We defend each answer with an explanation based on citations from the book. Often we quote more content than needed to justify our answers to put our answers into context and to make this quiz a richer learning experience. Citations from the book appear on a yellow background in Times-Roman.

Paragraphs labeled as Notes contain supplemental information we think useful but which is not used as the basis for any question on the course final. Paragraphs beginning with Comments represent the author’s comments and may be ignored.

Recommendation: If you don’t fully understand any particular question or our explanation of the answer, we suggest you carefully read the section in the book on which the question is based.

Caveat: The quiz questions are designed to be much more difficult than questions on the final. These quiz questions are longer, offer more choices, make liberal use of real estate jargon, and require you to think harder than do questions on the final. If you do well on this quiz, you almost certainly will pass the final.

1. 1.2.1.1.2: JOINT AND SEVERAL LIABILITY

The “deep pocket” rule states that a plaintiff awarded monetary damages from multiple defendants must collect his entire judgment from the defendant found most responsible for his injuries.

False

The ‘deep pocket’ rule states that when a plaintiff is awarded damages against multiple defendants, the plaintiff may recover the full amount of his judgment from any single defendant regardless of that defendant’s degree of liability.

Note: When multiple defendants are found liable, the plaintiff usually collects from the defendant with the greatest ability to pay. Often this is the defendant with the best insurance.

2. 1.2.1.2.3: NEGLIGENCE

A broker owes third parties the duty of utmost care.

False

A broker owes his principal the duties of “utmost care” and “loyalty” but does not owe these same duties to a third party.

Citation: The duties you, as a fiduciary, owe your client are loyalty, honesty, integrity, and utmost care (CC §2079.16). The duties you owe third parties are: competence, fairness, and disclosure.

Note: The Agency Disclosure form mandated by CC §2079.16 lists the fiduciary’s duties as “utmost care,” “integrity,” “honesty,” and “loyalty”; and the duties owed to third parties as “honesty,” “fair dealing,” and “good faith.”

3. 1.2.2.2.3: SMALL CLAIMS COURT

George signs a contract with Armando to paint his house for $4,500. Soon after starting, Armando realizes he can not make a profit because his contract requires him to pay for paint. Armando breaches his contract. George can take Armando to Small Claims court to compel Armando to paint his house for $4,500.
4. **1.2.2.3.1: ARBITRATION**

Arbitration decisions are a matter of public record.

False …unlike public justice where all documents and proceedings are open to the public; arbitration is 100% private.

Note: Arbitration findings, unlike the findings of a civil court, are not made public and are therefore unknown to the DRE.

5. **1.2.2.3.2: LITIGATION**

The standard of proof in civil cases is “clear and convincing proof to a reasonable certainty.”

False In civil cases the standard of proof is “a preponderance of the evidence.”

Administrative courts use the standard of “clear and convincing proof to a reasonable certainty” and criminal courts use the standard of “beyond a reasonable doubt.”

Note: An important consequence of these three different standards is that the DRE may not use the finding of a civil court to justify disciplining a licensee since the standard of proof in civil cases is lower than the standard used in administrative courts (the courts used by licensees when appealing disciplinary actions taken by the DRE). But since the standard of proof in criminal cases is higher than the standard used for administrative cases the DRE does use convictions for relevant crimes to justify suspending or revoking a license based. (The standard used by the DRE for determining if a crime is related to the duties of real estate licensee is “… if it involves … doing of any unlawful act with the intent of conferring a financial or economic benefit upon the perpetrator ….” This standard is discussed in more detail in §2.1.3.6: “real Estate License Can be Easily Lost.”)

6. **1.3.1.1: AVOID DUAL AGENCY**

By signing CAR®’s Residential Listing Agreement, the seller agrees his broker may also represent the buyer.

True CAR®’s Residential Listing Agreement permits the listing broker to elect dual agency.

Note: The clause in CAR®’s 2010 Residential Listing Agreement in which the seller pre-authorizes dual agency is 10(c) and is entitled “Possible Dual Agency with Buyer.” It states that in the event the broker procures a buyer the “… Seller hereby consents to Broker acting as a dual agent for Seller and such Buyer…” and this clause requires the seller’s initials.

