8 Hour GA SAFE Comprehensive: Compliance for 2020

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Rules of Conduct for NMLS Approved Pre-Licensure (PE) and Continuing Education (CE) Courses

The Secure and Fair Enforcement for Mortgage Licensing Act (SAFE Act), requires that state-licensed MLOs complete pre-licensing (PE) and continuing education (CE) courses as a condition to be licensed. The SAFE Act also requires that all education completed as a condition for state licensure be NMLS approved. Since 2009 NMLS has established course design, approval, and delivery standards which NMLS approved course providers are required to meet. To further ensure students meet the education requirements of the SAFE Act, NMLS has established a Rules of Conduct (ROC). The ROC, which have been approved by the NMLS Mortgage Testing & Education Board, and the NMLS Policy Committee, both of which are comprised of state regulators, are intended to stress that NMLS approved education be delivered and completed with integrity.

Rules of Conduct

As an individual completing either pre-licensure education (PE) or continuing education (CE), I agree to abide by the following rules of conduct:

1. I attest that I am the person who I say I am and that all my course registration information is accurate.

2. I acknowledge that I will be required to show a current government issued form of identification prior to, and during the course, and/or be required to answer questions that are intended to verify/validate my identity prior to, and during the course.

3. I understand that the SAFE Act and state laws require me to spend a specific amount of time in specific subject areas. Accordingly, I will not attempt to circumvent the requirements of any NMLS approved course.

4. I will not divulge my login ID or password or other login credential(s) to another individual for any online course.

5. I will not seek or attempt to seek outside assistance to complete the course.

6. I will not give or attempt to give assistance to any person who is registered to take an NMLS approved pre-licensure or continuing education course.

7. I will not engage in any conduct that creates a disturbance or interferes with the administration of the course or other students' learning.

8. I will not engage in any conduct that would be contrary to good character or reputation, or engage in any behavior that would cause the public to believe that I would not operate in the mortgage loan business lawfully, honestly or fairly.

9. I will not engage in any conduct that is dishonest, fraudulent, or would adversely impact the integrity of the course(s) I am completing and the conditions for which I am seeking licensure or renewal of licensure.

I understand that NMLS approved course providers are not authorized by NMLS to grant exceptions to these rules and that I alone am responsible for my conduct under these rules. I also understand that these rules are in addition to whatever applicable rules my course provider may have.

I understand that the course provider or others may report any alleged violations to NMLS and that NMLS may conduct an investigation into alleged violations and that it may report alleged violations to the state(s) in which I am seeking licensure or maintain licenses, or to other states.

I understand the CSBS Privacy Notice is applicable to these Rules of Conduct. The CSBS Privacy Notice can be found here:

https://nationwidelicensingsystem.org/about/policies/NMLS%20Document%20Library/CSBS%20External%20Priva cy%20Notice-6.18%20(1).pdf

I further understand that the results of any investigation into my alleged violation(s) may subject me to disciplinary actions by the state(s) or the State Regulatory Registry (SRR), including removal of any course from my NMLS record, and/or denial or revocation of my license(s).

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Course Number(s)

____	__________________
Signature	Date (mm/dd/yyyy)
____	__________________
Print Name	NMLS ID (If Known)

Module 1 & 2 Objective:

This module will provide the student with an understanding of the most common issues found with MMC examinations. With the MMC examination findings, regulators understood there was room for improvement of what is considered compliance as common threads of deficiencies were identified. Students will review the examination deficiencies and the regulations violated. With this knowledge, students will know their actions and company are in compliance with the federal laws that govern the mortgage lending industry.

In the following sections, "CFR" stands for "Code of Federal Regulations" and "USC" stands for "United States Code". Once Congress passes a law it is recorded in the United States Code (USC) books.The Code of Federal Regulations (CFR) are regulations issued by the various agencies which congress assigned to enforce the various laws (code) it adopted.   The agencies explain their interpretation of those laws assigned to them and how it intends to implement it.

Other abbreviations include:

"MMC" – Multi-State Mortgage Committee

"CSBS" – Conference of State Bank Supervisors

"AARMR" – American Association of Residential Mortgage Regulators

"CFPB" – Consumer Financial Protection Bureau

"MME" – Multi-State Mortgage Entities

"NMLS" – Nationwide Mortgage Licensing System

"SAFE Act" - Secure and Fair Enforcement for Mortgage Licensing Act

Module 1

Licensee Oversight Authority

The mortgage industry today has layers of regulators to ensure the financial services industry operates in a safe and sound manner. To accomplish this level of supervision the federal regulators' focus is on an overall health and safety of the financial services industry and enforceable consumer protections.

State agencies function on the first level of the industry to provide support for federal law enforcement and oversight. In addition, state agencies are charged with the tasks of issuing the licenses, supervision of licensees, coordinating examinations, and enforcing state laws governing the financial services industry including mortgage lending.

Multi-State Mortgage Committee

The Multi-State Mortgage Committee (MMC) is a representative body of 10 state mortgage regulators appointed by and reporting to the Conference of State Bank Supervisors (CSBS) and American Association of Residential Mortgage Regulators (AARMR). In addition, the MMC includes one member of Consumer Financial Protection Bureau (CFPB) to provide a team approach. The MMC was created to provide consistency across states and provide protocols and transparency for mortgage lenders and servicer examinations. MMC represent the examination interests of the combined states under the Nationwide Cooperative Protocol and Agreement for Mortgage Supervision.[1]

The MMC's primary focus is on Multi-state Mortgage Entities (MMEs), and works toward a less burdensome examination process. The MMC constructed a Mortgage Examination Manual to promote transparency and consistency in its examinations of these MMEs, and provides guidance for state agencies' examinations.

MMC Mortgage Examination Manual

The MMC Mortgage Examination Manual is comprised of several sections which provide information and/or guidance on specific topical areas. The general format of these sections are as follows:

- Introduction - Provides background information to introduce and support examination of the specific area.
- Examination Objectives - Outlines basic goals that should be of primary interest to the examiner in reviewing the respective area.
- Criteria and/or Guidance - Outlines applicable requirements, standards, or additional criteria relevant to the examination area.
- Examination Procedures - Provides procedural guidance to assist the examiner in evaluating the specific topical area.

State Agencies

State agencies use the MCCs Mortgage Examination Manual for guidance when examining licensees. An examination completed by State Regulators will identify if a financial institution is operating in compliance with state and federal laws. A review of a financial institutions loan files and corporate records are conducted to decide whether the entities are effectively meeting the requirement to operate, monitor, and control risks associated with mortgage loan origination activities.

State licensing is handled on a state level. The issuing of licenses to state-licensed mortgage professionals, supervision, and examinations are State Regulators responsibility with their authority over licensees and licensed activities of state chartered banks and non-bank entities including mortgage lenders. State agencies are to ensure financial services operate in a safe and sound manner.

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[1] https://www.csbs.org/system/files/2019-05/MMC%20Mortgage%20Examination%20Manual%20v2%20-%20May%202019.pdf

NMLS was created by the Conference of State Bank Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR). It is owned and operated by the State Regulatory Registry LLC (SRR) which is a nonprofit subsidiary of the Conference of State Bank Supervisors (CSBS) that operates NMLS on behalf of state financial services regulatory agencies.

CFPB is responsible for enforcing all federal laws for mortgage licensed activities including TILA, RESPA, ECOA and FCRA. Although CFPB may perform examination of state licensees that receive warranted complaints through its complaint portal, its primary focus is on multi-state large licensees or entities. MMEs are subject to state and federal examinations, and may have more scrutiny of its origination activities since it poses a large threat to consumers if the MME is not operating in compliance with the laws.

Examination Common Deficiencies

Licensees are required to follow all federal law that govern their licensing activities. The regulator examinations identified common deficiencies across state-licensees examined. With the examination findings, regulators understood there is room for improvement of what is considered compliance as common threads of deficiencies were identified. The Conference State Banking Supervisors (CSBS) has required all NMLS licensees take a continuing education course in 2020 that reviews and informs licensee of the examination deficiencies and provide guidance on how to correct the non-compliant behavior. The following reviews these identified deficiencies and what is considered compliant.

TILA Tolerance Violations

Regulation Z requires only certain closing cost fees disclosed on the Loan Estimate to not exceed the amount charged at closing on the Closing Disclosure. The regulation provides some fees have a tolerance for change, but prohibits certain other fees, such as loan origination fees, from increasing or change after disclosed. Any fee change must be in compliance with allowable change of circumstance.

For example, a discount point may be added if consumer requests lower rate when interest rate is locked.

The examination deficiency identified the creditor failed to cure zero tolerance charge violations within the required 60 days of consummation. For charges subject to zero tolerance, any amount charged beyond the amount disclosed on the loan estimate must be refunded to the consumer within 60 days of consummation.[2]

[2] Regulation Z, 12 CFR § 1026.19(e)(3)

Zero Tolerance Fee Review

Creditors must provide a revised Closing Disclosure to correct non-numerical clerical errors and document refunds for tolerance violations no later than 60 calendar days after consummation.[3] The general rule for disclosed closing costs is they are not in good faith if the charge paid by or imposed on the consumer exceeds the amount originally disclosed on the Loan Estimate. The zero tolerance loan fees include the following:

1. Fees paid to the lender
    a. For example, origination fee, processing fee, underwriting fee
2. Fees paid to a mortgage broker
    a. For example, origination fee, processing fee, broker fee
3. Fees paid to an affiliate of the lender or a mortgage broker
    a. For example, affiliated title company, appraiser, inspector
4. Fees paid to an unaffiliated third party, if the lender did not permit the consumer to shop for the third party service provider for settlement services
    a. For example, appraiser, property inspection required by lender
5. Transfer taxes – tax levied on the transfer of ownership of a property paid to the state entity requiring it.
    a. Mortgage lenders and originators must KNOW what transfer taxes to disclose as this is a zero tolerance fee.

The provision defines a charge as a charge "paid by or imposed on the consumer" which refers to the final amount for the charge paid by or imposed on the consumer at consummation or settlement, whichever is later.

For example, at closing, the consumer pays $85 for recording fees per the Closing Disclosure. After the loan records, the title agent identifies the actual recording fees were $70. The lender's funder identifies the discrepancy and provides the title company with corrected lender instructions to refund the $15 to the borrower and update the Closing Disclosure. The regulation considers it compliant if the lender corrects the violation within 60 calendar days of the settlement. If the Lender's funder did not catch the violation, the Lender's Quality Control Department likely would have.

Mortgage companies have layers of compliance checks to ensure compliance with TILA tolerances. The lender may…

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[3] § 1026.19(f)(2)(iv)-(v)

1. Use trained designated employees to send the disclosures as a means to ensure compliance

2. Require employee training of TILA and company policies for compliance

3. Use software that will flag or prohibit tolerances

4. Have quality control department perform file audits after closing

It is the Mortgage Company's responsibility to be in compliance, and how they layer their compliance and train employees will affect their level of compliance when examined. The higher the compliance level, the lower cost of fines and examination fees, and less likely it will lose its license to originate mortgage loans.

