



REGULATORY AGENCY ACTION

garding a nonprofit consumer group to represent consumers in insurance matters).

The industry primarily argues that the initiative is facially unconstitutional in that it fails to expressly set forth rate standards which will guarantee insurance companies a fair rate of return on their investment, and administrative procedures through which aggrieved insurers may seek effective relief from the 20% rate rollback and one-year rate freeze provisions of Proposition 103. The industry relies heavily on *Birkenfeld v. City of Berkeley*, 17 Cal. 3d 129 (1976), a case in which the city's rent control ordinance was invalidated. There, the Court found that landlords were deprived of due process because the part-time, five-member rent control board created by the ordinance was inundated with over 16,000 applications for rate exemptions, and lacked any regulatory authority to streamline the exemption procedures into an effective, manageable system.

Respondents (Attorney General John Van de Kamp and the State Board of Equalization) and Real Parties in Interest (proponents of Proposition 103) argue that the new statute is not required to set forth detailed standards and procedures for regulations. Rather, the statute leaves such rulemaking to the appropriate entity: the Insurance Commissioner, who is fully empowered to and (with over 500 employees) capable of adopting implementing regulations to streamline the exemption hearing process. Along with the filing of the responsive briefs of Respondents and Real Parties in Interest, several consumer groups— including Consumers Union and the Center for Public Interest Law— petitioned the Commissioner to engage in rulemaking to implement the effective provisions of Proposition 103, and also preparatory rulemaking to implement the rollback/freeze provisions once the stay imposed upon them is lifted.

Governor Deukmejian and Commissioner Gillespie, named as respondents in the action, have declared themselves neutral on the merits of the case. All briefing in the case has concluded; the Supreme Court set oral argument for March 7.

Antitrust Suit. The Attorneys General of eighteen states are pursuing the suit they have filed against 32 insurance companies and underwriters. The suit alleges that the companies used threats and boycotts to increase the cost and limit the availability of liability insurance to public agencies, businesses, and nonprofit organizations, as well as elimin-

ate coverage for long-term pollution damage. (See CRLR Vol. 8, No. 4 (Fall 1988) p. 87 and Vol. 8, No. 3 (Summer 1988) p. 91 for background information.)

In December, the insurers involved in the suit filed five motions for dismissal, asserting in one that their actions were merely "an agreement on policy terms" and not a boycott. Under the terms of the McCarran-Ferguson Act, insurance companies are exempted from most of federal antitrust law. The Act, however, provides for an exception in the case of insurance boycotts, eliminating immunity for those actions.

In another motion, the insurers allege that since insurance regulatory agencies "held and exercised ultimate control over the policy forms and their contents" in the various states now suing, the states have no valid cause of action.

The states claim that the insurers changed the customary "occurrence" form of insurance offered to their customers to a "claims-made" form. The change resulted in a shift from coverage of all accidents that occur while a policy is in effect, regardless of when the claim was filed, to a system that compensates losses that occur and are claimed while the policy is in effect.

The states have until April 28 to respond, and a hearing on the insurers' motions is set for July 7.

DEPARTMENT OF REAL ESTATE

Commissioner: James A. Edmonds, Jr.
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The Real Estate Commissioner is appointed by the Governor and is the chief officer of the Department of Real Estate (DRE). The commissioner's principal duties include determining administrative policy and enforcing the Real Estate Law in a manner which achieves maximum protection for purchasers of real property and those persons dealing with a real estate licensee. The commissioner is assisted by the Real Estate Advisory Commission, which is comprised of six brokers and four public members who serve at the commissioner's pleasure. The Real Estate Advisory Commission must conduct at least four public meetings each year. The commissioner receives additional advice from specialized committees in areas of education and research, mortgage lending, subdivisions and commercial and business brokerage. Various subcommittees also provide advisory input.

The Department primarily regulates two aspects of the real estate industry: licensees (as of September 1988, 216,365 salespersons, 90,211 brokers, 17,332 corporations) and subdivisions.

License examinations require a fee of \$25 per salesperson applicant and \$50 per broker applicant. Exam passage rates average 55% for salespersons and 47% for brokers. License fees for salespersons and brokers are \$120 and \$165, respectively. Original licensees are fingerprinted and license renewal is required every four years.

