INTRODUCTION

The purpose of this brochure is to provide basic information which you should know if you plan to purchase existing promissory notes or fund loans, the repayment of which is secured by deeds of trust recorded against California real property. **The funding of a loan or the purchase of a promissory note is an investment which involves risk.** Prior to becoming a lender of loans or a purchaser of promissory notes, you should be able to answer the following questions:

1. What is a "promissory note"?

A promissory note is a written promise to pay or repay a certain amount of money at a certain time, or in a certain number of installments, or on demand to a named person and it usually provides for payment of interest.

The person receiving the loan proceeds (**borrower**) becomes obligated to repay the debt by signing a promissory note which specifies: (1) the amount of the loan (**principal**); (2) the interest rate (**interest**); (3) the amount and frequency of payments (**debt service**); (4) when the borrower must repay the principal (**due date**); and (5) the penalties imposed if the borrower fails to timely pay or tender a payment (**late charge**) or decides to pay a portion or all of the principal prior to the due date (**prepayment penalty**). The promissory note identifies the borrower and the person who will receive the payments (**lender or note holder**).

2. How do you obtain a promissory note?

You obtain a promissory note (become a lender or note holder) by either making a loan or purchasing an existing promissory note. Unless the loan is made or arranged by a real estate broker, a private party when making a loan will be subject to an interest rate ceiling imposed by the California

State Constitution. Charging a rate in excess of this ceiling is referred to as usury. Even when purchasing an existing promissory note (unless the purchase is arranged by a real estate broker), a private party, depending upon the fact situation, may still be subject to usury.

A broker who for compensation, or in expectation of compensation (regardless of form) assists the public in making or arranging loans is commonly referred to as a mortgage loan broker (**MLB**).

3. What secures your investment?

Your investment is secured by a deed of trust recorded against the title of the borrower's property (**the Property**). Unlike deposits in a bank or savings and loan, which are generally insured by a federal agency (such as FDIC) and may usually be withdrawn with limited notice, the promissory note: (1) involves risk to principal (a typical feature of all **investments**); (2) establishes a specific and predetermined period of time for the repayment of your **investment**; and (3) does not benefit from insurance issued by a federal agency.

In a deed of trust, the borrower (**trustor**) transfers the Property, in trust, to an independent third party (**trustee**) who holds conditional title on behalf of the lender or note holder (**beneficiary**) for the purpose of exercising the following powers: (1) to reconvey the deed of trust once the borrower satisfies all obligations under the promissory note; or (2) to sell the Property if the borrower defaults (known as a **foreclosure**). Foreclosure involves the process of selling the Property to a third-party bidder or, in the absence of a sufficient third-party bid, acquiring title to the Property. The foreclosure sale, in most cases, satisfies the debt.

Depending upon the method of foreclosure, the nature of the loan, the circumstances of origination, and the value of the Property, you may or may not be able to recover your entire

investment. For example, if a third party bids at a nonjudicial foreclosure sale an amount equal to or greater than the amount you are owed (including fees, costs, and expenses of the foreclosure), your **investment** would be fully paid. On the other hand, if you bid the full amount that is owed to you, including all foreclosure fees, costs, and expenses (**full credit bid**) and there are no third-party bids, you will generally be limited to the Property and its value as the source of repayment of your **investment**.

If the loan is a nonpurchase money mortgage (deed of trust) and the Property's value is insufficient to recover all you are owed, a judicial foreclosure coupled with an action for a deficiency judgment may be the only way to recover your **investment**; i.e., collect any difference between the amount received at the foreclosure sale and the amount of money the borrower owes you.

Remember, the Property identified in the deed of trust is what secures your **investment**. This brochure includes, in Section 2, a discussion of what you should know about the Property.