



# Real Estate Bulletin

Real Estate MATTERS!

## MESSAGE FROM COMMISSIONER DAVI




### Implementation of SAFE

The end of 2010 proved to be incredibly eventful. With the implementation of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE), the DRE faced the challenge of processing thousands of Mortgage Loan Originator (MLO) license endorsement applications by December 31st. Meeting the deadline was crucial to ensure applicants could continue to originate residential mortgage loans in 2011. I am pleased to say that the DRE was able to process all of the MLO license endorsement applications that were complete and met the new licensing standards. As of January 1, the DRE issued over 22,000 MLO license endorsements. The DRE expects to eventually issue over 30,000 MLO license endorsements.

SAFE is a federal mandate that required states to adopt uniform standards for MLOs. To implement SAFE in California, the state legislature passed Senate Bill 36 which gave real estate licensees until January 1, 2011 to obtain a MLO license endorsement in order to continue to originate residential mortgage loans. Without the MLO license endorsement, a real estate licensee cannot legally originate or broker residential mortgage loans. Furthermore, the new requirements apply to the Department of Corporations (DOC) licensed companies and their employees. For the first time individual originators working for a DOC licensee must be individually licensed as a MLO in order to originate residential mortgage loans.

With SAFE, new license requirements are placed on real estate licensees who originate residential mortgage loans. These new standards include the testing of applicants on state and federal lending laws, pre- and post-endorsement educational requirements, and a more extensive background check with legislatively mandated limitations on who can be issued an endorsement. One may qualify for the issuance of a real estate license but not measure up to these new standards for the mortgage loan originator endorsement. These new requirements are intended to keep unscrupulous operators out of the business while ensuring those in the business have demonstrated an understanding of the laws and regulations regarding mortgage lending. In addition, all residential mortgage loan originators will have to register with a national database allowing consumers to check with a single source to make certain they are doing business with a properly licensed business. A licensee's MLO license endorsement status is also reflected in the DRE's licensing database through which a consumer can also access the national database.

The national database also allows regulators to determine if a MLO has been disciplined or revoked by another jurisdiction, preventing those originators from closing shop and opening a new business in a different state or location.

While I do not believe that SAFE is a cure all, I believe the higher standards are a step forward in enhancing consumer protection and restoring confidence in a beleaguered industry. For more information on SAFE, please visit the DRE's Web site at [www.dre.ca.gov](http://www.dre.ca.gov). 

### Informing the DRE about material changes in subdivision public reports

The Subdivided Lands Law requires that a developer (subdivider) obtain a Public Report from the Department of Real Estate (DRE) prior to marketing homes in a common interest development as well as other types of residential subdivisions. Once issued, the Public Report must reflect what is offered to a potential buyer accurately. Section 11012 of the Business and Professions Code (B&P) provides that it is unlawful for the owner, his agent, or subdivider to materially change the set-up of an offering after it has been submitted to the DRE without first notifying the DRE in writing of such intended change. Such changes must be reflected in the Public Report.

Although not intended to be all-inclusive, Commissioner's Regulation 2800 lists many of the possible material changes in a subdivision itself or in the program for marketing the subdivision interests. In reviewing any proposed changes, the Department may, under certain and limited circumstances, determine that an amended public report is not required. Generally, any change made which results in the subdivision public report not stating the true facts or omitting important facts will require an amended public report.

Anyone in doubt as to whether a proposed change will require an amended public report may contact the

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## New federal rule outlaws advance fees and false claims, and requires clear disclosures, regarding mortgage assistance relief (including loan modification, short sale, and deed-in-lieu of foreclosure) services

by Wayne S. Bell, *Chief Counsel*

The Federal Trade Commission (FTC) has issued a far-reaching rule with nationwide effect that bans providers of “mortgage assistance relief services”, which includes residential mortgage foreclosure rescue, loan modification, short sale, and deed-in-lieu of foreclosure services, from requesting or collecting fees or any other consideration from a homeowner until the homeowner has executed a written agreement with the loan holder or servicer which incorporates the offer of mortgage relief the provider obtained from the loan holder or servicer. The complete text of the new FTC rule, which is more restrictive than California law in a number of respects, can be found at 16 Code of Federal Regulations, Part 322, or at <http://www.ftc.gov/opa/2010/11/mars.shtm>. Real estate licensees should review the rule in its entirety.

