

FINAL STATEMENT OF REASONS  
FOR THE ADOPTION OF RULES UNDER THE  
CALIFORNIA FINANCE LENDERS LAW AND THE  
CALIFORNIA RESIDENTIAL MORTGAGE LENDING ACT

As required by Section 11346.9 of the Government Code, the California Corporations Commissioner (Commissioner) sets forth below the reasons for the adoption of Sections 1409.1, 1414, 1422.4, 1422.4.1, 1422.4.5, 1422.5, 1422.6, 1422.6.1, 1422.6.2, 1422.6.3, 1422.7, 1422.7.1, 1422.9, 1422.10, 1422.11, 1422.12, 1424, 1437, 1950.122.2.1, 1950.122.4, 1950.122.4.1, 1950.122, 1950.122.5, 1950.122.5.1, 1950.122.5.2, 1950.122.5.3, 1950.122.5.4, 1950.122.6, 1950.122.7, 1950.122.8, 1950.122.9, 1950.122.10, 1950.122.11, 1950.122.12, 1950.122.15, 1950.205.1, 1950.209, and 1950.307; amendment of Sections 1404, 1409, 1411, 1430.5, 1431, 1433, 1436, 1454, 1550, 1552, 1557, 1950.003, 1950.122.2, 1950.123, 1950.204.3, 1950.204.4, 1950.301, 1950.314.8, 1950.316, and 1950.317; and repeal of Section 1950.122 of Title 10 of the California Code of Regulations.

Introduction

The Department of Corporations (Department) licenses and regulates finance lenders and brokers under the California Finance Lenders Law (CFLL), and residential mortgage lenders and servicers under the California Residential Mortgage Lending Act (CRMLA). Both of these laws regulate licensees engaged in the business of residential mortgage lending.

On October 11, 2009, the Governor signed into law SB 36 (Chap.160, Stats. 2009 – Calderon) as an urgency measure. SB 36 implements the federal Secure and Fair Enforcement of Mortgage Licensing Act of 2008, or “SAFE Act” (contained in the federal Housing and Economic Recovery Act of 2008, HR 3221 (Public Law 110-289) enacted on July 30, 2008) that requires all states, including California, to license all individual mortgage loan originators who offer or negotiate residential mortgages. On January 4, 2010, the Department began accepting applications of mortgage loan originators through the Nationwide Mortgage Licensing System and Registry (NMLS), a national licensing system and registry. On April 1, 2010, the Department promulgated emergency regulations to implement SB 36 and the SAFE Act. The emergency rulemaking was effective until September 28, 2010, was readopted as an emergency rulemaking effective until December 27, 2010, and was readopted a second time on December 23, 2010. On December 10, 2010, this rulemaking action was filed to adopt permanent regulations to implement SB 36 and the SAFE Act. On January 25, 2011, a supplement providing the statement of necessity regarding the application fee was posted. The comment period ended February 9, 2011.

A. The SAFE Act

The SAFE Act was enacted to increase consumer protection and reduce fraud by mortgage providers by requiring states to license mortgage loan originators. As set forth in Section 1502 of the SAFE Act, the purpose of the act is to increase uniformity,

reduce regulatory burden, enhance consumer protection, and reduce fraud. The SAFE Act is intended to provide additional consumer protections with respect to loan originating activities, while promoting a more immediate and comprehensive recovery to the nation's housing market. To that end, the SAFE Act prohibits individuals from engaging in business as a mortgage loan originator unless the individuals are licensed or registered by a state regulatory agency, a federal banking regulatory agency, or under certain conditions, the Department of Housing and Urban Development (HUD).<sup>1</sup>

The SAFE Act is applicable to mortgage loan originators who offer or negotiate residential mortgages, and requires states to implement a system for licensing and registering individual mortgage loan originators. The SAFE Act also requires states to participate in a national licensing system and registry, the NMLS. The NMLS is a national depository that centralizes information on individual mortgage loan originators, such as disciplinary history and licensure information, including testing, criminal background, and pre- and post- licensure education information. The NMLS is patterned after the Central Registration Depository or CRD, a national licensing depository for securities broker-dealers and their agents.

The NMLS allows state and federal regulators to track the activities of mortgage loan originators through the assignment of a unique identifier number. Each mortgage loan originator is issued a unique identifier through the NMLS so that his or her licensing and disciplinary record is available to regulators and the public. The unique identifier number remains associated with the individual as he or she moves from firm to firm or state to state. Consequently, states and the public have increased access to information regarding mortgage loan activities, and have better regulatory and supervisory oversight of the actions of mortgage loan originators and their employers.

#### B. SB 36 (2009)

SB 36 implements the SAFE Act in California, and requires that all mortgage loan originators subject to regulation by the Department become licensed by the Department through the NMLS by July 31, 2010, to continue to engage in loan originator activity under the authority of a license issued by the Department. Prior to SB 36, the Department's lending laws (the CFLL and the CRMLA) did not require the licensure of the employees of the lenders (the individual mortgage loan originators). SB 36 implements the SAFE Act by amending both lending laws administered by the Department to provide for the licensure of the individual mortgage loan originators. SB 36 also provides authority to require that existing mortgage lender, broker, and servicer licensees (subsequently referred to as residential mortgage providers) transition onto and begin using the NMLS for licensure and other filings with the Department.

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<sup>1</sup> The SAFE Act provides that HUD will determine whether a state has laws in place for the licensing of mortgage loan originators that meet the minimum requirements of the SAFE Act, and if no such laws are in place, HUD will establish such a system. HUD published its proposed regulations in the Federal Register on December 15, 2009 (74 FR 66548). With the enactment of the federal Dodd-Frank Wall Street Reform and Consumer Protection Act (111 P.L. 203), signed by President Obama on July 21, 2010, various responsibilities held by HUD, including default regulatory actions and rulemaking related to the SAFE Act, will be transferred to the newly-created Bureau of Consumer Financial Protection on July 21, 2011.

