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SUBDIVISION INDUSTRY BULLETIN

Arnold Schwarzenegger, Governor
Dale Bonner, Secretary, Business, Transportation, & Housing Agency
Jeff Davi, Real Estate Commissioner

www.dre.ca.gov

Department of Real Estate

Spring 2009

Subdivision filing fee adjustments

Effective July 1, 2009, the Department of Real Estate will implement fee changes which will adjust subdivision filing fees to the statutory maximum, referenced on form RE 605.

The Department has for the past five years maintained fees at the same levels as those charged in 1982. Despite having taken steps to achieve functional efficiencies and reduce expenditures, the Department must now adjust fees to fund its operational needs. ♦

Foreclosure by lending institutions

If certain lenders as referenced in Business and Professions Code (B&P) Section 11010.5 informs DRE within 30 days of acquisition of title through foreclosure or deed in lieu of foreclosure and advises DRE that there are to be no material changes (other than change of ownership), DRE will issue an RE 618E. The RE 618E will be attached to the existing public report and it will be issued without an additional filing fee. Use the RE 637 to facilitate the notification process. An RE 635 does not need to be completed unless material changes have occurred. However, a letter signed by an officer of the foreclosing institution will be required listing the lots being foreclosed and a statement indicating that:

- ❖ The institution is familiar with the contents and representations made in connection with the subdivision offering as filed with DRE.
- ❖ The lots/units will not be sold subject to any blanket encumbrance.
- ❖ There have been no material changes to the offering as set forth

in Commissioner's Regulation 2800.

For common interest subdivisions, the new foreclosing owner must still comply with Regulation 2792.9 and the method of compliance must be as noted in the public report. The lender must use the identical method of compliance made by the previous owner/subdivider. Otherwise, the lender will be required to apply for an amended public report using RE 635.

Most subdividers select the method described in Regulation 2792.9(a)(2) (i.e., posting of a bond) and assuming the foreclosing lender selects the same method, compliance can be achieved by either of two methods: (1) Obtain a new surety bond or (2) have the existing

bond amended with the lender as the new obligor. The lender must also execute and return to the DRE for inclusion in the subdivision file RE 643. Changing to a set-aside letter or letter of credit would require an amendment to the subdivision public report if the subdivider had previously posted a surety bond. This requirement remains in effect until 80% of the lots/units are sold or leased.

The DRE has found that in the majority of cases, the foreclosing lender cannot utilize the exemption set

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AB 2881 – Notice of right to farm

AB 2881 –“Notice of Right to Farm” became effective January 1, 2009. This bill requires developers to disclose to potential buyers if the property being offered lies within one mile of a farm or ranch land, as set forth in the most current “Important Farmland Map” issued by the California Department of Conservation, Division of Land Resource Protection www.conservation.ca.gov/dlrp/fmmp/Pages/RE_Disclosure.aspx.

It is the responsibility of the developer to determine if the subdivision is located within one mile of property designated as “Prime Farmland,” “Unique Farmland,” “Farmland of Statewide Importance,” or “Grazing Land” on the most current “Important Farmland Map” issued by the California Department of Conservation, and if so, the following note shall be placed in the “Hazards” section of the Public Report:

Notice of Right to Farm

This property is located within one mile of a farm or ranch land designated on the current county-level GIS “Important Farmland Map,” issued by the California Department of Conservation, Division of Land Resource Protection. Accordingly, the property may be subject to inconveniences or discomforts resulting from agricultural operations that are a normal and necessary aspect of living in a community with a strong rural character and a healthy agricultural sector. Customary agricultural practices in farm operations may include, but are not limited to, noise, odors, dust, light, insects, the operation of pumps and machinery, the storage and disposal of manure, bee pollination, and the ground or aerial application of fertilizers, pesticides, and herbicides. These agricultural practices may occur at any time during the 24-hour day. Individual sensitivities to those practices can vary from person to person. You may wish to consider the impacts of such agricultural practices before you complete your purchase. Please be advised that you may be barred from obtaining legal remedies against agricultural practices conducted in a manner consistent with proper and accepted customs and standards pursuant to Section 3482.5 of the Civil Code or any pertinent local ordinance. ♦



Completion arrangements and related current issues

Due, in part, to the current economic climate, many developers are seeking to ease their financial burdens after the initial public report has been issued. As a result, a number of problematic situations related to completion arrangements have arisen.

Amendment applications have been filed for various purposes including: (a) amendments for new subdividers due to bulk sale transactions, (b) revised phasing plans to add more phases to a project and to extend completion of the overall project, and (c) CC&Rs amendments to meet FHA lender guidelines. Pursuant to these types of amendment applications, changes in the arrangements for the completion of common area may be proposed or deemed necessary.

