMA) single-family conforming loan limit (currently \$417,000).

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### *Assembly Bill 1729 (Houston)*

Provided clarifying language and technical cleanup to various mortgage loan related sections in the Business and Professions Code. Sections 10232.4 and 10233 were amended to eliminate obsolete references and Section 10238(g) was amended to clarify that a broker's obligation to record an interest in a trust deed in a timely manner is the same for multi-lender transactions as it is in single investor transactions.

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### *Assembly Bill 223 (Negrette McLeod)*

Expanded the mandatory continuing education subject matter for renewal of a **broker** license to also include a 3-hour course in risk management that includes principles, practices and procedures calculated to avoid errors and omissions in the practice of real estate licensed activities. **Effective July 1, 2007.**

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### *Senate Bill 833 (Bowen)*

Made it unlawful for a person or entity, if located in California or if the recipient is located in California, to use any device to send, or cause any other person or entity to use a device to send, an unsolicited advertisement to a telephone facsimile machine, except as specified, and authorizes the recipient to bring an action for injunctive relief and damages. The bill also makes it unlawful for a person or entity, if located in California or the recipient is located in California, to initiate a facsimile communication using a machine that does not provide specified identification, or to use a device to send a message via a telephone facsimile machine unless the message is clearly marked with certain identifying information.

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### *Senate Bill 97 (Murray)*

Amended existing law to add criminal penalties for using commercial e-mail advertisements containing certain false, misrepresented, obscured, or misleading information.

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### *Senate Bill 355 (Murray)*

Enacted the "Anti-Phishing Act of 2005" making it unlawful for any person, through the Internet or other electronic means, to solicit, request, or take any action to induce another person to provide identifying information by representing itself to be a business without the approval or authority of the business, and provides certain civil remedies and civil penalties.

## REMINDER!

# Residential Mortgage Loan Report (RE 857)



Real estate brokers who are *direct* lenders in certain types of loan transactions are required, pursuant to Health and Safety Code §35815 and §35816, to report to the Department of Real Estate activities related to the number of applications received from, and number and dollar amount of loans made to, the public for home purchase and/or home improvement purposes. ***If a real estate broker reports such lending activity to the U.S. Department of Housing and Urban Development (HUD) under the provisions of the federal Home Mortgage Disclosure Act (HMDA), it is NOT necessary for the real estate broker to report to the Department of Real Estate (DRE).***

Please review the following criteria from the *federal HMDA* website to determine if you meet the *federal* reporting criteria:

### 2005 REPORTING CRITERIA FOR NONDEPOSITORY INSTITUTIONS

Use information and data from the preceding December 31 date when determining whether you meet the reporting criteria. The following questions for a nondepository institution should be answered to determine if you should report CY 2005 HMDA data in 2006.

1. Is the nondepository institution a for-profit lender?
2. In the preceding calendar year, did the institution's home purchase loan originations (including refinancings of home purchase loans) equal or exceed 10 percent of its total loan originations, measured in dollars, or equal \$25 million or more?
3. Did the nondepository institution either: (a) have a home or branch office in an MSA/MD on the preceding December 31, or (b) receive applications for, originate, or purchase 5 or more home purchase or home improvement loans on property located in an MSA/MD in the preceding calendar year?
4. Did the nondepository institution either: (a) have assets (when combined with the assets of any parent corporation) exceeding \$10 million on the preceding December 31, or (b) originate 100 or more home purchase loans (including refinancings of home purchase loans) in the preceding calendar year?

If a nondepository institution responds 'YES' to question 1 above and 'YES' to at least one question in 2, and one question in 3, and one question in 4, then HMDA applies to the institution's loan originations, purchases, and applications in the current calendar year. A negative response to question 1, or to all the questions in 2, 3, or 4 exempts the institution from filing HMDA data for the current calendar year.

For nondepository institutions, a branch office is any office of the institution that takes applications from the public for home purchase or home improvement loans. It does not include offices of affiliates or other third parties such as loan brokers.

If you are a lender and do not meet the above *federal HMDA* reporting criteria please review the following:

The State of California Residential Mortgage Loan Report (RE857) must be submitted to the DRE by all real estate brokers whose assets total \$10 million or less and who regularly *make* real estate purchase and/or home improvement loans. "Regularly" is defined to mean twelve or more transactions annually during the immediately preceding calendar year that, in aggregate, total more than \$500,000. ***Licensees who only broker, and do not make, loans are NOT required to report.***

Mortgage lending data is to be collected annually and reported on the RE 857 by March 31 of the following year. The form and instructions are available on the DRE website [www.dre.ca.gov](http://www.dre.ca.gov) under **Forms**. If you qualify to file the Residential Mortgage Loan Report for calendar year 2005 and have not yet done so, or if you have any questions, please contact the Sacramento Mortgage Loan Activities Unit at (916) 227-0770. 📞

# Lender Notification (RE 859) Reminder



The lender notification that became an annual requirement as of January 1, 2005 is again due from **direct lenders** who meet specific criteria. The criteria, excerpted from Business and Professions Code Section 10131.8, are as follows:

(a) A real estate broker who acts pursuant to subdivision (d) of Section 10131 and who meets **all** of the following requirements shall notify the department annually in writing on a form that is acceptable to the commissioner:

(1) The real estate broker is an approved lender for the Federal Housing Administration, Veterans Administration, Farmers Home Administration, Government National Mortgage Association, Federal National Mortgage Administration, or the Federal Home Loan Mortgage Corporation.

