

ADVANCE NOTICE OF INTENT TO FILE EMERGENCY REGULATIONS

This notice is sent in accordance with Government Code Section 11346.1(a) (2), which requires that State of California agencies give a five working day advance notice of intent to file emergency regulations with the Office of Administrative Law (OAL). The Department of Real Estate (hereinafter the “Department”) intends to file an Emergency Rulemaking package with OAL, to apply the “Statement on Subprime Mortgage Lending” (the Statement) and the “Guidance on Nontraditional Mortgage Product Risks” (the Guidance) to real estate brokers acting within the meaning of Sections 10131(d) or 10131.1 of the Code, as required by Chapter 301 Statutes of 2007 effective January 1, 2008. As required by subdivisions (a) (2) and (b) (2) of Government Code Section 11346.1, the notice appends the following (1) the specific language of the proposed regulations and (2) the Finding of Emergency, including specific facts demonstrating the need for immediate action, the authority and reference citations, the informative digest and policy statement overview, attached reports, Form 399 and required determinations.

The Department plans to file the Emergency Rulemaking package with OAL at least five working days from the date of this notice. If you would like to make comments on the Finding of Emergency or the proposed regulations, they must be received within five calendar days of the Department’s filing at OAL by both the Department and OAL. Responding to comments at this point in the process is strictly at the Department’s discretion.

Comments should be sent simultaneously to:

David B. Seals, Real Estate Counsel
Department of Real Estate
2201 Broadway
P. O. Box 187000
Sacramento, CA 95818-7000

and

Office of Administrative Law
300 Capitol Mall, Suite 1250
Sacramento, CA 95814

Please note that this advance notice and comment period is not intended to replace the public’s ability to comment once the emergency regulations are approved.

The Department will hold a public hearing and 45-day comment period within the 180 day certification period following the effective date of the emergency regulations.

Please contact David B. Seals at (916) 227-0789 or via electronic mail to regulations@dre.ca.gov if you have any questions concerning this Advance Notice.

FINDING OF EMERGENCY

Jeff Davi, Real Estate Commissioner has found that an emergency exists and that the immediate adoption of the attached proposed regulations is necessary to avoid serious harm to the public peace, health and safety, or general welfare.

SPECIFIC FACTS DEMONSTRATING THE NEED FOR IMMEDIATE ACTION

On January 31, 2007, the California Senate Banking Committee held a hearing on nontraditional mortgage products and the application to State mortgage regulators of the Interagency Guidance on Nontraditional Mortgage Products Risks (Guidance). The Federal Guidance was jointly promulgated by the Office of the Comptroller of the Currency (Treasury Department), Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision (Treasury Department), and the National Credit Union Administration, to provide instruction to federally regulated entities on how to address the inherent risks to industry and consumers associated with the origination and funding of nontraditional mortgage products. The Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators promulgated a similar Guidance requesting that State regulators of mortgage lenders and brokers adopt the Guidance to maximize consumer protections when using high risk loan products.

In furtherance of the objectives of the Guidance, the Department embarked on the process of adopting appropriate regulations. Those regulations were placed into effect on September 28, 2007.

The Statement on Subprime Mortgage Lending (Statement) was published on July 17, 2007 by the Conference of State Bank Supervisors, the American Association of Residential Mortgage Regulators, and the National Association of Consumer Credit Administrators. The issuance of the Guidance and the Statement and the need for State regulators to implement their provisions contributed to the introduction of SB 385 by the Legislature.

The regulations promulgated by the Department in September of 2007 addressed the Guidance as it pertained to mortgage brokers, but further regulations are needed to fully address the Statement as required by SB 385. SB 385 successfully moved through the Legislature and was signed by the Governor in October of 2007 as Chapter 301, Statutes of 2007.

Chapter 301, Statutes of 2007 effective January 1, 2008, which the Department is seeking to implement through the proposed emergency regulations, contains a finding and declaration from the Legislature that consistent application of the Guidance and the Statement "...to state-regulated persons and institutions engaged in the brokering, originating, servicing, underwriting, and issuance of nontraditional and subprime mortgage products is critical to protect borrowers and lenders." It also declares that it is the intent of the Legislature that the Department as well as both the Department of Financial Institutions and the Department of Corporations take action to

ensure that mortgage lenders and brokers licensed by the State are made aware of the Guidance and the Statement “...as soon as possible and are encouraged to comply with those documents at the earliest possible date.” (Emphasis added).

