

ASSEMBLY BILL

No. 1830

Introduced by Assembly Member Lieu

(Principal coauthors: Assembly Members Nunez and Ruskin)

(Coauthors: Assembly Members Arambula, Bass, Beall, Berg, Brownley, Caballero, Carter, Coto, Davis, De Leon, DeSaulnier, Dymally, Eng, Feuer, Hancock, Hayashi, Huffman, Jones, Karnette, Krekorian, Laird, Leno, Levine, Ma, Mendoza, Mullin, Nava, Price, Salas, Saldana, Solorio, Swanson, Torrico, and Wolk)

January 23, 2008

An act to amend Sections 4970, 4973, 4974, 4975, 4977, 4978, 4978.6, and 4979 of, to amend the heading of Division 1.6 (commencing with Section 4970) of, and to add Sections 4973.2 and 4980 to, the Financial Code, relating to loans.

LEGISLATIVE COUNSEL'S DIGEST

AB 1830, as introduced, Lieu. High-cost, subprime, and nontraditional loans.

Existing law imposes certain limitations and prohibitions on licensed persons, including real estate brokers, finance lenders, residential mortgage lenders, and financial institutions, with respect to consumer loans and covered loans. Existing law defines a “consumer loan” as a consumer credit transaction secured by residential real property, subject to certain exceptions, and defines a “covered loan” as a consumer loan that meets certain other requirements. Existing law prohibits a covered loan from including a prepayment penalty after the first 36 months from the date of consumation of the loan but authorizes a covered loan to include a prepayment penalty before that time period if specified conditions are satisfied. Existing law prohibits a covered loan from

being made unless a specified disclosure is provided to the consumer no later than 3 business days prior to signing of the loan documents. Violations of these limitations and prohibitions by licensed persons are deemed to be violations of the person's licensing law and may be punishable by, among other things, disciplinary action, civil liability, and the imposition of administrative penalties and civil penalties up to \$25,000, as specified.

This bill would redefine a "covered loan" as a "high-cost loan," would establish "subprime loans" and "nontraditional loans," as defined, as new categories of regulated loans, and would make various conforming changes to existing law relative to these loans. The bill would prohibit a high-cost loan from including prepayment penalties and from including at origination a payment schedule with regular periodic payments that, when aggregated, do not fully amortize the principal balance as of the maturity date of the loan. The bill would prohibit a person from making a high-cost loan unless at the time the loan is consummated the person believes the consumer will be able to make the scheduled payments, including taxes and insurance and would prohibit a high-cost loan from being originated as a stated income loan, except as specified. The bill would prohibit a person who originates a high-cost loan from receiving a yield spread premium or other incentive compensation and would prohibit a person from originating a high-cost loan unless an escrow or impound account is established for a specified period of time. The bill would delete the provisions requiring a disclosure to be provided to a consumer prior to making a covered loan and would instead prohibit a high-cost loan from being made unless a consumer receives a certificate of certain counseling. The bill would establish similar limitations and prohibitions for subprime and nontraditional loans but would require a specified disclosure to be provided to a consumer before those loans could be made. The bill would authorize a licensing agency to levy administrative penalties in an amount up to \$10,000 against a person who violates the provisions regulating high-cost, subprime, and nontraditional loans and would make a person who makes a willful and knowing violation of those provisions of law liable to the consumer in the amount of \$25,000 or the consumers actual damages, whichever is greater. The bill would authorize private causes of action by a consumer against a licensed person to recover damages for a violation of the provisions regulating high-cost, subprime, or nontraditional loans. The bill would provide that it is a defense against foreclosure on a property secured by a high-cost, subprime, or nontraditional loan if the loan is

in violation of the laws regulating those loans. The bill’s provisions would apply to high-cost, subprime, and nontraditional loans originated on or after January 1, 2009.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. The heading of Division 1.6 (commencing with
2 Section 4970) of the Financial Code is amended to read:

3
4 DIVISION 1.6. *SUBPRIME LENDING REFORM ACT*
5

6 SEC. 2. Section 4970 of the Financial Code is amended to read:
7 4970. For purposes of this division:

8 (a) “Annual percentage rate” means the annual percentage rate
9 for the loan calculated according to the provisions of the federal
10 Truth in Lending Act and the regulations adopted thereunder by
11 the Federal Reserve Board.

12 (b) ~~“Covered loan”~~ “High-cost loan” means a consumer loan
13 in which the original principal balance of the loan does not exceed
14 the most current conforming loan limit for a single-family first
15 mortgage loan established by the Federal National Mortgage
16 Association in the case of a mortgage or deed of trust, and where
17 one of the following conditions are met:

18 (1) For a mortgage or deed of trust, the annual percentage rate
19 at consummation of the transaction will exceed by more than eight
20 percentage points *for first lien loans, or by more than 10*
21 *percentage points for subordinate lien loans*, the yield on Treasury
22 securities having comparable periods of maturity on the 15th day
23 of the month immediately preceding the month in which the
24 application for the extension of credit is received by the creditor.

25 (2) The total points and fees payable by the consumer at or
26 before closing for a mortgage or deed of trust will exceed ~~6~~ 5
27 percent of the total loan amount.

