

Date of Hearing: April 15, 2024

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Timothy Grayson, Chair

AB 3108 (Jones-Sawyer) – As Amended March 21, 2024

SUBJECT: Business: mortgage fraud

SUMMARY: Expands the situations under when person may be convicted of mortgage fraud and prohibits a person who originates a covered loan under the Covered Loan Law from committing mortgage fraud to avoid complying with specified rules.

Specifically, **this bill:**

- 1) Expands the types of situations when a person may be convicted of mortgage fraud to include the following:
 - a) When a broker or MLO instructs or otherwise causes a borrower to sign a document in conjunction with a loan, including a declaration of non-owner occupancy and a declaration of business purpose of loan proceeds, with the knowledge that the document contains information the broker or MLO knows to be a material misstatement, misrepresentation, or omission.
 - b) When a broker or MLO causes a lender to finance a loan transaction with actual knowledge that the loan application or other documents signed in conjunction with the loan contain a material misstatement, misrepresentation, or omission.
- 2) Prohibits a person who originates a covered loan under California’s Covered Loan Law (Law) from avoiding, or attempting to avoid, certain provisions of the Covered Loan Law by committing mortgage fraud, and applies this prohibition retroactively to any document signed on or after January 1, 2020.

EXISTING LAW:

Financial Code

- 1) Establishes the Covered Loan Law, which prohibits lenders who make “covered loans,” as defined, from engaging in prohibited acts (Financial Code Section 4970 et seq.).
- 2) Includes in the list of “prohibited acts” when a person who originates a covered loan shall from avoiding, or attempting to avoid, the application of the Covered Loan Law by doing the following:
 - a) Structuring a loan transaction as an open-end credit plan for the purpose of evading the provisions of this division when if the loan would have been a covered loan if the loan had been structured as a closed end loan.
 - b) Dividing any loan transaction into separate parts for the purpose of evading the provisions of the Covered Loan Law.

Penal Code

- 1) States a person commits mortgage fraud if, with the intent to defraud, the person does any of the following:
 - a) Deliberately makes any misstatement, misrepresentation, or omission during the mortgage lending process with the intention that it be relied on by a mortgage lender, borrower, or any other party to the mortgage lending process.
 - b) Deliberately uses or facilitates the use of any misstatement, misrepresentation, or omission, knowing the same to contain a misstatement, misrepresentation, or omission, during the mortgage lending process with the intention that it be relied on by a mortgage lender, borrower, or any other party to the mortgage lending process
 - c) Receives any proceeds or any other funds in connection with a mortgage loan closing that the person knew resulted from a violation of paragraph (a) or (b)
 - d) Files or causes to be filed with the recorder of any county in connection with a mortgage loan transaction any document the person knows to contain a deliberate material misstatement, misrepresentation, or omission (Penal Code Section 532f).

FISCAL EFFECT: Unknown. This bill is keyed Fiscal by Legislative Counsel.

COMMENTS:1) **Purpose.**

According to the author's office:

Predatory lending has evolved since the subprime mortgage crisis of 2008, but the statute has remained the same. Predatory brokers have developed new tactics to target vulnerable Californians and evade prosecution. Victims of predatory lending are almost always people of color, immigrants, the elderly, and low income households who lose everything when they are misled into a loan they can't afford. AB 3108 seeks to address current and future predatory mortgage lending by clarifying that a loan originator who knowingly causes a borrower to sign a loan or document containing misleading statements is committing mortgage fraud. In doing so, this bill helps attorneys better protect victims of predatory lending and prosecute predatory brokers.

2) **Background: Relevant licensing laws**

AB 3108 amends the Covered Loan Law, discussed in greater detail in Comment #3 below, which can apply to companies operating under a number of existing licensing laws. Those laws include:

- ***California Financing Law (CFL)***. The CFL licenses and regulates finance lenders and brokers making and brokering consumer or commercial loans. The CFL prohibits misrepresentations, fraudulent and deceptive acts, and provides a range of administrative,

civil and criminal remedies for violations of the law. CFL licensees can make unsecured or secured loans, and a secured loan may be secured by personal or real property.

- ***Real Estate Law (REL)***. The REL, administered by the Department of Real Estate (DRE), requires the licensure of real estate brokers and real estate persons, some of whom may also have a mortgage loan originator endorsement that allows the licensee to originate residential mortgage loans.
- ***California Residential Mortgage Lender Act (CRMLA)***. The CRMLA was enacted in 1994 to establish an alternative to the REL and the CFL. The primary purpose of the CRMLA is to provide mortgage bankers with a licensing law more appropriately tailored to their primary functions of originating and servicing residential mortgage loans.

The CRMLA authorizes licensees to make federally related mortgage loans, to make loans to finance the construction of a home, to sell the loans to institutional investors, and to service such loans. Licensees may purchase and sell federally related mortgage loans or act as a servicer of those loans.

