National Banker Call

Loan Originator Compensation and HOEPA Final Rules

Thursday, June 6, 2013
Agenda

Regulation Z Amendments (TILA)

- Loan Originator Compensation Rule (LO Final Rule)
  - Compensation restrictions
  - Qualification requirements

- HOEPA Amendments (HOEPA Rule)

- Questions and Answers
Email Address

E-mail your questions to:

bankerteleconference@fdic.gov
Loan Originator Rule

Background

• Federal Reserve Board (Board):
  ▪ August 2009 – issues proposed rule on loan originator compensation
  ▪ September 2010 – finalizes proposal
  ▪ April 2011 – loan originator final rule becomes effective

• Dodd-Frank Act:
  ▪ July 2010 – amends TILA
    • Codifies significant elements of the Board’s 2010 Loan Originator Rule and implements additional requirements.
  ▪ July 2011 – transfers the vast majority of Federal consumer financial laws to the Consumer Financial Protection Bureau (CFPB)
Loan Originator Rule

Effective Date

• LO Final Rule
  ▪ January 10, 2014

• Provision (h)
  ▪ June 1, 2013 (applies to transactions for which the creditor receives an application on or after this date)

• Provision (i)
  ▪ January 10, 2014 (delayed from its original effective date of June 1, 2013)
Loan Originator Rule

LO Final Rule Topics Covered

1. Restrictions and clarifications on loan originator compensation.
2. Exceptions to prohibition on compensation based on profits.
3. Exemption from the Dodd-Frank Act’s prohibition on consumer payment of upfront points and fees.
4. Loan originator qualification and training requirements and use of unique identifiers.
5. Prohibition on mandatory arbitration/waivers of consumer rights, and financing single-premium credit insurance.
6. Other provisions of the LO Final Rule.
Loan Originator Rule

Scope

• LO Final Rule applies to closed-end consumer credit transactions secured by a dwelling.
  ▪ Includes:
    • First- and subordinate-lien loans
    • Reverse mortgages that are not HELOCs
  ▪ Excludes
    • HELOCs (except provisions (h) and (i))
    • Timeshare plans
• Provisions (h) and (i) have same scope as LO Final Rule, except that these two provisions also apply to HELOCs when secured by consumer’s principal dwelling.
Loan Originator Rule

Definition of “Loan Originator” Revised and Expanded

• In expectation of direct or indirect compensation or other monetary gain or for direct or indirect compensation or other monetary gain, performs any of the following activities:
  ▪ Takes an application;
  ▪ Offers, arranges, assists a consumer with obtaining or applying to obtain, negotiates, or otherwise obtains or makes an extension of consumer credit for another person; or
  ▪ Through advertising or other means of communication represents to the public that such person can or will perform any of these activities.

• The definition may include anyone involved in the loan origination process.
Loan Originator Rule

Persons That May Be Loan Originators

- Anyone that meets the definition of loan originator, including:
  - Employees, agents and contractors of a creditor or loan originator organization.
  - Creditors engaged in origination activities but do not finance the transaction.
  - Producing managers if they perform loan originator activities.
Persons That May Not Be Loan Originators

• If they meet certain requirements:
  - Employees of manufactured home retailers;
  - Employees performing purely administrative and clerical tasks;
  - Processors, underwriters, and closers;
  - Bona fide third-party advisors;
  - Real estate brokers performing only real estate activity;
  - Seller financers; and
  - Servicers or their employees, agents or contractors – under limited circumstances.
Loan Originator Rule

Activities

• If performed would render a person a loan originator:
  ▪ Referring a consumer to any loan originator
  ▪ Arranging a credit transaction
  ▪ Advertising or communicating by any means that the person can or will perform loan origination services
  ▪ Assisting a consumer in obtaining or applying for consumer credit by advising on specific credit terms

• If performed would not render a person a loan originator:
  ▪ General explanation, information, or descriptions in response to consumer inquiries (such as explaining terminology or lending policies)
Loan Originator Rule

Individual Loan Originator

• Any natural person that meets the definition of a loan originator.

Loan Originator Organization

• Any loan originator that is not an individual loan originator.