28 (c) “Subprime loan” or “subprime mortgage” means a loan
29 secured by a dwelling that is, or will be, the borrower’s principal
30 dwelling and in which the annual percentage rate exceeds the
31 greater of either of the following:

1 (1) If the loan is a closed-end loan, the difference between the
 2 annual percentage rate for the loan and the yield on Treasury
 3 securities having comparable periods of maturity is either equal
 4 to or greater than (A) 3 percentage points if the loan is secured
 5 by a first lien mortgage or deed of trust, or (B) 5 percentage points
 6 if the loan is secured by a subordinate lien mortgage or deed of
 7 trust. If the loan is an open-end credit plan, the difference between
 8 the annual percentage rate for the loan and the yield on Treasury
 9 securities having comparable periods of maturity is equal to or
 10 greater than 3 percentage points, regardless of whether the
 11 open-end credit plan is secured by a first or subordinate lien
 12 mortgage or deed of trust. Without regard to whether the loan is
 13 subject to or reportable under the provisions of the federal Home
 14 Mortgage Disclosure Act (12 U.S.C. Sec. 2801, et seq.) (HMDA),
 15 the difference between the annual percentage rate and the yield
 16 on Treasury securities having comparable periods of maturity
 17 shall be determined using the same procedures and calculation
 18 methods applicable to loans that are subject to the reporting
 19 requirements of the HMDA.

20 (2) The difference between the annual percentage rate for the
 21 loan and the annual yield on conventional mortgages published
 22 by the Board of Governors of the Federal Reserve System, as
 23 published in statistical release H.15 or any publication that may
 24 supersede it, is either equal to or greater than (A) 1.75 percentage
 25 points, if the loan is secured by a first lien mortgage or deed of
 26 trust, or (B) 3.75 percentage points, if the loan is secured by a
 27 subordinate lien mortgage or deed of trust.

28 (d) “Nontraditional loan” or “nontraditional mortgage” means
 29 mortgage products that allow borrowers to defer payment of
 30 principal and, sometimes, interest, as set forth in the “Interagency
 31 Guidance on Nontraditional Mortgage Product Risks” (71 Fed.
 32 Reg. 58609 (Oct. 4, 2006)).

33 ~~(e)~~

34 (e) (1) “Points and fees” shall include the following:

35 ~~(A)~~

36 (A) All items required to be disclosed as finance charges under
 37 Sections 226.4(a) and 226.4(b) of Title 12 of the Code of Federal
 38 Regulations, including the Official Staff Commentary, as amended
 39 from time to time, except interest.

40 ~~(2)~~

1 ~~(B) All compensation and fees paid to mortgage brokers in~~
2 ~~connection with the loan transaction paid directly or indirectly to~~
3 ~~a mortgage broker from any source, including, but not limited to,~~
4 ~~any payment of a yield spread premium, and including a payment~~
5 ~~to a mortgage broker that originates a loan in its own name in a~~
6 ~~table-funded transaction.~~

7 ~~(3)~~

8 (C) All items listed in Section 226.4(c)(7) of Title 12 of the
9 Code of Federal Regulations, only if the person originating the
10 covered loan receives direct compensation in connection with the
11 charge.

12 (2) *“Points and fees” shall not include any of the following:*

13 (A) *Taxes, filing fees, recording fees, and other charges and*
14 *fees paid or to be paid to public officials for determining the*
15 *existence of or for perfecting, releasing, or satisfying a security*
16 *interest.*

17 (B) *Bona fide and reasonable fees paid to a person other than*
18 *the creditor or an affiliate of the creditor for fees for tax payment*
19 *services, flood certification, or pest infestation and flood*
20 *determination, appraisal fees, fees for inspections performed prior*
21 *to closing, credit report fees, survey fees, attorneys’ fees if the*
22 *borrower has the right to select the attorney from an approved list*
23 *or otherwise, notary fees, escrow charges, title insurance*
24 *premiums, and fire and hazard insurance and flood insurance*
25 *premiums, provided that the conditions in Section 226.4(d)(2) of*
26 *Title 12 of the Code of Federal Regulations are met.*

27 ~~(4)~~

28 (f) *“Consumer loan” means a consumer credit transaction that*
29 *is secured by real property located in this state used, or intended*
30 *to be used or occupied, as the principal dwelling of the consumer*
31 *that is improved by a one-to-four residential unit. “Consumer loan”*
32 *does not include a reverse mortgage, an open line of credit as*
33 *defined in Part 226 of Title 12 of the Code of Federal Regulations*
34 *(Regulation Z), or a consumer credit transaction that is secured by*
35 *rental property or second homes. “Consumer loan” does not include*
36 *a bridge loan. For purposes of this division, a bridge loan is any*
37 *temporary loan, having a maturity of one year or less, for the*
38 *purpose of acquisition or construction of a dwelling intended to*
39 *become the consumer’s principal dwelling.*

40 (e)

1 (g) “Original principal balance” means the total initial amount
2 the consumer is obligated to repay on the loan.

3 ~~(f)~~

4 (h) “Licensing agency” shall mean the Department of Real
5 Estate for licensed real estate brokers, the Department of
6 Corporations for licensed residential mortgage lenders and licensed
7 finance lenders and brokers, and the Department of Financial
8 Institutions for commercial and industrial banks and savings
9 associations and credit unions organized in this state.

10 ~~(g)~~

11 (i) “Licensed person” means a real estate broker licensed under
12 the Real Estate Law (Part 1 (commencing with Section 10000) of
13 Division 4 of the Business and Professions Code), a finance lender
14 or broker licensed under the California Finance Lenders Law
15 (Division 9 (commencing with Section 22000)), a residential
16 mortgage lender licensed under the California Residential Mortgage
17 Lending Act (Division 20 (commencing with Section 50000)), a
18 commercial or industrial bank organized under the Banking Law
19 (Division 1 (commencing with Section 99)), a savings association
20 organized under the Savings Association Law (Division 2
21 (commencing with Section 5000)), and a credit union organized
22 under the California Credit Union Law (Division 5 (commencing
23 with Section 14000)). Nothing in this division shall be construed
24 to prevent any enforcement by a governmental entity against any
25 person who originates a loan and who is exempt or excluded from
26 licensure by all of the licensing agencies, based on a violation of
27 any provision of this division. Nothing in this division shall be
28 construed to prevent the Department of Real Estate from enforcing
29 this division against a licensed salesperson employed by a licensed
30 real estate broker as if that salesperson were a licensed person
31 under this division. A licensed person includes any person engaged
32 in the practice of consumer lending, as defined in this division, for
33 which a license is required under any other provision of law, but
34 whose license is invalid, suspended or revoked, or where no license
35 has been obtained.