In addition to the restriction discussed above, the rule also mandates that such mortgage assistance relief providers disclose to consumers what the total cost of the services will be, that they have no connection to any government program or agency, and that homeowners are free to reject any offer from their lender or servicer with no requirement to pay a fee to the relief provider. Moreover, it bars the mortgage relief operators from providing false and misleading information, and from destructively advising consumers to stop communicating with their home loan lenders or servicers. The disclosure rules went into effect on December 29, 2010.

In a news release regarding the rule, the FTC stated that the rule was issued “to protect distressed homeowners from mortgage relief scams that have sprung up during the mortgage crisis. Bogus operations falsely claim that, for a fee, they will negotiate with the homeowner’s mortgage lender or servicer to obtain a loan modification, a short sale, or other relief from foreclosure. Many of these operations pretend to be affiliated with the government and government housing assistance programs”.

The broad and significant advance fee ban, which became effective on January 31, 2011, includes a narrow and qualified carve out for attorneys. If lawyers meet the following four conditions, they are generally exempt from the rule:

- They are engaged in the practice of law, and mortgage assistance relief is part of their practice.
- They are licensed in the State where the consumer or the dwelling is located.
- They are complying with State laws and regulations governing the “same type of conduct the [FTC] rule requires”.
- They place any advance fees they collect in a client trust account and comply with State laws and regulations covering such accounts. This requires that client funds be kept separate from the lawyers’ personal and/or business funds until such time as the funds have been earned.

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## Review of 2011 regulatory amendments for continuing education courses

Several amendments have been made to regulations affecting continuing education courses found in Article 25 of the Regulations of the Real Estate Commissioner. The amendments became effective January 1, 2011 and will impact the way continuing education courses are presented to licensees.


The following summarizes the changes that will affect a licensee seeking credit for a continuing education course:

- All courses shall require completion within one year from the date of registration.
- For correspondence courses, incremental assessments shall be required to measure a participant's mastery of the course content after each logical unit of instruction or chapter, i.e., case studies, quizzes or other form of exercises.
- A final examination consisting only of multiple choice, true/false and/or fill-in the blank questions shall be limited to a maximum of 10% true/false questions.
- Time calculations for the duration of the final examination consisting of multiple choice, true/false and/or fill-in the blank questions will be allowed a maximum amount of one (1) minute per each question.
- Questions used in a final examination shall not duplicate any more than 10% of questions used in any other quiz or examination utilized during the presentation of the course.
- A course may include a provision for one retaking of the final examination by a participant who failed the original examination provided the questions in the re-examination are different than those asked in the original final examination. A participant who fails the re-examination fails the course and receives no credit from that course. This participant is not barred from re-enrolling and attempting completion of the same course to receive credit for the course.



For more detail on the specific regulation amendments, you may visit [http://www.dre.ca.gov/pdf\\_docs/2009\\_Continuing\\_Education\\_final\\_adoption.pdf](http://www.dre.ca.gov/pdf_docs/2009_Continuing_Education_final_adoption.pdf).

Revised forms reflecting the amendments for continuing education offerings and pre-license course approvals can be found at: [http://dre.ca.gov/lic\\_course\\_providers.html](http://dre.ca.gov/lic_course_providers.html).

If you have any questions or comments concerning the Continuing Education Program, please contact the Education Section at (916) 227-0894. 

### Material Changes Continued from page 1

Department's Subdivision Section for advice.

Most subdividers are aware of the more obvious material changes and usually promptly submit an application for an amended public report when, for example, there is a change in the name or organization structure of the subdividing entity, a change in the purchase money handling procedures, or addition or deletion of common facilities.

Two types of frequently overlooked material changes are:

- An increase of 20% or more or a decrease of 10% or more in the regular assessments charged by an Association over the amount reflected in the current public report. The Department sometimes receives applications for subsequent phases in a common interest subdivision which indicate that assessments have been increased substantially over the amount of assessments listed in the public reports for prior phases. In these cases, amended public reports must be obtained for all prior phases which still contain unsold lots or units. In addition, delinquencies in the payment of regular assessments resulting in the receipt by the Association of income which is more than 10% less than scheduled, must be reported. As association receipts may be constantly changing, DRE policy permits

the computation of the 10% threshold based upon three consecutive months using a rolling average. The amended public report will usually contain a "special note" disclosing the possible problems to potential buyers that might result from a substantial delinquency in the receipt of assessments.