Moreover, a CRMLA licensee may provide brokerage services to a borrower, by attempting to obtain a mortgage loan on behalf of the borrower from an institutional lender. Employees who engage in brokering activities on behalf of the CRMLA licensee must be licensed mortgage loan originators employed by the licensee.

3) **Background: California's Covered Loan Law.**

In 2001, the California Legislature passed AB 489 (Migden), Chapter 732, Statutes of 2001 to curb predatory practices in real estate lending. AB 489 was a response to a number of disturbing practices affecting primarily low-income borrowers, including loan flipping (where an originator would refinance the loan repeatedly in a short period, charging prepayment penalties each time), excessive fees that were not properly communicated to the borrower, lending without the ability to repay, and outright fraud and abuse.

The Covered Loan Law applies to a consumer loan that meets a number of specific and narrow criteria. The consumer loan must be secured by a residential property used or intended to be used as consumer's principal dwelling unit, cannot exceed the most current conforming loan limit established by the Federal National Mortgage Association (roughly \$767,000 in 2024) and must meet one of the following two criteria:

- a) For a mortgage or deed of trust, the annual percentage rate (APR) at consummation of the transaction will exceed by more than eight percentage points the yield on Treasury securities having comparable periods of maturity.
- b) The total points and fees payable by the consumer at or before closing for a mortgage or deed of trust will exceed 6 percent of the total loan amount.

The of "consumer loan" also excludes a number of other products, including reverse mortgages and so-called "bridge loans," which are short-term loans designed for those who are purchasing a new primary residence and need temporary funding to help finance that purchase while they sell their existing home.

Because of the narrow definition of “consumer loan,” it is unclear how meaningful the law’s protections are for California borrowers. Even at the time of AB 489’s passage, it was understood as applying to only a small subset of overall real estate lending and exclusively to the most predatory practices embraced by the subprime lenders. To the Legislature’s credit, it identified major issues in the subprime lending market quite early and attempted to address them through AB 489, even though many of those problems would continue to fester until the 2007-08 financial crises. Today, to the extent there are still lending products out in the market that are covered by this area of law, these products are likely very high cost and far out of step with mainstream lending options.

Despite its limited scope, the Covered Loan Law contains robust enforcement mechanisms. It specifies that any licensee under the CFL, REL, the CRMLA, or under the Financial Institutions Law that violates the Covered Loan Law’s provisions shall be deemed to have violated their respective licensing law. There is also a cause of action for “actual damages” suffered, and it makes a provision in a contract unenforceable if it violates specified provisions.

4) **What is AB 3108 in response to?**

AB 3108 is inspired by instances when a lender tricks or otherwise deceives a homeowner into taking out a high-cost, short-term loan supported by improper or misleading documentation. Supporters argue that in such cases, a lack of clarity in statute makes it difficult for victims to find recourse.

In one example provided to committee staff, an elderly homeowner contacted a nonprofit advertising mortgage payment relief for help with his mortgage, which he was struggling to make payments on. This nonprofit promised the victim he could save his home through a reverse mortgage. However, the organization connected the senior to a short-term loan that he did not understand and had no ability to pay, resulting \$65,000 in up-front originated fees with a \$300,000 balloon payment after the end of the loan’s one-year term.

The above case is so obviously problematic and predatory, it is unclear how it was able to happen in the first place. According to legal aid attorneys, one strategy being deployed by unscrupulous actors is having the loan described as a “bridge loan” in accompanying documentation, thus ensuring the loan is not covered by existing consumer protection laws. A bridge loan is a short-term loan used to construct or purchase a new home while the existing home is being sold, and in this case the broker convinces the homeowner to sign a document saying the homeowner does not live at the property. The broker will also list the borrower’s primary residence as a different address to give the impression that the loan will be used to secure a new primary residence.

AB 3108 expands the scenarios in which a person could be charged with mortgage fraud to include situations like the above. In these cases, the mortgage broker uses misleading documentation to help deliver the predatory loan to the borrower, such as a “declaration of non-owner occupancy.” Importantly, AB 3108’s changes to the Penal Code apply to brokers and mortgage originators. The sponsor argues this is necessary because the existing provisions related to mortgage fraud may not be used to consider fraud originating from these entities.

Moreover, AB 3108 modifies the Covered Loan Law to ensure that it applies consumers who are steered by loan brokers into loans not typically covered by the law's provisions. This would help ensure that, at a minimum, the Covered Loan Law's existing enforcement provisions could apply in these cases.

5) Double referral

AB 3108 is also referred to the Assembly Committee on Public Safety, where it will be heard if and when AB 3108 advances from this committee.

REGISTERED SUPPORT / OPPOSITION:

Support

Support

Consumer Federation of California (Sponsor)
California Advocates for Nursing Home Reform
California Elder Justice Coalition (CEJC)
Elder Law & Advocacy
Housing and Economic Rights Advocates (HERA)
Justice in Aging
National Association of Consumer Advocates (NACA)
National Housing Law Project
Public Law Center
Rise Economy

Opposition

None on file

Analysis Prepared by: Luke Reidenbach / B. & F. / (916) 319-3081