• May be any of the following forms of legal existence (among others):
  ▪ Sole proprietorships
  ▪ Corporations
  ▪ Financial institutions (including FDIC-supervised institutions meeting loan originator definition)
Loan Originator Rule

“Takes an Application”

- **Includes, among other things:**
  - Filling out application, inputting the information to online application, taking information over the phone.
  - Processing or analyzing the information.
  - Discussing specific transaction terms.

- **Excludes, among other things:**
  - Providing an application form to consumer at consumer’s request.
  - Accepting a completed application form from the customer.
  - Delivering application to LO without assisting the consumer in completing the application; processing or analyzing the information; or discussing specific credit terms or products available.
  - Aiding a consumer to understand how to complete an application.
“Compensation”

- New definition under the LO Final Rule
- Includes:
  - Salaries;
  - Commissions; and
  - Any financial or similar incentive.

- Excludes bona fide and reasonable charges for:
  - Third-parties services that the LO receives but does not retain;
  - Services performed by LO organization or an affiliate that are not loan origination activities; or
  - Services that are not loan originator activities where the amounts are not retained by the LO but are paid to the creditor, its affiliate, or the affiliate of the LO organization.
## Loan Originator Rule
### Compensation Restrictions

<table>
<thead>
<tr>
<th>Existing Rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>No compensation based on “terms or conditions” of the transaction except where such compensation is paid directly by the consumer (existing commentary explained that compensation based on a proxy for a term of a transaction was also prohibited).</td>
</tr>
<tr>
<td>No dual compensation.</td>
</tr>
<tr>
<td>No steering.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>LO Rule</th>
</tr>
</thead>
<tbody>
<tr>
<td>No compensation based on “terms” or a proxy for a term (no exception for consumer-paid compensation based on terms of a transaction). Removes “condition” from related regulatory text and commentary.</td>
</tr>
<tr>
<td>No dual compensation (makes one exception).</td>
</tr>
<tr>
<td>No steering (makes one revision).</td>
</tr>
</tbody>
</table>
Loan Originator Rule
General Prohibition

No Compensation Based on the Terms of a Transaction or Proxy for a Term of a Transaction

- Definition “term of a transaction”

“Any right or obligation of the parties to a credit transaction”

<table>
<thead>
<tr>
<th>Term of transaction</th>
<th>Not a term of transaction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate</td>
<td>Overall loan volume</td>
</tr>
<tr>
<td>APR</td>
<td>Long term performance of loans</td>
</tr>
<tr>
<td>Collateral type</td>
<td>Hourly rate of pay for actual hours worked</td>
</tr>
<tr>
<td>Prepayment penalties</td>
<td>Compensation based on fixed % of amount of credit extended</td>
</tr>
<tr>
<td>Discount points; origination points, or fees</td>
<td>Quality of the loan originator’s files</td>
</tr>
</tbody>
</table>
Does the factor consistently vary with a transaction term?

If No, does not violate the rule.

If Yes, does LO have the ability to add, drop, or change the factor in originating transaction?

If No, compensation is not based on a proxy for a term of a transaction.

If Yes, does compensation based on a proxy for a term of a transaction?

If Yes, violates the rule.

If No, does not violate the rule.

START

Is the compensation based on term of transaction?

If No, does not violate the rule.

If Yes, does LO have the ability to add, drop, or change the factor in originating transaction?

If No, compensation is not based on a proxy for a term of a transaction.

If Yes, violates the rule.

If Yes, compensation based on a proxy for a term of a transaction.

Does not violate the rule.
Loan Originator Rule
Dual Compensation

Prohibition on Dual Compensation
• In connection with the same transaction, a loan originator cannot receive compensation from any other person if compensation is also received from the consumer.

Exception
• If a loan originator organization receives compensation from the consumer, compensation may be paid to the individual loan originator.
Loan Originator Rule
Steering

LO Final Rule continues the existing rules concerning the steering prohibition of § 1026.36 with a clarification to the types of options presented.

Where two or more loans have the same total dollar amount of discount points, origination points, or origination fees, the loan option with the lowest interest rate that also has lowest total dollar amount of discount points, origination points or origination fees must be presented by LO.