7. **1.3.1.2: AVOID VEXATIOUS CLIENTS**

Betty represents Bob. After working with Bob for two weeks she concludes Bob is wasting her time. But because Betty signed a representation agreement with Bob, she has a professional and ethical duty to continue representing him.
**False** Neither NAR’s Code, the Real Estate Law, or CAR’s Buyers Representation Agreement in anyway prohibits an agent from firing his client. As quoted from Robert Bass in the text, “the last time I looked, disagreeable SOB’s are not a constitutionally protected class!”

### 8. 1.3.2.2: TRANSACTION FILE

Although the DRE requires brokers to keep all signed documents for three years, Barbara Nichols, a risk management expert, maintains they should be kept longer. She believes all documentation should be kept at least ____ years and major contracts ____ years.

A. three/six  
B. five/ten  
C. ten/twenty

**B** According to her [website](#), “since 1994, Barbara [Nichols] has served as an expert witness in hundreds of real-estate-related lawsuits, most of which involved lawsuits against agents and their brokerages.” It is her opinion that … the best advice is to keep all transaction files for at least five years and major contracts, such as the listing agreement, purchase contract, and disclosure forms for 10 years.

### 9. 1.3.3.4.1.1: E&O

E&O covers the cost for the defense for lawsuits and consequent money judgments for all of the following violations resulting from professional negligence **except**:

A. failure to disclose.  
B. breach of duty.  
C. excessive compensation.  
D. conflict of interest.  
E. failure to secure adequate pricing.  
F. discrimination based on a protected group.

**F** Most [E&O] policies exclude: • intentional acts (except for innocent participants), • acts performed outside the scope of agency, • personal injury, • suits alleging environmental damage (especially toxic mold), • [fair housing violations](#) (except, possibly, for defense), • commission disputes, • transactions for properties owned by the broker, and • issues pertaining to trademarks.

Typical claims covered are those alleging misrepresentation, failure to disclose, breach of duty, excessive compensation, conflict of interest, and failure to secure adequate pricing.

E&O insurance (aka, “professional liability insurance”) is designed to cover the legal expenses and damage awards for “goofs”; that is, negligent acts where the broker (or an associate) has inadvertently neglected to do something he should have done pursuant to rule or custom.

**Note**: It is violation of the fair housing laws for any licensee to make any decision concerning another based in whole or in part on that individual’s membership in a legally-defined “protected group.” For example, steering Vietnamese immigrants to Vietnamese neighborhoods would be a fair housing violation (assuming the Vietnamese immigrants didn’t ask to see homes in Vietnamese neighborhoods).
10. **1.4.1.2.1: VISUAL**

Which picture is efflorescence?

A. Picture ‘A’
B. Picture ‘B’
C. Picture ‘C’

**B** Efflorescence is a white chalky substance consisting of minerals left from the evaporation of water.

**Notes:**
(A) depicts dry rot and choice.
(C) depicts termite shelter tubes.

**Comment:** We are aware that this question is a repeat of a quiz question from our Risk Management course.

11. **1.4.1.3: WATER**

The life cycle of dry rot is most similar to …

A. mistletoe.
B. moss.
C. a mushroom.
D. lichen.
E. a fern.

**C** Dry rots and mushrooms are both fungi; both feed on organic material in the presence of moisture.

**Citation:** The life cycle of dry rot is similar to that of the best known fungi – the mushroom.

**Note:** Molds are also fungi but differ from both dry rots and mushrooms in one important respect: Molds grow on the surface of the substances on which they feed while dry rots and mushrooms grow within the substances on which they feed. The visible portion of the mushroom, for example, is the mushroom’s bloom but the more massive body of the fungi lies below the surface. The same is true for a dry rot. This means when the dry rot’s bloom appears, it is too late to save the underlying wood.

12. **1.4.1.5: TERMITES**

These are termite galleries.

**True** Galleries: These are the most telling and distressing sign of termite damage since they reduce the strength of the lumber in which they are found.

13. **1.4.3: PROFESSIONAL PEST INSPECTION**

California law requires a pest inspection when selling a home.
False A pest inspection is not a legal requirement for the sale of a home but every mortgage lender requires every home {built of wood} it finances to pass one. When representing a buyer who does not require financing, it would almost certainly be dereliction of your fiduciary duty to fail to advise your buyer to make his purchase contingent to a pest inspection.

14. **1.4.4.3.1: LEGAL ISSUES**

California law prohibits any home inspector from contractually limiting his liability to the value of his inspection fee.

