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LO Comp Rules Now in Effect - Fed and HUD Provide Clarification

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The Federal Reserve Board's new rules governing originator compensation are now in effect. After a five day court-imposed administrative delay, the United States Court of Appeals denied a request to further delay implementation of the rule. In March, the industry received additional guidance related to the new loan originator compensation rules effective April 6, 2011. Attorneys for the Federal Reserve Board of Governors held an online webinar on Thursday, March 17, 2011, and on Friday, March 18, 2011, HUD released a newsletter addressing GFE related-questions which have arisen as new compensation structures form. Highlights from both the Federal Reserve Board webinar and the HUD newsletter are included below:

Federal Reserve Board Webinar Highlights

- The loan originator compensation rules will be enforced by whichever authority

examines an institution. For any entities that are not examined by an agency currently, the new Consumer Financial Protection Bureau will have extensive examining authority, including the authority to examine non-depository institutions.

- The FED has not found any scenario where "point banks" are used to permit loan originators to offer pricing concessions to borrowers to be permissible under the new rules. According to the FED, the point banks constitute originator compensation which may not be reduced based on terms or conditions of a loan. Pricing concessions must be made by the Creditor.

- GFE tolerance violations for a particular loan are not a permissible factor to consider when determining loan originator compensation. If closing costs must be reduced to satisfy RESPA tolerance requirements the creditor, not the loan originator must bear this cost.

- There is no Safe-Harbor - "disclosure requirement." Although the most logical method of documenting the provision of loan options required to qualify for the protection of the Safe-Harbor will involve some type of written document, the rule does not contain a "disclosure requirement." The rule prohibits *steering* and one method available to originators seeking to demonstrate compliance with the anti-steering rule is to qualify for the safe-harbor

continued on next page

protection by satisfying the requirements set forth in that provision of the rule.

- Factors related to a loan's "profitability" are problematic if used as a basis for setting originator compensation. According to the FED, only a very unusual definition of "profitability" would not turn upon a term or condition of the loan.

- One remaining unanswered question set forth by the FED involves a loan for which the yield disclosed as a credit in GFE Block 2 is larger than the Borrower's closing costs. This could result in a scenario whereby the consumer pays the broker but the lender pays the consumer, which is problematic. To date, HUD has not commented on this issue.

HUD "RESPA Roundup" Newsletter Highlights

- According to HUD, the guidance contained in its official FAQs (latest revision April 2010) anticipates various compensation scenarios, including where compensation is based on factors other than the loan's interest rate - such as a flat rate or a fixed percentage of the loan amount. Therefore, for mortgage brokers, GFE Block 1 will continue to include the fixed amount of Broker compensation even where the Broker's compensation is lender-paid. GFE Block 2 will continue to include the net payment from lender to mortgage broker, represented as a credit to the Borrower, even though this amount is no longer determined by the interest rate.

- HUD refers to lender-paid mortgage broker compensation as "indirect compensation"; however, this lender-paid compensation is not indirectly paid by the Borrower which would violate the FRB rule prohibiting dual compensation. HUD clarifies that the indirect

compensation to which it refers in this scenario is entirely lender-paid.

- HUD recognizes that the zero-tolerance requirement applicable to GFE Block 1, Block 2 and Line A disclosures will require "timely and effective communication amount the lender, its loan officers, and mortgage brokers to establish policies and procedures to ensure accurate calculation of compensation and credits in compliance with RESPA, as well as under the FRB compensation rule."

- Additionally, HUD made the following comment related to volume-based compensation: "If a lender is basing its compensation to mortgage brokers on loan volume as described in the new FRB rule, please not that RESPA Section 8 prohibits the payment of things of value or kickbacks in exchange for the referral of business to settlement service providers, including creditors."

To review both the Federal Reserve Board webinar and the HUD newsletter, each in its entirety, use the following links:

<http://www.philadelphiafed.org/bank-resources/publications/consumer-compliance-outlook/outlook-live/2011/031711.pdf>

<http://www.hud.gov/offices/hsg/rmra/res/mlocomplrodup31811v2.pdf>