36 ~~(h)~~

37 (j) “Originate” means to arrange, negotiate, or make a consumer
38 loan.

39 ~~(i)~~

1 (k) “Servicer” has the same meaning provided in Section 6 (i)(2)
2 of the Real Estate Settlement Procedures Act of 1974.

3 (l) “Fully indexed rate” means the index rate prevailing on a
4 residential mortgage loan at the time the loan is made plus the
5 margin that will apply after the expiration of any introductory
6 interest rates.

7 SEC. 3. Section 4973 of the Financial Code is amended to read:
8 4973. The following are prohibited acts and limitations for
9 covered *high-cost* loans:

10 (a) ~~(1) A covered *high-cost* loan shall not include a prepayment~~
11 ~~fee or penalty after the first 36 months after the date of~~
12 ~~consummation of the loan.~~

13 ~~(2) A covered loan may include a prepayment fee or penalty up~~
14 ~~to the first 36 months after the date of consummation of the loan~~
15 ~~if:~~

16 ~~(A) The person who originates the covered loan has also offered~~
17 ~~the consumer a choice of another product without a prepayment~~
18 ~~fee or penalty.~~

19 ~~(B) The person who originates the covered loan has disclosed~~
20 ~~in writing to the consumer at least three business days prior to loan~~
21 ~~consummation the terms of the prepayment fee or penalty to the~~
22 ~~consumer for accepting a covered loan with the prepayment penalty~~
23 ~~and the rates, points, and fees that would be available to the~~
24 ~~consumer for accepting a covered loan without a prepayment~~
25 ~~penalty.~~

26 ~~(C) The person who originates the covered loan has limited the~~
27 ~~amount of the prepayment fee or penalty to an amount not to~~
28 ~~exceed the payment of six months’ advance interest, at the contract~~
29 ~~rate of interest then in effect, on the amount prepaid in any~~
30 ~~12-month period in excess of 20 percent of the original principal~~
31 ~~amount.~~

32 ~~(D) A covered loan will not impose the prepayment fee or~~
33 ~~penalty if the covered loan is accelerated as a result of default.~~

34 ~~(E) The person who originates the covered loan will not finance~~
35 ~~a prepayment penalty through a new loan that is originated by the~~
36 ~~same person.~~

37 (b) (1) A covered loan with a term of 5 years or less *high-cost*
38 *loan* may not provide at origination for a payment schedule with
39 regular periodic payments that when aggregated do not fully
40 amortize the principal balance as of the maturity date of the loan.

1 (2) For a payment schedule that is adjusted to account for the
 2 seasonal or irregular income of the consumer, the total installments
 3 in any year shall not exceed the amount of one year’s worth of
 4 payments on the loan. This prohibition does not apply to a bridge
 5 loan. For purposes of this paragraph, “bridge loan” means a loan
 6 with a maturity of less than 18 months that only requires payments
 7 of interest until the time when the entire unpaid balance is due and
 8 payable.

9 (c) ~~A covered high-cost~~ loan shall not contain a provision for
 10 negative amortization such that the payment schedule for regular
 11 monthly payments causes the principal balance to increase, ~~unless~~
 12 ~~the covered loan is a first mortgage and the person who originates~~
 13 ~~the loan discloses to the consumer that the loan contains a negative~~
 14 ~~amortization provision that may add principal to the balance of~~
 15 ~~the loan.~~

16 (d) ~~A covered high-cost~~ loan shall not include terms under which
 17 periodic payments required under the loan are consolidated and
 18 paid in advance from the loan proceeds.

19 (e) ~~A covered high-cost~~ loan shall not contain a provision that
 20 increases the interest rate as a result of a default. This provision
 21 does not apply to interest rate changes in a variable rate loan
 22 otherwise consistent with the provisions of the loan documents,
 23 provided the change in the interest rate is not triggered by the event
 24 of default or the acceleration for the indebtedness.

25 (f) (1) A person who originates ~~covered high-cost~~ loans shall
 26 not make or arrange a ~~covered high-cost~~ loan unless at the time
 27 the loan is consummated, the person reasonably believes the
 28 consumer, or consumers, when considered collectively in the case
 29 of multiple consumers, will be able to make the scheduled
 30 payments, *including taxes and insurance at the fully indexed rate*,
 31 to repay the obligation based upon a consideration of their current
 32 and expected income, current obligations, employment status, and
 33 other financial resources, other than the consumer’s equity in the
 34 dwelling that secures repayment of the loan. In the case of a
 35 ~~covered high-cost~~ loan that is structured to increase to a specific
 36 designated rate, stated as a number or formula, at a specific
 37 predetermined date not exceeding 37 months from the date of
 38 application, this evaluation shall be based upon the fully indexed
 39 rate of the loan calculated at the time of application.