- The creation by the subdivider of a subsidy or maintenance arrangement for HOA expenses that has not been approved by the DRE. This usually takes the form of a maintenance agreement that permits the subdivider to defer all or a portion of their monthly assessments.

Any failure to notify the Department of material changes can result in administrative action such as the issuance of a Desist and Refrain Order, usually causing the cessation of sales. Civil action may also be brought against the subdivider by purchasers who did not receive the correct information in the public report.

The Department strongly recommends that all subdividers regularly review Commissioner's Regulation 2800 in conjunction with their business plans and promptly submit notification of any proposed material changes in subdivision offerings to the Department of Real Estate. 

## The Department of Real Estate has wide-ranging powers to discipline brokers who violate the public trust

*By Amelia Vetrone, Real Estate Counsel*

Roy Snyder, a truck driver, decided to take out a \$4000 loan against his mother's unencumbered home with her permission. At the time the loan was made, a loan broker's commission on loans up to \$4,999.99 was limited by law. Snyder's loan officer talked him into borrowing \$5,250, thereby avoiding the limit on the broker's commission. The higher loan amount was achieved by selling credit life insurance and disability insurance to Snyder for \$1,117.20, which Snyder was informed he had to buy to receive the loan. The insurance company was owned by one of the loan brokers, his sister, and the sister's husband. As a commission, the brokers took a second trust deed on Snyder's mother's property for \$2,500.

In total, Snyder borrowed \$7,750, of which he received \$3,874.60, while the brokers amassed \$3,875.40. If Snyder's loan had been under the statutory limit of \$4,999.99, the brokers' maximum commission would have been \$750. This fact was never disclosed to Snyder.

After an investigation and hearing, the DRE revoked the brokers' real estate licenses, along with the licenses of their salespeople. The DRE did so based on the brokers' violations of Business and Professions Code (B&P) provisions addressing misrepresentation, fraud, and dishonest dealing.

This scenario of self-dealing took place in 1967, when loan money was tight and real estate brokers often resorted to creative ways to earn commissions. Some of those methods were unlawful, as in the case involving Snyder. Now, once again, in another distressed real estate market, the DRE finds itself with a surge of real estate law violations involving many old tricks as well as new ones in the areas of loan modification, foreclosure rescue, and short sale fraud activity.

Created in 1917, the DRE's purpose has always been to require that brokers and salespeople be honest and trustworthy, as they generally act in a confidential and fiduciary capacity with the public. The DRE achieves this goal not only through licensing but also through disciplinary actions against licensed brokers and salespersons. Conduct that violates the Real Estate Law will result in formal disciplinary action against a licensed real estate broker—whether the broker was acting on behalf of others or as a principal, and whether or not the conduct occurred in the context of a real estate transaction.

In addition to revocation of a real estate license, the types of discipline imposed by the DRE include; revocation of the plenary license and issuance of a restricted license; suspension of the license with or without a monetary penalty (up to \$10,000); restitution to the victim; educational course completion and ethics testing; trust fund reporting requirements; chargeable audits; criminal arrest reporting requirements; desist and refrain orders; and, in extreme cases, an order of debarment.

An order of debarment, issued by the Real Estate Commissioner, suspends or bars an individual for up to three years from any position of employment, management, or control of any business activity involving real estate. Persons subject to such an order are also barred from conducting any real estate-related business activity on the premises where a real estate broker or salesperson is conducting business. In addition, the order bars an individual from participating in any real estate-related business activity of a finance lender, residential mortgage lender, bank, credit union, escrow company, title company, or

underwritten title company.

Since violators of the Real Estate Law may be subject to criminal penalties, the DRE coordinates its investigative efforts with other law enforcement agencies. If another administrative agency has prosecuted a broker or salesperson before the DRE commences its action, the DRE's ultimate disciplinary action may include, or be based on, the other agency's findings and results. A licensed real estate broker will be subject to discipline if his or her conduct demonstrates a lack of honesty and integrity—whether that determination has been made by the DRE alone, by some other agency, or by the court.

