

ADVERTISING NEGATIVE AMORTIZATION LOANS

The Department of Real Estate routinely receives complaints from both the public and the mortgage loan industry regarding a variety of mortgage loan advertising solicitations. Some of the solicitations the Department reviews lack the information that is required to fully inform the recipient of the loan terms which will allow the consumer to make an informed decision whether or not to contact the broker and initiate the loan application process.

Advertisements for adjustable rate loans that contain provisions for potential negative amortization (deferred interest) fall into this category. The solicitations usually tout how consumers may drastically reduce or cut their monthly mortgage payments, "save" substantial amounts of money and how the loan may be used as a financial planning tool. There may even be a description of how money that is "saved" each month can be used for other purposes, such as vacations, college expenses, and so forth. While this type of loan may benefit some borrowers, loans that may result in the loss of equity are clearly not for everyone. Unfortunately, these advertisements generally do not tell the whole story. For instance, there is often either incomplete or no disclosure stating that the initial interest

rate, the one on which the "low monthly payments" are based, will be in effect for only a short period of time such as 1, 3 or 6 months or how often the interest rate can change thereafter. Also, the ads emphasize the initial interest rate and "low monthly payments" but usually lack any disclosure that the rising interest rate, coupled with an annual payment cap, will result in negative amortization, and loss of equity, if the borrower cannot, or does not, make payments sufficient to cover the accrued interest.

For that reason, it is crucial that brokers and lenders who offer this type of loan fully comply with the provisions of Commissioner's Regulation 2848 which states, in part, "By way of illustration and not of limitation, advertising containing any of the following is considered to be false,

misleading or deceptive and will not ordinarily be approved for publication by the Commissioner:



(5) A representation of a specific installment in repayment of a loan without an equally prominent disclosure of the following information about the loan:

- (A) Principal amount,
- (B) Simple annual interest rate,
- (C) Annual percentage rate,
- (D) Number, amount, and period of payments scheduled to the date of maturity,
- (E) Balance due at maturity (balloon payment) if not fully amortized."

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CHANGES IN MORTGAGE LENDING LAWS



Several new and amended California statutes will be of interest to our licensees in the mortgage loan industry. Following are brief descriptions of relevant legislative changes which took effect January 1, 2003 unless otherwise noted:

AB1486 (Dutra) Mortgage Guarantee Insurance – Increases the allowable total indebtedness on which private mortgage insurance (PMI) may be written from 100% to 103% of fair market value as an attempt to

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



ADVERTISING

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When reviewing advertisements for adjustable rate loans, the Department will look for *equally conspicuous* disclosures that contain the above information, including how long the initial rate will be in effect, how often rates may adjust and by how much. For loans that contain the potential for negative amortization (deferred interest), there must also be an equally conspicuous disclosure of that fact.

Even advertisements that do not contain specific monthly payments, but only the initial interest rate and APR, may be considered false and misleading. If the advertised loan is an adjustable rate mortgage where the initial rate will increase, any claim of payment savings will be considered misleading, and in violation of Business and Professions Code Section 10235 unless further information

is included stating how long the initial interest rate will be in effect and the fact that the initial payment may increase.

Brokers should carefully review Business and Professions Code Section 10235 and Commissioner's Regulation 2848 and also review their advertising completely to ensure that the clear and conspicuous disclosure of all pertinent loan terms is included. That way, consumers can make informed decisions on whether or not to pursue a transaction that can affect their financial futures for many years.

The Business and Professions Code and Commissioner's Regulations are available at www.dre.ca.gov (click on **2003 Real Estate Law**). Questions regarding this article may be directed to the Mortgage Loan Activities Unit at (916) 227-0770. 📞

CHANGES IN LAWS

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increase the rate of homeownership in California. AB 1486 amended various sections of the Insurance Code.

AB2167 (Koretz) Real Estate Licenses – Effective July 1, 2003, requires persons to take, in addition to a college level class in Real Estate Principles, a college level class in Real Estate Practices, and one optional course, either prior to being issued a real estate salesperson license or, for conditional licenses, within 18 months of becoming licensed. (Currently, a person needs to take Real Estate Principles plus two optional courses). The bill also requires final examinations for all types of the four mandatory continuing education courses that a licensee needs in order to renew his or her real estate license for the first time.

SB1370 (Bowen) Servicing of Indebtedness – Requires any person transferring the servicing of a loan to a different servicing agent to provide the new servicing agent all existing insurance policy information that the person is responsible for maintaining. SB 1370 amended Section 2937 of the Civil Code.