In general, this rulemaking is necessary to implement the state and federal requirements of the SAFE Act and SB 36 for the licensure of mortgage loan originators and to require the use of the NMLS in the licensing and oversight of residential mortgage providers. Also, the rulemaking is necessary to clarify the requirements imposed by the SAFE Act on mortgage loan providers subject to the CFLL and the CRMLA.

### C. The License Application Process and NMLS

This regulatory action amends the application process for both individuals and companies making or brokering residential mortgage loans by discontinuing the use of the Department's previous application forms and the former process of submitting the forms by mail, and instead requires applicants to apply for licensure electronically through the NMLS on uniform national forms.<sup>2</sup>

#### Sections 1422.4 and 1950.122 – Electronic Filings

Under prior law, all finance lenders under the CFLL and all residential mortgage providers under the CRMLA were required to submit their paper license applications directly with the Department. Sections 1422.4 and 1950.122 provide that all residential mortgage provider and mortgage loan originator applications are required to be filed electronically through the NMLS. Under the CRMLA, this requirement is applicable to all residential mortgage lenders and servicers, and under the CFLL this requirement is applicable only to finance lenders engaged in the making or brokering of residential mortgage loans.<sup>3</sup> These rules provide that the electronic filing with the NMLS is mandatory for licensees making, brokering or servicing mortgage loans. The rules are necessary to ensure that all residential mortgage provider and mortgage loan originator applications, amendments, reports, notices, fees, and related filings required to be filed with the Commissioner are filed electronically through the NMLS, to the extent the NMLS is capable of accepting the filings, and to ensure that all of the Department's residential mortgage provider licensees are registered on the NMLS, and thus available to the public through the NMLS Consumer Access searchable website.

#### Sections 1422.4.1 and 1950.122.12 - Share Arrangements

The SAFE Act and SB 36 provide that state and federal mortgage industry oversight regulatory officials may share information collected and channeled through the NMLS. The rules specify the various state and federal mortgage industry oversight agencies with whom information may be shared. These agencies include, but are not limited to, the California Attorney General, the U.S. Department of Justice, the U.S. Department of

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<sup>2</sup> Because the CRMLA deals with residential mortgage lending licenses and no other licenses as under the CFLL, the paper application process under the CRMLA as provided in former Section 1950.122 is repealed, and the new electronic application process is added under a new Section 1950.122. Under the CFLL, a new Section 1422.4 is added to provide for the new electronic application process. No changes are proposed to Section 1422, the paper application process for finance lenders and brokers not making or brokering residential mortgage loans.

<sup>3</sup> With respect to CFLL finance lenders, lenders and brokers not making or brokering residential mortgage loans will continue to file their paper license applications directly with the Department, and are not subject to the new requirements related to the use of the NMLS or the licensing of individual employees.

Housing and Urban Development, including the Federal Housing Administration, the Federal Consumer Financial Protection Bureau, the Federal Bureau of Investigation, state, local, and federal regulatory agencies, state attorneys general, and county district attorney's offices. The rules are necessary to clarify and provide notice regarding the different governmental agencies that the Department may communicate and share information with, such as enforcement actions and investigations related to lenders, brokers, servicers and mortgage loan originators.

#### Sections 1422.4.5 and 1950.122.15 – Request for Confidential Treatment

Sections 1422.4.5 and 1950.122.15 of the rules alert licensees to the procedures for a residential mortgage provider and mortgage loan originator to seek confidential treatment of certain documents or parts of the documents relative to the application or filings through the NMLS in accordance with Government Code Section 6254(d). The procedures can be found in Chapter 3, Title 10 of the California Code of Regulations Section 250.10.

#### Sections 1422.5 and 1950.122.4 – Application Process for Residential Mortgage Lenders, Brokers and Servicers

Under prior law, paper license applications were filed directly with the Commissioner. As required by SB 36 and the SAFE Act, Sections 1422.5 and 1950.122.4 of the rules require the filing of residential mortgage provider applications through the NMLS. Generally, these sections specify that the procedures are applicable to residential mortgage lenders, mortgage brokers, and mortgage servicers required to be licensed pursuant to Section 22100 of the CFLL and Section 50002 of the CRMLA. The regulations make changes only with respect to residential mortgage providers, and finance lenders not engaged in residential mortgage lending will continue to file applications directly with the Commissioner.

Subsection (a) of the rules sets forth the requirements for the application and specifies what information must be provided in the NMLS. The rules provide that applicants are to provide the information requested on the NMLS uniform forms, Forms MU1, MU2 and MU3. Form MU1 is the Uniform Mortgage Lender/Mortgage Broker Form, and this form is used by the NMLS for the licensure of a company engaged in the lending, brokering, or servicing of residential mortgage loans. Form MU2 is the Uniform Mortgage Biographical Statement & Consent Form, and this form is used by the NMLS for the reporting of background information on direct and indirect control persons of a company. Form MU3 is the Uniform Mortgage Branch Office Form, and this form is used by the NMLS for the reporting or licensure of branch offices of a company. The rules clarify requests for information within the NMLS forms that may be optional or dependent upon the requirements of the various jurisdictions, such as fictitious business names, website information, and financial statements, and further set forth licensure requirements unique to California. The rules are necessary to provide instruction on whether the information may be submitted through the NMLS or directly to the Department.

The rules are also necessary to specify the types of information that are required to be filed directly with the Commissioner, including the Department's Customer Authorization of Disclosure of Financial Records form, a detailed description of the applicant's business, evidence of a surety bond, fictitious business name documents, and other business organizational documents.

Finally, the rules require that the application be attested by a duly authorized individual who has filed a Form MU2 or who has been delegated to attest to the filing by an individual who has submitted a Form MU2. This provision is necessary to ensure that authorized individuals submit the application through the NMLS on behalf of residential mortgage providers.

