
Section XIII

GUIDELINES FOR GIFT PROGRAMS AND CREATIVE FINANCING PLANS

A. Gift Programs Used as Sales Inducements

Gifts to purchasers such as landscaping, automobiles, appliances, furniture, cash, or any other item with intrinsic value ordinarily should be furnished prior to close of escrow (such as delivering a “pink slip” for a car, or the actual item at close of escrow).

If this is done at close of escrow, no bond or other guarantee is required, however, proper escrow instructions are needed.

If any such prizes are to be furnished *after escrow closes*, then proper financial arrangements (bond, etc.) will be required and the public report will contain disclosure concerning the program. In that case, the purchase agreement must also set forth contractual arrangements for delivery of prizes. (See RE 609.)

- ☞ Regulation 2800(d)(2) specifically requires notification to the DRE as a material change in the offering if the subdivider, subsequent to the initial issuance of the Final Public Report, elects to offer a special sales inducement involving a financial commitment to purchasers. Prior to permitting subdividers to offer the inducement to prospective buyers, the DRE will review the arrangement and any financial arrangements that may be necessary including possible modification to the escrow instructions. In most cases, the subdivision public report will not have to be amended if the inducement occurs at or before the close of escrow and only directly impacts the individual buyers. If the inducement/promotion occurs after the close of escrow, an amendment is necessary to include a disclosure concerning the program.

Since the variations of sales inducements and methods of financial arrangements can be complex, subdividers should inquire from the DRE as to what will be required and whether the public report will need to be amended.

B. Creative Financing Plans/Fact Sheets

A “fact sheet” procedure was instituted in October, 1982. Under this “creative financing” processing program, in lieu of special noting all features of the proposed financing packages the subdivider will make available to purchasers, the DRE will review and approve a separate fact sheet for each loan program to be used by the subdivider. A single condensed special note can then be placed in the public reports to describe the purchaser’s right to obtain such fact sheets.

It is imperative that prospective purchasers receive this financing information in a form that encourages them to read it prior to executing a purchase agreement.

“Creative financing” programs for subdivision sales are reviewed along with the applications for subdivision public reports. Originally, all pertinent information concerning this financing was included in the body of the public report. However, when multiple financing programs are available, the public reports would be too voluminous and overbalanced with this type of information.

Subdividers may use fact sheets by doing the following:

1. Submit a copy of the approved fact sheet to our District Office Subdivision Section along with a written statement representing that a copy of the approved fact sheet will be furnished to all prospective

purchasers who will obtain loans through the assistance of the subdivider; that a copy of the fact sheet will be furnished to prospective buyers before they are obligated to sign a purchase contract or give money to the seller;

and

2. Submit a copy of all applicable financing transaction documents (notes, trust deeds, leases, contracts, etc.) for review along with the fact sheet intended to be given to prospective purchasers to verify that the features of the financing documents are consistent in content with the features disclosed in the fact sheet.

If the fact sheet is “pre-approved” by DRE, only the fact sheet and the approval letter need be submitted.

- ☞ DRE will insert the following special note in the subdivision public report for the affected subdivisions:

Financing of Subdivision Purchases: Purchasers may obtain a loan from the lending institution of their choice or they may select from financing programs made available by the subdivider. One or more “creative financing” programs may be available to purchasers of lots or units in this subdivision. There is a fact sheet which describes each “creative financing” program. Prior to entering into a contract to purchase a lot or unit which involves one of these programs, the subdivider or the subdivider’s representative must give you a copy of the fact sheet for that program.

YOU SHOULD READ AND THOROUGHLY UNDERSTAND ALL LOAN DOCUMENTS BEFORE SIGNING THEM.

C. All-Inclusive Trust Deeds

Escrow instructions must provide for recording of a Request for Notice of Default on the underlying loan(s).

Escrow instructions must also provide for a third party collection agent to collect AITD payments from the purchaser and to disburse funds to proper beneficiaries.

Beneficiaries of underlying loan(s) must acknowledge that an AITD program is acceptable to them and that the AITD will not cause them to accelerate the loan(s) or disturb the possession of a non-defaulting buyer. Also, beneficiaries of underlying loan(s) must agree to accept payments directly from the trustor of the AITD in the event that the beneficiary of the AITD (the trustor on the underlying loan(s)) defaults. An underlying loan may not be a blanket encumbrance.

Payments on an AITD must be sufficient to cover all payments due on underlying loans unless an interest subsidy arrangement, properly guaranteed by bond or letter of credit, etc., has been approved to cover the subsidized amount. In some cases, the payments on the second trust deed (AITD) may not be collected until the end of the term of the note. If this happens, the loan payment will be larger and all of these eventualities must be considered prior to approving the program.

D. Negative Amortization Programs Coupled with Balloon Payments

Various programs of this type are used by subdividers. DRE will require a written statement from the lender concerning the lender’s intention to refinance such loans where the principal amount of the loan will be considerably larger when refinancing is required than when the property was originally purchased. The amount to be added to the principal sum of each loan must be disclosed to purchasers and a special “warning” note will be placed in public reports when it appears the amount due on the principal (to be refinanced) might increase faster than the value of the property. Also, the usual balloon payment special note will be used in the public report.

E. Interest Subsidy Programs (Buydowns)

DRE will require that the subdivider choose one of the following or an acceptable alternative plan:

1. Pay the lump sum of subsidy amount to the purchaser at the close of each escrow, or pay the lender prior to the close of escrow or provide a bond to the lender to guarantee the total amount of the payments for all lots in the subdivision.

DRE requires a statement from the lender verifying the arrangement and if a bond is posted to guarantee payments to the lender, the lender must agree to enforce the bond rather than to expect buyers to pay in the event that the subdivider fails to pay the subsidy. There must be a firm arrangement with the lender so that buyers will not lose the property whether or not the subdivider pays the subsidy.

2. The subdivider may place sufficient cash in an escrow account, with appropriate escrow instructions, to allow the escrow company to make monthly payments to the lender of the subsidized amounts. The lender must agree to this procedure. The public report will contain an appropriate statement.

F. Lease-Options

Such plans can easily result in problems similar to those related to real property sales contracts. As a general rule, money to be credited toward purchase of the property must be impounded, per Section 11013.2 or 11013.4 of the Business and Professions Code, until such time as the purchaser exercises the option to purchase.

G. Equity Sharing or Shared Appreciation Mortgage

All such plans contain substantial problem areas for both the investor and the occupier of the property. DRE needs enough information about the plan to determine whether or not it is reasonable and feasible and also to be able to properly explain the plan to the public (both occupier and investor) in the public report. Such plans nearly always involve resale of the property within a specified time and the splitting of proceeds between occupier and investor. DRE requires that the plan include an equitable method of disposition of the property and division of the proceeds.

H. Sale by Real Property Sales Contracts

Such programs are covered by DRE impound laws, DRE regulations, and by the Civil Code. Strict compliance is required. (See, among others, Regulation 2791.9; and Question 21 in the Item Analysis section hereof.)

I. Ordinary Deed of Trust Taken Back by Subdivider/Seller

DRE will review the terms of such notes and deeds of trust and will special note the public report accordingly. If some provisions therein are deemed to be unreasonable, those provisions must be deleted.

- ☞ There are other creative financing programs, sales inducements, subsidies, etc. Regardless of what is offered as a sales inducement, whether or not it is actually part of the real property to be delivered, DRE will evaluate to determine that the developer can deliver what he advertises and offers.