1 The consumer shall be presumed to be able to make the
 2 scheduled payments to repay the obligation if, at the time the loan
 3 is consummated, the consumer’s total monthly debts, including
 4 amounts owed under the loan, do not exceed ~~55~~ 45 percent of the
 5 consumer’s monthly gross income, as verified by the credit
 6 application, the consumer’s financial statement, a credit report,
 7 financial information provided to the person originating the loan
 8 by or on behalf of the consumer, or any other reasonable means.

9 ~~(2) No presumption of inability to make the scheduled payments
 10 to repay the obligation shall arise solely from the fact that at the
 11 time the loan is consummated, the consumer’s total monthly debts,
 12 including amounts owed under the loan, exceed 55 percent of the
 13 consumer’s monthly gross income.~~

14 (3)

15 (2) In the case of a stated income loan, the reasonable belief
 16 requirement in paragraph (1) shall apply, however, for stated
 17 income loans that belief may be based on the income ~~stated by the
 18 consumer, and other information in the possession of the person
 19 originating the loan after the solicitation of all information that the
 20 person customarily solicits in connection with loans of this type
 21 verified by using tax records, bank statements, payroll receipts,
 22 or other reasonable documentation from a third party.~~ A person
 23 shall not knowingly or willfully originate a ~~covered~~ *high-cost* loan
 24 as a stated income loan with the intent, or effect, of evading the
 25 provisions of this subdivision. *A high-cost loan shall not be
 26 originated as a stated income loan based solely on a consumer’s
 27 statement of income.*

28 (g) A person who originates a ~~covered~~ *high-cost* loan shall not
 29 pay a contractor under a home-improvement contract from the
 30 proceeds of a ~~covered~~ *high-cost* loan other than by an instrument
 31 payable to the consumer or jointly to the consumer and the
 32 contractor or, at the election of the consumer, to a third-party
 33 escrow agent for the benefit of the contractor in accordance with
 34 terms and conditions established in a written escrow agreement
 35 signed by the consumer, the person who originates a ~~covered~~
 36 *high-cost* loan, and the contractor prior to the disbursement of
 37 funds. No payments, other than progress payments for
 38 home-improvement work that the consumer certifies is completed,
 39 shall be made to an escrow account or jointly to the consumer and
 40 the contractor unless the person who originates the loan is presented

1 with a signed and dated completion certificate by the consumer
2 showing that the home-improvement contract was completed to
3 the satisfaction of the consumer.

4 (h) It is unlawful for a person who originates a ~~covered~~ *high-cost*
5 loan to recommend or encourage a consumer to default on an
6 existing consumer loan or other debt in connection with the
7 solicitation or making of a ~~covered~~ *high-cost* loan that refinances
8 all or any portion of the existing consumer loan or debt.

9 (i) A ~~covered~~ *high-cost* loan shall not contain a call provision
10 that permits the lender, in its sole discretion, to accelerate the
11 indebtedness. This prohibition does not apply if repayment of the
12 loan has been accelerated in accordance with the terms of the loan
13 documents (1) as a result of the consumer’s default, (2) pursuant
14 to a due-on-sale provision, or (3) due to fraud or material
15 misrepresentation by a consumer in connection with the loan or
16 the value of the security for the loan.

17 (j) A person who originates a ~~covered~~ *high-cost* loan shall not
18 refinance or arrange for the refinancing of a consumer loan such
19 that the new loan is a ~~covered~~ *high-cost* loan that is made for the
20 purpose of refinancing, debt consolidation or cash out, that does
21 not result in an ~~identifiable~~ *a net tangible* benefit to the consumer,
22 considering the consumer’s stated purpose for seeking the loan,
23 fees, interest rates, finance charges, and points.

24 ~~(k) (1) A covered loan shall not be made unless the following~~
25 ~~disclosure, written in 12-point font or larger, has been provided to~~
26 ~~the consumer no later than three business days prior to signing of~~
27 ~~the loan documents of the transaction:~~

28
29 CONSUMER CAUTION AND HOME OWNERSHIP
30 COUNSELING NOTICE
31

32 ~~If you obtain this loan, the lender will have a mortgage on your~~
33 ~~home. You could lose your home, and any money you have put~~
34 ~~into it, if you do not meet your obligations under the loan.~~

35 ~~Mortgage loan rates and closing costs and fees vary based on~~
36 ~~many other factors, including your particular credit and financial~~
37 ~~circumstances, your earnings history, the loan-to-value requested,~~
38 ~~and the type of property that will secure your loan. Higher rates~~
39 ~~and fees may be justified depending on the individual~~

1 circumstances of a particular consumer's application. You should
2 shop around and compare loan rates and fees.

3 This particular loan may have a higher rate and total points and
4 fees than other mortgage loans and is, or may be, subject to the
5 additional disclosure and substantive protections under Division
6 1.6 (commencing with Section 4970) of the Financial Code. You
7 should consider consulting a qualified independent credit counselor
8 or other experienced financial adviser regarding the rate, fees, and
9 provisions of this mortgage loan before you proceed. For
10 information on contacting a qualified credit counselor, ask your
11 lender or call the United States Department of Housing and Urban
12 Development's counseling hotline at 1-888-466-3487 or go to
13 www.hud.gov/fha/sfh/hec for a list of counselors.

14 You are not required to complete any loan agreement merely
15 because you have received these disclosures or have signed a loan
16 application.

17 If you proceed with this mortgage loan, you should also
18 remember that you may face serious financial risks if you use this
19 loan to pay off credit card debts and other debts in connection with
20 this transaction and then subsequently incur significant new credit
21 card charges or other debts. If you continue to accumulate debt
22 after this loan is closed and then experience financial difficulties,
23 you could lose your home and any equity you have in it if you do
24 not meet your mortgage loan obligations.

