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9 BEFORE THE DEPARTMENT OF BUSINESS OVERSIGHT  
10 OF THE STATE OF CALIFORNIA

11  
12 In the Matter of the Accusation of THE ) File Nos.: 413-0266 and 603-E734  
COMMISSIONER OF BUSINESS )  
13 OVERSIGHT OF THE STATE OF ) ACCUSATION IN SUPPORT OF NOTICE OF  
CALIFORNIA, ) INTENT TO ISSUE ORDERS SUSPENDING  
14 ) LICENSES AND IMPOSING PENALTIES  
15 Complainant, )  
16 vs. )  
17 PROSPECT MORTGAGE, LLC, )  
18 )  
19 Respondent. )

20  
21 The Complainant is informed and believes and based upon such information and belief,  
22 alleges and charges the Respondent as follows:

23 **I**

24 Prospect Mortgage, LLC (“Prospect”) is a residential mortgage lender and loan servicer  
25 licensed since August 25, 1999 by the Commissioner of Business Oversight (“Commissioner” or  
26 “Complainant”)<sup>1</sup> pursuant to the California Residential Mortgage Lending Act (“CRMLA”)  
27 (California Financial Code sections 50000 et seq.). Prospect has its principal place of business

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<sup>1</sup> As of July 1, 2013, the Department of Corporations and the Department of Financial Institutions merged to form the Department of Business Oversight.

1 located at 15301 Ventura Boulevard, Suite D300, Sherman Oaks, California 91403. Prospect  
2 employs mortgage loan originators.

3 Prospect is also licensed by the Commissioner as a finance lender and broker pursuant to the  
4 California Finance Lenders Law (“CFLL”) (California Financial Code sections 22000 et seq.) under  
5 license number 603-E734. Prospect’s principal place of business under the CFLL is also located at  
6 15301 Ventura Boulevard, Suite D300, Sherman Oaks, California 91403.

## 7 **II** 8 **Multi-State Examination**

9 On or about April 23, 2012, the Department of Business Oversight (“Department”) and  
10 seven other state banking and finance commissions (“Participating State Agencies”) commenced a  
11 Multi-State Examination of Prospect under the agreed authority of the Conference of State Bank  
12 Supervisors / American Association of Residential Mortgage Regulators (“CSBS/AARMR”)   
13 Nationwide Cooperative Agreement for Mortgage Supervision. Each Participating State Agency  
14 examined Prospect for the period of October 1, 2010 through March 31, 2012 under its respective  
15 regulatory authority.

## 16 **III** 17 **Violations of the CRMLA**

### 18 Trust Account Shortages

19 A review of the balance sheets provided by Prospect during the Multi-State Examination  
20 disclosed that Prospect’s trust assets held in its trust bank accounts were insufficient to cover its  
21 trust liabilities, causing a debit balance totaling \$1,075,665.72 as of June 30, 2012. California Code  
22 of Regulations, title 10, section 1950.314.6 prohibits debit balances in any loan or servicing account  
23 maintained by a CRMLA licensee. During the Multi-State Examination, Prospect was informed of  
24 this violation. By August 1, 2012, Prospect had replaced the debit balance of \$1,075,665.72 into its  
25 trust bank accounts.

### 26 Failure to Reconcile Escrow Liability Ledgers

27 The Multi-State Examination disclosed that Prospect did not reconcile its escrow liability  
28 ledgers to its control account at least once a week and to the bank statement at least once each  
month, in violation of California Code of Regulations, title 10, section 1950.314.1. To correct this

1 deficiency Prospect agreed to implement a new process for ensuring that the trust assets adequately  
2 cover trust liabilities and to strengthen the reconciliation processes.

3 Per Diem Interest Overcharges

4 The Multi-State Examination disclosed that for nine of 67 loans, or approximately 13% of  
5 the loans reviewed, Prospect was charging the borrower per diem interest in excess of one day prior  
6 to the date that the loan proceeds are disbursed from escrow, in violation of California Financial  
7 Code (“FC”) section 50204(o). For eight of the nine loans with per diem interest overcharges, a  
8 document entitled, “California Per Diem Interest Disclosure,” seeking the borrower’s authorization  
9 to charge per diem interest in excess of one day prior to the date the loan proceeds are disbursed  
10 from escrow, was included in the loan files. However, these documents did not comply with  
11 California Civil Code (“CC”) section 2948.5(b) in that six of them were signed with blanks, in  
12 violation of FC section 50204(e), and two of them were signed not authorizing Prospect to charge  
13 additional per diem interest. Therefore, the disclosures were not considered in calculating per diem  
14 interest charges. The range of per diem interest overcharges was between \$33.12 and \$158.34. The  
15 range of days in which interest was overcharged was between two and three days.

