

TITLE 10. CALIFORNIA DEPARTMENT OF REAL ESTATE

NOTICE IS HEREBY GIVEN

The Commissioner (Commissioner) of the Department of Real Estate (Department) proposes to adopt rules entitled, "California Foreclosure Prevention Act." The proposed regulatory action clarifies the application of Civil Code Sections 2923.52 and 2923.53 under the California Foreclosure Prevention Act. The proposed rules were adopted as emergency regulations on June 1, 2009, and readopted as emergency regulations on December 1, 2009. In this rulemaking action the Commissioner proposes to permanently adopt Article 16.5, Sections 2850.1, 2850.2, 2850.3, 2850.4, 2850.5, 2850.6, 2850.7, 2850.8, 2850.9, and Section 2850.10 to Chapter 6, Title 10 of the California Code of Regulations.

PUBLIC COMMENTS

No public hearing is scheduled. Any interested person or his or her duly authorized representative may request, in writing, a public hearing pursuant to Section 11346.8(a) of the Government Code. The request for hearing must be received by the Department contact person designated below no later than 15 days prior to the close of the written comment period.

WRITTEN COMMENT PERIOD

Any interested person or his or her authorized representative, may submit written comments relevant to the proposed regulatory action to the Department addressed as follows:

Regular Mail

Department of Real Estate
Attn: Daniel E. Kehew, Office of Legislation and Policy
2201 Broadway
P.O. Box 187007
Sacramento, CA 95818-7007

Electronic Mail

DRERegulations@dre.ca.gov

Facsimile

(916) 227-9458

Comments may be submitted until 5:00 p.m., February 10, 2010. If the final day for the acceptance of comments is a Saturday, Sunday, or state holiday, the comment period will close at 5:00 p.m. on the next business day.

INFORMATIVE DIGEST/PLAIN ENGLISH OVERVIEW

In the fall of 2008, in response to the continuing foreclosure crisis in California, the Governor proposed to the Legislature a concept to reduce foreclosures by encouraging loan modifications in the marketplace. This plan was a follow-up to the Administration's previous actions to encourage loan modifications by servicers, including a November 2007 agreement with servicers intended to address resetting

interest rates, and the signing of SB 1137 (Perata, Chapter 69, Statutes of 2008) in the summer of 2008, to require residential mortgage servicers reach out to borrowers at least 30 days before a notice of default is filed in a foreclosure proceeding, to attempt to work out a solution.

The Governor's proposal involved encouraging residential mortgage loan servicers to streamline the process for modifying loans by changing the requirements for nonjudicial foreclosures for loans serviced by mortgage loan servicers that had not implemented a comprehensive loan modification program. The initial parameters for a comprehensive loan modification program were modeled after the program that the Federal Deposit Insurance Corporation (FDIC) implemented to modify loans in the IndyMac Federal Bank portfolio after the FDIC was appointed conservator of that institution.

Through the legislative process, the Legislature further developed the Governor's proposal into the California Foreclosure Prevention Act. In February of 2009, during the second extraordinary session the Legislature sent to the Governor two bills enacting the California Foreclosure Prevention Act: ABX2 7 (Lieu, Chapter 5, Statutes of 2009) and SBX2 7 (Corbett, Chapter 4, Statutes of 2009). On February 20, 2009, the Governor signed these bills.

Among other things, the California Foreclosure Prevention Act required the Commissioners of Real Estate, Corporations, and Financial Institutions to adopt emergency regulations to clarify the application of Civil Code Sections 2923.52 and 2923.53; two sections added to the Civil Code by the California Foreclosure Prevention Act. The Commissioners adopted the emergency regulations and on June 1, 2009, the regulations were filed with the Secretary of State and became effective. In accordance with the law's provisions, 14 days after the effective date of the regulations, the act became operative. These emergency regulations were readopted on December 1, 2009.

In this rulemaking action the Commissioner seeks to permanently adopt the emergency regulations clarifying the application of Civil Code Sections 2923.52 and 2923.53 of the California Foreclosure Prevention Act.

The Commissioner proposes to adopt Article 16.5 to Chapter 6 of Title 10 of the California Code of Regulations, entitled "California Foreclosure Prevention Act." In addition, the Commissioner proposes to adopt Subarticle 1 to that subchapter, entitled, "Requirements." Within Subarticle 1 the Commissioner proposes to adopt six sections.