In sales or leases of most residential subdivisions, the Department protects the public by requiring that a prospective buyer be given a copy of the "public report." The public report serves two functions aimed at protecting buyers of subdivision interests: (1) the report requires disclosure of material facts relating to title, encumbrances, and similar information; and (2) it ensures adherence to applicable standards for creating, operating, financing, and documenting the project. The commissioner will not issue the public report if the subdivider fails to comply with any provision of the Subdivided Lands Act.

The Department publishes three major publications. The *Real Estate Bulletin* is circulated quarterly as an educational service to all real estate licensees. It contains legislative and regulatory changes, commentaries and advice. In addition, it lists names of licensees against whom disciplinary action, such as license revocation or suspension, is pending. Funding for the *Bulletin* is supplied from a \$2 share of license renewal fees. The paper is mailed to valid license holders.

Two industry handbooks are published by the Department. *Real Estate Law* provides relevant portions of codes affecting real estate practice. The *Reference Book* is an overview of real estate licensing, examination, requirements and practice. Both books are frequently revised and supplemented as needed. Each book sells for \$12.50.

The California Association of Realtors (CAR), the industry's trade association, is the largest such organization in the state. Approximately 105,000 licensed agents are members. CAR is often the sponsor of legislation affecting the Department of Real Estate. The four public meetings required to be held by the Real Estate Advisory Commission are usually on the same day and in the same location as CAR meetings.



MAJOR PROJECTS:

Proposed Regulatory Changes. On December 20 in Sacramento, the Commissioner was scheduled to hold a public hearing on numerous proposed changes to the DRE's regulations, which appear in Title 10 of the California Code of Regulations. The following is a list of proposed amendments being considered:

-Section 2710, which sets forth the procedure for license renewal, would be amended to require that the renewal applicant disclose the area of real estate practice to which he/she has devoted 25% or more time as a licensee for the preceding four years.

-Adoption of section 2746 would require the designating officer of a corporation licensed as a real estate broker to provide a background statement for each officer, director, and person owning more than 10% of the shares of the brokerage on the original and renewal applications for licensure, and whenever there is a change of the officers, directors, or shareholders of more than 10% of the shares of the corporate brokerage.

-Section 2763 would be amended to allow the use of programmable calculators during the licensing exam.

-Section 2791, which currently requires subdividers to maintain records of funds received from prospective buyers or lessees and to retain those records for three years, would be amended to require that the records be made available for examination on the request of the Commissioner or his/her representative during regular business hours.

-Section 2792.22, regarding the budget which a common interest subdivision homeowners' association must distribute to its membership, would be amended to conform to the requirements of section 11018.5 of the Business and Professions Code.

-Amended section 2792.30 would implement newly-enacted section 11000.2 of the Business and Professions Code. That law gives a person who offers to buy an interest in an undivided interest subdivision the right to rescind the transaction until midnight of the third day after the day on which the offer was made. Section 2792.30 would prescribe the times at which the notice is deemed to have been given (depending upon the manner in which it is given).

-New section 2792.31 would also implement Code section 11000.2, by prescribing the form and content of the rescission notice to be used and by requiring that it be attached to the front page of every public report for an un-

divided interest subdivision.

-Existing section 2810.1 would be amended to delete references to several Code sections which have been repealed.

-Section 2834, which currently provides that withdrawal of a real estate broker's trust funds may be made only by a salesperson licensed to the broker or an unlicensed employee of the broker covered by a fidelity bond, would be amended to authorize withdrawals by an unlicensed and unbonded employee of the broker if all the funds in the trust account are owned by any of several specified government and private lending institutions.

-Section 2846.5 currently pertains to annual CPA-certified reports which must be filed by real estate brokers whose business activity under section 10131(d) or (e) of the Business and Professions Code meets specified monetary or transaction criteria. An amendment to section 2846.5 would require the accountant to include confirmation that the prescribed records are reconciled in accordance with sections 2831, 2831.1, and 2831.2 of DRE's regulations; the amendment would also require the report to include other specified information.