16 A prior regulatory examination conducted on or around March 5, 2007 similarly disclosed  
17 violations of overcharging per diem interest for 13 out of 29 loans, or approximately 44% of the  
18 loans reviewed. Prospect was directed on October 12, 2007 to review all loans on mortgages that  
19 had been originated since September 15, 2004 to October 12, 2007 to determine the number and  
20 amount of overcharges collected from California borrowers. Prospect was also to provide a  
21 detailed report of the files reviewed and the dollar amount of the overcharges established through  
22 the review, including, but not limited to, the loan number, borrower’s name, loan amount, interest  
23 rate, date disbursed, date interest commenced, interest overcharged and date refunded. Pursuant to  
24 FC section 50504(b) the borrowers were to be refunded the amount of the overcharge plus interest  
25 at the rate of 10 percent per annum. Prospect failed to submit a complete self-audit report or make  
26 the appropriate refunds.

27 A subsequent regulatory examination conducted on or around August 9, 2009 again  
28 disclosed violations of overcharging per diem interest in nine out of 29 loans, or approximately

1 31% of the loans reviewed. Prospect was directed on January 7, 2010 to review all of the loans on  
2 mortgages originated since August 10, 2006 to determine the number and amount of overcharges  
3 collected from borrowers. Prospect was to provide a detailed report of the files reviewed and the  
4 dollar amount of the overcharges established through the review of its originated loans, including,  
5 but not be limited to, the loan number, borrower's name, loan amount, interest rate, date disbursed,  
6 date started collecting interest, interest overcharged and date refunded. Prospect was again notified  
7 that pursuant to FC section 50504(b) the borrowers were to be refunded the amount of the  
8 overcharge plus interest at the rate of 10 percent per annum. Furthermore, Prospect was notified  
9 that "[t]his is a repeat violation, which was also noted in our previous examination during March  
10 2007." Prospect again failed to submit a complete self-audit report or make the appropriate refunds.

11 During the Multi-State Examination, Prospect again was notified of violations of  
12 overcharging per diem interest. Prospect again was informed that it was required to conduct a self-  
13 audit in which it reviewed all California loans originated from August 10, 2006 through March 31,  
14 2012, to determine the number and amount of overcharges collected from borrowers, and to make  
15 appropriate refunds in the amount of the overcharge plus 10 percent per annum. Prospect was again  
16 required to provide a detailed report of the files reviewed and the dollar amount of interest  
17 overcharges discovered in the review, including, but not limited to, the loan number, borrower's  
18 name, loan amount, interest rate, and date of disbursement from the settlement agent, date interest  
19 commenced, interest overcharged, and the date of refund.

20 Failure to Make Report to the Commissioner by the Extended Deadline

21 On May 2, 2013, the Department notified Prospect that its response was due within 30 days.  
22 On or around May 24, 2013, the Department considered Prospect's request for a 90-day extension,  
23 and granted an extension only until June 30, 2013. On or around August 21, 2013, having failed to  
24 meet the deadline, Prospect requested another extension until October 31, 2013, and the Department  
25 granted an extension only until September 10, 2013. On or around September 9, 2013, Prospect  
26 provided a status report to the Department regarding the self-audit and reiterated its prior request for  
27 an extension until October 31, 2013. On September 16, 2013, the Department denied this request  
28 for an extension.

1 Prospect failed to submit the self-audit report as required by September 10, 2013. Because  
2 Prospect failed to submit the self-audit report by the extension of time granted Prospect shall forfeit  
3 to the People of the State a sum of up to one hundred dollars (\$100) for every day up to the 10th  
4 day, pursuant to FC section 50236.

### 5 **III** 6 **Incomplete Self-Audit Report**

7 On or around October 8, 2013, Prospect notified the Department that it had completed its  
8 per diem interest self-audit of all California loans originated, not for the period of August 10, 2006  
9 through March 31, 2012 as the Department directed, but for an extended period of August 10, 2006  
10 through June 28, 2013. Prospect stated that the total population of loans during this period was  
11 81,133. However, Prospect's self-audit report listed details for only the 8,375 loans it alleged  
12 required refunds because of per diem interest overcharges.