(2) The real estate broker makes residential mortgage loans to a loan applicant for a residential mortgage loan by using or advancing the broker's own funds, or by making a commitment to advance the broker's own funds.

(3) The real estate broker makes the credit decision in the loan transaction.

(4) The real estate broker at all times maintains a tangible net worth, computed in accordance with generally accepted accounting standards, of a minimum of two hundred fifty thousand dollars (\$250,000).

(b) As used in paragraph (2) of subdivision (a), "own funds" means (1) cash, corporate capital, or credit lines at commercial banks, savings banks, savings and loan associations, industrial loan companies, or other sources that are liability items on the real estate broker's financial statements, whether secured or unsecured, or (2) cash, corporate capital, or warehouse credit lines at commercial banks, savings banks, savings and loan associations, industrial loan companies, or other sources that are liability items on the financial statements of an affiliate of the real estate broker, whether secured or unsecured. "Own funds" does not include funds provided by a third party to fund a loan on condition that the third party will subsequently purchase or accept an assignment of the loan.

If you are a **lender** that meets **all** of the above criteria please file the notice with the DRE no later than March 31, 2006 stating whether it is your initial notification or your annual notification. If you are a lender that previously met the above criteria but no longer do, please file the notification stating you no longer meet the criteria. The Residential Mortgage Lender Notification (RE859) form is available on the DRE website [www.dre.ca.gov](http://www.dre.ca.gov) under **Forms**.

**Please note that this notice is separate from, and should not be confused with, the report entitled "Residential Mortgage Loan Report" for which there is also a reminder in this Bulletin.**

Questions regarding this or any other mortgage loan compliance issue should be directed to the Mortgage Loan Activities Unit at (916) 227-0770. 📞

The eLicensing online system available at [www.dre.ca.gov](http://www.dre.ca.gov) offers expedited processing of the following services:



- 🔗 Broker and salesperson license renewals
- 🔗 Duplicate license requests (broker, salesperson, officer and branch office)
- 🔗 Salesperson requests to change employing broker
- 🔗 Broker certification of salesperson employment
- 🔗 Licensee mailing address changes
- 🔗 Broker main office address changes
- 🔗 Examination services: *apply for salesperson exam; reschedule exam date; apply to re-take exam; change exam mailing address; view exam records; check scheduled exam date; time and location; view exam results; request duplicate schedule notices and result notices; see if license has been issued.*

Unless you are a first-time salesperson examination applicant, you must have an existing examination record or license on file with the DRE to use eLicensing. To use eLicensing for the first time, you need to register at [www.dre.ca.gov](http://www.dre.ca.gov) to create a user name and password.

## *Then and Now*

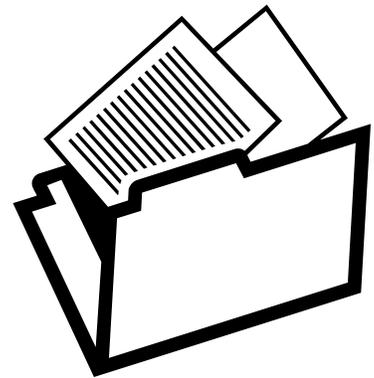
# Regulation 2725: Broker Supervision

**R**eal estate brokers and designated officers of corporate brokers are, and have been, responsible for providing reasonable supervision over the licensed activities of their salespersons and companies.

Prior to November of 1996, Commissioner's Regulation 2725 required the broker or designated officer to review, initial and date, within a specified time, every instrument that could have a material effect on a party to the transaction and that was prepared or signed by a real estate salesperson. A broker or designated officer could delegate that responsibility to specified licensees under certain conditions.

In November of 1996, the Regulation was amended to establish the requirement for a broker or designated officer to put in place policies, rules, procedures and systems to review, oversee and manage:

- Transactions requiring a real estate license,
- Documents which may have a material effect upon the rights or obligations of a party to the transaction,
- Filing, storage and maintenance of such documents,
- Handling of trust funds,
- Advertising of any service for which a license is required,
- Familiarizing salespersons with the requirements of federal and state laws relating to prohibition of discrimination, and
- Regular and consistent reports of licensed activities of salespersons.