-Section 2975, which currently prescribes the information which shall be provided by an applicant for a permit to offer for sale real property securities, would require that the financial statements currently required contain the original signature of the accountant who prepared the statements.

-New section 2977 would implement section 10238.1 of the Business and Professions Code, which requires that a real property securities dealer file with the Commissioner an annual report containing financial statements containing specified information. The new regulatory section would set forth all information required to be disclosed in the annual report.

-Section 3000, which prescribes the basic criteria used by the Commissioner in determining whether a license applicant possesses an "equivalent course of study" to one required for licensure in California, would be amended to provide that examination questions shall not be reviewed with the students before, during, or after the particular course in question.

-Section 3006, which currently requires DRE continuing education (CE) instructors to maintain their address on file with the Commissioner, would require instead that they maintain on file the address of their principal place of business or mailing address at which

they may be contacted. The proposed amendment would also require that correspondence courses consist of enough study materials to assure that the course cannot be completed in less time than the number of hours for which the course is approved.

-Section 3007, which currently sets forth the content of the application for CE course approval, would require advertising and promotional material to be included with the application prior to its distribution or publication. The change would also add a prohibition against the use of any question in a final examination which is duplicated in any other test included in the course.

-Section 3007.3, regarding identification of licensees at CE course examinations, would be amended to require identification immediately before or upon completion of the examination.

-Section 3007.6, regarding advertisement of certain CE course offerings, would be amended to require that offerings in the CE category of agency relationships and duties in brokerage practice be identified in advertising. This section would also be amended to prohibit language in advertisements or promotional material which implies or states directly or indirectly that a CE course can be completed in less time than the number of hours for which it is approved.

-Section 3012.2, which currently sets forth the standards for recordkeeping by sponsors of CE offerings, would be amended to require that the sponsor's student records include a designation of agency courses in addition to the other three categories of CE required by law.

Long-Term Condominium Projects. DRE's newly created position of Subdivisions Compliance Manager is currently processing two condominium projects which include medical and other facilities for their senior citizen purchasers. The tax deferral feature of section 1034 of Internal Revenue Code is the apparent impetus for the expected increase in such projects.

Critical Path Program for Subdivisions. This program has as its purpose the reduction of overall response time from those people who represent subdividers in the public report application process. Those representatives are referred to as "single responsible parties." (See CRLR Vol. 8, No. 4 (Fall 1988) p. 88 for background information.)

The final report of the Critical Path Committee was presented at the DRE Management Development Conference on September 8 in Sacramento. The



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report indicated that the pilot program conducted by a team of deputies in DRE's Los Angeles office was a success. Consequently, as of October 1, the Critical Path Program was implemented in both subdivisions offices. From October 1 forward, a follow-up notice will be sent to the developer as well as the single responsible party when DRE has not received a response to its deficiency notice within thirty days in the case of standard subdivisions, and within sixty days in the case of common interest subdivisions.

LITIGATION:

In *Davey v. Real Estate Commissioner of the State of California*, No. B037692, 88 D.A.R. 15091 (Dec. 2, 1988), the Second District Court of Appeal ruled that a victim of a real estate licensee's fraud could not be compensated from the Real Estate Recovery Account because the victim failed to ascertain whether the licensee was able to satisfy the judgment from his own funds. The Recovery Account is available to compensate those who are defrauded by licensed real estate brokers and salespersons once they have obtained a final judgment against the licensee based on fraud.

Plaintiff's claim was filed pre-1987, and thus was governed by former Business and Professions Code sections 10471 and 10472, which required the victim to make "all reasonable searches and inquiries to ascertain whether the judgment debtor is possessed of real or personal property or other assets" that may be used to satisfy the judgment against the licensee. With respect to post-1987 claims, the issue appears to have been resolved by recent statutory amendment. Section 10471(c)(7)(F), added in 1987, requires that the claimant represent that the licensee's debt has not been discharged in bankruptcy or, if a bankruptcy case is pending, that the bankruptcy court has already declared the debt nondischargeable.