25 Property taxes and homeowner's insurance are your
26 responsibility. Not all lenders provide escrow services for these
27 payments. You should ask your lender about these services.

28 Your payments on existing debts contribute to your credit ratings.
29 You should not accept any advice to ignore your regular payments
30 to your existing creditors.

31 (2) It shall be a rebuttable presumption that a licensed person
32 has met its obligation to provide this disclosure if the consumer
33 provides the licensed person with a signed acknowledgment of
34 receipt of a copy of the notice set forth in paragraph (1).

35 (k) A person who originates a high-cost loan shall not receive,
36 directly or indirectly, any incentive compensation, including a
37 yield spread premium, that is based on, or varies with, the terms
38 of any high-cost loan.

39 (l) A licensed person shall not originate a high-cost loan unless
40 the licensed person requires and collects the monthly escrow of

1 *property taxes and hazard insurance calculated in accordance*
2 *with the requirements of Section 2609 of Title 12 of the United*
3 *States Code and regulations promulgated pursuant thereto. The*
4 *provisions of this paragraph do not apply to a high-cost loan that*
5 *is secured by a subordinate lien when the taxes and insurance are*
6 *escrowed through another loan.*

7 *(m) A licensed person shall not originate a high-cost loan unless*
8 *an escrow or impound account is established that remains in*
9 *existence for a minimum period of five years or until the consumer*
10 *has sufficient equity in the dwelling securing the loan that private*
11 *mortgage insurance is not required.*

12 *(n) A licensed person shall not originate a high-cost loan unless*
13 *the consumer provides certification from a housing counselor*
14 *approved by the United States Department of Housing and Urban*
15 *Development that the consumer received counseling on the*
16 *advisability of the loan transaction.*

17 ~~(t)~~

18 *(o) (1) A person who originates a ~~covered~~ high-cost loan shall*
19 *not steer, counsel, or direct any prospective consumer to accept a*
20 *loan product with a risk grade less favorable than the risk grade*
21 *that the consumer would qualify for based on that person's then*
22 *current underwriting guidelines, prudently applied, considering*
23 *the information available to that person, including the information*
24 *provided by the consumer.*

25 ~~A person shall not be deemed to have violated this section if the~~
26 ~~risk grade determination applied to a consumer is reasonably based~~
27 ~~on the person's underwriting guidelines if it is an appropriate risk~~
28 ~~grade category for which the consumer qualifies with the person.~~

29 *(2) If a broker originates a ~~covered~~ high-cost loan, the broker*
30 *shall not steer, counsel, or direct any prospective consumer to*
31 *accept a loan product at a higher cost than that for which the*
32 *consumer could qualify based on the loan products offered by the*
33 *persons with whom the broker regularly does business.*

34 ~~(m)~~

35 *(p) A person who originates a ~~covered~~ high-cost loan shall not*
36 *avoid, or attempt to avoid, the application of this division by doing*
37 *the following:*

38 *(1) Structuring a loan transaction as an open-end credit plan for*
39 *the purpose of evading the provisions of this division when the*

1 loan would have been a ~~covered~~ *high-cost* loan if the loan had been
2 structured as a closed end loan.

3 (2) Dividing any loan transaction into separate parts for the
4 purpose of evading the provisions of this division.

5 ~~(n)~~

6 (q) A person who originates a ~~covered~~ *high-cost* loan shall not
7 act in any manner, whether specifically prohibited by this section
8 or of a different character, that constitutes fraud.

9 SEC. 4. Section 4973.2 is added to the Financial Code, to read:

10 4973.2. The following are prohibited acts and limitations for
11 subprime and nontraditional loans:

12 (a) A licensed person shall not originate a subprime or
13 nontraditional loan unless at the time the loan is consummated,
14 the licensed person reasonably believes the consumer, or
15 consumers, when considered collectively in the case of multiple
16 consumers, will be able to make the scheduled loan payments, real
17 estate tax payments, and insurance payments associated with the
18 loan.

19 (b) (1) A licensed person shall base its determination of the
20 consumer's ability to pay on documentation of all sources of
21 income verified by tax returns, payroll receipts, bank records, or
22 the best and most appropriate form of documentation available,
23 and the debt-to-income ratio, the consumer's residual income after
24 payment of current expenses, and the proposed loan payments.

25 (2) A statement provided by the consumer of the income and
26 financial resources of the consumer, without other documentation
27 referred to in this subdivision, is not sufficient verification for
28 purposes of assessing the ability of the consumer to pay.

29 (3) The calculation assumptions used in evaluating the ability
30 to repay a subprime or nontraditional loan shall include the
31 following:

32 (A) The monthly payment amounts based on, at a minimum,
33 the fully indexed rate, assuming a fully amortizing repayment
34 schedule, as well as amounts for taxes and insurance.

35 (B) Verification of all sources of income, as provided in
36 paragraph (1).

37 (4) With regard to subprime and nontraditional loans, there is
38 a rebuttable presumption that a mortgage was made without regard
39 to repayment ability if, at the time the loan is consummated, the
40 consumer's total monthly debts, including total monthly housing

1 payments, taxes, property and private mortgage insurance, any
2 required homeowner or condominium fees, and any subordinate
3 mortgages including those that will be made contemporaneously
4 to the same consumer, exceed 45 percent of the consumer's
5 monthly gross income established. To rebut the presumption of
6 inability to repay, the licensed person shall, at minimum, determine
7 and consider the consumer's residual income after payment of
8 current expenses and proposed loan payments. However, no
9 presumption of ability to make the scheduled payments to repay
10 the obligation shall arise solely from the fact that, at the time the
11 loan is consummated, the consumer's total monthly debts, including
12 amounts owed under the loan, do not exceed 45 percent of the
13 consumer's monthly gross income.