True For example, suppose a home inspector fails to find a leak in a master shower pan which subsequently costs the new owner $5,000 to repair. In this situation, the home inspector may not limit his liability to his inspection fee.

Citation: BPC §7198 states that contracts with provisions which waive the inspector’s duty to conduct a professional home inspection (per §7196) or limit the inspector’s liability to his inspection fee are invalid as such provisions are contrary to public policy. In other words, home inspectors are liable for negligence.

15. **1.4.4.3.3: QUALIFYING HOME INSPECTORS**

Which section title in a home inspector’s report would make you suspicious of the inspector’s objectivity?

A. “Energy Saving Recommendations”
B. “Areas Not Examined”
C. “Cost Estimate of Suggested Repairs”
D. “Priority List of Repairs”
E. “Problems Which Should by Assessed by other Professionals”
F. “Safety Issues”
G. “Recommended Service Providers”

One of the questions you should ask when qualifying a home inspector for future engagements is: If your inspection finds defects, can you perform repairs or recommend someone who can? The answers should be “no” and “no.” You want a professional home inspector who makes his living only from home inspection and not from making repairs.

Another question you should ask: Can you provide me a sample of your home inspection report? The answer should be “yes.” When you receive the sample home inspection report you will want to make sure it includes these seven sections: 1) a description of areas not examined with corresponding explanations for why they were excluded, 2) guidelines for estimating the cost of repairs, 3) recommendations for consulting other professionals such as arborists or structural engineers, 4) a prioritization of repairs with justifications, 5) estimates for the remaining life expectancy of critical home systems such as the roof, 6) a list of potential safety issues, and 7) a list of recommendations for improving the energy efficiency of the home.

16. **1.4.5.5: CLUE REPORTS**

Before an insurer writes a homeowners insurance policy, the insurer checks the home’s claims history on CLUE.

True When homeowners file a claim on their homeowners insurance policy for a wind-damaged roof, for injuries from a dog bite, for damage from a tree falling onto the roof; most insurers post a record of the claim to a cooperative database called CLUE (Comprehensive Loss Underwriting Exchange).
When an insurer is asked to write a homeowners insurance policy, the insurer checks the home’s claims history on CLUE. If the insurer finds an unacceptable claims history the insurer may refuse to write the policy or he may charge an exorbitant premium. In particular, insurers are reluctant to provide homeowners insurance for homes having had any claim for significant water damage.

17. **2.1.1.1.2: HOUSING AND ECONOMIC RECOVERY ACT OF 2008**

Which of the following statements about the Housing and Economic Recovery Act of 2008 (HERA) is **false**?

A. HERA provided incentives to lenders to write-down mortgages for at-risk borrowers.
B. HERA bailed out Fannie and Freddie and placed both under government conservatorship.
C. HERA created the Federal Housing and Finance Agency (FHFA) to regulate Fannie and Freddie.
D. HERA eliminated an IRS provision which had required a short-seller to pay taxes on forgiven debt.

**[D]** It was the Mortgage Forgiveness Debt Relief Act of 2007 (enacted one year before HERA and described in the preceding section) which gave tax relief to short sellers. HERA may be thought of as “emergency legislation” enacted by Congress to give relief to at-risk borrowers and to keep the two GSE’s functioning after they had become insolvent following the bust of the Real Estate Bubble.

HERA was designed to restore “confidence in Fannie and Freddie by strengthening regulations and injecting capital into the two large U.S. suppliers of mortgage funding.” HERA “replaced several regulatory bodies with the independent FHFA (Federal Housing Finance Agency) … to provide stricter oversight of the GSEs.” HERA also authorizes the FHA to guarantee up to $300 billion in new 30-year fixed rate mortgages for at-risk borrowers if lenders write-down principal loan balances to at least 90% of current appraisal value. Finally, it should be emphasized the HERA is a huge act, almost 700 pages long, which established many more programs, funding sources, and laws than those mentioned in this paragraph.

**Note:** The FHFA is now a major presence in the real estate industry because it controls both Fannie, Freddie, and the Federal Home Loan Banks. Under the FHFA’s conservatorship, the two agencies have lost most of their pre-Bubble individuality and many authorities of the mortgage lending industry believe that FHFA will, at some time in the future, combine the two GSE’s into one agency (source).

18. **2.1.1.1.2.6: 6/6 SAFE ACT OF 2008**

The federal legislation which requires each state to register all residential loan originators in a national database is known as the “SAFE Act.”