Section 2850.1, entitled, "Scope of Regulations," defines the scope of the regulations. The section provides that the subchapter clarifies the application of Civil Code Sections 2923.52 and 2923.53, and sets forth the minimum requirements for a mortgage loan servicer to obtain an order of exemption from Civil Code Section 2923.52. Civil Code Section 2923.52 provides that a trustee may not proceed with a foreclosure sale until the lapse of 90 days in addition to the 3 months after a notice of default is filed on a borrower under Civil Code Section 2924. However, Civil Code Section 2923.52 provides that a mortgage loan servicer may obtain an order exempting it from the prohibition on proceeding with a foreclosure until after the lapse of 90 days, if

the mortgage loan servicer has implemented a comprehensive loan modification program.

The section further provides that the modification of loans in conformance with the Home Affordable Modification Program Guidelines issued by the U.S. Department of the Treasury on March 4, 2009, as amended, shall constitute the implementation of a comprehensive loan modification program and shall be deemed to meet all of the requirements in the article. The section also defines “residential mortgage loan” and “borrower.”

Section 2850.2, entitled “Eligibility,” sets forth the minimum eligibility requirements for a borrower and residential mortgage loan under a comprehensive loan modification program, in order for the program to obtain an order of exemption from the Commissioner. A mortgage loan servicer’s comprehensive loan modification may be more inclusive than the minimum requirements set forth in this section, but may not be less inclusive, to obtain an order of exemption. Generally, modifications must be available for borrowers and loans meeting the following requirements:

1. The loan was made between January 1, 2003 and January 1, 2008,
2. The borrower lives in the property,
3. The loan is in default,
4. The loan is a first lien on property in California,
5. The borrower can document the ability to pay the modified loan,
6. The borrower has not surrendered the property, the borrower is not engaged in a bankruptcy proceeding, and the borrower has not contracted to delay the foreclosure process while intending to leave the property.

Section 2850.3, entitled, “Availability,” requires the loan modification program to be made available to all persons and loans meeting the eligibility requirements who contact their servicer to notify the servicer of a financial hardship or to request a loan modification. In addition, the section requires a servicer to reach out to borrowers in financial hardship by including information on the comprehensive loan modification program in the contact with borrowers required at least 30 days before the service of a Notice of Default under Civil Code section 2923.5 (see SB 1137(Perata -2008), which requires that borrowers be contacted before the filing of the Notice of Default).

Sections 2850.4, 2850.5 and 2850.6 set forth the minimum requirements for a comprehensive loan modification program. Section 2850.5, entitled, “Loan Modification Features,” provides that loans refinanced in accordance with the Hope for Homeowners Program or the Home Affordable Refinance Program meet the minimum requirements of a comprehensive loan modification program. While loan work outs under these federal programs constitute refinancings rather than modifications, the recognition of the federal programs in the rules was intended to clarify that servicers may continue participating in those programs even for borrowers meeting the minimum eligibility requirements for modifications under these rules.

The California Foreclosure Prevention Act provides that a servicer need only modify a loan where the anticipated recovery from a modification exceeds the anticipated recovery from a foreclosure, on a net present value basis. Consequently,

Section 2850.5 of the proposed rules provides clarification on determining the net present value. The rule provides that the net present value must be based on reasonable assumptions regarding discount rates, property values, costs of foreclosure, costs of modification, and the ability of the borrower to repay the loan. The proposed rule requires a servicer to have internal or external evidence to support the assumptions, and provides that the “Net Present Value Model Parameters” in the Home Affordable Modification Program Guidelines, meets the requirements of the section and does not require supporting evidence. The proposed rules further require servicers to explain deviations from the “Net Present Value Model Parameters” in the exemption application. The proposed rules require that a loan be modified where the net present value of modifying the loan exceeds the net present value of foreclosing on the loan, provided that the borrower can document income, and provided that after the loan is modified, the borrower can establish the ability to pay the modified loan.

The California Foreclosure Prevention Act provides that a comprehensive loan modification program must target a ratio of a borrower’s housing-related debt to a borrower’s gross income of 38% or less, on an aggregate basis. Consequently, Section 2850.5 of the proposed rules provides that a servicer’s loan modifications are to target a 38% housing-related debt to gross income ratio, on an aggregate basis. The rules clarify that a servicer is not required to meet this ratio for every loan modified under the program. The rules further provide that a servicer must identify the reasons in its application the reasons its program does not achieve a 38% housing-related debt to gross income ratio, on an aggregate basis, if such is the case.

Section 2850.5 of the proposed rules provide that a comprehensive loan modification program must include at least two of the following features:

1. An interest rate reduction, as needed, for at least 5 years,
2. An extension of amortization period for the loan term to no more than 40 years from the original date of the loan,
3. Deferral of some portion of the principal until maturity,
4. A reduction in principal,
5. Compliance with a federally mandated loan modification program, or
6. Any other feature that Commissioner determines is appropriate, as described in the servicer’s application.

The proposed rules clarify that a program must include at least two of the identified features, but a single loan modification need not include more than one feature. The rules further require that a servicer have criteria in place to define when borrower qualifies for the potential concessions or modifications.