14 (c) (1) A subprime loan or nontraditional loan shall not include
15 a prepayment fee or penalty.

16 (2) A consumer loan that is not a subprime or nontraditional
17 loan and that has an adjustable interest rate shall not include a
18 prepayment fee or penalty within six months of the date of the first
19 interest rate adjustment for the loan.

20 (d) (1) A person originating a subprime or nontraditional loan
21 shall not refinance or arrange for the refinancing of a consumer
22 loan such that the new loan is a subprime or nontraditional loan
23 that is made for the purpose of refinancing, debt consolidation or
24 cash out, that does not result in a net tangible benefit to the
25 consumer, considering all of the circumstances, including, but not
26 limited to, the terms of both the new and refinanced loans, the cost
27 of the new loan including, fees, interest rates, finance charges, and
28 points, and the consumer's individual circumstances.

29 (2) For a period of one year after the consummation of a
30 subprime or nontraditional loan originated by a licensed person to
31 a consumer, neither the licensed person who made the loan, nor
32 any licensed person who holds the loan, or an affiliate of either,
33 shall engage in direct marketing or initiate any communication
34 with the consumer regarding refinancing. "Direct marketing" and
35 "communication" shall include any communication directed at a
36 specific person without the use of intervening media, including,
37 but not limited to, the following methods: telephone, electronic
38 mail, United States mail or other form of courier service, and
39 in-person communication. This paragraph shall not restrict a

1 licensed person from responding to specific consumer inquires
2 regarding refinancing.

3 (e) In connection with a subprime or nontraditional loan, a
4 licensed person shall not steer, counsel, or direct a consumer to a
5 loan with rates, charges, principal amount, or prepayment terms
6 that are more costly than that for which the consumer qualifies.

7 (f) (1) A licensed person shall not receive, directly or indirectly,
8 any incentive compensation, including a yield spread premium,
9 for originating a subprime or nontraditional loan with an interest
10 rate above the wholesale par rate for which the consumer qualifies.

11 (2) Notwithstanding paragraph (1), in a consumer loan other
12 than a subprime or nontraditional loan, a licensed person may
13 receive compensation in the form of an increased rate not to exceed
14 200 basis points above the par rate for which the consumer qualifies
15 if:

16 (A) The licensed person receives no other compensation,
17 however denominated, directly or indirectly, from the consumer
18 or from another licensed person.

19 (B) The loan does not include discount points, origination points,
20 or rate reduction points, however denominated, or any payment
21 reduction fee, however denominated, or any other fees or charges
22 except bona fide and reasonable charges itemized in Section
23 226.4(c)(7) of Title 12 of the Code of Federal Regulations,
24 provided they are payable to a third party unaffiliated with the
25 licensed person.

26 (C) The loan does not include a prepayment penalty.

27 (g) A subprime or nontraditional loan shall not contain a
28 provision that increases the interest rate as a result of a default.
29 This provision does not apply to interest rate changes in a variable
30 rate loan otherwise consistent with the provisions of the loan
31 documents, provided the change in the interest rate is not triggered
32 by an event of default or the acceleration of the indebtedness.

33 (h) A subprime or nontraditional loan shall not contain a call
34 provision that permits the lender, in its sole discretion, to accelerate
35 the indebtedness. This prohibition does not apply if repayment of
36 the loan has been accelerated in accordance with the terms of the
37 loan documents (1) as a result of the borrower's default, (2)
38 pursuant to a due-on-sale provision, or (3) due to fraud or material
39 misrepresentation by a consumer in connection with the loan or
40 the value of the security for the loan.

1 (i) It is unlawful for a person who originates a subprime or
 2 nontraditional loan to recommend or encourage a consumer to
 3 default on an existing consumer loan or other debt in connection
 4 with the solicitation or making of a subprime or nontraditional
 5 loan that refinances all or any portion of the existing consumer
 6 loan or debt.

7 (j) (1) A licensed person shall not originate a subprime or
 8 nontraditional loan unless the licensed person requires and collects
 9 the monthly escrow of property taxes and hazard insurance
 10 calculated in accordance with the requirements of Section 2609
 11 of Title 12 of the United States Code and regulations promulgated
 12 pursuant thereto. The provisions of this paragraph do not apply to
 13 a subprime or nontraditional loan that is secured by a subordinate
 14 lien when the taxes and insurance are escrowed through another
 15 loan.

16 (2) An escrow or impound account established pursuant to
 17 paragraph (1) shall remain in existence for a minimum period of
 18 five years and until the consumer has sufficient equity in the
 19 dwelling securing the subprime or nontraditional loan so that
 20 private mortgage insurance is no longer required, unless the
 21 underlying mortgage establishing the account is terminated.

22 (k) (1) A subprime or nontraditional loan shall not be made
 23 unless the following disclosure, written in 12-point typeface or
 24 larger, has been provided to the consumer no later than three
 25 business days prior to signing of the loan documents of the
 26 transaction:

27 **CONSUMER CAUTION NOTICE**

28 Because you are receiving this notice, it is likely that this
 29 particular loan is a “subprime loan” that has a higher interest
 30 rate than other mortgage loans and is intended for people with
 31 less than excellent credit, or a “nontraditional loan,” such as
 32 a no interest loan or a payment option ARM, that are both
 33 subject to specific disclosure requirements and protections
 34 under California law (Division 1.6 (commencing with Section
 35 4970) of the Financial Code). Federal regulators have noted
 36 the risky nature of the features of these loans.