For instance, a subdivider under an amended public report may propose to extend the time for completion of common area improvements, or a new applicant (subdivider) may propose to change the completion arrangement from a completion bond (RE 611) in favor of using escrow instructions.

If a completion bond (RE 611) was posted as the completion arrangement and escrows have closed in the project, extensions of the estimated date for completion of the common area improvements requires the written consent of both the association and the surety. The reasons consents from these parties are required are as follows:

- A) The subdivider stated and provided an estimated completion date for the common area improvements on the Planned Construction Statement (RE 611A) which is appended to and incorporated by reference into the Bond (Completion of Common Facilities) (RE 611).
- B) The Common Area Completion Security Agreement (RE 613), Part One, Covenant 6, provides that the subdivider may extend the estimated completion date for a longer period upon the approval of the homeowner association (HOA). This section of the agreement also provides that the subdivider (with notification to the Commissioner) may extend

the estimated completion date for up to six months due to events beyond the reasonable control of the subdivider.

- C) The completion Bond provides as follows:

“The condition of this obligation is such that if Principal shall complete or cause to be completed said improvements free of liens and claims on or before the latest completion date specified in said “Planned Construction Statement”, or an extension thereof given in writing by Oblige to Principal and assented to in writing by Surety, then this obligation shall be null and void; otherwise, it shall remain in full force and effect.

A suit or action of this bond must be filed within two (2) years after the latest completion date set forth in the Planned Construction Statement or any extension thereof given in writing by Oblige to Principal and assented to in writing by Surety.”

NOTE: Whether the Surety provides a rider to the original bond or a written statement accepting the extension to the completion date, it must be signed by a party who has authority to sign on behalf of the Surety; therefore a Power of Attorney statement must accompany these documents.

Below are some examples of other situations that we hope will at least help to alert subdividers of factors to be considered and/or problems that may be encountered:

- ❖ A new Subdivider files for an amendment on a two-phase Planned Development which included a proposed change of Common Area completion arrangement from a



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Capital contributions and start-up funds

In order to provide “start-up” funds for an association, the subdivider may set aside a portion of the purchase price of lots or units to be added to the homeowners' association's (HOA's) account, or may charge each purchaser a specified amount to be paid directly to the HOA upon close of escrow. This is generally called a Capital Contribution and is not a prepayment of the periodic assessment obligation.

It is not necessary to obtain financial assurances or a pre-payment from the subdivider to ensure timely payment of these funds unless the subdivider opts to have a like sum paid to the association for each unsold lot/unit on a future date (usually six (6) months).

If the subdivider chooses the latter,

he/she must arrange for a like sum to be paid on behalf of each unsold lot or unit in the subdivision. This may be accomplished by either depositing an amount equal to the obligation for all interests in the project, in the association's account up front and then provide through escrow instructions for reimbursement from the additional fees to be collected for purchasers.

Alternatively, the subdivider may arrange during the initial period for the payment by each purchaser directly to the HOA as each escrow closes, and then deposit a lump sum at the end of the date certain covering the obligation of all unsold lots or units. As the remaining interests are sold, the subdivider may be reimbursed directly from funds paid by the purchasers.

Unless all the start-up funds are paid in one lump sum upfront by the subdivider, it will be necessary for the subdivider to post a security along with applicable escrow instructions in favor of the HOA to assure the obligation to pay the fees at the end of the date certain for all unsold lots or units covered by the public report.

Alternatively, the subdivider may include in the escrow instructions a provision that before the first close of escrow proof has been provided to the escrow holder that the subdivider has deposited to the account of the association the entire amount of funds to be collected and shall be entitled to reimbursement of the start-up funds paid by each purchaser at the close of each escrow. ♦

Lender Foreclosure

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forth in §11010.5 of the Code if the subdivision is a common interest type subdivision. The reason relates to the homeowners association (HOA) budget and the assessments owners must pay.

Experience has shown that if the lender has taken title, then it is highly likely that the subdivider did not pay HOA assessments for unsold units as well. In that event there may be a material change as defined in Regulation 2800, resulting in the expiration of the public report. Generally, the DRE does not require a foreclosing lender to restore the HOA's reserve accounts.

However, if the shortage is not corrected and is severe enough to fall within Regulation 2800(k), then the foreclosing lender cannot use the exemption of §11010.5. An amended public report will be necessary to warn prospective buyers of the depleted reserve accounts, and that the buyer may be subject to a large increase of the regular assessments or a special assessment to restore the association's reserve accounts. ♦

Completion Arrangements

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bond to escrow instructions. Since escrows closed in Phase 1, the HOA would have to consent to release the security.