Existing Rule

- Cannot steer consumer to transaction with higher commission to LO unless in consumer’s interest
- Must present several loan options to consumer

Dodd-Frank Revises Existing Rule
# Loan Originator Rule

## Exception – Profits Based Compensation

### Exception – Profits-Based Compensation

**Designated Tax-Advantaged Plan**

<table>
<thead>
<tr>
<th>Plan Type</th>
<th>Requirements</th>
</tr>
</thead>
</table>
| Defined Contribution Plan     | • Compensation permitted even if based directly or indirectly on the terms of multiple transactions of multiple individual loan originators.  
                               |   ➢ But...compensation may not be based on the terms of the transactions of the individual loan originator receiving the compensation. |
| Defined Benefit Plan           | • Compensation permitted even if based directly or indirectly on the terms of multiple transactions of multiple individual loan originators. |

### Exception – Profits-Based Compensation

**Non-Deferred Profits-Based Plan**

| Non-Deferred Profits Based Plan | • Compensation may not be based directly or indirectly on the terms of the transactions of the individual loan originator receiving the compensation; and either  
                                |   ▪ Compensation cannot exceed 10 percent of individual loan originator’s total compensation; or  
                                |   ▪ The individual loan originator was the originator for 10 or fewer mortgage loans during the 12 month period of determination.  
                                | • Includes, without limitation, bonus pools, profits pools, bonus plans, and profit-sharing plans. |
New Dodd-Frank Qualification Requirements

1. Imposes qualification requirements, and when applicable, registration and training, on:
   - Individual loan originators;
   - Mortgage brokers; and
   - Creditors.

   ➢ For purposes of qualification requirements, “loan originator” includes natural persons, and does not exclude creditors.

2. Requires the use of NMLSR unique identifier on specific loan documents.
Qualification Requirements Under Regulation Z

• Qualification requirements:
  ▪ Comply with all applicable State law requirements for legal existence and foreign qualifications;
  ▪ Each LO who works for LO organization must be licensed or registered before the individual acts as a loan originator; and
  ▪ For individual loan originators not required to be licensed obtain:
    • Criminal background; and
    • Credit report.

• Based on the above information ensure individual loan originators has:
  ▪ Not been convicted or pleaded nolo contendere to specific crimes; and
  ▪ Demonstrated financial responsibility, character, and general fitness.
Qualification Requirements Under Regulation Z

- **Employees not required to be licensed include:**
  - Depository institutions
  - Bona fide nonprofits

- **Requirements for individuals not required to be licensed:**
  - Provide training appropriate and consistent with the individual's loan origination activities; and
  - Meet financial responsibility, character, and general fitness, and criminal background standards.

- **Requirement applies to loan originator employees:**
  - Hired by the loan originator organization on or after January 10, 2014;
  - Hired by the loan originator organization before January 10, 2014, but for whom there were no applicable screening standards in effect at the time of hire; and
  - Regardless of when hired, those who, based on reliable information known to the loan originator organization, would likely not meet the above requirements.
Identifier Requirements Under Regulation Z

- **Name & Unique identifier or NMLSR ID required for:**
  - Individual loan originators;
  - Mortgage brokers; and
  - Creditors.

- **Name & NMLRS ID required on the following documents:**
  - The credit application;
  - The note or loan contract; and
  - The security instrument.

- **The documents should have the name & NMLSR ID of the individual with primary responsibility for the transaction at the time document is issued.**
Loan Originator Rule

Two More New Dodd-Frank Requirements

1. Prohibition on mandatory arbitration clauses and waivers of certain consumer rights.

2. Prohibition on financing single-premium credit insurance.
Prohibition on Mandatory Arbitration

- Creditors may not include terms requiring arbitration or other non-judicial procedure.

- Applies to closed-end consumer credit transactions secured by a dwelling and HELOCs when secured by the consumer’s principal dwelling.

- Prohibition applies to transactions for which the creditor receives applications on or after June 1, 2013.
Prohibition on Mandatory Arbitration

- Prohibition applies to the terms of the entire transaction.
  - Including the promissory note, the security instrument, or any other document executed as part of the transaction.

- Consumer and creditor may agree after dispute arises to use arbitration or other non-judicial procedure to settle such dispute.
Prohibition on Waivers

- Creditors may not include waivers of Federal statutory causes of action in contracts or other agreements.

- Applies to closed-end consumer credit transactions secured by a dwelling and HELOCs when secured by the consumer’s principal dwelling.

- Prohibition applies to transactions for which the creditor receives applications on or after June 1, 2013.