RESPA Creditor Responsibilities

If a mortgage broker issues any disclosure required in the creditor's place, the creditor remains responsible for ensuring that the requirements of RESPA have been satisfied.

For example, if a mortgage broker receives a consumer's application and provides the consumer with the required early disclosures the creditor does not satisfy the requirements if it provides duplicative disclosures to the consumer.

In this same example, even if the broker provides an inaccurate disclosure, the creditor is responsible and may not issue a revised disclosure correcting the error outside the allowable change of circumstances. The creditor is expected to maintain communication with the broker to ensure that the broker is acting responsibly in place of the creditor when it is providing the early application disclosures. [4]

Mortgage Broker Provision

Regulation X provides that if a mortgage broker receives a consumer's application, either the creditor or the mortgage broker must provide the consumer with the required early application disclosures within three business days of application. The continuity of RESPA disclosures provided to the consumer by the mortgage broker and creditor have been defined in the regulations.

If the mortgage broker issues the application disclosures, this regulation gives the term "mortgage broker" the same responsibility as the "creditor" for all provisions of RESPA disclosures, except it's a creditor's responsibility to ensure disclosures provided by mortgage brokers comply with all requirements, including those to satisfy the creditor's obligation to disclose. Regulations do not allow a mortgage broker to provide the closing disclosure.

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[4] See interpretation of 19(e)(1)(ii) Mortgage broker. in Supplement I

For example, if a mortgage broker provides the early application disclosures, it must maintain early disclosure records for three years, in compliance with RESPA. The creditor must accept the fees quoted by the mortgage broker, and stay compliant with change of circumstance tolerances.

Required 10% Tolerance Charges

TILA Regulation Z requires loan estimate fees quoted for 'services the borrower may shop for' to be within a 10% limitation prescribed by the regulation.

The examination deficiency identified the creditor failed to cure 10% tolerance charge(s) within the prescribed 60 days of consummation. For charges subject to a 10% cumulative tolerance, to the extent the total sum of the charges added together exceeds the sum of all such charges disclosed on the loan estimate by more than the 10%, the difference must be refunded to the consumer.

Binding Loan Estimate (LE)

The creditor is limited by the tolerances for fee changes provided in this regulation once fees are disclosed to the borrower. If the creditor needs to change a fee and redisclose the Loan Estimate, the creditor must remain within the change of circumstance tolerances allowed by regulation including the 10% tolerance fees. If a creditor provides a revised LE, the loan originator must document for compliance the reason a revised LE was provided.

Creditors must retain the LE and compliance documentation of any reason for providing a revised LE for no less than three years after settlement.

<u>Changed of Circumstances</u>

If changed circumstances result in increased costs for any settlement services that causes the charges at settlement to exceed the tolerances, a revised LE may be provided. The revised LE may increase charges for services listed on the LE only to the extent the changed circumstances resulted in cumulative higher charges not to exceed the 10% limitation for change.

If changed circumstances result in a change in the borrower's eligibility for the loan terms identified in the LE, the loan originator may provide a revised LE to the borrower. If a borrower requests changes to the settlement charges or the terms of the loan, the loan originator may provide a revised LE to the borrower. For all revised LEs provided, the loan originator must do so within three business days of receiving information sufficient to establish a changed circumstance. All other charges and terms must remain the same as on the original LE.

If a borrower requests changes to the settlement charges or the terms of the loan, the loan originator may provide a revised LE to the borrower.

If a borrower does not express an intent to continue with an application within 10 business days after the initial LE is provided, the loan originator is no longer bound by the LE. A revised LE does not require another intent to proceed from the borrower, and the creditor is committed to the fees disclosed upon delivery without another 10 business days waiting period as the borrower does not need to accept the revised LE.

If the interest rate has not been locked, or a locked interest rate has expired, the charge or credit for the interest rate chosen, the adjusted origination charges, per diem interest, and loan terms related to the interest rate may change when locked as an allowable change of circumstance. The creditor must provide the revised LE within three business days of the interest rate lock, or for an expired interest rate, re-locked.

The creditor must provide the revised LE within three business days of the interest rate lock, or for an expired interest rate, re-locked. All other charges and terms must remain the same as on the original LE.

In transactions involving new construction home purchases, where settlement is anticipated to occur more than 60 calendar days from the time a LE is provided, the creditor may provide the LE to the borrower with a clear and conspicuous disclosure stating at any time up until 60 calendar days prior to closing, the creditor may issue a revised LE. If no such separate disclosure is provided, the creditor cannot issue a revised LE.

Loan Estimate Violation

A creditor that violates the RESPA disclosure requirements is deemed to have violated section 5 of RESPA. If any charges at settlement exceed the charges listed on the LE by more than the permitted tolerances, the loan originator may cure the tolerance violation by reimbursing the borrower the amount exceeded, at settlement or deliver or place the payment in the mail within 30 calendar days after settlement.[5]

TILA Loan Estimate Timing

TILA Regulation Z requires the creditor deliver or place in the mail the initial disclosures not later than the third business day after the creditor receives the consumer's application, as defined by RESPA.[6]

The examination deficiency identified the Initial Loan Estimates (or early disclosures) were not delivered to the borrowers within the required three business day timeframe.

For example, if an application is received on Tuesday, the creditor satisfies this requirement by either electronic deliver or placing the disclosures in the mail on or before Friday, assuming each weekday is a business day.

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[5] https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1024/7/#h

[6] 12 CFR § 1026.19(e)(1)(iii)

Regulations define the term **“business day”** for the loan estimate as a day on which the creditor's offices are open to the public for carrying out substantially all its business functions.

Regulations requires a **seven business-day waiting period** to start when the creditor delivers the disclosures or places them in the mail, not when the consumer receives or is considered to have received the disclosures. The creditor may not fund the loan until the waiting period is over to allow consumers time to understand the transaction, shop other lenders and decide if they want to close the transaction.

For example, if a creditor delivers the early disclosures to the consumer by email or places them in the mail on Monday, August 3, consummation may occur on or after Tuesday, August 11. The 7th business day following delivery of the early disclosures. Saturday is considered a business day for early disclosure delivery, Sunday and federal holidays are not.

Recording Fee Cost on Closing Disclosure

Regulation Z states the creditor will disclose required information as applicable. Required information includes, under the master heading "Closing Cost Details", all costs in connection with the transaction, including taxes and other government fees.[7]

The examination deficiency identified recording fees were not properly marked to reflect the government fee covered. Companies failed to detail the amount for each type of recording fee in the closing costs details section of the Closing Disclosure. Instead including recording fees with government fees in violation of the regulations.

Per the regulations, the “Closing Cost Details” table must contain the items and amounts described below:[8]

- Under the subheading “Taxes and Other Government Fees,” an itemization of each amount expected to be paid to State and local governments for taxes and government fees and the total of all itemized amounts that are designated borrower-paid at or before closing.
- The creditor may itemize the transfer taxes paid on as many lines as necessary to disclose all the transfer taxes paid as part of the transaction. The taxes should be allocated in the applicable columns as borrower-paid or seller-paid at or before closing, or paid by others, as provided.
    - Remember, transfer taxes are a zero tolerance for change after disclosure. Recording fees may change.

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[7] 12 CFR § 1026.38(g)(1)(i)

[8] https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1026/38/#38-g-1-Interp-ii

- Fees for recording deeds and security instruments are required on the first line under the subheading "Taxes and Other Government Fees". Creditors must disclose the total fees expected to be paid to State and local governments for **recording deeds** and separately, the total fees expected to be paid to State and local governments for recording **security instruments**.[9] Deeds transfer the title from seller to buyer, and security instruments provide the lender's security for repayment of the Note.

Required Loan Estimate in Good Faith

Regulation Z states an estimated closing cost disclosed on the Loan Estimate is in good faith if the charge paid by or imposed on the consumer does not exceed the amount originally disclosed for a third party service the consumer cannot shop for.[10]

The examination deficiency identified companies are failing to disclose properly.

A creditor in a closed-end consumer transaction secured by real property or a cooperative unit, other than a reverse mortgage, must provide the consumer a loan estimate disclosure in compliance with loan estimate content requirements.[11] These early disclosure of credit terms must be provided in good faith.

A disclosure is considered in good faith if it provides information necessary for an accurate disclosure as known to the creditor, and makes the disclosure based on the best information reasonably available to the creditor at the time the disclosure is provided to the consumer.

The "reasonably available" standard requires that the creditor, acting in good faith, exercise due diligence in obtaining fee information.[12]

Closing Disclosure Accuracy

Regulation Z states that for each transaction subject to 1026.19(f) the creditor will disclose the information required including an itemization of origination charges and lender credits. In addition, the information required to be disclosed in the summary of borrower's transaction and summary of seller's transaction may be disclosed on separate pages to the consumer and the seller, respectively.[13] This provides privacy to either party of the fees, costs and proceeds received.

For example, if the creditor requires the consumer to pay money into a reserve account for the future payment of taxes, the creditor must disclose to the consumer the exact amount that the consumer is required to pay into the reserve account. If the disclosures provided do not contain the

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9 Section 1026.38(g)(1)(i)(A)
10 12 CFR. § 1026.19(e)(3)(i)
11 https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1026/37/
12 See interpretation of 19(e)(1)(i) Creditor. in Supplement I
13 12 CFR., § 1026.38

actual terms of the transaction, the creditor does not violate RESPA if the creditor provides corrected disclosures of the actual terms and complies with the other requirements, including the corrected disclosure timing requirements.

For example, if the creditor provides the disclosures required on Monday, June 8, but the consumer adds for their convenience a mobile notary service to the terms of the transaction on Tuesday, June 9, the creditor complies if it provides disclosures reflecting the notary fee on or after Tuesday, June 9, assuming that the corrected disclosures are also provided at or before consummation requirements. The mobile notary was an unforeseen fee requested by the borrower.

As with the Loan Estimate, creditors may estimate the closing disclosures provided using the best information reasonably available when the actual term is unknown to the creditor at the time disclosures are made.

- An actual term is unknown if it is not reasonably available to the creditor at the time the disclosures are made.
- The "reasonably available" standard requires that the creditor, acting in good faith, exercise due diligence in obtaining the information. [14]

For example, the creditor must look to the most obvious choice for who may have the information to obtain the accurate fee or charge. Creditor might look to the consumer for information, to insurance companies for the cost of insurance, to title for taxes and escrow fees, or to a realtor for homeowner's association dues or other information in connection with a real estate settlement.

The following examples illustrate the reasonably available standard:

1. Assume a creditor provides the disclosure for a transaction in which the title insurance company providing the title insurance policy is acting as the settlement agent in the transaction, but the creditor does not request the actual cost of the lender's title insurance policy that the consumer is purchasing from the title insurance company and instead discloses an estimate based on information from a different transaction. The creditor has not exercised due diligence in obtaining the information about the cost of the lender's title insurance policy required under the "reasonably available" standard.
2. Assume that in the prior example the creditor obtained information about the consumer's transaction from the settlement agent regarding the amounts disclosed, or can document their multiple attempts to obtain the information from the title company prior to using an estimate from similar transactions. The creditor has exercised due diligence in obtaining the information

[14] §1026.19(f)(1)(i)

about the costs for purposes of the “reasonably available” standard in connection with this disclosure.