Subsection (b) of the rules sets forth the filing fee requirements for applicants. Some filing fees are statutory and include application fees (\$200 under the CFLL, \$900 under the CRMLA), investigation fees (\$100), and fingerprint processing fees (\$20 per set, plus any fees required by the Department of Justice or the Federal Bureau of Investigation) related to fingerprint and background checks of the applicants. When applicable, these fees are required to be paid through the NMLS. The rules also provide that some fees may be required to be paid directly with the Commissioner until such time as the NMLS can accept the fees. The rules also specify that fees are not refundable. These provisions are necessary to clarify the fee requirements in the submission of applications to the Department.

Subsection (c) of the rules identifies when an application is complete. The rules specify that an application is not complete until all required fees, all required submissions, and the background and investigative reports are received by the Commissioner. Moreover, the regulations provide that the application may be considered withdrawn if not all required submissions are received within 90 days of a written notification of deficiency. These provisions are necessary for the Department to efficiently review the application within the statutory timeframe.

Subsection (d) of the rules provides instruction for the filing of an amendment to the application or licensure record, and provides that an applicant or licensee must follow the procedures in Sections 1409.1 and 1950.122.9 of the rules to report to the Commissioner changes to license or application information. This provision is necessary to provide applicants instruction on how to amend an application.

#### Sections 1422.6 and 1950.122.5 – Application Process for Mortgage Loan Originators

Sections 1422.6 and 1950.122.5 set forth application procedures for the licensure of mortgage loan originators under the CFLL and the CRMLA, respectively.

Subsection (a) requires that a licensed residential mortgage provider sponsor in the NMLS each mortgage loan originator employed by it. The adopted rules also provide that the residential mortgage provider proactively ascertain that the mortgage loan originator meets the qualification requirements of the rules regarding the licensure requirements generally, and the character, business reputation, and experience of the

individual, specifically. This provision is necessary to ensure that the residential mortgage provider has actively considered the qualifications of the mortgage loan originators that it sponsors.

Subsection (b) specifies that upon employment of a mortgage loan originator, the residential mortgage provider must ensure that a mortgage loan originator has filed Form MU4 (the Uniform Individual Mortgage License/Registration & Consent Form) in the NMLS and has obtained a license from the Commissioner. This provision is necessary to ensure that a residential mortgage provider only employs licensed mortgage loan originators for loan origination activities, as required by the SAFE Act.

Subsection (c) of the rules clarify that a mortgage loan originator sponsorship is not effective until the Commissioner affirmatively approves the sponsorship and issues the mortgage loan originator license. Furthermore, the rules specify that a sponsorship will not be approved unless the residential mortgage provider has obtained a license through the NMLS or transitioned its license onto NMLS. This provision is necessary to ensure that the Department is only licensing mortgage loan originators sponsored by licensed mortgage loan providers under the CFLL and the CRMLA, and to ensure the timely transition for existing licensees onto the NMLS.

Subsection (d) sets forth fee requirements for a mortgage loan originator license. The rules provide that the application fee is \$300 and the fee for the criminal history background check is \$20, and that both fees are required to be paid through the NMLS. The rules further clarify that the fees specified in the rules are in addition to any fees required by the NMLS, any other regulatory agency, or any other entity that may require the payment of fees in relation to the license application (such as, for example, education or test providers). These provisions are necessary to inform applicants of the fees charged by the Department and by NMLS with respect to the application process. The application fee was determined based on the number of applicants and the Department's experience with the workload necessary to license and regulate mortgage loan originators. The fee keeps a license in effect until December 31 of the year the license is issued. The \$300 application fee is necessary to support the administration of the licensing, regulatory, and enforcement program.

Subsection (e) clarifies that the application may be considered withdrawn if not all required submissions are received by the Commissioner within 90 days of a written notification of deficiency. This provision is necessary for the Department to identify abandoned applications and comply with the required statutory timeframes.

Subsection (f) prohibits a residential mortgage provider from allowing a mortgage loan originator to engage in mortgage loan originator activities if the mortgage loan originator's license or sponsorship has lapsed, unless reinstated. This provision is necessary to ensure that only licensed mortgage loan originators are engaged in mortgage loan originator activity, and to ensure that residential mortgage loan providers do not permit unlicensed mortgage loan originator activity under their authority of their licenses.

Subsection (g) requires a residential mortgage provider to require each mortgage loan originator it employs to file an amendment to the mortgage loan originator's Form MU4 within twenty days of any change in any of the licensure information contained in the form. This provision is necessary to ensure that the NMLS, which makes records available to the public, reflects only current information; that the Department's records are current and accurate; and that the CFLL and CRMLA mortgage loan providers have procedures to ascertain that employed mortgage loan originators maintain accurate license records with the Department.

Subsection (h) prohibits a mortgage loan originator from engaging in business under any name other than a name approved by the Commissioner for use by the residential mortgage provider employing the mortgage loan originator. This provision is necessary to ensure that the public is not misled or deceived about the identity of the mortgage loan provider or the mortgage loan originator's lack of authority to originate loans independent from the oversight of the mortgage loan provider sponsoring the mortgage loan originator. This provision is further necessary to ensure a supervisory relationship exists between the mortgage loan originator and the residential mortgage provider, and to ensure that sponsorships are not sold, leased, rented, franchised, or otherwise transferred in a manner that would permit the mortgage loan originator to evade the lending or brokering licensure requirement under the CFLL.