The DRE will file formal disciplinary proceedings against any licensee who has been found guilty of, or been convicted of, a felony or a crime "substantially related" to the qualifications, functions, or duties of a real estate licensee.

It is not necessary that the crimes committed by the licensee involve real estate. The DRE will examine the conduct at issue to determine whether it is substantially related to the standard of conduct for a real estate licensee.

For example, in *Arneson v. Fox*, a real estate broker's license was revoked after he was found guilty in federal court of participating in a scheme to boost the financial statements and stock price of a real estate development company. The broker set up various shell corporations as straw buyers to purchase property from the development company in paper deals made to appear as if they were arm's-length transactions. In fact, the development company was supplying the funds for the purchases. Following the broker's felony conviction, the DRE revoked the broker's real estate license.

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The DRE also revoked the license of the real estate broker in *Robbins v. Davi*. In *Robbins*, the real estate broker managed over 20 properties

consisting of more than 1,000 residential apartments. He was found guilty of misdemeanor violations of the Los Angeles Municipal Code relating to fire prevention and safety.

The DRE's action was based on the broker's conviction of three misdemeanor violations of the fire protection and prevention provisions of the Los Angeles Municipal Code. However, the broker previously was convicted of 50 municipal code violations in the period between 1986 and 1995. A substantial relationship to real estate was found because the broker's activities in ignoring fire code laws involved the intent to confer a financial benefit by reducing operating expenditures while simultaneously risking the safety of the apartment tenants.

Real estate brokers frequently hold other professional licenses in addition to a real estate license, and real estate brokers engaged in mortgage loan activities often are licensed in more than one state. A broker's real estate license will be subject to suspension or revocation if another licensing agency within California or in any other state suspends or revokes that broker's other license based on acts that would also constitute a violation of the Real Estate Law.

In some cases, the DRE's discipline might be more severe. For example, in *Herrera v. Department of Real Estate* the Department revoked the real estate broker license of a lawyer whose law license was merely suspended by the State Bar of California. The State Bar

found that Herrera had received client funds without notifying the client and then misappropriated the client's funds for his own use. The State Bar suspended Herrera's law license for 60 days with one year of probation. While the DRE's action was based on the State Bar discipline, Herrera's misappropriation of trust funds was conduct that would have warranted the revocation if it had occurred in the context of a real estate transaction.

The DRE's "substantially related" standard also applies to brokers who have incurred civil liability. A real estate broker's license will be subject to discipline after a final civil court judgment that is related to a real estate matter and is based on the grounds of fraud, misrepresentation, or deceit.

An illustrative case is *Denny v. Watson*, in which a group of real estate brokers had their licenses revoked following a civil judgment against them for fraud. In that case, the brokers had secured the deed to a motel from one of their clients for no money down. The brokers promised that they would 1) not record the deed until they had sold the property, 2) make the payments on the trust deeds and liens against the property, 3) manage the property, and 4) when they sold it, pay the client \$5,500, clear of the debts. Instead, the brokers recorded the deed, failed to make the necessary trust deed payments, permitted the property to be sold under power of sale in one of the trust deeds, and, through a confederate, purchased the property for themselves at the trustee's sale for a reduced price. The seller sued the brokers and obtained a civil judgment for fraud. The DRE revoked the brokers' licenses based on the judgment.

In addition to accepting the findings of other agencies and tribunals, the DRE conducts its own investigations into alleged real estate broker misconduct. A real estate broker's license will be subject to discipline for violations of the laws that were

enacted to address or prevent direct losses to the public as the result of misrepresentation, fraud, dishonest dealing, negligence, unlicensed activity, trust fund mishandling, and lack of broker supervision.

In keeping with the DRE's mandate to protect the public, a real estate broker's license will be subject to disciplinary action whether the broker was acting on behalf of a client or as a principal. When a broker's wrongful conduct occurs during the course of performing licensed real estate activities, B&P §10176 governs the discipline for that conduct. B&P §10177 provides for discipline of a broker's wrongful conduct that is not strictly within the course and scope of real estate activity.