37 You are not required to complete any loan agreement merely
 38 because you have received these disclosures or have signed a
 39 loan application.

1 If you proceed with this mortgage loan, you should also
2 remember that you may face serious financial risks if you use
3 this loan to pay off credit card debts and other debts in
4 connection with this transaction and then subsequently incur
5 significant new credit card charges or other debts. If you
6 continue to accumulate debt after this loan is closed and then
7 experience financial difficulties, you could lose your home
8 and any equity you have in it if you do not meet your mortgage
9 loan obligations.

10 You should consider consulting a qualified independent credit
11 counselor or other experienced financial adviser regarding the
12 rate, fees, and provisions of this mortgage loan before you
13 proceed. For information on contacting a qualified credit
14 counselor, ask your lender or call the United States Department
15 of Housing and Urban Development's counseling hotline at
16 1 - 8 0 0 - 5 6 9 - 4 2 8 7 o r g o t o
17 www.hud.gov/offices/hsg/sfh/hcc/hccprof14.cfm for a list of
18 counselors.

19
20 (2) It shall be a rebuttable presumption that a licensed person
21 has met its obligation to provide the disclosure required by
22 paragraph (1) if the consumer provides the licensed person with a
23 signed acknowledgment of receipt of a copy of that disclosure.

24 (l) It shall be a violation of this division for any person to
25 attempt in bad faith to avoid the application of this division by
26 dividing any loan transaction into separate parts or otherwise
27 structuring a loan transaction for the purpose of evading the
28 provisions of this division or by engaging in any other subterfuge
29 with the intent of evading any provision of this division.

30 (m) A licensed person shall not make or cause to be made,
31 directly or indirectly, any false, deceptive, or misleading statement,
32 representation, or omission in connection with a subprime or
33 nontraditional loan.

34 (n) A licensed person shall not finance, directly or indirectly,
35 into a subprime or nontraditional loan, or finance to the same
36 consumer within 30 days of consummation of the loan, any credit
37 life, credit disability, credit property, or credit unemployment
38 insurance premiums, or any debt cancellation or suspension
39 agreement fees, provided that credit insurance premiums, debt
40 cancellation, or suspension fees calculated and paid on a monthly

1 basis shall not be considered financed by the person originating
2 the loan. For purposes of this section, credit insurance does not
3 include a contract issued by a government agency or private
4 mortgage insurance company to insure the lender against loss
5 caused by a mortgagor's default.

6 (o) A subprime or nontraditional loan shall not contain a
7 provision for negative amortization such that the payment schedule
8 for regular monthly payments causes the principal balance to
9 increase.

10 SEC. 5. Section 4974 of the Financial Code is amended to read:

11 4974. (a) Any compliance failure that was not willful or
12 intentional and resulted from a bona fide error, that occurred
13 notwithstanding the maintenance of procedures reasonably adopted
14 to avoid those errors, including, but not limited to, those involving
15 clerical, calculation, computer malfunction and programming, and
16 printing errors shall be corrected no later than 45 days after receipt
17 of the complaint or discovery of the error. A person who originates
18 ~~a covered~~ *high-cost, subprime, or nontraditional* loan shall not be
19 administratively, civilly, or criminally liable for a bona fide error
20 corrected pursuant to this section.

21 (b) If a person who originates ~~covered~~ *high-cost, subprime, or*
22 *nontraditional* loans makes a loan where the person knew, *or*
23 *should have known*, of and showed reckless disregard for a
24 violation of this division by a broker, the person and broker shall
25 be jointly and severally liable for all damages awarded under this
26 division with respect to the broker's unlawful conduct.

27 This section does not impose or transfer liability for a breach of
28 the broker's fiduciary duty.

29 SEC. 6. Section 4975 of the Financial Code is amended to read:

30 4975. (a) (1) Any licensed person who violates any provision
31 of Section 4973, 4973.2, 4979.6, or 4979.7 shall be deemed to
32 have violated that person's licensing law.

33 (2) After a knowing and willful violation, the licensing agency
34 may bring a proceeding to suspend the license of the licensed
35 person for not less than six months and not more than three years.

36 (b) After a knowing and willful violation resulting in a second
37 or subsequent administrative or civil action, the licensing agency
38 may bring a proceeding to permanently revoke the license of the
39 licensed person or impose any lesser licensed sanction for at least
40 three years.

1 (c) A licensing agency may exercise any and all authority and
2 powers available to it under any other provisions of law, to
3 administer and enforce this division including, but not limited to,
4 investigating and examining the licensed person's books and
5 records, and charging and collecting the reasonable costs for these
6 activities. The licensing agency shall not charge a licensed person
7 twice for the same service. Any civil, criminal, and administrative
8 authority and remedies available to the licensing agency pursuant
9 to its licensing law may be sought and employed in any
10 combination deemed advisable by the licensing agency to enforce
11 the provisions of this division.

12 (d) Nothing in this section shall be construed to impair or impede
13 a licensing agency's authority under any other provision of law.

14 SEC. 7. Section 4977 of the Financial Code is amended to read:

15 4977. (a) A licensing agency may, after appropriate notice and
16 opportunity for hearing, by order levy administrative penalties
17 against a person who violates any provision of this division, and
18 the person shall be liable for administrative penalties of not more
19 than ~~two thousand five hundred dollars (\$2,500)~~ *ten thousand*
20 *dollars (\$10,000)* for each violation. Except for licensing agencies
21 exempt from the provisions of the Administrative Procedure Act,
22 any hearing shall be held in accordance with the Administrative
23 Procedure Act (Chapter 5 (commencing with Section 11500) of
24 Part 1 of Division 3 of Title 2 of the Government Code), and the
25 licensing agency shall have all the powers granted under that act.