Inaccurate Fee Disclosure

The examination deficiency identified companies provided borrowers with Closing Disclosures that inaccurately disclosed a Property Inspection Waiver (PIW).

The PIW fee is charged to Companies by Fannie Mae on the secondary market when it buys the loan that did not involve an appraisal. Since the PIW fee is a secondary market loan level price adjustment (LLPA), and not a settlement fee, if the Companies want to pass it through to borrowers, it must be included in Section A - Origination Charges—rather than Section B - Services You Cannot Shop For.

Inaccurate Identification of Credits

Lender Credits

Lender credits are payments from the creditor to the borrower, not the application of upfront deposits collected from the consumer since these monies are sourced from the borrower not the lender. The good faith deposits from borrowers should be disclosed in the “borrower paid before closing” column on page two of the Closing Disclosure, or they could be disclosed as an “other credit” in section L on page three.

The examination deficiency identified companies disclosed borrower good faith deposits as “Lender Credits” on the Closing Disclosure.

The disclosure of “lender credits”, if applicable, is required by regulation. If the interest rate is locked, then the lender credit disclosed may not change as origination fees and credits have no tolerance for change. “Lender credits” as identified in the regulations represents the sum of non-specific lender credits and specific lender credits.[15]

- Non-specific lender credits are generalized payments from the creditor to the consumer that do not pay for a particular fee on the disclosures provided.
- Specific lender credits are specific payments, such as a credit, rebate, or reimbursement, from a creditor to the consumer to pay for a specific fee.
- Non-specific lender credits and specific lender credits are negative charges to the consumer which lowers the borrower’s costs.

[15] §1026.37(g)(6)(ii)

The actual total amount of lender credits provided by the creditor that is less than the estimated "lender credits" and disclosed per regulation is an increased charge to the consumer for purposes of determining a good faith violation.

For example, if the creditor discloses a $950 estimate for "lender credits", but only $700 of lender credits is actually provided to the consumer, the creditor has not complied with good faith regulations because the actual amount of lender credits provided is less than the estimated "lender credits" disclosed, and is therefore, an increased charge to the consumer for purposes of determining good faith.[16]

If the creditor discloses a $750 estimate for "lender credits" to cover the cost of a $750 appraisal fee, and the appraisal fee subsequently increases by $150, and the creditor increases the amount of the lender credit by $150 to pay for the increase, the creditor has not violated the requirements because, although the credit increased from the amount disclosed, the amount paid by the consumer did not.

However, if the creditor discloses a $650 estimate for "lender credits" to cover the cost of a $650 appraisal fee, but subsequently reduces the credit by $50 because the appraisal fee decreased by $50, then the requirements have been violated because, although the amount of the appraisal fee decreased, the amount of the disclosed lender credit decreased.

For purposes of conducting the good faith analysis for lender credits, the total amount of lender credits, whether specific or non-specific, actually provided to the consumer is compared to the amount of the "lender credits" disclosed. [17]

Seller Paid Credits

The examination identified seller paid closing costs provided to borrowers on purchase transactions were not disclosed on Closing Disclosures. Regulation Z allows specific seller paid costs to be exempted from disclosure on the Closing Disclosure; however, all other charges must be disclosed.

For example, Regulation Z states section (g) "Closing Cost Details" has columns stating whether the charge was borrower-paid at or before closing, seller paid at or before closing, or paid by others. All costs in connection with the transaction, other than those disclosed under paragraph (f) of this section, must be listed in a table with a heading "Other Costs."[18]

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[16] §1026.19(e)(3)(i)

[17] Sections 1026.37(o)(4) and 1026.38(t)(4)

[18] 12 C.F.R., §1026.38(g)

This requirement, along with the limitation on the separation of borrower and seller information indicates that seller paid fees such as real estate commissions and escrow fees must be disclosed on page two of the borrower's Closing Disclosure.

Closing Disclosure Timing

The regulations state, in a closed-end consumer credit transaction secured by real property, the creditor will provide the consumer with the Closing Disclosure form reflecting the actual terms of the transaction and ensure that the consumer receives the Closing Disclosure no later than three business days before consummation.

The examination deficiency identified companies are failing to deliver the Closing Disclosure on time.

For example, if consummation is scheduled for Thursday, the creditor satisfies this requirement by electronic delivering the disclosures on Monday, assuming each weekday is a business day. For this purpose, to issue a closing disclosure, the term "business day" means all calendar days except Sundays and legal public holidays.

The receipt of disclosures three business days before consummation provides the consumer time to review the documents prior to signing the loan documents and consummation. To comply, the creditor must provide for this delivery to meet this timing requirement. If any disclosures required are not provided to the consumer personally, the consumer is considered to have received the disclosures three business days after they are delivered or placed in the mail (mailing period), or upon electronic acknowledgement of receipt. Upon receipt of the acknowledgement, the three business day waiting period may begin. The borrower may sign the documents on the third business day, as there is no midnight rule like rescission period.

For example, if consummation or signing the closing documents is scheduled for Thursday, a creditor would satisfy the requirements if the creditor places the disclosures in the mail on Thursday of the previous week. For mail waiting periods, Saturday is a business day. The consumer would be considered to have received in the mail the disclosures on the Monday before consummation is scheduled. (mailing period – Friday, Saturday & Monday; CD waiting period – Tuesday, Wednesday & Thursday) The borrower may sign the closing documents or consummate the loan on Thursday.

A creditor would not satisfy the requirements in this example if the creditor places the disclosures in the mail on the Monday before consummation. However, the creditor in this example could satisfy the requirements faster by delivering the disclosures on Monday by electronic mail, provided the requirements relating to disclosures in electronic form are satisfied and provided that the creditor obtains evidence that the consumer acknowledges receipt of the disclosures on Monday.

Kickbacks and Unearned Fees

The payment of prohibited kickbacks and unearned fees has been an ongoing problem for mortgage regulators. RESPA states that no person will give, and no person will accept any fee, kickback, or other thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or part of a settlement service involving a federally related mortgage loan will be referred to any person.[19] A referral is not a compensable service for mortgage professionals, and putting a different spin on a referral fee by calling it a marketing fee is a violation.

The examination deficiency identified companies who are receiving such prohibited kickbacks and unearned fees may result in a referral to the Non-Depository Supervisory Committee for a multi-state enforcement action. States may also choose to pursue enforcement or administrative actions separately.

In accordance with RESPA, a company may not pay any other company or the employees of any other company for the referral of settlement service business. This includes, no person may give, and no person may accept any portion, split, or percentage of any charge made or received for the rendering of a settlement service in connection with a transaction involving a federally related mortgage loan other than for services performed.

Kickbacks includes monies, things, discounts, salaries, commissions, fees, duplicate payments of a charge, stock, dividends, distributions of partnership profits, franchise royalties, credits representing monies that may be paid at a future date, the opportunity to participate in a money-making program, retained or increased earnings, increased equity in a parent or subsidiary entity, special bank deposits or accounts, special or unusual banking terms, services of all types at special or free rates, sales or rentals at special prices or rates, lease or rental payments based in whole or in part on the amount of business referred, trips and payment of another person's expenses, or reduction in credit against an existing obligation.[20]

According to RESPA, an agreement or understanding for the referral of business incident to or part of a settlement service need not be written or verbalized but may be established by a practice, pattern or course of conduct. This provides a wide interpretation for regulators to determine when a violation occurs.

For example, CFPB’s view of Marketing Service Agreements between real estate agents and originators were just a diversion of illegal kickbacks masked as the originator paying the real estate

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[19] RESPA §1024.14(b)

[20] Defined in section 3(2) of RESPA (12 U.S.C. 2602(2))

agent for marketing services. The CFPB identified there were no marketing services perform, the payment exceeded the value of marketing services provided, and/or the payment was tied to the volume of business referred to the originator.

§1024.14(a) states that any violation of this section is a violation of section 8 of RESPA. CFPB and previous regulator have actively enforced this regulation with administrative actions and fines for this violation.

Referral

A referral includes any oral or written action directed to a person which has the effect of affirmatively influencing the selection by any person of a provider of a settlement service for payment in whole or part for the business.

A referral also occurs whenever a person paying for a settlement service or business incident is required to use a particular provider of a settlement service or business incident.

Allowable compensation

Payments are allowed when services have been provided to earn the fees, salaries, or compensation.

For example, section 8 of RESPA permits:

- A payment to an attorney at law for services rendered;
- A payment by a title company to its duly appointed agent for services performed in the issuance of title insurance;
- A payment by a lender to its duly appointed agent for services performed in the origination, processing, or funding of a loan;
- A payment to any person of a bona fide salary or compensation for goods or services performed;
- A payment to cooperative brokerage and referral arrangements or agreements between real estate agents and real estate brokers. The statutory exemption refers only to fee within real estate brokerage and has no applicability to any fee arrangements between real estate brokers and mortgage brokers or between mortgage brokers.);
- Normal promotional and educational activities that are not conditioned on the referral of business and that do not involve the defraying of expenses that otherwise would be incurred by persons in a position to refer settlement services.
    - For example, Lunch-n-Learns provided by mortgage loan originator to a real estate office may not be based on referral business received or expected in return;
- An employer's payment to its own employees for any referral activities.

Any supporting information to document compliance to RESPA section 8 must be **retained for 5 years** from the date of execution.

CFPB Guidance - Marketing Services Agreements

CFPB issued a bulletin in October 2015 providing guidance to the mortgage industry regarding marketing services agreements (MSAs). The bulletin offers an overview of the federal prohibition on mortgage kickbacks and referral fees and describes examples from the CFPB's enforcement experience as well as the risks faced by lenders entering into these agreements. During the course of supervising mortgage lenders and enforcing federal law, the CFPB found that marketing services agreements carry legal and regulatory risk for lenders.

"We are deeply concerned about how marketing services agreements are undermining important consumer protections against kickbacks," said the then active CFPB Director Richard Cordray. "Companies do not seem to be recognizing the extent of the risks posed by implementing and monitoring these agreements within the bounds of the law." [21]

The bulletin explains that while marketing services agreements are usually framed as payments for advertising or promotional services, in some cases the payments are disguised compensation for referrals. Any agreement that entails exchanging a thing of value for referrals of settlement service business likely violates federal law, regardless of whether a marketing services agreement is part of the transaction.

Per CFPB, some MSA participants attempted to disguise the illegal activity. Regulators understand steering business in connection with kickbacks and referral fees often results in consumers paying higher prices for mortgages than they would likely have paid without disguised kickbacks. These practices indirectly undermine consumers' ability to shop for mortgages with lower costs or fees. The Bureau found many examples of settlement service providers keeping payments received from other providers without performing any contractually-obligated services.