The Regulation requires the form and extent of the policies, rules, procedures and systems to take into consideration the number of salespersons employed and the number and location of branch offices. Therefore, a broker who has many salespersons working in branch offices will have to establish much more comprehensive policies and procedures than the broker who has only a few salespersons employed at one office.

A broker or designated officer must also establish a system for monitoring compliance with the policies, rules, procedures and systems and may use the services of brokers or salespersons to assist in carrying out these requirements as long as the broker or designated officer does not relinquish overall responsibility for supervision.

While the Mortgage Loan Disclosure Statements (RE882 and 883) still contain signature lines for the broker or designated officer to indicate their review, simply signing and dating these forms does not satisfy all of the Regulation's requirements. Brokers and designated officers should carefully review Regulation 2725 to ensure they are in compliance. The Commissioner's Regulations can be viewed on the DRE website [www.dre.ca.gov](http://www.dre.ca.gov) under **Regulations**.

Questions about this or other mortgage loan related issues can be answered by calling the Mortgage Loan Activities Unit at (916) 227-0770. 📞

## RESPA's provisions

Continued from page 1

tempting to employ real estate agents as loan officers to pay them a percentage of the loan amount for performing minimal, duplicative, or unnecessary services, such as completing or helping with loan applications.

- Real estate agents receiving additional payment without performing additional work. (Remember that providing referral services is not a compensable service.)
- Real estate brokers receiving above-market rates for renting desk or office space to loan officers, mortgage brokers, lenders, or title companies. Or, collecting rent for desk or office space that is rarely used by the loan officers, mortgage brokers, lenders, or the title companies.

Real estate brokers and agents who enter into marketing agreements with lenders to provide marketing services, but only provide referral services.

### **Affiliated Business Arrangements**

In 1983, Congress amended RESPA to permit referrals between settlement service providers in an Affiliated Business Arrangement (Af BA), under certain conditions. An Af BA exists when a person in a position to refer business, or their "associate," owns more than 1 percent of a provider of settlement services, and either person directly or indirectly refers business to that provider. An associate of a person in a

position to refer business includes a partner, employer, officer, spouse, parent, or child; or where an entity is a corporation related to another corporation as parent to a subsidiary by an identity of stock ownership.

Under the 1983 rule, referrals made between affiliates do not violate RESPA so long as the following three conditions are met:

(1) The consumer receives a written disclosure of the nature of the relationship and an estimate of the affiliate's charges. (This disclosure must be provided at the time the referral is made, by the person making the referral. HUD provides the format for this disclosure at Appendix D of the regulations, 24 CFR 3500.)

(2) The consumer is not required to use the affiliate.

(3) The only thing of value received from the arrangement, other than payments for services rendered, is a return on ownership interest.

An example of a RESPA-compliant Af BA might include a real estate broker who owns a mortgage broker company and the real estate agents refer loan business to the broker. Under this scenario, the broker and agents would satisfy the law provided the agents give the customer the Af BA disclosure at the time they make the referral, the broker does not require agents to refer loan business, and the broker does not compensate agents

for making referrals.

Finally, participation in "sham" affiliated business arrangements violate RESPA's anti-kickback and unearned fee provisions. HUD has recently increased its investigation and enforcement activity of sham affiliated business arrangements as more settlement service providers try to circumvent RESPA's prohibitions by establishing shell settlement service businesses to function as a conduit for paying referral fees. Often, title companies or lenders create sham arrangements with persons in positions to refer business. Additional guidance on Af BAs is contained in HUD's 1996-2 Statement of Policy, "Sham Controlled Business Arrangements." The following are a couple of examples of sham arrangements:

A title company and a real estate firm establish an affiliated title agency. The affiliate title agency has the same business address as the partner title company, the real estate firm is the affiliated title agency's sole source of business, and employees of the partner title company perform the core title functions.

Several real estate agents create an LLC to purchase an interest in a title company. The title company and the LLC share profits based upon their ownership interest. However, the LLC disburses profits to its member real estate agents based on the volume of title business referrals.

All licensees should operate in compliance with RESPA, particularly the provisions of Section 8, as the violation of this part may carry a fine of up to \$10,000 or imprisonment of up to one year, or both.

*For more information about RESPA, visit HUD's website at [www.hud.gov/offices/hsg/sfh/res/respa\\_hm.cfm](http://www.hud.gov/offices/hsg/sfh/res/respa_hm.cfm). If you cannot find the information you are seeking on HUD's website, you may contact the Office of RESPA and Interstate Land Sales at (202) 708-0502.*

## On the lighter side...

A mortgage broker called the Mortgage Loan Activities Unit regarding two separate advertisements that he submitted for approval, wanting to know what action had been taken. Upon checking, we found he had been sent responses about a week earlier. The broker then said that he had two envelopes from the DRE but had not yet opened them.



**Moral:** If you are waiting for information from the DRE and receive mail from us – open it. It may be what you have been waiting for!