- ❖ When considering re-phasing a project, even if the developer bonded to assure completion of amenities in it's original phasing plan, he must also assure sufficient easement reservations are in place for access to complete amenities.
- ❖ Common errors in the completion security agreement, escrow instructions and the security instrument (e.g. bond, etc.) can present headaches in the future. Examples of common errors/issues include:
 - (1) not reflecting the HOA as the obligee,
 - (2) not properly identifying the property,
 - (3) not being signed by authorized parties,
 - (4) not accurately identifying the local authority (city or county) in which plans and specifications for the project are on file,
 - (5) Planned Construction Statement does not reflect an estimated completion date, or said date has already passed, and
 - (6) future mechanic lien assurances, particularly for phased single lot condominiums or single phases condominium projects in which there is more than one structure, should be included in Escrow Instructions. ♦

When does DRE require reserve studies?

The Department of Real Estate requires a reserve study to be submitted with duplicate budget packages for those projects that include buildings converted to, or were previously built as, condominiums, stock cooperatives or tenancy in common projects. A reserve study must be prepared in accordance with the requirements as set forth in Civil Code Section 1365.5(E). The reserve study should at the minimum include the items listed below:

- (1) Identification of the major components that the association is obligated to repair, replace, restore, or maintain that, as of the date of the study, have a remaining useful life of not more than 30 years.
- (2) Identification of the probable remaining useful life of the components identified in paragraph (1) as of the date of the study.
- (3) An estimate of the cost of repair, replacement, restoration, or maintenance of the components identified in paragraph (1).
- (4) An estimate of the total annual contribution necessary to defray the cost to repair, replace, restore, or maintain the components identified in paragraph (1) during and at the end of their useful life, after subtracting total reserve funds as of the date of the study.
- (5) A reserve funding plan that indicates how the association plans to fund the contribution identified in paragraph (4) to meet the association's obligation for the repair and replacement of all major components with an expected remaining life of 30 years or less, not including those

components that the board has determined will not be replaced or repaired. The plan shall include a schedule of the date and amount of any change in regular or special assessments that would be needed to sufficiently fund the reserve funding plan. The plan shall be adopted by the board of directors at an open meeting before the membership of the association as described in §1363.05. If the

board of directors determines that an assessment increase is necessary to fund the reserve funding plan, any increase shall be approved in a separate action of the board that is consistent with the procedure described in §1366.

A Common Interest Subdivision Conversion Supplementary Questionnaire (Form RE 639) must also be included in the duplicate budget filings. It is important to note the date of past or future renovations when completing the form. It is also recommended to include copies of paid invoices for those renovations that have been recently completed for DRE's verification purposes. Projects over 10

years old are required to have a roof certification completed by a licensed roofing contractor. The certification should indicate the estimated remaining life of the roof and the cost to replace. A copy of the certification must be included with the duplicate budget package.

For additional information on reserve studies, reference our Website's Publications Tab for "A Reserve Study Guidelines For Homeowner Association Budgets". ♦

Frequently used form packets

All DRE forms can be found at www.dre.ca.gov

Preliminary Public Report Packet

Includes: 603, 603A, 603B, 603C, 603D, 605, 612, 612A, 695C, 909

Common Interest Packet

Includes: 350, 603, 603A, 603B, 603C, 605, 611, 611A, 611B, 612, 612A, 619, 623, 624, 624A, 639, 643, 648, 681, 684A, 695C, 699, 699C, 909

Standard Packet

Includes: 350, 603, 603A, 603B, 603D, 605, 612, 612A, 619, 628, 695C, 699A, 909

In-State Amendment/Renewal Packet (*non time-share*)

Includes: 350, 600C, 605, 619, 635, 635A, 643, 695C, 909

Out-of-State Registration Packet (*in- and out-of-state*)

Includes: 608, 608A, 608B, 608C, 608D, 626C

Completion of Common Facilities Packet

Includes: 611, 611A, 611B, 611C, 611D

Completion Arrangements Packet (*in-state*)

Includes: 621, 621A, 621B

Time-Share Packet (*in- & out-of-state*)

Includes: 350, 605, 608, 608A, 608B, 608C, 608D, 609, 611, 611A, 611B, 611C, 611D, 613, 619, 623, 624A, 626D, 629, 631, 639, 643C, 648A, 656A, 668, 668A, 681, 695C, 909