Subsection (i) provides that the residential mortgage provider is responsible for the acts and conduct of the mortgage loan originator until the sponsorship with the mortgage loan originator is terminated through the NMLS. The subsection further sets forth specific termination procedures and requires that the termination be reported by the residential mortgage provider within fifteen days after the termination of the mortgage loan originator. In addition, the subsection requires the mortgage loan originator to terminate a relationship with the mortgage provider through the NMLS within fifteen days of the termination, and prohibits a mortgage loan originator from originating loans if the mortgage loan originator does not have a sponsor. These provisions are necessary to ensure the timely reporting of sponsorship information so that the Department's records and the NMLS will accurately reflect whether a mortgage loan originator is authorized to engage in mortgage loan originator activities. Since the information provided to the NMLS is available to the public through the NMLS website, these provisions will assist in ensuring that the public is notified of a mortgage loan originator's current status, and will help to ensure that only licensed and sponsored mortgage loan originators are originating loans.

Subsection (j) sets forth the procedures for a sole proprietor mortgage loan originator. A sole proprietor must obtain a license as a residential mortgage provider through the filing of Forms MU1 and MU2 with the NMLS, and also must obtain a mortgage loan originator license by filing Form MU4 with the NMLS. These provisions are necessary to clarify how a sole proprietor complies with the requirement for licensure as a mortgage loan provider and a mortgage loan originator under the CFLL and the CRMLA.

### Sections 1422.6.1 and 1950.122.5.1 – Qualifications of Mortgage Loan Originator Applicants

Sections 1422.6.1 and 1950.122.5.1 of the rules clarify the minimum education and testing requirements for mortgage loan originators under the CFLL and the CRMLA. The rules provide that an applicant for a mortgage loan originator license must pass a test administered by the NMLS within a year of obtaining a license, and that the test will consist of a national and state component. The rules further provide that applicants must complete 20 hours of instruction, including 3 hours on federal law, 3 hours on ethics, and 2 hours on nontraditional mortgage products. The rules are necessary to implement SB 36 and the Federal SAFE Act and to set forth the time period for passing the test and obtaining a license.

### Sections 1422.6.2 and 1950.122.5.2 – Evidence of Financial Responsibility

Sections 1422.6.2 and 1950.122.5.2 of the rules clarify the requirements that the Commissioner may consider when evaluating whether a mortgage loan originator applicant has demonstrated financial responsibility, character, and general fitness to command the confidence of the community and to warrant a determination that the mortgage loan originator will operate honestly, fairly and efficiently. The rules provide that an applicant may be precluded from obtaining a mortgage loan originator license if his or her personal history includes any liens or judgments for fraud, misrepresentation, dishonest dealing or the mishandling of trust funds, or other liens, judgments, or financial or professional conditions that indicate a pattern of dishonesty. These provisions are necessary to inform the mortgage loan originator applicants that the credit report will be used to validate information provided by the applicant on his or her application for licensure.

### Sections 1422.6.3 and 1950.122.5.3 – Continuing Education and Renewal Procedures for Mortgage Loan Originators

The SAFE Act and SB 36 require that mortgage loan originator licenses be renewed on an annual basis. If the license is not renewed within the time prescribed, the license lapses or expires. Sections 1422.6.3 and 1950.122.5.3 of the rules provide that a mortgage loan originator with a lapsed or expired license may not engage in any business as a mortgage loan originator. The rules also specify that the renewal fee is \$300, and clarify the continuing education requirements of a mortgage loan originator when renewing a license. These rules are necessary to clarify the consequences of a lapsed or expired license, and to clarify the requirements for renewing a license. The licensing renewal fee is necessary to support the administration of the licensing and regulatory program.

### Sections 1422.7 and 1950.122.8 – Notices

Under current state and federal law, various written notices are required to be provided to the public when personal information is collected. Sections 1422.7 and 1950.122.8 of the rules incorporate the notices into the uniform applications that the residential



mortgage providers, control persons, and mortgage loan originators file electronically through the NMLS. The notices are required pursuant to the Information Practices Act of 1977 (California Civil Code Section 1798.17), Section 17520 of the Family Code (child support), and the Federal Privacy Act of 1974 (social security number). The rules are necessary to ensure that the notices are part of the licensure applications. Moreover, the SAFE Act requires that the NMLS collect social security numbers and other personal information from applicants. These rules are necessary to inform the applicants of the potential uses for the personal information provided to NMLS.

#### Sections 1422.7.1 and 1950.122.7 – Statement of Citizenship, Alienage, and Immigration Status

Under current state and federal law, to engage in business, only specified aliens are eligible to receive a license or certificate issued by the Department. (See Section 411 of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996 (Pub.L. No. 104-193), 8 U.S.C. Section 1621 et seq.) Current regulations clarify that individuals seeking various licenses are required to submit a Statement of Citizenship, Alienage, and Immigration Status form to establish eligibility to receive the license or certificate from the Department. The Department's rules extend the requirement to include mortgage loan originator applicants. These rules are necessary to comply with current state and federal law regarding the individuals that may be issued licenses from the Department.

#### Sections 1422.9 and 1950.122.10 – Expiration of Licenses

Existing law provides for residential mortgage provider licenses that are perpetual in nature, provided that a licensee complies with the requirements of the license. The residential mortgage provider licenses do not have an expiration date. However, SB 36 and the SAFE Act require mortgage loan originator licenses to be renewed on an annual basis. The Department regulations clarify that a residential mortgage provider license continues in effect until revoked or suspended by the Commissioner, or surrendered by the licensee, subject to surrender procedures under the rules. The rules further provide that mortgage loan originator licenses are not perpetual and must be renewed on an annual basis. These rules are necessary to clarify the terms of the licenses.

#### Sections 1422.10 and 1950.123 – Surrender of license

Current law provides that a licensee may surrender its license, but the surrender is not effective until approved by the Commissioner. Section 1422.10 and the changes to Section 1950.123 clarify that an application to surrender a license as a residential mortgage provider must be filed with the Department on the applicable Forms MU1, MU2, MU3, and MU4 through NMLS. These provisions are necessary to clarify the process for surrendering a license.