For example, the CFPB found a title insurance company that entered into marketing services agreements where the fees paid by the company were based in part on the number of referrals it received, as well as the revenue generated by those referrals. A direct violation of Section 8.

For example in another case, a settlement service provider did not disclose its affiliate relationship with an appraisal management company, and did not tell consumers they had the option of shopping for services before directing them to the affiliate.

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[21] https://www.consumerfinance.gov/about-us/newsroom/cfpb-provides-guidance-about-marketing-services-agreements/

Creditors need clear policies regarding payments to realtor and title partners, and document shared 'fair market' expense are supported by the marketing services agreed upon as required by RESPA. Overpayment for the value of the services is another way referral fee may be masked, but a blatant violation of RESPA.

Third Party Service Fees Exceed Actual Costs

RESPA prohibits a lender from accepting any fees that are not for actual services performed.[22]

The examination deficiency identified companies are charging Third Party Service Fees in excess of the actual cost. A charge by a person for which no or nominal services are performed or for which duplicative fees are charged is an unearned fee and violates RESPA. Any fees collected in excess of the actual fee incurred, must be refunded to the borrower or party who paid the fee.

Consent to Receive Electronic Records

Electronic Signatures in Global and National Commerce Act (E-Sign Act) states information required by law to be in writing but allows it to be made available electronically to a consumer only if he or she affirmatively consents to receive the information electronically and the business clearly and conspicuously discloses specified information to the consumer before obtaining his or her consent.[23]

The examination deficiency identified companies are failing to properly obtain consumer's consent to receive electronic records.

Lenders are required to enforce their policies and procedures for uniform compliance to the E-Sign Act.

General Rule of Validity

E-Sign Act consent to electronic records requires that information relating to a transaction or affecting interstate or foreign commerce may be provided or made available to a consumer in writing. The use of an electronic record to provide or make available such information satisfies the requirement that information be in writing if:

- the consumer has affirmatively consented to such use and has not withdrawn consent
- the consumer, prior to consenting, is provided with a clear and conspicuous statement informing the consumer of any right or option to have the record provided on paper or in non-electronic form, and the right to withdraw the consent, or any fees in the event of such withdrawal

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[22] RESPA 12 C.F.R. § 1024.14

[23] 15 U.S.C. § 7001(c)(1)

- the consumer-
    - prior to consenting, is provided with a statement of the hardware and software requirements for access to and retention of the electronic records; and
    - consents or confirms his or her consent electronically, in a manner that reasonably demonstrates that the consumer can access information in the electronic form

Oral Communications

An oral communication or a recording of an oral communication will not qualify as an electronic record except as provided. CFPB allows mortgage loan disclosures required by mortgage regulations be provided in electronic form, subject to written consumer consent and compliance to the provisions of the E-sign Act along with policies and procedures in place to ensure compliance. Consumer consent allows the required form to be received and accepted by the creditor in electronic form.[24]

[24] §§ 1026.47

Module 2

Appraisal and/or Other Valuation

ECOA requires a creditor to provide an applicant a copy of all appraisals and other written valuations developed in connection with an application for credit that is secured by a first lien on a dwelling. A creditor must provide a copy of each appraisal or other written valuation promptly upon completion, or three business days prior to consummation of the transaction (closed-end credit), whichever is earlier. If the applicant provides a waiver and the transaction is not consummated, the creditor must provide these copies no later than 30 days after the creditor determines consummation will not occur.[25]

The examination deficiency identified companies are not providing an appraisal and/or other valuation properly or timely.

ECOA Valuation Rules

TILA and ECOA provide regulations for creditors on appraisal and valuations handling in a credit transaction. Regulations require a creditor provide to the applicant a copy of any and all appraisals or other written valuations used in connection with an application for credit when the loan is secured by a first lien on a dwelling. A creditor is required to provide a copy of each valuation promptly upon completion, or three business days prior to consummation of the transaction (for closed-end credit) or account opening (for open-end credit), whichever is earlier.

HMPL Valuation Rules

If the mortgage loan is a Higher Priced Mortgage Loan (HPML), TILA has HPML Appraisal Rules. There are several differences between the types of loans that may be covered by the HPML Appraisal Rule and the types of loans covered by the ECOA Valuations Rule. These differences include several variances in the scope of the rules: [26]

1. First, while the ECOA Valuations Rule does not apply to subordinate liens, the HPML Appraisal Rule does apply to subordinate liens.
2. Second, while the ECOA Valuations Rule covers any transactions secured by a dwelling for any purpose, the HPML Appraisal Rule applies only when the covered loan is for a consumer purpose and is secured by a principal dwelling.
3. Third, while the ECOA Valuations Rule does not exempt any types of transactions secured by a first lien on a dwelling, the HPML Appraisal Rule exempts several types of transactions.

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[25] 12 C.F.R. § 1002.14(a)(1)
[26] https://files.consumerfinance.gov/f/201305_compliance-guide_ecoa-appraisals-rule.pdf

In addition, some of the requirements of the HPML Appraisal Rule are different. The HPML Appraisal Rule implements Dodd-Frank Act amendments to TILA, which requires lenders:

- Perform interior-inspection appraisals that comply with the Uniform Standards of Professional Appraisal Practice (USPAP) and the Financial Institutions Reform Recovery and Enforcement Act (FIRREA)
- Provide free copies of the appraisals
- Make disclosures at application when originating certain higher-priced mortgage loans

The Consumer Financial Protection Bureau, Federal Reserve Board, and Office of the Comptroller of the Currency increased the threshold for exempting loans from special appraisal requirements for higher-priced mortgage loans during 2020 . Effective, January 1, 2020, the exemption threshold amount for HPMLs increased from $26,700 to $27,200.

The smaller loan exemption provides an exemption from the special appraisal requirements TILA imposes on HPMLs, including a requirement that creditors must obtain a written appraisal based on a physical visit to the property interior before extending an HPML to a consumer.

Waiver of Appraisal Deliver Timing Rights

An applicant may waive the timing requirement and agree to receive a copy of the appraisal at or before consummation. Any such waiver must be obtained at least three business days prior to consummation, unless the waiver pertains solely to the applicant's receipt of a copy of an appraisal that contains only clerical changes from a previous version received.[27]

If the applicant provides a waiver and the transaction is not consummated, the creditor must provide copies of the appraisal or valuation no later than 30 days after the creditor determines consummation will not occur.

ECOA Disclosure Requirement

A creditor will mail or deliver to an applicant, not later than the third business day after the creditor receives an application for credit secured by a 1st lien on a dwelling, a notice in writing of the applicant's right to receive a copy of all written appraisals developed in connection with the application. A creditor may not charge an applicant for providing a copy of appraisals and other written valuations as required, but may require applicants pay a reasonable fee for the cost of the appraisal or other written valuation.

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[27] §1002.14

The requirements apply whether credit is extended or denied or if the application is incomplete or withdrawn. The copies required may be provided to the applicant in electronic form, subject to compliance with the consumer's consent and other applicable provisions of the E-Sign Act.

If there is more than one applicant, the written disclosure about written appraisals, and the copies of appraisals and other written valuations, need only be given to one applicant. However, these materials must be given to the primary applicant when one is clear. Similarly, if there is more than one applicant for credit in the transaction, one applicant may provide a waiver, but it must be the primary applicant when one is clear.

Definitions

- The term "consummation" means the time that a consumer becomes contractually obligated on a closed-end credit transaction. This may vary based on state regulations.
- The term "dwelling" means a residential structure that contains 1 to 4 units whether or not that structure is attached to real property. The term includes an individual condominium or cooperative unit, and a mobile or other manufactured home.
- The term "valuation" means any estimate of the value of a dwelling developed in connection with an application for credit.

CFPB Appraisal Compliance Guidance

CFPB has provided the following examples for what would satisfy the "promptly upon completion" standard:

- On day 15 after receipt of the application, the creditor's underwriting department reviews an appraisal and determines it is acceptable. One week later, the creditor sends a copy of the appraisal to the applicant. The applicant receives the copy more than three business days before the date of consummation (or account opening). The creditor has provided the copy of the appraisal promptly upon completion.
- An appraisal is being revised, and the creditor does not receive the revised appraisal until day 45 after the application, and the next day the creditor determines the revised appraisal is acceptable. A week later, the creditor sends a copy of the revised appraisal to the applicant and does not send a copy of the initial appraisal to the applicant. The applicant receives the copy of the revised appraisal three business days before the date of consummation. The creditor has provided the appraisal copy promptly upon completion.
- The creditor receives an automated valuation model (AVM) report on day five after receipt of the application and treats the AVM report as complete when received. On day twelve after receipt of the application, the creditor sends the applicant a copy of the valuation. The applicant receives the valuation more than three business days before the date of

consummation. The creditor has provided the copy of the AVM report promptly upon completion.

For example, the following would **NOT** satisfy the "promptly upon completion" standard:

- On day twelve after receipt of the application, the creditor's underwriting department reviews an appraisal and determines it is acceptable. Although the creditor has determined the appraisal is complete, the creditor waits to provide a copy to the applicant until day 42, when the creditor schedules the consummation to occur on day 50. The creditor has not provided the copy of the appraisal promptly upon completion.
- The creditor receives an AVM report on day five after application and completes its review of the AVM report the day it is received. The creditor also has ordered an appraisal, but the initial version of the appraisal received by the creditor is found to be deficient and is sent for review. The creditor waits 30 days to provide a copy of the completed AVM report, until the appraisal is completed on day 35. The creditor then provides the applicant with copies of the AVM report and the revised appraisal. While the appraisal report was provided promptly upon completion, the AVM report was not.

Waiver provision permits the applicant to waive the timing requirement if the creditor provides the copies at or before consummation, except where otherwise prohibited by law.[28] An applicant's waiver is effective in either of the following two situations:

1. If, no later than three business days prior to consummation, the applicant provides the creditor an affirmative oral or written statement waiving the timing requirement; or
2. If, within three business days of consummation, the applicant provides the creditor an affirmative oral or written statement waiving the timing requirement and the waiver pertains solely to the applicant's receipt of a copy of a valuation that contains only clerical changes from a previous version provided to the applicant three or more business days prior to consummation.[29]

Required Notice of Action Taken/Content

The Equal Credit Opportunity Act (ECOA), requires a creditor to notify the applicant of the specific reasons for the action taken.[30] The Notice of Adverse Action must be specific and indicate the principal reason(s) for the credit denial. ECOA has as timing provisions that requires creditors must

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[28] ECOA Section 1002.14(a)(1)
[29] See interpretation of 14(a)(1) In general. in Supplement I
[30] ECOA 12 C.F.R. § 1002.9(a)(2)(i)

notify the applicant of the action taken (for example, approve or deny) generally within 30 days of application.[31]

The examination deficiency identified companies were not providing the applicants with specific reasons for an action taken, and/or not providing the notice within the required timeframe.