**True** Only residential loan originators must register in the National Mortgage Licensing System (NMLS) – a requirement of the SAFE Act.

**Citation:** It [the SAFE Act] requires all residential loan originators to pass an exam to obtain an “endorsement” (i.e., a license) to legally originate home loans and to meet annual continuing education requirements to maintain the endorsement.

19. **2.1.1.2.1.9: SB 706. BUSINESS AND PROFESSIONS**

The DRE has all of the following powers to enforce the Real Estate Law except the power to …

A. discipline a licensee for failure to report having been disciplined by another licensing authority.
B. discipline a licensee found liable in a civil court for misrepresentation.
C. request an administrative judge to force a licensee to pay the costs of its investigation.
D. automatically suspend the license of any licensee sent to prison for a felony conviction.
E. publish its investigative reports and findings on its License-Lookup site.

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SB 706 requires licensees to report to the DRE when he or she has been indicted, charged with a felony, convicted of a crime, or had another license disciplined by another licensing agency. “Indictments,” “criminal charges,” and “convictions” are all terms associated with the criminal justice system – they are not applicable to the civil courts.

All the other enforcement powers have been newly granted to the DRE by our State legislators via the enactment of SB 706.

Notes:

#1: BPC §10177.5 gives the Commissioner authority to suspend or revoke the license of any licensee found liable in a civil action for "fraud, misrepresentation, or deceit with reference to any transaction for which a license is required." However, that power was rendered moot by a 2011 decision of the Court of Appeals in Grubb Company Inc. v. Department of Real Estate. In that case, the Court of Appeals voided the Commissioner’s revocation of a license for a licensee found liable for fraud in a civil action. The reason cited: the standard of proof in a civil action (“preponderance of the evidence”) is lower than the standard required by law for the revocation of a professional license (“clear and convincing evidence”) (details). Nevertheless, because all legal documents associated with any lawsuit are available to the public the Commissioner could cite any incriminating findings found in any such document in its own independent investigation. If the Commissioner believed the facts presented “clear and convincing evidence” that the licensee violated the Real Estate Law, the Commissioner could suspend or revoke the licensee’s license. (And, according to a new law – SB 53, demand the licensee pay the costs of its investigation). Of course any decision rendered by the commissioner is subject to appeal via the Administrative Courts.

#2: If a licensee is found liable for defrauding or stealing from a former real estate client and if that licensee fails to pay the money damages awarded to his former client, that client could apply to DRE’s Consumer Recovery Account for payment of the money damages from the fund. In that event, the DRE would suspend the licensee’s license until such time the licensee repaid the fund plus 10% interest (source).

Comment: Coincidentally, while writing the above quiz question the author received a call from a broker needing to retake a trust fund course in partial satisfaction of an agreement with the DRE to settle its finding that the broker had violated the Real Estate Law. The broker told the author that a spiteful tenant had reported him to the DRE for some spurious offence in retaliation for his refusal to repaint her bedroom. The DRE sent investigators to his office but quickly determined that the complaint was baseless. But instead of leaving empty-handed, the investigators decided to audit the broker’s trust fund. After four days the DRE investigators found a minor trust fund violation: the broker had failed to log his earnest money deposits which were checks written to title companies. The DRE formally charged the broker with a trust fund violation and, for good measure, added an accusation of “failure to supervise.”

After a long period of negotiation between the DRE and the broker’s attorney, the matter was finally settled: the DRE agreed to not restrict or suspend the broker’s license providing that the broker completed a trust fund accounting course and repaid the DRE for the cost of its investigation – a sum of $3,900.

20. 2.1.1.2.3.2: AB260: MORTGAGE LOANS

For years Sally has referred her buyers to her favorite mortgage broker, José. Sally sends Chloë to José and José finds Chloë a loan from Fidelity Mortgage Lenders. To whom does José owe his fiduciary duties?

A. Chloë
B. Sally
C. Fidelity Mortgage Lenders
D. José
E. Nobody

AB 260 codifies that mortgage brokers are fiduciaries of the borrower and prohibits a broker from steering a borrower into a loan that is more beneficial to the broker than the borrower. Therefore despite José’s long and
fruitful association with Sally, José has a legal responsibility to place Chloë’s economic interests above his own and certainly above that of Sally or the lender. For example, it would be a violation of AB260 if José selected for Chloë a loan which suited Sally’s need to quickly close escrow instead of Chloë’s need for the lowest cost loan for which she could qualify.

