Some Frequently Asked Questions, and Answers from the California Department of Real Estate, Regarding California Senate Bill 94 (Which Prohibits Upfront or Advance Fees for Residential Loan Modifications and Mortgage Loan Forbearance Services)

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The California Department of Real Estate (DRE) continues to receive many questions regarding the effect, scope and applicability of Senate Bill 94, which took effect upon its signature on October 11, 2009.

The four (4) questions below are asked repeatedly, and this writing is intended to address only those four questions.

For additional information about the Senate Bill, please visit www.leginfo.ca.gov, and click on bill information. Then see Senate Bill 94 (Calderon). Also, the DRE has other information about the bill (such as sunset date, required notices, penalties, limitations relative to property type, and mandates for language translations) that can be accessed from the department via its website at www.dre.ca.gov. Further, The State Bar of California has a set of Frequently Asked Questions about Senate Bill 94. Those FAQs and answers can be found at the State Bar's website at www.calbar.ca.gov.

Question 1.

If a real estate licensee previously had a "no objection" letter from the DRE with respect to an advance fee agreement, and the licensee had the advance fee agreement signed by a borrower and the agreement was in place before October 11, 2009, can "advance fee" payments continue to be paid under the terms of the agreement ***after*** October 11, 2009?

Answer: No. Under new section 10085.6 of the California Business and Professions Code and new section 2944.7 of the California Civil Code, a licensee who performs residential loan modification services or other forms of mortgage loan forbearance cannot collect, claim, charge, demand or receive any compensation from the borrower until after the licensee has performed each and every service he or she contracted to perform or represented that he or she would perform.

Because the law is not retroactive, advance fees paid pursuant to a proper and lawful advance fee agreement before October 11, 2009 are not affected by Senate Bill 94. But after that date, as stated above, no further advance fees can be collected -- even if the agreement states otherwise.

Question 2.

Can a licensee take monies upfront from a borrower if the funds are placed in an "escrow account", "fiduciary" trust account, joint account, "special retainer" account, or some other sort of special, neutral, independent, or restricted account where the licensee does not have unrestricted access to those funds?

Answer: No. There are two reasons for this answer. First, under new section 10085.6 of the California Business and Professions Code and new section 2944.7 of the California Civil Code, the language clearly and plainly prohibits a licensee from claiming, demanding, collecting, charging or receiving any pre-performance compensation.

So taking or "receiving" the money upfront itself violates the law. Ingenuity or creativity in the labeling of an account as an "escrow", "fiduciary" trust, "special retainer" or some other type of special account does not cure the violation of receiving the funds.

Second, both of the new code sections provide that licensees cannot take any "other security to secure the payment of compensation". Many of the inquiries the DRE receives suggest that the "special" accounts are being contemplated or designed to provide the licensees with a security device to secure the payment of compensation. That is clearly forbidden by Senate Bill 94.

Question 3.

Does Senate Bill 94 provide a "loophole" for a licensee to break down the services of a loan modification so that a licensee can charge after respective services are performed (but before the loan modification services are fully "performed")?

Answer: No. The DRE is aware of licensees who are attempting to evade the plain intent of the new law by breaking the loan modification process and services into various steps. For instance, step 1 might be meeting with a borrower and completing the necessary paperwork (including a hardship letter). The fee for that step service is quoted as $2500. Step 2 might be to submit the package to the servicer/lender. The fee for that service is listed as $500. Step 3 might be the actual loan modification discussions and negotiations with the servicer/lender. The fee for this step is shown as $100.

The problem with this attempt at creative contractual expression is that it violates the new section 10026 of the California Business and Professions Code embodied in Senate Bill 94 with respect to "advance fees". The new language provides that "Neither an advance fee nor the services to be performed shall be separated or divided into components for the purpose of avoiding the application of this section".
It is the position of the DRE that the clever but unlawful scheme set forth above is an endeavor to avoid and skirt the clear intention and public policy expression of the California Legislature and the Governor in passing and signing Senate Bill 94, to violate the "advance fee" mandates of the California Business and Professions Code, and to obtain for a licensee immediate "upfront" and sizeable payments for services that are of littleor no value to the borrower.

Based on the experiences of those in the department who have communicated regularly with the public regarding loan modifications, the only thing a desperate, vulnerable borrower wants is an affordable, sustainable loan modification or other type of forbearance. He or she does not care about pre-loan modification paperwork processing services.

The artificial breaking down of residential loan modification services into components or steps (with only vague, ambiguous, or no real value) by a licensee clearly violates the mandate of Senate Bill 94 that no person can receive any pre-performance compensation from a borrower for residential loan modifications or other forms of mortgage loan forbearance.

Question 4.

Does Senate Bill 94 allow licensees, lawyers or others to claim, demand, charge, collect or receive compensation for loan modification or forbearance work from borrowers who are not California residents, or who live and/or work outside of California?

Answer: No. The language of the new code sections added by the State Senate legislation is broad and the prohibitions are not in any way limited by residency or place of employment. Thus, for example, a California real licensee cannot claim, demand, charge, collect or receive any pre-performance compensation for loan modification or forbearance work from a borrower who lives in Nevada.

Also, and importantly, the plain language of the legislation would forbid any person (whether a real estate licensee, lawyer or company) who or which operates from outside of California from seeking or obtaining any advance or upfront fees from a California borrower for residential loan modifications and mortgage loan forbearance services .

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