The California Foreclosure Prevention Act provides that when determining a loan modification solution for a borrower, a servicer must seek to achieve long-term sustainability. Consequently, Section 2850.5 sets forth characteristics that are presumed to constitute long term sustainability, including:

1. The modification reduces a borrower’s monthly payment for at least 5 years,
2. The modification results in a housing-related debt to income ratio of 38% or less,
3. After a modification, the borrower’s back-end debt-to-income ratio is equal to or

- less than 55%,
4. The borrower is current under the terms of a modified loan at the end of a 3 month period, or
 5. The modification is in accordance with a federal program.

In addition to the foregoing, Section 2850.6 sets forth additional proposed requirements for a loan modification program. Subsection (a) sets forth conditions when a loan modification consists solely of a repayment plan. In particular, a servicer must be able to validate that the borrower has a housing-related debt to gross income ratio of 38% or less, and that the borrower can repay the loan. The subsection further defines a repayment plan as a plan or arrangement where amounts past due are added to the principal amount due on a loan and re-aged so that a loan is no longer delinquent, and no other loan concessions are provided to the borrower.

Subsection (b) requires all eligible loans to be considered for modification under the plan unless an applicable pooling and servicing agreement prohibits the modification. Subsection (c) requires a servicer to use reasonable efforts to remove any prohibitions and obtain waivers or approvals from all necessary parties, including junior lien holders and investors. Subsection (d) requires a servicer to act on a loan modification request within a reasonable time period, and requires a servicer to have procedures in place to ensure that delays in the process not caused by a borrower do not adversely impact a borrower in the loan modification or foreclosure process. Subsection (d) further requires a servicer to acknowledge the receipt of a loan modification request.

Subsection (e) permits a servicer to deny a loan modification request when a borrower abandons or unduly delays the process. Prior to denying the modification request, the servicer must notify the borrower in writing of the time period to respond and the consequence of failing to respond in a reasonable time. Subsection (f) provides that a comprehensive loan modification program may include foreclosure alternatives for borrowers who do not qualify for a loan modification program. Subsection (g) provides that a servicer is not required to modify a loan more than once.

Within Subarticle 2, the Commissioner proposes to adopt 2 sections. Section 2850.7, entitled "Initial Application," sets forth instructions on the filing of the application. This section provides that an applicant shall be temporarily exempt from Civil Code Section 2923.52(a) upon the filing of a substantially complete application. Item 1 instructs applicants on where to file the application, and identifies how an applicant determines whether to file an application with the Department of Corporations, the Department of Financial Institutions, or the Department of Real Estate. Item 2 instructs applicants on when to file an application, and provides that an applicant will be temporarily exempt from Civil Code Section 2923.52(a) upon the appropriate department's receipt of the application.

Item 3 sets forth the manner for the Department to notify an applicant of the temporary order. Item 4 provides that the Department will notify the applicant of whether the applicant has a comprehensive loan modification program within 30 days of the receipt of an application, and notify the applicant of the issuance of a final order. Item 5 provides that upon the denial of an application, the Department will immediately

notify the servicer, and the temporary order will remain in effect for 30 days following the denial. Item 6 provides that the Department will accept changes to an application while the application is under consideration.

Section 2850.8, entitled “Changes to Program after Final Order,” sets forth procedures for the modification of a program after the receipt of a final order. Subdivision (a) prohibits a servicer from modifying a program after a final order is issued unless the servicer informs the Commissioner of the change. Subsection (b) provides that a change to a federal program does not constitute a change to a comprehensive loan modification program and does not require notice to the Commissioner.

Subarticle 3 consists of Section 2850.9, which incorporates the application form. The application requests identifying information from an applicant, requests information on whether an applicant is participating in a loan modification program administered by a federal agency, and requires an applicant to submit several exhibits. Exhibit 1 requires an applicant to describe its loan modification program, and to direct the Department to where within the submitted documentation specified program requirements are met. Exhibit 2 requires an applicant to submit copy of the declaration to be included with the notice of sale, as required by Civil Code section 2923.54. Exhibit 3 requires an applicant to provide the notice to consumers required by Section 2850.3 of these rules. Exhibit 4 requires an applicant to submit 3 months of recent loss mitigation data.

Exhibit 5 requires an applicant to provide additional documentation for other items in the application, if applicable, including the differences between the net present value used by the applicant and the Department of the Treasury’s Net Present Value Model Parameters, the reasons the servicer’s program is unable to achieve an aggregate debt-to-income ratio of 38% or less, and a description of any additional features in the program to be considered by the Commissioner. The application provides that exhibits 1, 4 and 5 are confidential, and requires the application to be signed under penalty of perjury by a specified control person.