Notification of action taken, ECOA notice, and statement of specific reasons are the names of forms a creditor may use to notify an applicant of action taken within:[32]

- 30 days after receiving a completed application concerning the creditor's approval of, counteroffer to, or adverse action on the application;
- 30 days after taking adverse action on an incomplete application, unless notice is provided in accordance with this regulation;
- 30 days after taking adverse action on an existing account; or
- 90 days after notifying the applicant of a counteroffer, if the applicant does not expressly accept or use the credit offered.

Adverse Action Notice Content

An adverse action notification given to an applicant must be in writing and contain a statement of the action taken; the name and address of the creditor; a statement of the provisions; the name and address of the Federal agency that administers compliance for the creditor; and either:

- A statement of specific reasons for the action(s) taken; or
- A disclosure of the applicant's right to a statement of specific reasons within 30 days,
    - if the statement is requested within 60 days of the creditor's notification the disclosure must include the required information.

The notice of action taken requires the statement of reasons for adverse action to be specific and indicate the principal reason(s) for the adverse action.[33] The statement of reasons for adverse action must be specific and not vague statements the adverse action was based on the creditor's internal standards or policies or that the applicant failed to achieve a qualifying score on the creditor's credit scoring system.

The following are CFPB's official interpretations of this section of the Act.[34]

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[31] 12 C.F.R. § 1002.9(a)(1)
[32] §1002.9 Notifications
[33] 12 C.F.R. § 1002.9(b)(2)
[34] https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1002/9/#b-1

- **Number of specific reasons.** A creditor must disclose the principal reasons for denying an application or taking other adverse action. The regulation does not mandate that a specific number of reasons be disclosed, but disclosure of more than four reasons is not likely to be helpful to the applicant.
- **Source of specific reasons.** The specific reasons disclosed must relate to and accurately describe the factors considered or scored by a creditor.
- **Description of reasons.** A creditor need not describe how or why a factor adversely affected an applicant.
  - For example, the notice may say "length of residence" rather than "too short a period of residence."
- **Credit scoring system.** If a creditor bases the denial or other adverse action on a credit scoring system, the reasons disclosed must relate only to those factors scored in the system. No principal reason for adverse action may be excluded from disclosure. The creditor must disclose the actual reasons for denial.
  - For example, "age of manufactured home", even if the relationship of that factor to predicting creditworthiness may not be clear to the applicant
- The regulation does not require that any one method be used for selecting reasons for a credit denial or other adverse action that is based on a credit scoring system. Various methods will meet the requirements of the regulation.
  - For example, one method is to identify the average factors the applicant's score fell furthest below or was at or slightly above the minimum passing score. The scoring system explanation in the notification should allow the consumer to understand why they were denied access to credit, and the score they achieved.
- **Judgmental system.** If a creditor uses a judgmental system, the reasons for the denial or other adverse action must relate to those factors in the applicant's record reviewed by the person making the decision.
- If a creditor denies an application based on a credit evaluation system that employs both credit scoring and judgmental components, the reasons for the denial must come from the component of the system that the applicant failed.
  - For example, if the application passes the credit scoring stage but the creditor then denies the credit request based on a judgmental assessment, the reasons disclosed must relate to the factors reviewed judgmentally. If the application fails the credit score, but falls into a gray band causing the creditor to perform a judgmental assessment and then denies the credit, the reasons disclosed must come from both components.

- **Automatic denial.** Some credit decision methods contain features that call for automatic denial because of one or more negative factors in the applicant's record. When a creditor denies the credit request because of an automatic-denial factor, the creditor must disclose that specific factor.
  - For example, the applicant's previous bad credit history with the creditor, the applicant's declaration of bankruptcy, or the fact the applicant is a minor.
- **Combined ECOA-FCRA disclosures.** The ECOA requires disclosure of the principal reasons for denying or taking other adverse action on an application for an extension of credit. The Fair Credit Reporting Act (FCRA) requires a creditor to disclose when it has based its decision in whole or in part on a source other than the applicant or its own files. Disclosing that a credit report was obtained and used in the denial of the application, as the FCRA requires, does not satisfy the ECOA requirement to disclose specific reasons.
  - For example, if the applicant's credit history reveals delinquent credit obligations and the application is denied for that reason, to satisfy ECOA the creditor must disclose the application was denied because of the applicant's delinquent credit obligations. The FCRA also requires a creditor to disclose the credit score it used in taking adverse action along with related information, including up to four key factors that adversely affected the consumer's credit score.[35] Lenders are required to comply with both requirements on one adverse action disclosure.

Notice of Incompleteness

When a borrower does not supply the additional information necessary to make a credit decision, the creditor may send a written notice to the applicant specifying the information needed, designate a reasonable period of time for the applicant to provide the information, and inform the applicant that failure to provide the information requested will result in no further consideration being given to the application. Termed in the industry as the 10-day letter.

After providing this 10-day letter to the borrower, the creditor may have no further obligation under ECOA if the applicant fails to respond within the designated time period provided in the letter. If the applicant supplies the requested information within the designated time period, the creditor is then required to provide a notice of action taken within the 30 day receipt of sufficient information to make a credit decision.

No ECOA Notice Required

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[35] See interpretation of Paragraph 9(b)(2). in Supplement I

The creditor may determine within the three business day period the loan request will not or cannot be approved on the terms requested, such as when a consumer's credit score is lower than the minimum score required for the loan program, or the consumer applies for a type or amount of credit the creditor does not offer.

In that case, or if the consumer withdraws the application within the three business-day period for whatever reason, the creditor need not make the required disclosures.

TILA Ability to Repay

Regulation B does not require or permit the creditor to make inquiries or verifications prohibited by ECOA Regulation B.[36] A lender must determine the borrower qualifies for the loan request, but may not require more information from a borrower than is necessary to make a credit decision.

TILA 12 C.F.R. § 1026.43(c)(1) states, "a creditor shall not make a loan that is a covered transaction unless the creditor makes a reasonable and good faith determination at or before consummation that the consumer will have a reasonable ability to repay the loan according to its term."

For examination deficiency identified companies are not reasonably determining the borrower's ability to repay a loan.

For compliance with TILA's Ability to Repay Rule, a lender must obtain sufficient verification the borrower has the ability to repay the debt. Lender's struggle with this regulation due to the initial vague statement in the regulation. To provide guidance to the mortgage industry CFPB has provided official interpretations and guidance. The following reviews the key points CFPB has provided the mortgage industry for Ability to Repay compliance.

In making the repayment ability determination, a creditor must consider the following points:

- The consumer's current or reasonably expected income or assets, other than the value of the dwelling.
- A creditor may base its determination of repayment ability on current or reasonably expected income from employment or other sources, assets other than the dwelling that secures the covered transaction, or both. The creditor may consider any type of current or reasonably expected income.
- The creditor may consider any of the consumer's assets.
- A creditor needs only the income or assets necessary to support a determination that the consumer can repay the covered transaction.

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[36] See interpretation of 43(c)(1) General requirement. in Supplement I

- For example, if a consumer's loan application states that the consumer earns an annual salary from both a full-time job and a part-time job and the creditor reasonably determines that the consumer's income from the full-time job is sufficient to repay the loan, the creditor need not consider the consumer's income from the part-time job. Further, a creditor need verify only the income (or assets) relied on to determine the consumer's repayment ability.[37]

- Reasonably expected income in excess of the consumer's income may be used either in addition to or instead of current income. The expectation that the income will be available for repayment must be reasonable and verified with third-party records that provide reliable evidence of the consumer's expected income.
  - For example, if the creditor relies on a consumer's expected salary from a job the consumer has accepted and will begin after receiving an educational degree, the creditor may verify that expectation with a written statement from an employer indicating the consumer will be employed upon graduation at a specified salary.
- Seasonal or irregular income may determine that a consumer can make periodic loan payments even if the consumer's income, such as self-employment income, is seasonal or irregular.
  - For example, a consumer receives seasonal income from the sale of crops or from agricultural employment. Each year, the consumer's income arrives during only a few months. If the creditor determines that the consumer's annual income divided equally across 12 months is sufficient for the consumer to make monthly loan payments, the creditor reasonably may determine that the consumer can repay the loan, even though the consumer may not receive income during certain months including the months the loan is closing.
- When two or more consumers apply for an extension of credit as joint borrowers, regulations do not require the creditor to consider income or assets that are not needed to support the creditor's repayment ability determination.
  - For example, if a husband and wife jointly apply for a loan and the creditor reasonably determines that the wife's income is sufficient to repay the loan, the creditor is not required to consider the husband's income.[38]
  - If in determining the consumer's repayment ability, the creditor relies on income from the consumer's employment, then that employment may be full-time, part-time, seasonal,

[37] See comment 43(c)(4)-1
[38] See interpretation of Paragraph 43(c)(2)(i). in Supplement I

irregular, military, or self-employment, so long as the creditor considers those characteristics of the employment.[39]

  - For example, if a creditor relies wholly on a consumer's investment income to determine repayment ability, the creditor need not verify or document employment status. Tax returns to support investment dividends, interest, and capital gain, along with investment account statements would document the qualifying income.

- The consumer's monthly payment on any simultaneous loan that the creditor knows or has reason to know will be made. Simultaneous loan includes any covered transaction or home equity line of credit (HELOC) that will be made to the same consumer at or before consummation and secured by the same dwelling that secures the covered transaction.
  - For example, where a covered transaction is a home purchase loan, the creditor must consider the consumer's periodic payment obligation for any “piggyback” second-lien loan such as a seller carry back. The creditor needs to take measures and provide instructions to the title/escrow company to identify any other known financing.[40]
- The consumer's monthly payment for mortgage-related obligations.
  - Mortgage-related obligations must be included in the creditor's determination of repayment ability regardless of whether the amounts are included in the monthly payment or whether there is an escrow account established.
  - Regulations define mortgage-related obligations to include obligations owed to a condominium, cooperative, or homeowners association.
  - Regulations do not require a creditor to include special assessments in the consumer's monthly payment if the special assessments are fully satisfied at or before consummation.[41]
  - The creditor may divide the recurring payments for mortgage-related obligations into monthly, pro rata amounts.
  - Assume that a subject property is in a special water district, the assessments for which are billed separately from local property taxes. The creditor complies by dividing the full amount that will be owed by the number of months in the assessment period and including the resulting amount in the calculation of monthly mortgage-related obligations.[42]

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[39] See comments 43(c)(2)(i)-5 and 43(c)(4)-2 for guidance on multiple consumers loans.
[40] See interpretation of Paragraph 43(c)(2)(iv). in Supplement I
[41] § 1026.43(c)(2)(v)
[42] § 1026.43(c)(2)(v)

- Estimates of mortgage-related obligations should be based upon information that is known to the creditor at the time the creditor underwrites the mortgage obligation, and need not project potential changes, such as by estimating possible increases in taxes and insurance.[43]