21. **2.1.2.1: NEW ENFORCEMENT PROGRAM**

Which service would DRE’s Enforcement Advocacy Program **not** provide? Helping a ...

A. buyer find out where his earnest money is.
B. buyer contact their agent concerning a current transaction.
C. buyer and seller settle a dispute concerning the agent’s commission.
D. homeowner find a pest inspection service.
E. new homeowner having trouble with his subdivider.
F. distressed home owner obtain a refund for an illegal advance fee.

[D] The mission of the {DRE’s Enforcement} Advocacy Program is to respond quickly and informally to concerns of consumers and members of the real estate industry by serving as an informal mediator or facilitator to resolve conflicts and/or to mitigate or prevent Real Estate Law violations.

(D) is the correct answer for two reasons:

1. Pest inspection services are regulated and licensed by the California Pest Control Board and not the DRE. The law that the Pest Control Board enforces is not the law the DRE enforces (the Real Estate Law).
2. The Advocacy Program is established to help consumers resolve conflicts or other difficulties with licensees and others that the DRE regulates (e.g., timeshare operators and subdividers).

22. **2.1.2.2: BROKER SUPERVISION: THE BUCK STOPS HERE**

Corporations are “persons” under the Real Estate Law and, as such, may obtain real estate licenses.

**True** Because corporations are “persons” under the Real Estate Law, corporations may obtain real estate broker licenses.

**Note:** A corporation may be licensed as a real estate broker through one or more of its officers each of which must be an active broker or have qualified for a broker license by examination within the twelve months preceding receipt of application.

23. **2.1.3.1: CONVICTIONS AND DISCIPLINARY ACTIONS TAKEN BY ANOTHER LICENSING AUTHORITY**

Sally is licensed by the DRE and the Nevada Board of Cosmetology (NBC). The NBC fines Sally $25 for failure to sterilize her cuticle nippers. Sally must report this incident to the DRE.

**True** The article on which this question is based was written by DRE’s Chief Counsel, Wayne Bell. In describing the disciplinary actions which licensees must self-report to the DRE he writes ... any disciplinary action taken by another licensing entity or authority of this state or of another state or an agency of the federal government.

Mr. Bell writes that because the law is written in “plain language” it permits **no** exceptions emphasizing that this means ‘Any disciplinary action taken’ against a licensee (again meaning filed, initiated, and/or completed) must
be reported to the DRE within the relevant 30 day window. If it is not, the department has the power to discipline the licensee for a violation of {BPC}§10186.2.

He does admit that the term “disciplinary action” is open to interpretation but also writes that ... if the action is actually or deemed to be ‘disciplinary,’ the licensee must report the same to the DRE in writing within the applicable 30 day window or face discipline by the Department.

Sally’s circumstance meets all the criteria of a disciplinary action which must be reported to the DRE: 1) Sally is a DRE licensee, 2) the NBC is a licensing authority in the United States, 3) Susie has an NBC license, and 4) she was disciplined by the NBC for a violation.

24. 2.1.3.3: LICENSE REGULATIONS AFFECTED BY SB 53

Which statement about the Commissioner’s power to levy fines is false?

A. The Commissioner may only levy fines for violations of the Real Estate Law.
B. The recipient has only thirty days to contest the fine.
C. The Commissioner may levy a fine against an unlicensed person.
D. The fine may be for no more that $2,500.00.
E. Fines paid to the Commissioner are deposited into DRE’s General Operating Fund.

(E) Any money collected from the citations would be placed into the {Consumer} Recovery Account of the Real Estate Fund.

Notes:
1. The power to levy fines is a new (2012) power granted to the Commissioner by the enactment of SB 53.
2. The Consumer Recovery Account is that fund maintained by the Commissioner to compensate consumers who have been defrauded or have been the victims of theft by real estate licensees (details).

25. 2.1.3.5: SUPERVISING RESTRICTED REAL ESTATE SALESPERSONS

The DRE imposes upon brokers special responsibilities when managing employees with restricted licenses. Which is not such a responsibility?

A. To petition the DRE to remove the licensee’s restriction after his probationary period ends.
B. To read the Commissioner’s decision outlining the basis for the licensee’s restriction.
C. To notify the DRE that he (the broker) has accepted responsibility to closely supervise the licensee.
D. To work with the licensee to ensure his professional conduct.