### Sections 1422.11 and 1950.122.5.4 – Reinstatement

Sections 1422.11 and 1950.122.5.4 of the rules specify that if a mortgage loan originator license is not renewed by December 31<sup>st</sup>, the license is considered lapsed and the licensee is not authorized to do business as a mortgage loan originator unless the license is reinstated. The rules further clarify how a mortgage loan originator license may be reinstated. In particular, the licensee must submit the request for reinstatement through NMLS after December 31<sup>st</sup> and before March 1<sup>st</sup>, and pay a reinstatement fee of \$100. Furthermore, all minimum requirements for license renewal, including education requirements and the payment of fees, including the renewal fee of \$300, must be satisfied.

The regulations also clarify that if the mortgage loan originator license has expired and reinstatement has not taken place, the mortgage loan originator must apply for a new license. These regulations are necessary to clarify the reinstatement requirements of lapsed mortgage loan originator licenses, and are consistent with the functionality of NMLS.

### Sections 1422.12 and 1950.122.11 - Challenge Process

The SAFE Act and SB 36 require that state licensing authorities provide applicants and licensees the ability to challenge the accurateness of information that is entered into and maintained by NMLS. Sections 1422.12 and 1950.122.11 set forth a process to comply with this requirement. The Department's challenge process is patterned after California Penal Code Section 11126, administered by the Attorney General's Bureau of Criminal Identification and Information, regarding criminal background check information. The rules outline the process for a licensee to challenge the information contained in NMLS, and require the Commissioner to review the challenge and issue a finding.

The SAFE Act also requires that the challenge process comport with due process requirements. Consequently, the rules provide that the licensee or applicant may, subject to the procedure specified, seek judicial review of the Commissioner's finding pursuant to the Administrative Procedure Act, Section 11523 of the Government Code. The rules are necessary to prescribe a fair process for applicants to challenge information in the NMLS through the Department.

## B. Changes Common to Both CFLL and CRMLA Regulations

### Sections 1404 and 1950.003 – Definitions

Sections 1404 and 1950.003 clarify and define some terms used in the regulations, such as "NMLS," "MU1," "MU2," "MU3," "MU4," and "to sponsor." With respect to the CFLL, where licensees can make or broker many types of loans beyond residential mortgage loans, the term "mortgage lender, mortgage broker, or mortgage lender and broker" is defined as those finance lenders who make, broker, or service residential

mortgage loans and who are required to be licensed under the CFLL. The definitions are necessary in order to define the lenders and brokers required to participate in NMLS.

#### Sections 1409 and 1950.122.2.1 – List of Officers, Directors, and Other Control Persons

Under current Section 1409 of the rules, a finance lender is required to file a list of officers, directors, and other control persons with the Department and to report any change with respect to the information within thirty days from the date of the change. Section 1409 is amended to provide that a mortgage lender, broker, and mortgage lender and broker must maintain a record of its officers, directors, and other control persons through the NMLS, and to file any amendments to the change in information regarding those control persons through the NMLS within 30 days of the change. Section 1950.122.2.1 requires a residential mortgage provider under the CRMLA to file a similar list of officers, directors, and other control persons with the Commissioner through NMLS, and to file amendments upon changes to the information. These provisions are necessary to ensure that the NMLS has current information about control persons of licensees, and that the public has access to current information about control persons of licensees through the NMLS.

#### Sections 1409.1 and 1950.122.9 – Notice of Changes

Current regulations require licensees to provide the Commissioner a notice of change in the information contained in an application for licensure. Sections 1409.1 and 1950.122.9 require residential mortgage providers and mortgage loan originators to make any changes in the information contained in the application promptly. Amendments are required to be filed through the NMLS or, if changes cannot be submitted through the NMLS, directly with the Commissioner. The notice of change in information extends to the employment of new mortgage loan originator employees in California, and any termination of employment of mortgage loan originator employees.

With respect to mortgage loan originators, the rules clarify that a mortgage loan originator must make the required changes in NMLS within twenty days of the changes to the information, and may not renew his or her license unless the Form MU4 has been amended. Furthermore, the rules require that upon discovery that a sponsored mortgage loan originator has not filed an amendment to his or her Form MU4, a residential mortgage provider must make a demand upon the mortgage loan originator to make the change. If the change is not made within five days from the date of the demand, the residential mortgage provider is required to inform the Commissioner, in writing.

These regulations are necessary to require applicants and licensees to keep their NMLS records current, since the NMLS is a real-time system where the information may be viewed and acted upon by multiple regulatory jurisdictions and the public at the same time. Moreover, these rules are necessary to ensure that residential mortgage providers are responsible for ascertaining that sponsored mortgage loan originators keep their licensure information current.

### Sections 1411 and 1950.316 - Disciplinary Actions

Existing Section 1411 requires that a finance lender report to the Commissioner any criminal action filed against it or its directors, officers, or management. The rules amend Section 1411 to require that a residential mortgage provider report changes in criminal, regulatory, and civil action and other information contained in the application, through the NMLS on Forms MU1, MU2, MU3, and MU4, as applicable. Current Section 1950.316 requires a residential mortgage provider to report to the Commissioner any civil, criminal, or disciplinary action against the mortgage provider or any of its controlling persons, including specified employees. The amendments extend the reporting requirement to mortgage loan originators with regard to civil, criminal or disciplinary action. The rules require the civil, criminal, or disciplinary actions be reported by amendment to the applicable uniform form through the NMLS. These changes are necessary to ensure that disciplinary actions are reported to the Commissioner and the NMLS.

### Sections 1414 and 1950.122.6 – Supervision of Mortgage Loan Originators

Under both SB 36 and the SAFE Act, residential mortgage providers are required to supervise their sponsored mortgage loan originators. Sections 1414 and 1950.122.6 of the rules require residential mortgage providers to exercise diligent supervision over the mortgage loan origination and lending activities of their sponsored mortgage loan originators, and to establish and enforce written procedures for the supervision of their loan origination and lending activities. The rules provide that every mortgage loan originator must be subject to the supervision of a branch manager. Every branch manager is required to be identified on the Form MU3 in the NMLS, and required to file a Form MU2 in the NMLS. The rules further require a provider to designate an individual to supervise the activities of the branch managers, and to periodically inspect each business office to ensure that the written procedures are enforced. If there are no branches, the rules provide that a supervisor would directly supervise and review the activities of the mortgage loan originator. The rules also require a licensee to maintain the written procedures as part of the books and records of the licensee at each business office.