- The regulations required creditors to consider a consumer's current debt obligations and any alimony or child support the consumer is required to pay.
- Creditors should consider whether debt obligations in forbearance or deferral at the time of underwriting are likely to affect the consumer's ability to repay based on the payment liable upon expiration of the forbearance or deferral period and other relevant facts and circumstances, such as when the forbearance or deferral period will expire.[44]
  - For example, if a monthly student loan payment is provided on the credit report, the lender may use that amount for qualifying purposes. If the credit report does not reflect the correct monthly payment, the lender may use the monthly payment that is on the student loan documentation (the most recent student loan statement) to qualify the borrower.
  - If the credit report does not provide a monthly payment for the student loan, or if the credit report shows $0 as the monthly payment, the lender must determine the qualifying monthly payment using one of the options below.
    - If the borrower is on an income-driven payment plan, the lender may obtain student loan documentation to verify the actual monthly payment is $0. The lender may then qualify the borrower with a $0 payment.)
    - For deferred loans or loans in forbearance, the lender may calculate a payment equal to 1% of the outstanding student loan balance (even if this amount is lower than the actual fully amortizing payment), or a fully amortizing payment using the documented loan repayment terms.[45]

Reasonable and Good Faith Determination

Creditors generally are required by to make reasonable and good faith determinations of consumers' ability to repay. CFPB commentary described requirements for making this ability-to-repay determination, but it does not provide comprehensive underwriting standards to which creditors must adhere.[46]

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[43] See interpretation of Paragraph 43(c)(2)(v). in Supplement I
[44] Section 1026.43(c)(2)(vi)
[45] https://www.fanniemae.com/content/guide/selling/b3/6/01.html
[46] §1026.43(c)(1)

For example, the rule and commentary do not specify how much income is needed to support a particular level of debt or how credit history should be weighed against other factors. So long as creditors consider the credit decision factors in accordance with the requirements, creditors are permitted to develop their own underwriting standards and make changes to those standards.

Whether a particular ability-to-repay determination is reasonable and in good faith will depend not only on the underwriting standards adopted by the creditor, but on the facts and circumstances of an individual extension of credit and how a creditor's underwriting standards were applied to those facts and circumstances.

A consumer's statement or attestation that the consumer has the ability to repay the loan is not indicative of whether the creditor's determination was reasonable and in good faith. Regulators and the industry as a whole learned that lesson after the mortgage meltdown.

Repayment Ability at Consummation

TILA requires the creditor to determine, at or before the time the loan is consummated, that a consumer will have a reasonable ability to repay the loan. A change in the consumer's circumstances after consummation that cannot be reasonably anticipated from the consumer's application is not relevant to determining a creditor's compliance or noncompliance with the rule.[47]

For example, a significant reduction in income due to a job loss or a significant obligation arising from a major medical expense was an unknown factor when the loan closed.

However, if the application or records considered before consummation indicate there will be a change in a consumer's repayment ability after consummation, the creditor must consider that information under the rule.

For example, if a consumer's application states that the consumer plans to retire within twelve months without obtaining new employment or that the consumer will transition from full-time to part-time employment. Creditor would not be acting in good faith if it failed to identify the borrower’s continued ability to repay the debt in light of this financial change information.

For example, since inquiries on the credit report may lead to added debts after closing lenders require the borrower to identify if additional debts have or will be obtained prior to or after closing. Not satisfactorily addressing these inquires may be considered negligent for compliance to ability to repay provision.

Required Home Ownership Counseling List

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[47] Section 1026.43(c)(1)

RESPA requires a lender, mortgage broker, or dealer to provide to the applicant, not later than three business days after it receives an application or sufficient information to complete an application, with a clear and conspicuous written list of homeownership counseling organizations. The list must provide relevant HUD or CFPB approved counseling services in the loan applicant's location, and list obtained no earlier than thirty days prior to the time it is provided to the applicant.[48]

The lender obtains the list from either the Web site maintained by the Consumer Financial Protection Bureau (CFPB), or from data made available by the Bureau or the Department of Housing and Urban Development (HUD).[49]

The examination deficiency identified companies are failing to properly provide in a timely manner the list of counselors and/or providing an inaccurate list of counselors to an applicant.

The loan files reviewed by the examiners found the following:

- Appeared the homeownership counseling disclosure was provided, but the list of homeownership counseling organizations provided were missing all the required information.
- The Companies provided applicants with Homeownership Counseling Lists that did not appear to be within the appropriate distance from the applicants.

A mortgage broker may provide the list of homeownership counseling organizations to any loan applicant from whom it receives or for whom it prepares an application. If the mortgage broker has provided the required list of homeownership counseling organizations, the lender is not required to provide an additional list. The lender is responsible for ensuring that the list of homeownership counseling organizations provided to a loan applicant is in compliance.

If the lender, mortgage broker, or dealer does not provide the list of homeownership counseling organizations to the loan applicant, the lender must deliver the list to the loan applicant. The list may be provided in electronic form, subject to compliance with the consumer’s consent in compliance with the E-Sign Act.

The lender is not required to provide the list of homeownership counseling organizations if, before the end of the three business day period, the lender denies the application, or the loan applicant withdraws the application.

If a mortgage loan transaction involves more than one lender, only one list of homeownership counseling organizations must be given to the loan applicant and the lenders may agree among themselves which lender will comply with the requirements. If there is more than one loan applicant,

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[48] RESPA 12 C.F.R. § 1024.20(a)(1)
[49] RESPA 12 C.F.R. §§ 1024.20(a)(1)(i) and (ii)

the required list of homeownership counseling organizations may be provided to any primary loan applicant.

Housing Counseling List Exemptions

- **Reverse mortgage transactions.** A lender is not required to provide an applicant for a reverse mortgage transaction the list of homeownership counseling organizations. Reverse mortgages regulations have special borrower homeownership counseling requirements.
- **Timeshare plans.** A lender is not required to provide an applicant for a mortgage loan secured by a timeshare the list of homeownership counseling organizations.

Adequate Settlement Service Provider List

TILA requires lenders to provide an adequate Settlement Service Provider List. The written list of settlement service providers of which the creditor is permitting them to shop for gives the consumer the ability to shop for the best service or cost.[50]

The examination deficiency identified creditor failed to provide an adequate settlement service provider list the consumer could shop for.

Regulations require the following to meet this requirement:

- Creditor must identify at least one available provider for each service for which the consumer is permitted to shop
- Written list must be disclosed in compliance with regulations
- Provide sufficient information to allow consumer to contact the provider
- Include statement that consumer may choose a provider that is not included on the list
- Must be provided to consumer within three business days of application

CFPB Interpretations

CFPB provides regulation interpretation on certain mortgage and variable-rate transactions that the regulation permits creditors to impose reasonable requirements regarding the qualifications of the provider.[51]

For example, the creditor may require that a settlement agent chosen by the consumer must be appropriately licensed in the relevant jurisdiction.[52]

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[50] TILA 12 CFR § 1026.19(e)(1)(vi)(C)
[51] https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1026/19/#e-1-v
[52] §1026.19(e)(1)(vi)

In contrast, a creditor does not permit a consumer to shop if it requires the consumer to choose a provider from a provided list only. The requirements do not apply if the creditor does not permit the consumer to shop.

The creditor may include a statement the listing of a settlement service provider does not constitute an endorsement. The creditor may also identify providers of services the consumer is not permitted to shop, provided the creditor clearly distinguishes those services from the services the consumer is permitted to shop for. This may be accomplished by placing the services under different headings.

For example, if the list provided identifies providers of pest inspections and surveys, but the consumer may not shop for the survey, then the list must specifically inform the consumer he's permitted to select another provider, except for a provider identified on the list for the survey.

RESPA and Regulation X do not prohibit creditors from including affiliates on the written list of providers. However, a creditor that includes affiliates on the written list must comply with RESPA affiliated business disclosure and referral requirements.[53]

Items included under the subheading "Services You Can Shop For" are for those services:[54]

- That the creditor requires in connection with its decision to make the loan;
- That would be provided by persons other than the creditor or mortgage broker; and
- For which the creditor allows the consumer to shop

For example, the services listed under this subheading might include a pest inspection fee, survey fee, title - closing agent fee, and title - closing protection letter fee.[55]

'Services You Can Shop For' Fee Identification

On the Loan Estimate, under the subheading "Services You Can Shop For," the creditor provided an itemization of each amount and subtotal of all fees the consumer will pay for settlement services the consumer can shop for or are provided by persons other than the creditor or mortgage broker.[56]

Title companies are the most common fee in this area. For any item that is a component of title insurance or is for conducting the closing, the creditor must label the fee with introductory description "Title" at the beginning of the item description.

For example, Title-Lender's Title Policy $900

Required to Disclose Additional Credit Terms in Advertisements

[53] 12 CFR 1024.15
[54] §1026.37(f)(3)
[55] See interpretation of 37(f)(3) Services you can shop for. in Supplement I
[56] 12 CFR §1026.37(f)(3)

Regulation Z states that if an advertisement includes any of the following terms additional disclosure is required within the same advertisement. Those triggers are:[57]

1. the amount or percentage of any down payment
2. the number of payments or period of repayment or
3. the amount of any payment or
4. the amount of any finance charge

If included in advertisement, then the advertisement must also state the amount or percentage of the down payment, the terms of repayment, and the annual percentage rate and if the rate may be increased after consummation.

The examination deficiency identified companies failed to disclose the TILA Regulation Z required additional credit terms in advertisements to the consumer.

Whenever the stated TILA trigger terms appear in credit advertisements, the additional credit term disclosures must also appear to provide clear information to the consumer. These provisions apply even if the trigger term is not stated explicitly, but may be readily determined from the advertisement.

For example, an advertisement may state "80% financing available," which is in fact indicating that a 20% down payment is required.[58] Down payment is a trigger term.

CFPB Official Interpretations of Triggering Terms

1. Down payment.

The dollar amount of a down payment or a statement of the down payment as a percentage of the price requires further information. By the definition of down payment, this trigger term is limited to credit sale transactions.

For example, it includes such statements as:

- Only 5% down
- As low as $100 down
- Total move-in costs of $800

This provision applies only if a down payment is required; statements such as no down payment do not trigger the additional disclosures.

2. Payment period.

The number of payments required, or the total period of repayment.

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[57] Regulation Z, 12 C.F.R., § 1026.24(d)
[58] See interpretation of 24(d) Advertisement of Terms That Require Additional Disclosures in Supplement I

For example, includes statements such as:

- 48-month payment terms
- 30-year mortgage
- Repayment in as many as 36 monthly installments

But it does not include such statements as “bi-weekly,” “monthly payment terms arranged,” or “take years to repay,” since these statements do not indicate a time period over which a loan may be financed.

3. Payment amount.

The dollar amount of any payment amount.

For example, includes statements such as:

- “Payable in installments of $503”
- “$435 bi-weekly”
- “$500,000 loan for just $1,650 per month”
- “$120,000 balance payable in 180 equal installments”

In the last example, the amount of each payment is readily determinable, even though not explicitly stated. Statements such as “monthly payments to suit your needs” or “regular monthly payments” are not deemed to be statements of the amount of any payment.