Consistent with these declarations, Section 10240.3 was added to the Business and Professions Code, as follows:

“10240.3. (a) The commissioner shall apply the guidance on nontraditional mortgage product risks published on November 14, 2006, by the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators, and the Statement on Subprime Mortgage Lending published on July 17, 2007, by the aforementioned entities and the National Association of Consumer Credit Administrators, to real estate brokers acting within the meaning of Section 10131.1 or subdivision (d) of Section 10131.

(b) The commissioner may adopt emergency and final regulations to clarify the application of this section as soon as possible.

(c) A real estate broker acting within the meaning of Section 10131.1 or subdivision (d) of Section 10131 shall adopt and adhere to policies and procedures that are reasonably intended to achieve the objectives set forth in the documents described in subdivision (a).” (Emphasis added).

Section 10131.1 was also amended to add, among other things, subsection (c) which defines as a real estate broker anyone who engages as a principal in the business of making eight or more loans to the public during a calendar year from the principal’s own funds ”... when those loans are held or resold and are secured directly or collaterally by a lien on residential real property consisting of a single dwelling unit in a condominium or cooperative or on any parcel containing only residential buildings if the total number of units on the parcel is four or less.” As a result, the Department must also quickly establish appropriate policies and procedures to address the newly regulated lending activity of real brokers consistent with the Guidance and the Statement, as required by SB 385.

To put this in prospective, the Mortgage Bankers Association published in December 2007 their National Delinquency Survey for the third quarter of 2007. That survey found on a nationwide basis that the seasonally adjusted delinquency rate for mortgage loans on one-to-four-unit residential properties was 5.59% in the third quarter of 2007 and 4.67% for the same period in 2006 which puts the rate at its highest point since 1986. The inventory of loans in foreclosure for the third quarter of 2007 was up 64 basis points to 1.69% - the highest level on record. Furthermore, the percentage of loans with installments past due was higher in California than any other state in the Pacific region (Alaska, California, Hawaii, Oregon, and Washington) and the percentage of homes in foreclosure in California was 2.66% over 92% - more than the next highest rate (Hawaii 1.38%).

In California from December 2006 to October 2007, according to DataQuick Information Systems, the number of residential notices of default per month increased from 12,135 in December of 2006 to 24,966 in October of 2007 – more than doubling. During the same time-period the number of residential foreclosures in California increased from 2,450 in December of 2006 to 10,430 in October of 2007 – more than four fold.

Further delays in implementation of these regulations will not provide consumers with the protection they warrant and will negatively impact the nontraditional and subprime loan situation.

AUTHORITY AND REFERENCE

The changes to the regulations are authorized by Business and Professions Code Sections 10080, 10131.1(c), 10240.3, and 10245 to implement, interpret or make specific Business and Professions Code Sections 10131.1(c), 10236.4, 10240, 10240.2, 10240.3, 10241, and 10245.

INFORMATIVE DIGEST/POLICY STATEMENT OVERVIEW

SUMMARY OF EXISTING LAWS AND REGULATIONS

Real estate brokers acting within the meaning of Section 10131(d) of the Business and Professions Code (hereinafter the “Code”) have been required to provide a disclosure statement to borrowers within three days of receiving a completed written loan application that provides all of the information required by Section 10241 of the Code. Sections 2840 and 2840.1, Title 10, California Code of Regulations (hereinafter the “Regulations”) contained the formats for the approved disclosure statements. Regulation 2840 was amended, and Regulation 2840.1 was repealed, effective September 28, 2007 in order to remove the text of the Mortgage Loan Disclosure Statement, RE882 and the Mortgage Loan Disclosure Statement/Good Faith Estimate, RE883 from the regulations.

On January 1, 2008, Senate Bill 385 (Chapter 301 Statutes of 2007) became effective. The bill requires the Department of Real Estate to apply the “Statement on Subprime Mortgage Lending” (the Statement) and the “Guidance on Nontraditional Mortgage Product Risks” (the Guidance) to real estate brokers acting within the meaning of Sections 10131(d) or 10131.1 of the Code. The bill further permits the Department to adopt emergency and final regulations to clarify application of its provisions. In order to provide all of the consumer information recommended by the Statement and the Guidance and mandated by Senate Bill 385, the RE882 and RE883 disclosure statements must be amended. The RE882 and RE883 disclosure statements relate to traditional and/or subprime mortgage products only and are incorporated by reference into Regulation 2840.

To further consumer protection and in anticipation of SB 385 becoming law, the Department promulgated Regulation 2842 effective on September 28, 2007. A new disclosure form, “Mortgage Loan Disclosure Statement/Good Faith Estimate – Nontraditional Mortgage Product (One to Four Residential Units), RE885, was incorporated by reference into Regulation 2842 to provide a vehicle for real estate brokers to comply with the consumer protection mandate of Senate Bill 385. In order to provide all of the consumer information recommended in the Guidance and the Statement and mandated by the finally adopted version of Senate Bill 385, the RE885 disclosure statement must be amended.