For complete information, you should consult each statute. The bills are available at www.leginfo.ca.gov (choose the 2001/2002 legislative session). The Mortgage Loan Activities Unit may be reached at (916) 227-0770 for questions regarding statutes and regulations related to mortgage lending. 📞



TO REPORT OR NOT REPORT . . . HMDA to HUD or RML Report to the DRE?

The Health and Safety Code requires real estate brokers who are **direct** lenders in certain types of loan transactions to report to the Department of Real Estate (DRE) all activities related to applications made by, and loans made to, the public for home purchase and/or home improvement purposes. If a real estate broker reports such lending activity to the 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 DRE.**

RML Reports for 2002 are due to the DRE by March 31

The State of California Residential Mortgage Loan (RML) Report (RE 857) must be submitted to the DRE by all real estate brokers required to report in accordance with the provisions of the Health and Safety Code Sections 35815 and 35816, i.e. those 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. For brokers who meet the threshold standards, mortgage lending data is to be collected annually and reported on the RE 857 by March 31 of the following year. Thus, the report for calendar year 2002 must be submitted to the DRE by March 31, 2003.

In the past, the Department has received RML Reports from lenders who, on the basis of the data submitted, appear to qualify for filing under HMDA and, therefore, would be exempt from filing with DRE. The following information from the Federal Financial Institution Examination Counsel’s Web site www.ffiec.gov is intended to reduce any confusion for DRE licensees so that they may file only the report required of them.

Are you required to report to HUD under HMDA?

A lender must report under HMDA if:

- 1. it is a for profit, nondepository lending institution (other than a bank, savings association or credit union); AND*
- 2. 10% or more of its total loan originations, measured in dollars, in the preceding calendar year were for home purchase loans (including refinancings of home purchase loans); AND*
- 3. it has a home or branch office in a Metropolitan Statistical Area (MSA) OR it received, originated or purchased 5 or more home purchase or home improvement loans in the preceding calendar year; AND*
- 4. it had assets exceeding \$10 million (when combined with the assets of any parent corporation) on the preceding December 31 OR it originated 100 or more home purchase loans (including refinancings of home purchase loans) in the preceding calendar year.*

If a lender meets the requirements for HMDA reporting, it **should not** submit the RML Report to the DRE. If it **does not** meet the HMDA reporting requirements, it must determine if it qualifies for filing the RML Report with the DRE using the criteria set forth below.

. . . or should you submit an RML Report to the DRE?

A lender must report to the DRE if the lender does not meet the requirements for HMDA reporting **and** the lender regularly makes loans on 1-4 unit residential real property. “Regularly” is defined to mean twelve or more transactions annually during the immediately preceding calendar year that, in aggregate, total more than \$500,000 in value. Only licensed lenders making 10% or more in qualifying loans must report. It is important to note that **only lenders** are required to file these reports. **Brokers who are merely arranging or packaging loans need not file.** Lenders reporting to the DRE should continue to use the 1990 census data.

The RML Report (RE 857) is available on the DRE Web site www.dre.ca.gov under **Forms, Mortgage Lending Brokers.**

Questions regarding the RML Report may be directed to the Mortgage Loan Activities Unit at (916) 227-0770. 📞

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Regulation 2846.1 – Material Changes



Brokers who conduct private-money multi-lender loan transactions (fractionalized notes) are required by Business and Professions Code Section 10229(a) to file a specified notice, the Multi-Lender Transaction Notice (RE 860), with the Department of Real Estate within 30 days after the broker's first multi-lender transaction and within 30 days of any material change to the information required in the notice.

Commissioner's Regulation 2846.1 clarifies what constitutes a material change requiring an amended notice to the Department. Regulation 2846.1 reads as follows:

“A material change requiring notice under Section 10229(a) of the Code shall include but shall not be limited to the following:

- (a) A change of the month in which the broker's fiscal year ends.
- (b) A change with respect to whether the broker is (or expects to be) required to file reports of inspection of its trust account(s) with the Real Estate Commissioner pursuant to paragraph (3) of subdivision (j) of Section 10229 of the Code.
- (c) A change with respect to the identity of the Servicing Agent.”

Questions concerning the filing of the Multi-Lender Transaction Notice may be directed to the Mortgage Loan Activities Unit at (916) 227-0770. 📞