13 In its October 8, 2013 letter Prospect listed various reasons why it had excluded 9,038 loans  
14 from the self-audit, bringing the total self-audited loan files down from 81,133 to 72,095. Prospect  
15 then explained that it could not locate applicable documentation necessary to accurately recalculate  
16 the per diem interest on 2,214 loans, thus bringing the total of self-audited files down further to  
17 69,881. Prospect omitted to provide any information regarding the 61,506 loan files that were self-  
18 audited but allegedly *did not* require refunds. Because the self-audit report did not include all the  
19 information required by the Department and Prospect's explanations were insufficient to allow the  
20 Department to test the accuracy of the self-audit, the self-audit report was incomplete as of October  
21 8, 2013, which is 28 days past the Commissioner's extended deadline.

22 Moreover, by failing to locate documentation necessary to accurately recalculate the per  
23 diem interest on 2,214 loans, Prospect failed to keep documents and records that would properly  
24 enable the Commissioner to determine whether Prospect complied with the CRMLA, in violation of  
25 FC section 50314.

### 26 **IV** 27 **Refusal to Make Refunds for Violations Pursuant to FC Section 50504**

28 California Financial Code section 50504, subdivision (b) states:

1 (b) If interest on the principal amount of a loan in excess of the amount  
2 authorized by this division is willfully charged, contracted for, or received,  
3 in addition to any other penalties or remedies, the commissioner may order  
4 the licensee to refund the excess interest amount to all borrowers charged  
5 the excess amount, with interest at the rate of 10 percent per annum,  
6 calculated from the date the improper charge was imposed.

7 “Willful conduct does not require a purpose or specific intent to bring about a result.  
8 However, it does require more than negligence or accidental conduct . . . The word ‘willfully’ when  
9 applied to the intent with which an act is done or omitted means with a purpose or willingness to  
10 commit the act or to make the omission in question.” *Patarak v. Williams* (2001) 91 Cal.App.4<sup>th</sup>  
11 826, 829-830.

12 As of October 11, 2013, Prospect stated that it had not made any refunds to the borrowers  
13 whom it admits were overcharged, objecting to the requirement of FC section 50504 to refund the  
14 excess interest at the rate of 10 percent per annum, because it believed that the violations were not  
15 willful but rather a system-based issue that was not adequately addressed.

16 However, Prospect was notified by the Department on October 12, 2007 and again on  
17 August 9, 2009 that Prospect was overcharging borrowers per diem interest in violation of FC  
18 section 50204(o) and Prospect failed or refused to conduct the required self-audits and make the  
19 appropriate refunds. Hence, Prospect’s continued overcharging of per diem interest was not  
20 negligent or accidental, but demonstrates a purpose and willingness to act or make the omission in  
21 question, namely continually failing to address the violations. For at least six years, Prospect had  
22 full knowledge and prior notice that the failure to “adequately address” the “system-based issue”  
23 would adversely affect borrowers. Therefore, Prospect should refund the excess interest amount  
24 with interest at the rate of 10 percent per annum pursuant to FC section 50504.

#### 25 IV

26 The violations of the CRMLA described above, if committed by Prospect on or before  
27 having originally sought a license from the Department under the CFLL, would have constituted  
28 grounds for the Commissioner to deny the application of Prospect under FC section 22109.  
Pursuant to FC section 22714, the Commissioner may suspend any CFLL license if “a fact or

1 condition exists that, if it had existed at the time of the original application for the license,  
2 reasonably would have warranted the commissioner in refusing to issue the license originally.”  
3 Pursuant to FC section 22109, the Commissioner may refuse to issue a license if the “applicant . . .  
4 has violated any provision of this division or the rules thereunder or any similar regulatory scheme  
5 of the State of California . . . .”

6 Thus, a fact or condition now exists that, if it had existed at the time of the original  
7 application of Prospect for a license under the CFLL, reasonably would have warranted the  
8 Commissioner in refusing to issue the license.

9 **VI**

10 California Financial Code section 50326 provides in pertinent part:

11 If any licensee fails to do any of the following, the licensee shall forfeit to  
12 the people of the state a sum of up to one hundred dollars (\$100) for every  
13 day up to the 10th day: (a) to make any report required by law or by the  
14 commissioner within 10 days from the day designated for the making of  
15 the report, or within any extension of time granted by the commissioner,  
16 or (b) fails to include therein any matter required by law or by the  
17 commissioner. Thereafter, any failure shall constitute grounds for the  
18 suspension or revocation of the license held by the residential mortgage  
19 lender or residential mortgage loan servicer.