4. Finance charge.

The dollar amount of the finance charge or any portion of it.

For example, includes statements such as:

- “$500 total cost of credit”
- “$2 monthly service charge”
- “$50,000 mortgages at 2 points to the borrower”

In the last example, the $1,000 prepaid finance charge can be readily determined from the information given ($50,000 x 2% =$1,000). Statements of the annual percentage rate or statements that there is no charge for credit (such as “no closing costs”) are not trigger terms.[59]

Additional Information Required

An advertisement stating any of the trigger terms must include the following terms.

- The amount or percentage of the down payment

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[59] See interpretation of 24(d)(1) Triggering Terms in Supplement I

- The terms of repayment, which reflect the repayment obligations over the full term of the loan, including any balloon payment
- The “annual percentage rate,” and if the rate may be increased after consummation

1. The total down payment as a dollar amount or percentage must be shown, but the word “down payment” need not be used in making this disclosure.

For example, “10% cash required from buyer” or “credit terms require minimum $10,000 down” would suffice.

2. The phrase “terms of repayment” generally has the same meaning as the “payment schedule” required to be disclosed, the interest rate and payment summary table, or the projected payments table required to be disclosed, as applicable.

The regulations provide flexibility to creditors in making this disclosure for advertising purposes. Repayment terms may be expressed in a variety of ways in addition to an exact repayment schedule; this is particularly true for advertisements that do not contemplate a single specific transaction. Repayment terms, however, must reflect the consumer's repayment obligations over the full term of the loan, including any balloon payment, not just the repayment terms that will apply for a limited period of time.

For example:

- A creditor may use a unit-cost approach in making the required disclosure, such as “360 monthly payments of $27.83 per $1,000 borrowed.”
- When any series of payments varies because of the inclusion of mortgage insurance premiums, a creditor may state the number and timing of payments, the fact that payments do not include mortgage insurance premiums, and that the actual payment obligation will be higher.
- When one series of monthly payments will apply for a limited period of time followed by a series of higher monthly payments for the remaining term of the loan, the advertisement must state the number and time period of each series of payments, and the payment amounts.
- In some transactions, a balloon payment will occur when the consumer only makes the minimum payments specified in an advertisement. If a balloon payment will occur when the consumer makes only the minimum payments specified in an advertisement, the advertisement must state with equal prominence and proximity to the minimum payment statement the amount and timing of the balloon payment that will result from minimum payments.

3. The advertised annual percentage rate may be expressed using the abbreviation "APR." The advertisement must also state, if applicable, the APR is subject to increase after consummation.

A creditor may use illustrative credit transactions to make the necessary disclosures. That is, where a range of possible combinations of credit terms is offered, the advertisement may use examples of typical transactions, so long as each example contains all the applicable terms required by TILA. The examples must be labeled as such and must reflect representative credit terms available by the creditor to present to prospective customers.[60]

Accurately Complete the Privacy Policy Notice

Gramm-Leach-Bliley Act (GLBA) Regulation P governs the treatment of nonpublic personal information (NPI) about consumers collected by financial institutions. Regulations prohibits a financial institution from disclosing consumers' NPI to nonaffiliated third parties, unless the institution satisfies various notice and opt-out requirements.

Regulation P requires each financial institution to provide a clear notice that accurately reflects the institution's privacy policies and practices at the time of establishing a customer relationship, and annually with a continuous relationship if information is shared or policies change.[61]

The examination deficiency identified companies have failed to accurately complete the Privacy Policy Informational Purposes Only form.

In addition to failing to accurately complete the Privacy Policy Information Purposes Only form, some companies failed to provide clear and conspicuous notices that accurately reflect the policies and practices of the institution and/or the borrowers were not provided the opt out notices in violation of regulations.[62]

Regulation P's Model Privacy Form states that the model privacy form is a standardized form, including page layout, content, format, style, pagination, and shading. Institutions seeking to obtain the safe harbor through use of the model form may modify it only as described in the instructions.[63]

Regulation P Privacy Policies

12 C.F.R. § 1016.4(a) requires each financial institution to provide a clear and conspicuous notice that accurately reflects the institution's privacy policies and practices at the time of establishing a customer relationship.

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[60] See interpretation of 24(d)(2) Additional Terms in Supplement I
[61] 12 C.F.R. § 1016.4(a)
[62] https://www.law.cornell.edu/cfr/text/12/appendix-to_part_1016
[63] Regulation P, 12 C.F.R., § 1016, Appendix A – Model Privacy Form

12 C.F.R. § 1016.9(a) requires privacy and opt out notices to be provided so that each consumer can reasonably be expected to receive actual notice in writing or electronically, if the consumer agrees to the company's policies on the sharing for their information.

Non-Public Private Information Defined

The categories of nonpublic personal information (NPI) that financial institutions may collect, and share must be disclosed to the consumer prior to sharing the information including:

- What categories of NPI are shared
- Categories of affiliates and non-affiliated third parties' NPI
- If the financial institution discloses NPI to a nonaffiliated third party (and no other exception applies to that disclosure), a separate statement of the categories of information disclosed and the categories of third parties contracted
- An explanation of the consumer's right to opt out of the disclosure of NPI to nonaffiliated third parties, including the method(s) by which the consumer may exercise that right
- Any disclosures made under the Fair Credit Reporting Act (that is, notices regarding the ability to opt out of disclosures of information sharing among affiliates)[64]
- Policies and practices with respect to protecting the confidentiality and security of NPI
- Any disclosure required under this section

If a financial institution discloses NPI to third parties in compliance with the regulations, it is not required to list those exceptions in the initial or annual privacy notices required. When describing the categories with respect to those parties, it is sufficient to state that disclosures are made to other nonaffiliated companies.

Short-form Initial Notice with Opt-Out Notice

Lenders may satisfy the initial notice requirements for a consumer who is not a customer by providing a short-form initial notice at the same time as you deliver an opt out notice.

- A short-form initial notice must:
  - Be clear and conspicuous;
  - State that the company's privacy notice is available upon request; and
  - Explain a reasonable means by which the consumer may obtain that notice.

Lenders are not required to deliver the privacy notice with your short-form initial notice, if they provide the consumer a reasonable means to obtain the privacy notice, or must be delivered upon request.[65]

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[64] (15 U.S.C. 1681a(d)(2)(A)(iii))
[65] §1016.9

You provide a reasonable means by which a consumer may obtain a copy of your privacy notice if you:

- Provide a toll-free telephone number that the consumer may call to request the notice; or
- For a consumer who conducts business in person at your office, maintain copies of the notice on hand to provide the consumer immediately upon request
- Provide access to online copy of the notice

Who Receives Initial Privacy Notice

You must provide a clear and conspicuous notice that accurately reflects your privacy policies and practices to:

- Customer. An individual who becomes your customer, not later than when you establish a customer relationship, except as provided in the regulations; and
- Consumer. A consumer, before you disclose any NPI about the consumer to any nonaffiliated third party.

Financial Institutions must provide any privacy notices and opt out notices, including short-form initial notices required so each consumer that can reasonably be expected to receive actual notice in writing or electronically.[66]

Regulation P provides an annual policy notice exception for financial institutions that meet certain conditions. To qualify for this exception, a financial institution must not share NPI about customers, and must not have changed its policies and practices regarding disclosing NPI from those that the institution disclosed in the most recent privacy notice it sent.[67]

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[66] 12 C.F.R. §1016.9(a)
[67] https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/amendment-annual-privacy-notice-requirement-under-gramm-leach-bliley-act/

Module 3

Ethics –2 Hours of Ethics, Fraud, and Consumer Protection

Module 3 Objective:

This module provides a review of the Fair Credit Reporting Act and its Identity Theft provision. The student will understand what their responsibility is to comply with the FCRA's Red Flag Rules, understand what are considered red flags, and review current mortgage fraud scams. It is important for MLOs to understand how to prevent originating mortgage fraud.

MLOs Ethical Originations

In the mortgage industry, ethics is essential. Mortgage loan originators are required by federal laws to function in an ethical manner, and not commit fraud. In addition, mortgage loan originators are required to ensure the loans they originate are not funding fraud. Since the mortgage market crash of 2008, efforts were taken to ensure mortgage loan file contains no fraud.

Mortgage regulators found the market crash of 2008 was caused in large part by the unethical behavior of some mortgage loan originators and mortgage lenders. When Washington pushed to raise the percentage of the population owning homes, lenders relaxed the loan program underwriting guidelines and created loan programs to meet the demand.

As qualifying income was a hurdle for many consumers, stated income loans became their solution. It was assumed borrowers would know what they could afford, and they were allowed to state the income they made with little or no income documentation. The amount of income stated was then used to determine if the borrower met the loan program debt ratios.

The unethical mortgage loan originators took this a step further, and would have the borrower leave the income blank and then they would fill in the income needed to qualify for the loan's debt ratios. Disregarding the fact, the borrowers may not be able to afford the house payment after closing.

The easier loan program guidelines and stated income loan programs made it too easy for the bad players in the industry to justify their unethical behavior. They wanted the commission the loan brought so they could buy a new car or continue to fund their over-the-top lifestyles. They justify they were helping the consumer by ignoring problems, borrower's ability to pay after closing, lack of borrower benefits, or true ability to qualify. To ensure this never happens to another primary residence for a borrower, TILA requires lenders to document in the file a borrower's ability to repay the debt. No more is the lender to rely on the borrower determining if they can afford the house payment.

The following are some TILA provisions enacted to stop unethical behavior in mortgage loan originations.

Dual compensation

Regulation Z provides that where a loan originator receives compensation directly from a consumer in connection with a mortgage loan, the loan originator may receive no additional compensation from another person in connection with the same transaction. The Dodd-Frank Act codified this prohibition, which was designed to address consumer confusion over mortgage broker loyalties where the brokers were receiving payments both from the consumer and the creditor. The final rule implements this restriction but provides an exception to allow mortgage brokers to pay their employees or contractors commissions, although the commissions cannot be based on the terms of the loans that they originate. [TILA Regulation Z §1026.36(d)(2)(i)(A)]

Prohibited Anti-Steering

To stop the incentive for loan originators to be unethical to increase their compensation, updated TILA § 1026.36(e)(1) stated, a loan originator may not direct or steer a consumer to consummate a transaction based on the fact that the loan originator would increase the amount of compensation that the loan originator would receive for that transaction compared to other transactions, unless the consummated transaction is in the consumer's interest.

In determining whether a consummated transaction is in the consumer's interest, that transaction must be compared to other possible loan offers available through the originator, if any, and for which the consumer was likely to qualify, at the time that transaction was offered to the consumer.

TILA allows to be considered a possible loan offer available through the loan originator, an offer need not be extended by the creditor. The offer need only be an offer that the creditor likely would extend upon receiving an application from the applicant, based on the creditor's current credit standards and rate sheets. A loan originator need not inform the consumer about a potential transaction if the originator makes a good faith determination that the consumer is not likely to qualify for it.