- Consumer and creditor may settle after the dispute arises:
  - Post-dispute may in effect act as a waiver of the consumer’s right to bring that particular claim in court, even if it is a Federal law claim.
Prohibition on Financing Single-Premium Credit Insurance

- Creditors may not *finance* directly or indirectly, premiums or fees for credit insurance, except for unemployment credit insurance if certain requirements are met.

- Applies to closed-end consumer credit transactions secured by a dwelling and HELOCs when secured by the consumer’s *principal* dwelling.

- Prohibition applies to covered transactions on or after January 10, 2014 (delayed from June 1, 2013).
Record Retention Requirements

• Expanded record retention requirements:
  ▪ Creditors must maintain records sufficient to evidence compensation payments and copy of compensation agreement governing payments.
  ▪ Loan originator organizations must maintain records sufficient to evidence:
    • Compensation received from a creditor, a consumer, or another person and the compensation it pays to its loan originators; and
    • Compensation agreements that govern those payments.

• Records must be maintained for three-years from date of payments or receipts.

• “Sufficient to evidence” requirement will based on facts and circumstances of each case.
Policies and Procedures for Depository Institutions

- Depository institutions must establish and maintain written policies and procedures reasonably designed to ensure compliance with:
  - Restrictions on payments to loan originators;
  - Prohibitions on steering;
  - Loan originator qualification requirements; and
  - Loan originator identifier requirements.

- Policies and procedures must be appropriate to the nature, size, complexity and scope of the mortgage credit activities.
Amendments to HOEPA

New Rules for High-Cost Mortgages
HOEPA

The new rules would:

• Expand the types of mortgages potentially subject to HOEPA;
• Revise and expand the triggers; and
• Revise the ability-to-repay requirements and make other changes to restrictions on high-cost loans.
• Also implement two homeownership counseling provisions unrelated to high-cost loans.

Effective date: January 10, 2014
Types of loans subject to HOEPA:

- Closed-end refinancing and home-equity loans;
- Purchase-money mortgages (NEW); and
- HELOCs (NEW).

Loans must be secured by the consumer’s principal dwelling, and for a consumer purpose.
HOEPA

Types of loans exempt from HOEPA:

• Loans to finance the initial construction of a dwelling;
• Loans originated and financed by Housing Finance Agencies;
• Loans originated through a U.S. Department of Agriculture Rural Housing Service program; and
• Non-recourse reverse mortgages.
Three Independent Triggers

A loan potentially subject to HOEPA will be subject to its special rules if it meets any one of three independent triggers:

- The **APR** trigger;
- The **Points and Fees** trigger; or
- The **Prepayment Penalty** trigger (NEW).
The APR Trigger

• 6.5% above APOR for first-lien loans

• 8.5% above APOR for:
  ▪ Subordinate-lien loans; or
  ▪ Loans under $50,000 secured by dwellings that are personal property.
## HOEPA

### The Points and Fees Trigger

Dollars to be adjusted annually

<table>
<thead>
<tr>
<th>Loan Amount</th>
<th>Trigger</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loans of $20,000 and up</td>
<td>5% of total loan amount</td>
</tr>
<tr>
<td>Loans below $20,000</td>
<td>The lesser of 8% of total loan amount or $1000</td>
</tr>
</tbody>
</table>
The Prepayment Penalty Trigger

• Loans with a prepayment penalty of:
  ▪ more than 2% of the amount prepaid; or
  ▪ imposed more than 36 months after consummation.

• Prepayment penalties are banned generally except in fixed-rate, prime-rate qualified mortgages (QMs).
Points and Fees: Closed-End Loans & Open-End Credit Plans

• Total points and fees trigger lowered from 8% to 5%.

• Points and fees definition and calculation rules are the same for QM and HOEPA loans.