20 California Financial Code section 50327 provides in pertinent part:

21 (a) The commissioner may, after notice and a reasonable opportunity to  
22 be heard, suspend or revoke any license, if the commissioner finds that:  
23 (1) the licensee has violated any provision of this division or rule or order  
24 of the commissioner thereunder; or (2) any fact or condition exists that, if  
25 it had existed at the time of the original application for license, reasonably  
26 would have warranted the commissioner in refusing to issue the license  
27 originally.

28 California Financial Code section 50513 provides in pertinent part:

(a) The commissioner may do one or more of the following:  
...  
(4) Impose fines on a mortgage loan originator or any residential mortgage  
lender or servicer licensee employing a mortgage loan originator pursuant  
to subdivisions (b), (c), and (d).

...

1 (b) The commissioner may impose a civil penalty on a mortgage loan  
2 originator or any residential mortgage lender or servicer licensee  
3 employing a mortgage loan originator, if the commissioner finds, on the  
4 record after notice and opportunity for hearing, that the mortgage loan  
5 originator or any residential mortgage lender or servicer licensee  
6 employing a mortgage loan originator has violated or failed to comply  
7 with any requirement of this division or any regulation prescribed by the  
8 commissioner under this division or order issued under authority of this  
9 division.

10 (c) The maximum amount of penalty for each act or omission described in  
11 subdivision (b) shall be twenty-five thousand dollars (\$25,000).

12 (d) Each violation or failure to comply with any directive or  
13 order of the commissioner is a separate and distinct violation or  
14 failure.

## 15 VII

16 The Commissioner finds that, by reason of the foregoing, Prospect has violated FC sections  
17 50314 and 50204, and California Code of Regulations, title 10, sections 1950.314.1 and 1950.314.6  
18 of the CRMLA. Furthermore, based upon Prospect's violations of the CRMLA, a fact or condition  
19 now exists, that if it had existed at the time of original licensure under the CFLL, reasonably would  
20 have warranted the Commissioner in refusing to issue a CFLL license to Prospect.

21 For all the foregoing reasons, grounds exist to:

22 (1) suspend Prospect's CRMLA residential mortgage lender license and CFLL finance  
23 lender and broker license, and

24 (2) levy penalties against Prospect pursuant to FC sections 50326 and 50513(b).

25 WHEREFORE, IT IS PRAYED that:

26 1. The residential mortgage lender license and the finance lender and broker license of  
27 Prospect be suspended, pursuant to FC sections 50327 and 22714, for the *greater* period of:

28 a. 12 months, or

b. Until (i) Prospect has submitted a complete self-audit report providing all the  
information demanded by the Commissioner on October 12, 2007, January 7, 2010, and during the  
Multi-State Examination; (ii) the complete self-audit report has been determined by the



1 Commissioner to be trustworthy; *and* (iii) Prospect has complied fully with the Order to Refund  
2 Excessive Per Diem Interest Charges Pursuant To California Financial Code Section 50504;

3       2. Pursuant to FC section 50326, a penalty be levied against Prospect for failure to  
4 make any report required by law or by the Commissioner within 10 days from the day designated  
5 for the making of the report, or within any extension of time granted by the Commissioner, or  
6 failure to include therein any matter required by law or by the Commissioner, in an amount of at  
7 least \$1,000, or according to proof;

8       3. Pursuant to FC section 50513(b), a penalty be levied against Prospect for debit  
9 balances in its trust bank accounts, in violation of California Code of Regulations, title 10, section  
10 1950.314.6, in an amount of at least \$25,000, or according to proof;

11       4. Pursuant to FC section 50513(b), a penalty be levied against Prospect for failure to  
12 reconcile its escrow liability ledgers to its control account at least once a week and to the bank  
13 statement at least once each month, in violation of California Code of Regulations, title 10, section  
14 1950.314.1, in an amount of at least \$10,000, or according to proof;

15       5. Pursuant to FC section 50513(b), penalties be levied against Prospect for at least  
16 3,534 violations of FC section 50204(o), whereby Prospect overcharged borrowers per diem interest  
17 during the period from January 1, 2010 through June 28, 2013, in an amount of at least \$2,500 per  
18 violation, for an amount of at least \$8,835,000 or according to proof;

19       For a total amount of penalties of at least \$8,871,000, or according to proof.

20  
21 Dated: November 26, 2013  
22       Los Angeles, CA

JAN LYNN OWEN  
Commissioner of Business Oversight

23 By \_\_\_\_\_  
24       Sophia C. Kim  
25       Corporations Counsel  
26       Enforcement Division  
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