Subarticle 4 consists of Section 2850.10, entitled “Reports.” This section provides that upon request of the Commissioner, a servicer shall report loan modification data to the Commissioner on a quarterly basis. The section further incorporates by reference a form for quarterly reporting, entitled Foreclosure Prevention Loan Modification Data, and dated November 25, 2009. The section provides that a servicer may request a hardship exemption from the Commissioner, and provides that the Commissioner may accept a report required by a federal loan modification program, in lieu of the report required in this section.

AUTHORITY

Sections 2923.52 and 2923.53, Civil Code.

REFERENCE

Sections 2923.52 and 2923.53, Civil Code.

AVAILABILITY OF MODIFIED TEXT

The text of any modified regulation, unless the modification is only non-

substantial or solely grammatical in nature, will be made available to the public at least 15 days prior to the date the Department adopts the regulation(s). A request for a copy of any modified regulation(s) should be addressed to the contact person designated below. The Commissioner will accept written comments on the modified regulation(s) for 15 days after the date on which they are made available. The Commissioner may thereafter adopt, amend or repeal the foregoing proposal substantially as set forth above without further notice.

AVAILABILITY OF STATEMENT OF REASONS, TEXT OF PROPOSED REGULATIONS/INTERNET ACCESS

The express terms of the proposed action may be obtained upon request from the Sacramento offices of the Department. An initial statement of reasons for the proposed action containing all the information upon which the proposal is based is available from the contact person designated below. These documents are also available at the Department's website at www.dre.ca.gov. As required by the Administrative Procedure Act, the Department's Sacramento Legal Office maintains the rulemaking file. The rulemaking file is available for public inspection at the Department of Real Estate, 2201 Broadway, Sacramento, California.

AVAILABILITY OF THE FINAL STATEMENT OF REASONS

Upon its completion, the Final Statement of Reasons will be available and copies may be requested from the contact person named in this notice or may be accessed on the website listed above.

CONSIDERATION OF ALTERNATIVES

In accordance with Government Code section 11346.5, subdivision (a)(13), the Department must determine that no reasonable alternative it considered or that has otherwise been identified and brought to the attention of the Department 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.

FISCAL IMPACT

- Cost or savings to any state agency: The Department has determined that the implementation of the California Foreclosure Prevention Act will have an estimated cost of \$120,000 to the Department. This cost represents the cost of implementing and administering the statutory California Foreclosure Prevention Act, including the adoption of regulations, development of procedures and information technology applications, acceptance of applications, review and approval of applications, data collection and reporting. While this cost is attributable to the implementation of the act, it is not necessarily attributable to this rulemaking action.
- Direct or indirect costs or savings in federal funding to the state: none.
- Cost to local agencies and school districts required to be reimbursed under Part 7 (commencing with Section 17500) of Division 4 of the Government Code: none.
- Other nondiscretionary costs/savings imposed on local agencies: none.
- Costs to private persons or businesses directly affected: The Department has determined that the cost to directly affected businesses that seek to submit an application for an order of exemption under the California Foreclosure Prevention

Act may be up to \$5000 in one time costs for the application, and may be up to \$5000 a year if reporting is required.

BUSINESS REPORTING REQUIREMENT

The Commissioner finds that it is necessary for the health, safety, or welfare of the people of this state that this regulation that requires a report apply to businesses.

DETERMINATIONS

The Commissioner has made an initial determination that the proposed regulatory action:

- Does not impose a mandate on local agencies or school districts, or a mandate that is required to be reimbursed pursuant to Part 7 (commencing with Section 17500) of Division 4 of the Government Code.
- Does not have an effect on housing costs.
- Does not have a significant statewide adverse economic impact directly affecting businesses, including the ability of California businesses to compete with businesses in other states.
- Does not significantly affect the creation or elimination of jobs within the State of California; the creation of new businesses or the elimination of existing businesses within the State of California; or the expansion of businesses currently doing business within the State of California.

COST IMPACTS ON REPRESENTATIVE PRIVATE PERSON OR BUSINESS

The Department has determined that the cost to directly affected businesses that seek to submit an application for an order of exemption under the California Foreclosure Prevention Act may be up to \$5000 in one time costs for the application, and may be up to \$5000 a year if reporting is required.

EFFECT ON SMALL BUSINESS

The proposed regulatory changes may affect small business.

CONTACT PERSON

Inquiries concerning this action may be directed to Daniel Kehew at (916) 227-0425, or via email at DRERegulations@dre.ca.gov. The backup contact person is Mary Clarke at (916) 227-0780.

Dated:

Sacramento, California

Daniel E. Kehew
Real Estate Counsel
Sacramento Legal Office