For example, in *Realty Projects v. Smith*, the case involving overcharged borrower Roy Snyder, the brokers' licenses were revoked for violations of B&P §10176(a) (making any substantial misrepresentation), §10176(i) (conduct that constitutes fraud or dishonest dealing), §10177(d) (willfully disregarding or violating the Real Estate Law), §10177(j) (conduct that constitutes fraud or dishonest dealing), and §10177(f) (conduct supporting license denial). The disciplinary proceedings against the brokers and their sales agents were based on the B&P §10176 requirement of fair and honest dealing while acting as mortgage loan brokers, but B&P §10177 was applied to the manner in which they dealt with Snyder and others before the execution of loan agreements and the performance of real estate activities.

Brokers can also be disciplined for their conduct as a party to a transaction. In *Small v. Smith*, the DRE revoked a real estate broker's license for violating §10177(j). A real estate broker purchased 20 acres of land through an installment sales contract. At the time of the down payment, 10 acres were immediately conveyed to the broker,

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and the other 10 were to be conveyed when the sale price had been fully paid. The broker sold part of the unconveyed 10 acres to a third party in an installment sale. After a few months, the broker stopped making his installment payments to the original seller but continued to collect payments from his buyer—even after being issued a notice of forfeiture. The original seller foreclosed on the broker's contract, while the broker continued to collect payments from his uninformed buyer. The broker's buyer did not know about the broker's forfeiture until after the land was resold to someone else, and he received nothing. The broker refused to issue a refund to his buyer.

Regarding the license revocation, the court reiterated that the object of an administrative proceeding aimed at revoking a license is to protect the public and “to keep the regulated business clean and wholesome.” When a real estate broker's misconduct shows a complete lack of honesty and trustworthiness, it renders that broker unfit to hold the unique position of trust that real estate licensees are given by members of the public.

Consumers all too frequently suffer losses when they deal with unlicensed representatives in connection with real estate activities. B&P §10131 lists the activities which require a real estate license. Disciplinary issues arise when a licensee compensates an unlicensed person for performing activities that require a real estate license or when a salesperson accepts compensation for real estate activities from someone other than their employing broker. The payment or collection of compensation for unlicensed real estate activity is a crime punishable by a fine up to \$20,000, imprisonment up to six months in jail, or both.


Under the Real Estate Law, a salesperson who is not working under the auspices of a licensed broker is not licensed to conduct real estate activities. In *Grand v. Griesinger*, a real estate salesperson operated a company that listed rental properties. He formed a partnership with a real estate broker for 25 percent of the net profits. The broker had no ownership in the company and no responsibilities. The DRE refers to this type of uninvolved broker as a “rent-a-broker.” The salesperson involved his whole family in the business, including his father and wife, who were also licensed salespersons. The salesperson licenses of the real estate salesperson, his father, and his wife were all revoked because their real estate activities were conducted without actual supervision by the broker under whom they were licensed at the time or without their being licensed under any broker.

A recent DRE license revocation of two mortgage loan brokers shows the interplay of trust fund mishandling, in violation of B&P §10145, with unlicensed activity causing a

direct loss to a consumer. In that case, a real estate broker operated two mortgage loan companies. The broker's husband was a real estate salesperson whose license had expired long before. The unlicensed husband solicited a consumer to provide funds to be used as hard money loans secured by real property. In exchange for checks totaling \$150,000, which the consumer obtained by taking out equity loans against her home, the consumer was given deeds of trust for two different properties.

The consumer/lender later learned that the deeds of trust were completely false. In one deed of trust, the property was not owned by the person who was named as the owner in the deed of trust. The other deed of trust was for a residential property that the broker and her husband were renting as their home for a few months. The consumer's checks were deposited in the general bank accounts of the two mortgage loan companies, and the funds were converted by the broker and her husband to their own personal use. Moreover, the designated officer of the company receiving the bulk of the funds was a rent-a-broker living in a nursing home in a remote part of the state.