(A) is not a responsibility of the employing broker.

There is no fixed “probationary period” (see below note). The duration of the restriction is indefinite; that is, it remains in effect until such time the licensee (not the employing broker) petitions the DRE to remove it. In his petition, the licensee (not his broker) must convince the DRE that he no longer deserves the restriction(s) the Commission had placed on his license.

Citations: ... the broker is also extending the opportunity for the restricted licensee to exhibit evidence of rehabilitation which will be required at a later date should the individual [i.e., “licensee”] seek to petition for a plenary [full] license.

Re the employing broker’s responsibilities: As a condition of employment, you, as the prospective employing broker, are required to complete the RE 552 form, in which you certify that you have read the Decision of the Real Estate Commissioner outlining the basis under which this licensee was disciplined. In addition, you promise to ensure that all transactional documents which the RRES licensee prepares will be reviewed and you will otherwise exercise “close supervision” over the licensed activity of that applicant. Before the broker can consider the parameters...
leading to “close supervision” of the RRES, the broker should first of all become thoroughly familiar with the reasons for the licensee’s discipline.

Note: The article upon which this article is based goes into considerable detail as to how a licensee may successfully petition the Commissioner for removal of his restrictions. The article says that the petition may not be made any earlier than one year following the first day of the salesperson’s restricted license and the “burden of proof” is on the licensee to convince the Commissioner that the restrictions should be removed. The Commissioner investigates the petitioner’s claims on a case-by-case basis and, if convinced that the licensee no longer requires close supervision may issue the licensee a full (“plenary”) and unrestricted license.

26. 2.1.3.6: Real Estate Can Be Easily Lost

The DRE may revoke the license of any licensee convicted of a felony or misdemeanor “substantially related to the qualifications, functions, or duties of a real estate licensee.” Which standard is used by the DRE to determine if a conviction is “substantially related”?

A conviction is substantially related if the conviction is for ...

A. a crime of moral turpitude substantially related to real estate licensure.
B. a theft or fraud concerning a real estate transaction if perpetrated during the preceding ten years.
C. any act of physical violence, coercion, theft, or fraud which occurred during the preceding ten years.
D. a crime involving any unlawful act with the intent of conferring a financial benefit upon the perpetrator.

[D] A crime shall be considered substantially related “… if it involves … doing of any unlawful act with the intent of conferring a financial or economic benefit upon the perpetrator” …

Mr. Hunt, the article’s author, is critical of this standard because he considers it too broad. He jests that this standard could be used to revoke the license of a licensee convicted of fixing a high school basketball game.

Mr. Hunt describes how the Commissioner at that time (Jeff Davi) revoked the license of a “slum lord” (Lance Robbins – [click here for his DRE record]) for his failure to correct some 50 municipal building code violations. Some of the violations were issued by the Fire Department for Mr. Robbins’ failure to inspect fire extinguishers. In applying the standard, the Commissioner argued that Mr. Robbins’ failure to correct the municipal violations was a crime committed by Mr. Robbins for the purpose of saving money for his own economic benefit.

Notes:

(A) was the standard (the “Moral Turpitude Standard”) used by the DRE until 2006. In that year, a California Court of Appeal decision ([Petropoulos v. Department of Real Estate](details)) ruled that the “moral turpitude” standard was too elusive and nebulous to be meaningful. Consequently the DRE changed the standard to (A).

27. 2.1.4.3: CA Fair Housing Now Covers Gender Identity

It is illegal to discriminate based on “gender identity;” that is, based on a person’s …

A. sexual attraction to one’s own or one’s opposite sex.
B. choice of feminine or masculine dress.
C. internal sense of being male or female.
D. gender assignment at birth.

[C] Gender identity refers to a person’s deeply felt internal sense of being male or female. Gender expression refers to one’s behavior, mannerisms, appearance, and other characteristics that are perceived to be masculine or feminine.
Note:
California law has at least three other ways to define the protected category of sex besides the traditional biologically-based definition; that is, by one’s (1) sexual orientation (answer A), (2) gender expression (answer B), or (3) gender identity (answer C). No matter which definition is used, California law makes it illegal for a licensee to take an individual’s to sex into consideration when performing licensed activities.

28. 2.1.5.3: ARE APPRAISAL AND CREDIT REPORT FEES TRUST FUNDS?