The rules are necessary to ensure that residential mortgage providers maintain and implement procedures for the supervision of mortgage loan originators, while allowing the residential mortgage providers flexibility in determining the internal procedures that adequately accommodate their business models.

### Sections 1424 and 1950.122.4.1 - Branch Office Instructions

Current law and regulations provide specific requirements for finance lenders that seek to do business at additional, or branch locations (See Section 1423 of these rules). The rules clarify the procedures for the submission of a branch application for a residential mortgage provider. Specifically, the regulations require that the Form MU3 (Uniform Mortgage Branch Office Form) be filed through NMLS for each location, and Form MU2 (Biographical Statement & Consent Uniform Mortgage Lender/Mortgage Broker Form)

be filed by the branch manager. The regulations continue to require that every branch office of a CFLL licensee be separately licensed, as required by statute. Section 1424 retains the restriction on a branch manager managing more than one location (see existing CFLL Short Form Application in Section 1423 of these rules).

These provisions are necessary to set forth new procedures and requirements for branch office locations when filing through the NMLS.

#### Sections 1430.5 and 1950.307 – Reports of Condition

Existing law provides that residential mortgage providers are required to file an annual report with the Commissioner, and SB 36 provides the Commissioner with authority to require residential mortgage providers to submit to the NMLS reports of condition (call reports). The amendments clarify that residential mortgage providers must file the call report through the NMLS for transmission to the Commissioner.

Furthermore, the regulations require that a mortgage loan originator ensure that all residential mortgage loans that close pursuant to his or her loan origination activities be included in the call report of his or her employer. This requirement is consistent with the draft regulations published by HUD which require that “[t]he supervisory authority must require a loan originator to ensure that all residential mortgage loans that close are included in reports of condition submitted to the NMLSR.” (See Section 3400.111(f), Federal Register, Vol. 74, No. 239, p. 66559.)

These provisions are necessary to implement Section 1505 of the SAFE Act, which requires the submission of reports of condition to the NMLS.

#### Sections 1433 and 1950.209 – Unique Identifier Numbers

Current rules under the CFLL provide specific requirements for forms, such as minimum font size. Moreover, Section 1433 of the rules provides that a finance lender may not use a loan form that the Commissioner objects to. SB 36 requires mortgage loan application forms and advertisements, among other things to include the unique identifier number of the mortgage loan originator.

The changes to Section 1433 and the adoption of Section 1950.209 conform SB 36 by providing that mortgage loan originators and residential mortgage providers must include unique identifier numbers on specified documents and advertising used by the residential mortgage provider and mortgage loan originator. These provisions are necessary to conform to the SAFE Act and to ensure that the public and regulators can determine the licensure status and disciplinary history of persons making residential mortgage loans and providing services.

#### Sections 1436 and 1950.314.8 – Nontraditional and Adjustable Rate Mortgage Products

Existing rules set forth requirements for licensees related to nontraditional and adjustable rate mortgage products. Existing Sections 1436 and 1950.314.8 require licensees to: (1) implement best practices, as defined, on a continuous basis; (2) report

annually to the Department on whether they have made or arranged nontraditional and adjustable rate mortgage products, whether they have implemented risk-management best practices, whether they have put into place internal controls or procedures, as specified, and the number of any consumer complaints; (3) maintain specified documentation as part of their books and records; (4) provide clear disclosures for nontraditional and adjustable rate loans, as specified; and (5) prohibit certain false, misleading, and deceptive advertising.

Both rules are amended to (1) require that all mortgage loan originators follow the best practices developed by their employers, (2) make technical and grammatical changes, and (3) extend the books and records requirements contained in current regulation regarding annual financial reports, to also apply to reports of condition (call reports).

With respect to Section 1436, since non-residential finance lenders are not subject to the requirements of the Guidance, the changes to the rule remove references to “finance lender” and replace them with “mortgage lender, broker, and mortgage lender and broker.”

The amendments are necessary to clarify that the Guidance is applicable only to residential mortgage loan providers. Moreover, the changes are needed to ensure that mortgage loan originators are expressly required to follow their sponsors’ best practices with respect to nontraditional and subprime mortgage lending.

#### Sections 1437 and 1950.205.1 – Surety Bond

The SAFE Act requires that states establish minimum net worth or surety bond requirements based on the total aggregate value of residential mortgage loans originated by the company, or the establishment of a recovery fund option.

#### Section 1437 - CFLL

The CFLL requires that a finance lender that does not make residential mortgage loans and does not employ one or more mortgage loan originator maintain a \$25,000 surety bond, as a condition to licensure. SB 36 provides that the Commissioner may establish higher amounts by regulation. The purpose of the surety bond is for the recovery of expenses, fines, and fees levied by Commissioner or for losses or damages incurred by borrowers or consumers as the result of a licensee’s noncompliance with the law. The law provides that the Commissioner may require a higher bond amount or a new bond if an action is commenced. Based on an evaluation of total aggregate residential loan values reported by current licensees for purposes of the 2008 annual report (loan values for 2007), the Department added four graduated surety bond levels: \$25,000 for aggregate loans of \$1,000,000 or less; \$50,000 for aggregate loans of \$1,000,001 to \$50,000,000; \$100,000 for aggregate loans of \$50,000,001 to \$500,000,000; and \$200,000 for aggregate loans greater than \$500,000,001.