Here, the court held that Davey failed to establish that he had made reasonable efforts to ascertain whether the licensee could satisfy the judgment against him. Although Davey had filed a complaint in the licensee's bankruptcy case to determine whether the licensee's debt was dischargeable, the court found that he did not pursue the matter sufficiently and did not explain his failure to do so. The purpose behind the diligence requirement is to conserve the Account's resources by making the fund a last resort for victims and to protect the interests

of the DRE as a potential subrogee to the victim's rights against the licensee.

Attorney General's Opinion. In a December 1 Opinion (No. 87-1002, 88 D.A.R. 15253), Attorney General John Van de Kamp concluded that certain practices by banks and other lenders in retaining services of trustees in foreclosure proceedings do not violate Civil Code section 2924(c) or the Cartwright Act, but do violate California's Unfair Business Practices Act.

In his opinion, the Attorney General explained that when a borrower defaults on a loan secured by real estate, the lender often retains the services of a business specializing in foreclosures, known as a "foreclosure trustee," to handle the foreclosure procedures. Foreclosure trustees customarily charge the maximum fees allowed by Civil Code section 2924 for their services. However, because federal regulations limit the amount the federal government will reimburse the lender for foreclosure trustee fees on loans insured by the Federal Housing Administration (FHA) or Veterans Administration (VA), lenders typically insist that a foreclosure trustee limit its fees for handling these loans to the amount of the reimbursement limit—significantly lower than the maximum trustee's fee allowed by state law.

The Attorney General concluded that the practice of lenders to designate as foreclosure trustees on defaulted FHA and VA loans only those who will agree to charge up to the amount the federal government will reimburse is an unfair business practice under Business and Professions Code section 1700 *et seq.*, because it results in third parties paying higher foreclosure fees than the lender for the same trustee services, in contravention of public policy. Additional unfairness results in the inevitable impact the practice has on fees charged for trustee services in foreclosure of loans not secured by the FHA or VA. The pressure to charge higher fees for the rest of the foreclosure trustee's services makes the practice unfair to those who must reimburse the higher fees.

RECENT MEETINGS:

At the October meeting of the Advisory Commission, Assistant Commissioner (Regulatory) Betty Ludeman reported on the issue of whether the amount of personal funds which may be maintained in a real estate broker's trust account may be increased to reflect the minimum deposit required by financial institutions to waive monthly service fees. Currently, brokers are allowed to maintain up to

\$100 of their own funds in a trust account. According to 48 major financial institutions, the median deposit necessary to waive service fees is \$1,000-2,000. The sole purpose of allowing up to \$100 in personal funds to be maintained in a broker's trust account is to cover bank service charges, since many banks are unwilling to charge the broker's commercial account for service charges on the trust account. The DRE's Audit Division conducted an investigation and concluded that a maximum of \$100 is sufficient to cover monthly service charges. Ludeman cited several reasons why the \$100 limit should not be increased: (1) if a broker were to maintain a substantial sum of personal funds in his/her trust account, it could be argued that the account is noncustodial and, consequently, the account would be subject to attachment or possibly be frozen during litigation; and (2) the FDIC has held that funds of various owners which are placed in a custodial deposit in an insured bank will be recognized for insurance purposes to the same extent as if their names and interests were disclosed on the records of the bank. Thus, the DRE will not increase the amount of personal funds which may be maintained in a trust account.

The DRE also addressed the issue whether employees of telemarketing services must obtain real estate licenses. Generally, telemarketing service companies contract with a real estate brokerage to make calls to property owners to inquire as to their interest in selling their property. If the owner is interested, then an appointment is made for the owner to contact a specific licensee. Because the term "real estate broker" is defined to include the solicitation of prospective sellers and purchasers of real property and the solicitation of listings of real property, and because the sole goal of telemarketing is to eventually effect a sale, DRE has concluded that telemarketing company personnel using the telephone to solicit potential buyers and sellers must be licensed as real estate agents.

FUTURE MEETINGS:

To be announced.

DEPARTMENT OF SAVINGS AND LOAN

Commissioner: William J. Crawford
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The Department of Savings and Loan (DSL) is headed by a commissioner who has "general supervision over all associa-