George is a mortgage broker and Sally is his client. Before finding Sally a lender, George obtains from Sally an advance of $550 for credit report and appraisal fees. George explains to Sally that these fees will be repaid at the close of escrow.

When escrow closes, George receives a commission check from escrow for $7,550 – $7,000 for his commission plus $550 to repay Sally. He should deposit this check into his ...

A. business account and from it write a check for $550 to his trust account in care of Sally.
B. personal account and from it write a check to Sally for $550.
C. trust account and from it write a check to himself for $7,000.

[C] If the credit report and appraisal fees are included in the broker’s commission check (from escrow), the entire check would need to be deposited into the trust account and the part of the funds belonging to the broker should be disbursed not later than twenty-five days after their deposit.

Notes:
1. The advance payments collected by George from Sally are trust funds but are not interpreted by the DRE as advance fees as the broker collects an amount equal to the cost of performing such services. This means that all the regulations which apply to advance fees (e.g., the requirement to secure the DRE’s permission before charging an advance fee) do not apply. However, the article explains that any excess funds above and beyond the cost to perform these services would be considered advance fees. So had George received from Sally a check for $1,000, then the excess funds ($450) would be regarded as an advance fee. (This DRE document explains the essential elements of an advance fee agreement.)


29. 2.1.6.2: RIGHT-TO-RENT LEGISLATION BECOMES LAW IN CA

Joe inherits his mother’s townhouse. Joe wants to rent the townhome but the association’s CC&Rs prohibit owners from renting their units. Nevertheless, Joe has the legal right to rent his townhouse if ...

A. the association’s CC&Rs did not prohibit renting when his mother bought the townhome.
B. more than half the HOA units are owner-occupied.
C. he fails to find a buyer for the townhome after six months.

[A] On July 7, 2011, Governor Brown signed into law a new law that says: If you own a property in a CID and, if, when you purchased the unit, the governing documents permitted you to rent your property, then a change in those documents cannot now prohibit you from renting out your property. This right to rent the property would transfer to your heirs, but not to a subsequent purchaser. The law is not retroactive. It takes effect relative to governing document provisions on or after January 1, 2012.
30. **2.1.7.1: Undisclosed Short Sale Payments May Lead to Trouble**

In short sale transactions, settlement payments outside of escrow are illegal.

**False**: Payments made outside of escrow are illegal only if they are not disclosed to the senior lien holder and not marked as “P.O.C.” for Paid Outside of Closing on the lender’s HUD-1.

**Citation**: Appendix A to RESPA (24 C.F.R. Part 3500) says that “The settlement agent shall complete the HUD-1 to itemize all charges ... whether to be paid at settlement or outside of settlement ....” Charges paid outside of settlement “shall be included on the HUD-1 but marked P.O.C. for Paid Outside of Closing... .”

**Note**: Mr. Hunt makes the point that a buyer may be tempted to make an undisclosed payment outside of escrow to encourage a junior lien holder to agree to extinguish his loan without, at the same time, rousing the cupidity of the senior lien holder, who, in coveting the extra cash, might then deny the short sale.

31. **2.2.1.2: Congress Limits Gain Exclusion on the Sale of Some Primary Residences**

The capital gains exclusion for personal residences may include the capital gains rolled into the acquisition of the property through a §1031 exchange.

**True** IRS law excludes $250,000 of the gain from taxation if you’re single and $500,000 if you’re married when you sell a primary residence you’ve lived in for at least two years of the last five years. This is so even if a portion of the gain was rolled over into the property in a §1031 exchange transaction.

**Note**: You might be thinking, “if the tax-free exclusion applies only to personal residences and a §1031 exchange only to investment properties” then how could any part of a §1031 gain be included in the tax-free exclusion? ¶ **Answer**: If the personal residence was originally bought as a rental property through a §1031 exchange only to investment properties then how could any part of a §1031 gain be included in the tax-free exclusion? ¶ For example, suppose the Smiths have a rental home in San Diego which has appreciated $500,000 (for simplicity, let’s assume the Smith’s didn’t depreciate it). Now suppose they wish to retire in Boise Idaho. They could make a §1031 exchange for their San Diego home, rent out the Boise home for a couple of years (an IRS requirement), and then retire to their Boise home. After living in the home for two years they could then sell it and pay no tax on their $500K gain (source).