## Section 1950.205.1 - CRMLA

The CRMLA also requires that mortgage providers subject to the CRMLA maintain a minimum \$50,000 surety bond. SB 36 allows the Commissioner to prescribe higher surety bond requirements based on the aggregate mortgage loan amounts originated by mortgage loan originators of the mortgage provider. The Department requires bond amounts which are similar to bond amounts for residential mortgage providers under the CFLL. Therefore, the surety bond amounts required are \$50,000 for aggregate loans equal to or less than \$50,000,000; \$100,000 for loans between \$50,000,001 to \$500,000,000; and \$200,000 for loans greater than \$500,000,001.

Both rules provide that a residential mortgage provider applicant with no operating history must make a good faith estimate of the loans anticipated to be originated in the upcoming year to determine the bond amount. The graduated bonding level is necessary to ensure the bond amount bears a relationship to the aggregate residential loans made by a licensee, to ensure that levels are staggered in a manner that does not cause unnecessary fluctuation in a licensee's established minimum bonding amount, and to comply with the SAFE Act.

## Sections 1557 and 1950.204.4 – Blind Advertising

Under current rules, "blind" advertising is prohibited. "Blind" advertising is defined as advertising that gives insufficient contact information or misleading information. Both Sections 1557 and 1950.204.4 are amended to prohibit mortgage loan originators from using such potentially false, misleading, and deceptive advertising. The provisions are necessary to clarify what "blind" advertising is, so that licensees can understand and guard against the practice as they implement the SAFE Act requirements on an ongoing basis.

## C. Amendments Specific to CFLL Regulations

### Section 1431 – Special Report

Current regulation provides that if the Commissioner requires a special report from a CFLL licensee, that report is to be signed by an authorized officer of the corporation, among other specified persons. However, the rule fails to account for all of the different types of business entities that may form a finance lender under the CFLL. Therefore, Section 1431 is amended to clarify that the special report shall be signed by an authorized officer of any type of business entity that can be licensed as a CFLL.

### Section 1454 – Statement of Loan Documents

Current regulation prescribes the form and content of loan documents to be used in finance lender transactions. The amendments to the rule provide that any statement of loan form used by a mortgage lender, broker, mortgage lender and broker, or mortgage loan originator must include the unique identifier number. This clarification is necessary to comport to the SB 36 requirement that a mortgage loan originator's unique identifier number be placed on forms and other documents.

### Section 1550 - Advertising

Current regulation requires a finance lender to provide advertisements to the Commissioner for review. A finance lender may use an advertisement only after having been notified in writing that the advertisement has not been disapproved. However, Senate Bill 1146 (Chapter 640, Statutes of 2010) amends the law, operative January 1, 2011, to require the Commissioner to issue an order to require a finance lender to submit advertising to the Commissioner for approval. Consequently, Section 1550 of the rules is amended to strike the current requirement that all advertising be submitted to the Commissioner for review prior to its use.

Instead, the amendments clarify that any advertisement used by a licensed mortgage lender, broker, mortgage lender and broker, or mortgage loan originator is required to indicate the unique identifier number of the licensee. This requirement is necessary to conform the rules to the requirements of SB 36.

### Section 1552 – Advertising Copy

Current regulation requires a finance lender to maintain all advertising copy for at least ninety days after the last date of its use. However, Senate Bill 1146 (Chapter 640, Statutes of 2010) amended the law, operative January 1, 2011, to require that advertising be maintained for two years. The amendments to the rule reflect the two year retention requirement, and require a residential mortgage provider to retain the advertising of its sponsored mortgage loan originators. The amendments are necessary to conform to both SB 1146 and SB 36.

### D. Amendments Specific to the CRMLA

#### Section 1950.122.2 – Notice of Officers, Directors, and Control Persons

Under current Section 1950.122.2 of the CRMLA rules, a residential mortgage provider is required to file a specified notice with the Commissioner with information regarding officers, directors, partners, and other control persons. This notice must be filed with the fingerprint application and fees for purposes of a background check of such control persons by the California Department of Justice pursuant to Section 50317 of the Financial Code.

The NMLS does not currently provide the capability to process fingerprint information of officers, directors, and other control persons for purposes of criminal history background checks. Therefore, it is necessary to specify that such control persons of mortgage loan providers must continue to submit the notice and application directly to the Department.

#### Section 1950.204.3 – Prohibited Advertising

Current regulation prohibits a residential mortgage provider from specified types of advertising and requires that all providers refer to their license in any written, printed, or communicated advertisements. The amendments to the rule extend the requirements



of the rule to mortgage loan originators. These amendments are necessary to ensure that any advertising by a mortgage loan originator identifies the mortgage loan originator's license information.

#### Section 1950.301 - Fingerprinting

Current regulation provides that if an employee of a licensee who is prohibited from employment causes the loss of trust funds, the Commissioner may request a Statement of Identity and Questionnaire, a Notice of Officers, Directors, and Control Persons in accordance with Section 1950.122.2, and fingerprints from all other employees of the licensee in order to determine whether other prohibited individuals are employed by the licensee. The amended rule provides that the Commissioner may request a Form MU2 in lieu of a Statement of Identity Questionnaire. This provision is necessary to clarify that individuals need not submit the duplicative information in both paper format and electronically through the NMLS, but rather, filing the information through the NMLS is the preferable method for submission of information to the Department.

#### Section 1950.317 – Report of Defalcation

Current regulation requires a residential mortgage provider to report any defalcation, embezzlement, or theft to the Commissioner. The amendments to the rule extend the requirement for reporting to include mortgage loan originators. This rule is necessary to ensure that mortgage loan originators are also responsible for reporting theft to the Commissioner.

#### DETERMINATION GOVERNMENT CODE SECTION 11346.9(a)(2)

The Commissioner has determined that the adoption of the regulation does not impose a mandate on local agencies or school districts, which require reimbursement pursuant to Part 7 (commencing with Section 17500) of Division 4 of the Government Code.