• Six categories of charges are captured by the points and fees definition.
## HOEPA

### Points and Fees:
**Closed-End Loans & Open-End Credit Plans**

<table>
<thead>
<tr>
<th>Points and Fees Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>First</td>
<td><strong>Prepaid Finance Charges</strong></td>
</tr>
<tr>
<td></td>
<td>• Includes points, underwriting fees or processing fees, etc.</td>
</tr>
<tr>
<td></td>
<td>• New flexibility in calculating the 5% amount primarily found in this category. Possible exclusions:</td>
</tr>
<tr>
<td></td>
<td>- <em>Bona fide</em> discount points under certain circumstances;</td>
</tr>
<tr>
<td></td>
<td>- Government guaranty fees and <em>monthly</em> private mortgage insurance;</td>
</tr>
<tr>
<td></td>
<td>- <em>Upfront</em> private mortgage insurance in certain circumstances;</td>
</tr>
<tr>
<td></td>
<td>and</td>
</tr>
<tr>
<td></td>
<td>- <em>Bona fide</em> third party charges to unrelated parties, if not required to be included by other parts of the definition.</td>
</tr>
</tbody>
</table>
# HOEPA

## Points and Fees:
Closed-End Loans & Open-End Credit Plans

<table>
<thead>
<tr>
<th>Points and Fees Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Second</strong></td>
<td><strong>Loan Originator Compensation</strong></td>
</tr>
<tr>
<td></td>
<td>• Count compensation attributable to the transaction at time rate is set (including rate-paid compensation to brokers), except:</td>
</tr>
<tr>
<td></td>
<td>▪ Where direct consumer-payment to broker already counted under first category; and</td>
</tr>
<tr>
<td></td>
<td>▪ Payments by broker firms <em>and creditors</em> to individual loan originator-employees. (These are excluded under the May 29 amendments.)</td>
</tr>
<tr>
<td><strong>Third</strong></td>
<td><strong>Real Estate Settlement Charges</strong></td>
</tr>
<tr>
<td></td>
<td>• May include title-related fees, document fees or appraisal fees.</td>
</tr>
<tr>
<td></td>
<td>• Included only if they are paid to the creditor, an affiliate or are unreasonable.</td>
</tr>
</tbody>
</table>
## HOEPA

### Points and Fees: Closed-End Loans & Open-End Credit Plans

<table>
<thead>
<tr>
<th>Points and Fees Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fourth</td>
<td>Credit insurance related premiums and charges</td>
</tr>
<tr>
<td>Fifth</td>
<td>Maximum prepayment penalty that could be charged on the loan being made</td>
</tr>
<tr>
<td>Sixth</td>
<td>Prepayment penalty actually charged on a loan being refinanced by the current holder, a servicer acting on its behalf, or an affiliate of either</td>
</tr>
</tbody>
</table>
### HOEPA

#### Points and Fees: Open-End Credit Plans Only

<table>
<thead>
<tr>
<th>Points and Fees Category</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Seventh</td>
<td>Fees payable at or before closing charged for participation in the plan.</td>
</tr>
<tr>
<td>Eighth</td>
<td>Required transaction fees to make a draw on the line (assume one draw).</td>
</tr>
</tbody>
</table>
Non HOEPA–Related Counseling Requirements

Two New Counseling-Related Requirements are Unrelated to HOEPA Loans

• RESPA/Reg. X Amendment:
  ▪ Creditors must provide list of homeownership counseling organizations within 3 business days of application.
  ▪ List to be available through CFPB or HUD.

• TILA/Reg. Z Amendment:
  ▪ Mandatory counseling for first-time borrowers considering loans that will or may negatively amortize.
# Mortgage Rule Exemptions and Flexibility by Bank–Type

<table>
<thead>
<tr>
<th>Rule/Provision</th>
<th>“Community Banks” (less than $2 Billion in assets; 500 or fewer first lien loans; portfolio limitations)</th>
<th>“Community Banks” Rural/Underserved</th>
<th>Other Banks</th>
</tr>
</thead>
<tbody>
<tr>
<td>QM Balloon Exemption</td>
<td>✓ (2-year transition)</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>“Small Lender” QM (no 43% DTI requirement)</td>
<td>✓</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Legal Protection: Higher Safe Harbor Threshold for Subprime Portfolio (up to APOR + 350 bps)</td>
<td>✓</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>MLO Flexibility</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Escrow Exemption</td>
<td>✓</td>
<td></td>
<td>✓</td>
</tr>
<tr>
<td>Partial Servicing Exemptions</td>
<td>Available to “Small Servicers” = creditor or affiliate service 5,000 or fewer mortgage loans. Also available to Housing Finance Agencies (as defined by HUD).</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Questions and Answers

bankerteleconference@fdic.gov
Thank You

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