26 (b) Any person who willfully and knowingly violates any
27 provision of this division shall be liable for a civil penalty of not
28 more than twenty-five thousand dollars (\$25,000) for each violation
29 which shall be assessed and recovered in a civil action brought in
30 the name of the people of the State of California by the licensing
31 agency in any court of competent jurisdiction.

32 (c) Nothing in this section requires exhaustion of administrative
33 remedies prior to an injured party bringing a civil action.

34 (d) If the licensing agency determines that it is in the public
35 interest, the licensing agency may include, in any action for
36 penalties authorized by subdivision (b), a claim for relief in
37 addition to the penalties, including a claim for restitution or
38 disgorgement, and the court shall have jurisdiction to award the
39 additional relief.

1 (e) Nothing in this section shall be construed to impair or impede
2 the Attorney General from representing a licensing agency in
3 bringing an action to enforce this division at the request and on
4 behalf of the licensing agency.

5 (f) In any action brought by the licensing agency, or the Attorney
6 General acting at the request and on behalf of the licensing agency,
7 under this division in which a judgment against a person is
8 rendered, the licensing agency or the Attorney General shall be
9 entitled to recover costs which, in the discretion of the court, may
10 include an amount representing reasonable attorney's fees and
11 investigative expenses for services rendered for deposit in the
12 appropriate fund of that licensing agency.

13 (g) The amounts collected under subdivisions (a) and (b) shall
14 be deposited in the appropriate fund of the licensing agency to be
15 used by that licensing agency, subject to appropriation by the
16 Legislature, for the purposes of *financial literacy* education and
17 enforcement in connection with abusive lending practices.

18 SEC. 8. Section 4978 of the Financial Code is amended to read:

19 4978. (a) A person who fails to comply with the provisions
20 of this division is civilly liable to the consumer in an amount equal
21 to any actual damages suffered by the consumer, plus attorneys
22 fees and costs. For a willful and knowing violation of this division,
23 the person shall be liable to the consumer in the amount of ~~fifteen~~
24 ~~thousand dollars (\$15,000)~~ *twenty-five thousand dollars (\$25,000)*
25 or the consumers actual damages, whichever is greater, plus
26 attorneys fees and costs.

27 (b) (1) If a provision in a contract in a ~~covered~~ *high-cost* loan
28 violates ~~subdivision (a), (b), (c), (d), (e), or (i)~~ of Section 4973, *or*
29 *a provision in a contract in a subprime or nontraditional loan*
30 *violates Section 4973.2, or a provision in a contract of any of those*
31 *loans violates Section 4979.6, or Section 4979.7, that provision is*
32 *unenforceable. A court in which any action is brought by, or on*
33 *behalf of, an aggrieved consumer for relief may issue an order or*
34 *injunction to reform the terms of the ~~covered~~ *high-cost, subprime,**
35 *or nontraditional loan to conform to the provisions of this division.*

36 (2) A court may, in addition to any other remedy, award punitive
37 damages to the consumer upon a finding that such damages are
38 warranted pursuant to Section 3294 of the Civil Code.

1 (c) Nothing in this section is intended, nor shall be construed,
2 to abrogate existing common law provisions prohibiting double
3 recovery of damages.

4 (d) *Without regard to whether a consumer is acting individually,*
5 *jointly, or on behalf of others similarly situated, any provision in*
6 *a contract of a high-cost, subprime, or nontraditional loan that*
7 *allows a party to require the consumer to assert any claim or*
8 *defense in a forum that is less convenient, more costly, or more*
9 *dilatory for the resolution of a dispute than a judicial forum*
10 *established in this state where the consumer may otherwise*
11 *properly bring a claim or defense or that limits in any way any*
12 *claim or defense the consumer may have is unconscionable and*
13 *void.*

14 (e) *Any provision in a contract of a high-cost, subprime, or*
15 *nontraditional loan that purports to waive the consumer's right*
16 *to participate in a class action, or to pursue any claims in a class*
17 *action or other consolidated or joint action, is unconscionable*
18 *and void.*

19 (f) *In addition to any other enforcement provisions provided*
20 *under this division, a consumer may bring a private cause of action*
21 *against any licensed person to recover damages associated with*
22 *a violation of this division.*

23 SEC. 9. Section 4978.6 of the Financial Code is amended to
24 read:

25 4978.6. A person who originates ~~covered~~ *high-cost, subprime,*
26 *or nontraditional* loans shall inform any employee, who originates
27 ~~covered~~ *those* loans on behalf of the person, of the administrative
28 or civil penalties for a violation of this division.

29 SEC. 10. Section 4979 of the Financial Code is amended to
30 read:

31 4979. Upon request, a person who originates a ~~covered~~
32 *high-cost, subprime, or nontraditional* loan shall provide the
33 licensing agency or the consumer, at no cost, documentation
34 regarding his or her loan that clearly demonstrates whether any
35 loan is a ~~covered~~ *high-cost, subprime, or nontraditional* loan. This
36 documentation shall include, but not be limited to, full disclosure
37 of the original principal balance, the annual percentage rate, and
38 the total points and fees, as defined in Section 4970.

39 SEC. 11. Section 4980 is added to the Financial Code, to read:

1 4980. It shall constitute a defense against foreclosure on a
2 property secured by a high-cost, subprime, or nontraditional loan
3 if that loan is in violation of this division.

4 SEC. 12. The provisions of this act shall apply to high-cost,
5 subprime, and nontraditional loans originated on and after January
6 1, 2009.

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