**Disclaimer**: We are not tax experts. Any one considering this strategy should verify it with a tax expert.

32. **2.3.1.3: New CA Law Allows Greater Responsibility for Branch Managers**

**BACKGROUND**: Bob is a branch manager of Sally’s Realty. When Sally appointed Bob she gave the DRE written notification of Bob’s appointment. Sally also signed an employment agreement with Bob in which Bob agreed to accept responsibility for enforcing the Real Estate Law.

**SITUATION**: Gertrude works for Bob. The DRE finds Gertrude guilty of a serious violation of the Real Estate Law. Who will the DRE hold responsible?

A. Only Bob and Gertrude.
B. Sally, Bob, and Gertrude.
C. Only Gertrude.
D. Only Sally and Gertrude.
E. Only Sally.
**33. 2.3.2.2: NAR® MEETING MARKED BY A SENSE OF URGENCY**

Which of the following is not a worry of NAR®’s membership? The Federal government will ...

A. lower the cap on the mortgage interest deduction.
B. eliminate Fannie and Freddie.
C. lower the loan limits for FHA and GSE loans.
D. require banks to retain too large a percentage of their mortgages.
E. allow banks to compete with real estate brokerages.

**E**  Mr. Hunt cites the controversy to allow banks into the brokerage business as a settled issue that is no longer of concern to REALTOR®s: the battle to keep banks out of the real estate brokerage business went on for years. He then cites and describes four proposed legal changes which will almost certainly affect the real estate market.

*Note:* Recently (October 4, 2011) the Progressive Policy Institute and e21 hosted a conference entitled “New Solutions for America’s Housing Crisis.” Among the attendees were U.S. Senator Johnny Isakson, Ronald Phipps (president of NAR®), David Stevens (president of the Mortgage Bankers Association), and many other notables in the real estate business. The worry these experts expressed over the issues Mr. Hunt described, particularly the worry about the regulatory definition of Qualified Residential Mortgage (the types of loans that banks may sell without restriction), was palpable. You can watch the four hour (!) presentation here.

**34. 2.3.2.3: LANDMARK CONSUMER PROTECTION LAW HEAVY WITH STRONG MORTGAGE RULES**

The restoring American Financial Stability (RAFS) Act of 2010 {aka, “Dodd-Frank”} ...

A. provides funding for the construction of public housing for evicted homeowners.
B. mandates that each state set standards for its home loans.
C. sets limits for yield spread premiums indexed to loan size.
D. provides foreclosure assistance to lending institutions.
E. requires credit reporting agencies to provide all loan applicants with their credit score at no cost.
F. empowers the CFPB to levy fines on lending institutions for irresponsible lending.
G. provides funding for legal assistance to homeowners facing eviction.
The law {RAFS} authorizes a HUD-administered program for making grants to provide foreclosure legal assistance to low- and moderate-income homeowners and tenants related to homeownership preservation, home foreclosure prevention, and tenancy associated with home foreclosure.

Notes:
All the other answers are false.

(A) Dodd-Frank does not provide public housing for evicted homeowners but it does provide foreclosure legal assistance to low- and moderate-income homeowners and tenants related to homeownership preservation, home foreclosure prevention, and tenancy associated with home foreclosure.

(B) The standards set by Dodd-Frank are federal, not local to the states.

(C) Dodd-Frank makes yield spread premiums illegal.

(D) Dodd-Frank provides foreclosure assistance to homeowners, not lending institutions.

(E) Dodd-Frank requires the credit reporting agencies to disclose credit scores only if the consumer’s score negatively affects them in a financial transaction or a hiring decision.

(F) The CFPB does not penalize irresponsible lenders; rather consumers may sue lenders who do not follow the rules.

35. 2.3.3.1: Economy Brings Generations Together Under One Roof

Why is Toll Brothers (a large home builder) replacing some of its family rooms with guest suites complete with a kitchenette? To appeal to homebuyers ...

(A) in need of rental income.
(B) needing servants’ quarters.
(C) seeking multi-generational living arrangements.

The reason that Toll Brothers is designing homes with guest suites is to accommodate the growing number of households that are “doubling-up” usually to save money as when retired grandparents live with their children and take care of their children’s children while they are at work.

Citation: Three generations living in one home is becoming so popular that builders are designing for this target market. Toll Brothers is replacing some of its family rooms with floor plans that include a guest suite complete with a kitchenette (perfect for grandma.)