While a licensed real estate broker may solicit funds for use as loans secured by real property, the funds received must be treated as trust funds. Funds acquired for the benefit of others that are not immediately placed into a neutral escrow depository or into the hands of the broker's principal must be deposited into a trust fund account maintained by the broker in a bank or recognized depository in the state. The broker must be a signatory to the trust fund account, with other signatories limited to those who possess a real estate license or fidelity bond coverage. In the DRE license revocation action, one check was written to the consumer/lender as a partial repayment of the loans by one of the mortgage loan companies. The check was signed by the broker's unlicensed son and was returned by the bank for insufficient funds. The DRE revoked the licenses of the real estate corporations, the broker, and the rent-a-broker for multiple violations of the Real Estate Law, including trust fund mishandling and fraud.

Brokers also may be subject to license discipline for failure to exercise reasonable supervision over their corporation, employees, or salespersons. While it may never be known whether the broker in the recent DRE license revocation case actually instructed her unlicensed husband to solicit funds from the consumer, the failure of the broker and the rent-a-broker to provide adequate supervision over the husband's conduct as well as the mortgage loan brokerage activities of the two corporations led to disastrous consequences for the affected consumer/lender and, ultimately, for the brokers' futures as real estate licensees. 

# WANTED

## Locations of Neglected Swimming Pools



Depressed housing markets and foreclosures have led to many neglected swimming pools in California.

- ☞ Pools that are not maintained grow algae and bacteria.
- ☞ Mosquitoes lay their eggs in neglected pools. These eggs hatch into larvae that become adult mosquitoes.
- ☞ Mosquitoes from neglected pools can transmit WNV once they feed on an infected bird.
- ☞ These WNV-infected mosquitoes can bite you and infect you with WNV!

What do I do if someone I know has a neglected pool?

- ☞ Locate the mosquito control agency in your area by visiting: [www.westnile.ca.gov](http://www.westnile.ca.gov) or calling 1-877-WNV-BIRD (1-877-968-2473).
- ☞ Contact your local mosquito control agency about the best course of action.

What can the local mosquito control agency do?

The mosquito control agency can do the following:

- ☞ Work with realtor or property owner if necessary;
- ☞ Place mosquito fish in the pool to eat the mosquito larvae;
- ☞ Put a product in the pool that inhibits or kills the larvae;
- ☞ Help you decide how to manage the pool, if you own the pool, so no more mosquitoes are produced.
- ☞ These actions stop mosquito production, but the pool water remains dark or brackish until it is properly maintained.

What if there is not a local mosquito control agency in my area?

You can take a few simple actions to prevent mosquito production in your pool:

- ☞ Contact your city government;
- ☞ Use mosquito control slow-release products available at the local garden center or hardware store.

For more information

- ☞ Contact your local mosquito control program or health department ☞
- ☞ To locate the mosquito control program in your area visit: [www.westnile.ca.gov](http://www.westnile.ca.gov) or call 1-877-WNV-BIRD (1-877-968-2473) ☞



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## New Federal Rule Continued from page 2

It is important to note that the carve out for lawyers discussed above only applies to the FTC rule.

In California, since the passage of Senate Bill 94, which became effective on October 11, 2009, State law has prohibited any person, including real estate licensees and attorneys, from demanding, claiming, charging, collecting or receiving an upfront fee from a borrower in connection with a promise to modify the borrower's residential loan or to do some other form of mortgage loan forbearance. The California Department of Real Estate has information about Senate Bill 94 and its broad advance fee ban, and that information can be accessed at [http://dre.ca.gov/cons\\_adv\\_fees\\_alert.html](http://dre.ca.gov/cons_adv_fees_alert.html). Thus, the more comprehensive advance fee ban applicable to lawyers with respect to loan modifications and other forms of home loan forbearance under

Senate Bill 94 is still in effect, and the FTC rule's limited attorney exception does not provide a safe harbor under California law.

Stated otherwise, the FTC rule does not supplant the greater protections of California law with respect to the services covered by Senate Bill 94. Rather, it adds another (Federal) layer of enforcement, and goes a step farther than current State law in covering short sales and deed-in-lieu of foreclosure services. The FTC has promised robust enforcement of the new rule, and the FTC, federal prosecutors, and some State Attorney Generals will be able to enforce the rule by issuing injunctions, obtaining harsh civil penalties, and by seeking damages on behalf of victimized consumers.

If you have questions regarding the FTC rule, you should contact the Federal Trade Commission. 

## Real Estate Bulletin

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