#### INCORPORATION BY REFERENCE

The following document is incorporated by reference in the regulation text:

Customer Authorization for Disclosure of Financial Records form MBL 1950.122B (Rev. 02/01).

The size and format of this document, as well as the propensity for the document to affect the clarity of the regulation text, result in it being impractical and cumbersome to publish this document in the California Code of Regulations. The Department of Corporations has made the document available upon request, and further the document is available on the Department's website at [www.corp.ca.gov](http://www.corp.ca.gov).

## ALTERNATIVES CONSIDERED

The regulations implement the federal SAFE Act and SB 36, which require that all mortgage loan originators be licensed through the NMLS. Therefore, no alternatives to this process were considered. The Department considered not requiring the sponsors of mortgage loan originators to transition onto the NMLS. However, this consideration proved impractical and burdensome to licensees and the Department, and disregarded the benefits of an electronic national licensing depository. Therefore, the alternative was rejected. Under Government Code Section 11342.610(b), residential mortgage lending activities are not within the definition of small business, and therefore no alternatives were considered that would specifically lessen the impact of the regulations on small business.

## ADDENDUM, REGARDING PUBLIC COMMENTS

No request for hearing was received during the 45-day public comment period, which ended on January 24, 2011. Accordingly, no hearing was scheduled or held.

## COMMENTS RECEIVED

### 1. Invitation for Comments and Emergency Regulation

The initial draft regulations that the Department requested comments on were similar to the rules ultimately adopted, and included sections on definitions, the application, the application forms, and education requirements. The initial draft regulations, dated February 22, 2010 are hereby incorporated by reference. In response to this invitation the Department received one letter during the invitation for comments period prior to the promulgation of the emergency regulation.<sup>4</sup>

On March 17, 2010 the Department released revised regulations on its website, electronically and by mail to interested parties. The revised regulations are incorporated by reference. The Department received additional comments from the California Mortgage Bankers Association, K&L Gates law firm, and DHI Mortgage. After reviewing and considering these comments, additional changes were made to the emergency regulations and on March 23, 2010, they were filed with the Office of Administrative Law. With minor changes, the Office of Administrative Law approved the regulations and filed them with the Secretary of State on April 1, 2010.

The commentors noted concerns regarding branch requirements, termination procedures, and unique identifier requirements, among other things. All three commentors stated that the proposed rule requiring an onsite branch manager for each branch location CRMLA was burdensome and onerous.<sup>5</sup> One commenter requested that the Department reconsider the new requirement that CRMLA licensees not be required to register its

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<sup>4</sup> See the March 8, 2010 letter from Susan DeMars, Executive Director of the California Mortgage Bankers Association. Because many of the comments were similar to a subsequent letter dated March 30, 2010 after the emergency regulation comment period, the comments are summarized together infra.

<sup>5</sup> See March 29, 2010 letter from Mr. Costas Avrakotos, K&L Gates; March 25, 2010 letter from Craig Pizer of DHI Mortgage; and the March 30, 2010 letter from Susan DeMars, Executive Director of the California Mortgage Bankers Association.

branch office through the NMLS but rather requested that CRMLA licensees submit its branch office notice directly to the Commissioner through the mail.<sup>6</sup> For consistency, uniformity, and workload reasons, and because SB 36 specifically authorizes the Commissioner to "...require an applicant or licensee to make some or all filings...through the [NMLS]", the Department is requiring that both CRMLA and CFLL mortgage providers file branch application forms through the NMLS.<sup>7</sup>

The commentors also commented that under the proposed branch manager CRMLA regulations, disallowing an individual from managing multiple locations was too onerous, especially for single-person branch offices. To address their concerns, the Department amended the proposed emergency regulation with respect to the CRMLA only, to delete the requirement that an individual could not manage multiple locations. Under the CFLL, the Department retained this requirement, as it is an existing regulatory requirement for all finance lender and broker licensees, not only mortgage providers.<sup>8</sup>

The California Mortgage Bankers Association commented that requiring an MLO's unique identifying number be included on all documents related to a residential mortgage loan was too broad. Accordingly, the Department provided that an MLO's unique identifier be shown on residential mortgage loan application forms, solicitation, and advertisements.

The California Mortgage Bankers Association also commented that the proposed time of five days to provide notice to the Department that a mortgage loan originator was being terminated was not sufficient. Therefore, the Department amended the regulation to require that the mortgage provider terminate the sponsorship and mortgage loan originator terminate the relationship within 15 days after the termination of the individual.

Upon consideration of all of the comments, the rules were amended to incorporate many of the changes recommended by interested parties. However, not all of the recommendations were incorporated into the rules. In incorporating recommendations, the Department attempted to balance the competing goals of encouraging as many mortgage providers as possible to transition onto the NMLS system, while at the same time facilitating the orderly licensure of mortgage loan originators in an efficient manner, given the federally-imposed deadline of July 31, 2010. Moreover, the Department tried to weigh and balance the changes to the regulations under both the CRMLA and the CFLL. Although both these laws have similarities, there are many differences which the Department attempted to balance with the requirements of the Federal SAFE Act. The main difference being that the CFLL requires the regulation of many types of loan providers, not just residential mortgage loan providers.

## 2. 45-Day Public Comment Period

The Department did not receive comments during the 45-day public comment period.

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<sup>6</sup> See March 29, 2010 letter from Mr. Costas Avrakotos.

<sup>7</sup> See Financial Code Sections 22102(a), 50120(f) and 50130(i).

<sup>8</sup> The Department also received a follow-up email from Ms. Patricia J. Williams, DHI Mortgage on April 21, 2010 regarding the onsite branch manager requirements.

### 3. 15-Day Comment Period

The Department included a supplement to the Initial Statement of Reasons to the rulemaking file to clarify the necessity of the \$300 application fee, and a Notice of a 15-Day Public Comment Period was posted and mailed. No written comments were received during the 15-day public comment period, which ended on February 9, 2011.

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