As amended by Senate Bill 385, Section 10131.1 defines persons who make eight (8) or more loans secured by real property from their own funds, unless exempted, as real estate brokers. Section 2844 must be adopted to clarify the lending practices to be adopted pursuant to Section

10240.3 of the Code by those newly covered brokers resulting from the SB 385 amendment of Section 10131.1 of the Code.

SUMMARY OF THE EFFECT OF THE PROPOSED ACTION

AMENDMENT OF SECTION 2840

Would modify forms RE882 and RE883 to include (1) expanded information regarding loan terms; (2) information regarding possible increased costs of “no documentation” or “no asset” loans; (3) increased disclosures of prepayment penalty information; and (4), in the case of the RE882, additional, and, in the case of the RE883, expanded, information regarding real estate taxes and insurance that must be paid.

AMENDMENT OF SECTION 2842

Would modify form RE885 (1) to include information regarding possible increased costs of “no documentation” or “no asset” loans; (2) to increase the disclosure of prepayment penalty information; and (3) to provide information regarding real estate taxes and insurance that must be paid.

ADOPTION OF SECTION 2844

Would clarify the required lending practices related to nontraditional and subprime mortgage products, under Section 10240.3 of the Code, for real estate brokers newly covered by the amendment to Section 10131.1 of the Code which was contained in SB 385 (Chapter 301 Statutes of 2007).

DISCLOSURES REGARDING THE PROPOSED ACTION

1. Plain English drafting: The Commissioner has confirmed that these regulations have been drafted in plain English pursuant to Government Code sections 11342.580 and 11346.2(a) (1).
2. Mandate on local agencies and school districts: None.
3. Cost or savings to any state agency: None.
4. Cost to any local agency or school district which must be reimbursed in accordance with Government Code section 17561: None.
5. Other non-discretionary cost or savings imposed upon local agencies: None.
6. Cost or savings in federal funding to the state: None.
7. The Department is aware that there may be cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action. However, such cost impact will not be significant.

8. The Commissioner has made an initial determination that the adoption, amendment or repeal of these regulations will not have a significant state-wide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

9. Impact on jobs and business expansion, elimination or creation: The Commissioner has determined that this regulatory proposal will not have a significant impact on the creation or elimination of jobs within the State of California nor will it significantly affect the creation of new businesses, the elimination of existing businesses within the State of California, or the expansion of businesses currently doing business within the State of California.

10. Significant effect on housing costs: None.

EFFECT ON SMALL BUSINESS

The proposed regulatory changes may affect small business.

TECHNICAL, THEORETICAL, AND EMPIRICAL STUDIES OR REPORTS

1. GUIDANCE ON NONTRADITIONAL MORTGAGE PRODUCT RISKS.
2. STATEMENT ON SUBPRIME MORTGAGE LENDING.
3. National Delinquency Survey for the third quarter of 2007, Mortgage Bankers Association published in December 2007.
4. Monthly Residential Notices of Defaults by County and Monthly Residential Trustees Deeds by County, DataQuick Information Systems.

CONSIDERATION OF ALTERNATIVES

In accordance with Government Code section 11346.5, subdivision (a)(13), the Commissioner must determine that no reasonable alternative he considered or that has otherwise been identified and brought to his attention would be more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons than the proposed action.

The Commissioner invites interested persons to present statements or arguments with respect to alternatives to the proposed regulatory action during the written comment period.

COMPLIANCE WITH GOVERNMENT CODE §11346.4(A) (1) THROUGH (4)

The Department of Real Estate (the Department) has complied with Government Code §11346.4(a) (1) through (4) and Section 86, Title 10 of the California Code of Regulations, by mailing or delivering a copy of this Notice of Proposed Changes in the Regulations of the Real Estate Commissioner and of the Proposed Regulations with changes indicated in strikeout and underline to the Department's list of interested persons including:

1. Every person who has filed a Request for Notice of Regulatory Action with the Department.
2. The Director of the Department. (The Real Estate Commissioner and the Secretary of the Business, Transportation and Housing Agency).
3. A substantial number of real estate brokers. They are predominantly small businesses, some of which may be, or have been in the past, affected by our Proposed Regulation change. The Department has no way of knowing which are small businesses.
4. The California Association of Realtors, a real estate licensee trade organization, the California Building Industry Association, a homebuilders trade organization, and the California Association of Mortgage Brokers, a mortgage loan broker trade organization.

DATED: _____

Jeff Davi
Real Estate Commissioner