TILA does not require a loan originator to direct a consumer to the transaction that will result in a creditor paying the least amount of compensation to the originator. However, if the loan originator reviews possible loan offers available from a significant number of the creditors with which the originator regularly does business, and the originator directs the consumer to the transaction that will result in the least amount of creditor-paid compensation for the loan originator, the requirements of § 1026.36(e)(1) are deemed to be satisfied.

In the case where a loan originator directs the consumer to the transaction that will result in a greater amount of creditor-paid compensation for the loan originator, TILA is not violated if the terms and conditions on that transaction compared to the other possible loan offers available through the originator, and for which the consumer likely qualifies, are the same.

A loan originator who is an employee of the creditor on a transaction may not obtain compensation that is based on the transaction's terms or conditions pursuant to § 1026.36(d)(1). However, if a creditor's employee acts as a broker by forwarding a consumer's application to a creditor other than the loan originator's employer, such as when the employer does not offer any loan products for which the consumer would qualify, the loan originator is not an employee of the creditor in that transaction and is subject to § 1026.36(e)(1) if the originator is compensated for arranging the loan with the other creditor.

CFPB Steering Examples

Assume a loan originator determines that a consumer likely qualifies for a loan from Creditor A that has a fixed interest rate of 6%, but the loan originator directs the consumer to a loan from Creditor B having a rate of 6.5%. If the loan originator receives more in compensation from Creditor B than the amount that would have been paid by Creditor A, the prohibition in § 1026.36(e) is violated unless the higher-rate loan is in the consumer's interest.

For example, a higher-rate loan might be in the consumer's interest if the lower-rate loan has a prepayment penalty, or if the lower-rate loan requires the consumer to pay more in up-front charges that the consumer is unable or unwilling to pay or finance as part of the loan amount.

Ethical MLO Pitfalls

With laws and practices in place to stop unethical behavior, even an ethical mortgage loan originator can be a victim of a fraud scam. Borrowers may pose as legitimate borrowers, but be funding terrorism, identity theft rings, or other illegal activities. You can become an unknowing party and victim of these fraudsters if you fail to identify fraud and act on it when you find misrepresentation, mistakes, or fraud in your loan files.

Misrepresentation

To present a borrower’s information falsely or unfairly would be the dictionary definition. As a mortgage loan originator, it is your job to present the borrower to the underwriter in the best possible light, up to not committing fraud or misrepresenting the borrower’s true financial picture. When going into underwriting, the cover letter on the file should outline the challenges of the file. Then overcome those issues with documented compensating factors. When the loan originator hides information or presents false information there is intent to misrepresent the borrower’s true picture, which is mortgage fraud or deception.

Mistakes

To make a mistake is to be wrong about something. Do you come forward and admit it was an honest mistake and take the measures to correct the issue. Or do you ignore it and continue to claim it was not wrong and hope it goes away. Some may confuse honest mistakes with fraud. Determining the difference may be in how someone handles the aftermath of the mistake once it is discovered.

It's been said, 'If you are not making a mistake in the mortgage business, you are not doing anything.' There are too many laws, regulations, guidelines, and restrictions to be perfect. Too often making mistakes and finding out ourselves you were wrong is how we learn the mortgage business.

If you make a mistake you need to determine if correcting it will cause more problems, yet make sure the mistake will not be interpreted as fraud. If the mistake changes the credit decision on a loan file, the mistake needs to be addressed with the funding lender or underwriter. Honesty is needed to bring trust to lending practices.

For Example, if you make a mistake in the borrower being a US citizen. If you find out they are a resident alien, the proper identification is needed for the file. This, however, would not change the loan decision. However, if the borrower is an illegal alien, this would change the loan decision and would need to be documented in the file for the underwriter to determine if the loan may be approved with illegal alien status. Likely no, but if the borrower has an ITIN there maybe another loan program you may offer to meet their financing needs.

It is important how you handle the mistake with a borrower as well. If you made a mistake, apologize and move forward with how you are going to correct the mistake. Do not get caught in the blame game. Even if you did not make the mistake and it was someone you work with or is on your team, remember you chose the team of people to assist you in getting this loan closed. Take the responsibility as solve the issue, don't try to save face.

How you handle the situation will determine if you are an ethical professional. Even when a borrower gets angry with you about the mistake, stay professional. This is business, it is not personal. These are clients, not friends. Treat them professionally, and they will most likely treat you professionally even when you do make a mistake.

Fraud

Fraud is an Act or course of deception, an intentional concealment, omission, or perversion of truth, to

1. gain unlawful or unfair advantage,
2. induce another to part with some valuable item or surrender a legal right, or
3. inflict injury in some manner.

Willful fraud is a criminal offense which calls for severe penalties, and its prosecution and punishment (like that of a murder) is not bound by the statute of limitations. However, incompetence or negligence in managing a business or even a reckless waste of firm's assets (by speculating on the stock market, for example) does not normally constitute a fraud.

For this ethics course, we will review the federal laws that require mortgage loan originators to make an ethical effort to ensure the loans they are originating do not contain fraud. We will also review current fraud statistics and the clues to watch for, so you don't fall victim to becoming an unknowing party to a fraud scam.

Fair Credit Reporting Act

The Consumer Financial Protection Bureau (CFPB) enforces the Fair Credit Reporting Act and its Red Flags Rule. The FCRA continues to be modified to increase consumer protections. Consumer reporting agencies are required to ensure when furnishing consumer reports to creditors, they require the prospective users of the information to identify themselves, certify the purposes for which the information is sought, and certify that the information will be used for no other purpose. No consumer reporting agency may furnish a consumer report to any person if it has reasonable grounds for believing that the consumer report will not be used for the identified purpose.[68]

For example, a mortgage lender may only use the consumers credit report for making a credit decision on qualifying for a residential home loan. To use a consumer credit report for any other purpose, the mortgage lender would need to certify the other allowable purpose with the consumer reporting agencies.

Consumer reporting agencies are also tasked to ensure the accuracy of the information in a consumer's report, and monitor the information provided by creditors is placed on the proper consumers report.

The FCRA provides requirements for users of consumer reports that may take adverse actions on the basis of the information contained in consumer reports. A lender that takes adverse actions with respect to any consumer based on consumers credit report, in whole or in part, is required to:

- Provide oral, written, or electronic notice of the adverse action to the consumer
- Provide the consumer written or electronic disclosure of their credit score
- Provide the consumer orally, in writing, or electronically the name, address, and telephone number of the consumer reporting agency that furnished the report, with a statement the agency did not make the decision to take adverse action
- Provide the consumer an oral, written, or electronic notice of the consumer's right to obtain a free copy of a credit report from that consumer reporting agency if requested within 60 days of the action taken, and their right to dispute the accuracy or completeness of the information in the consumer records.[69]

These consumer protections allow a consumer to identify if they have been a victim of identity theft or if a creditor is supplying inaccurate information. FCRA is an important federal law that requires ethical

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[68] https://www.ftc.gov/system/files/545a_fair-credit-reporting-act-0918.pdf; § 607. Compliance procedures 15 U.S.C. § 1681e
[69] § 615. Requirements on users of consumer reports [15 U.S.C. § 1681m]

behavior in regard to the borrowers' credit. Credit is an important factor for consumers, and anyone accessing credit or reporting credit history must be compliant with FCRA.

Identity Theft Consumer Rights

To modernize consumer rights and increase credit protection from increasing threats of Identity Theft, the 2003 Fair and Accurate Credit Transaction Act (FACT Act) amended the Fair Credit Reporting Act (FCRA) (15 U.S.C. §1681). These added provisions were designed to improve the accuracy of consumers' credit records, and provide specific identity theft consumer protections. The regulations put the onus on creditors to disprove a consumer's claim the debt was due to identity theft, and prohibited creditors from collecting the debts from identity theft victims.

Prior to the FACT Act, creditors held consumers responsible for the debt acquired by identity thieves. Consumers had to pay the creditor or ruin their credit reports. Many consumers were stuck with the fraudulent delinquent debts on their credit reports with collectors dunning them to pay the debts taken out in their names. For those that could afford protection, they could hire expensive attorneys or maintain prepaid legal services to fight in court for removal and forgiveness of the fraudulent debts. Consumers that fought the system to have the debts removed, were often disheartened when later the debts would show back up on their credit reports.

This regulation provides consumers the right to one free credit report a year from each of the credit reporting agencies through online access at www.annualcreditreport.com. In addition, consumers may place fraud alerts on their credit files or freeze their credit files (no access to pull credit without consumer unfreezing their credit report).[70] For a reasonable fee, the consumer may purchase their credit score with information about how the credit score was calculated.

With FACT Act, the consumer has rights and procedures to have debts acquired by identity thieves removed from their credit reports, access to monitor their credit files, and the burden of proof placed on the creditor to prove the consumer truly acquired the debt. Once the creditor identifies the debts are fraudulent purchases, the creditor must remove the debt from the victim's report, and stop the collection of the debt from the victim. Creditors must make sure the person acquiring the credit, is who they say they are, or suffer the loss from issuing credit to an identity thief.

As a mortgage loan originator, the FACT Act added provisions requiring mortgage originators take steps to prevent and mitigate identity theft. This provision relating to data security includes the "Red Flags" rules.

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[70] Identity Theft Rules 16 CFR 681

The Red Flags Rules provision was further amended by the Red Flag Program Clarification Act of 2010. It defined the type of creditor that must comply with the Red Flag Rules. If the creditor offers or maintains accounts subject to a reasonably foreseeable risk of identity theft, they must comply with the Red Flag Rules, which includes mortgage loan originators and lenders. All mortgage lenders in compliance, have red flag rule policies and procedures as well as annual employee training.[71]

Identity Theft Program Requirement

Identity theft happens when someone uses another person's identity including Social Security number or other personal information with illegal intentions to open new accounts, make purchases, buy a home, or get a tax refund.

One common mortgage fraud scam is identity theft with income and asset falsification. This form of identity theft occurs when a buyer fraudulently obtains financing using an unwilling and unaware victim's information, including Social Security numbers, birth dates, and addresses. Identity theft for mortgage purposes may also include stolen pay stubs, bank records, tax returns, W2s and falsified employment verification letters. Even property ownership records can be falsified to obtain a fraudulent mortgage on a property they neither own nor occupy.

Identity Theft Program

For compliance with the Red Flag Rules, a mortgage lender must have a policy and procedure with safeguards to detect fraudulent information, and employee training on how to recognize fraud, report identity theft red flags, and designated a person to act on those red flags by following the mortgage company's policies and procedures.

Identity Theft Program Compliance: A Four Step Process

Creditors comprehensive Fraud Prevention Program should be designed to detect the warning signs (red flags) of identity theft in their day-to-day operations. Regulators entrust this will combat identity theft and related mortgage fraud. The Federal Trade Commission offers the following four step process for compliance.[72]

1. Identify Relevant Red Flags

What are "red flags"? They're the potential patterns, practices, or specific activities indicating the possibility of identity theft. Creditors must consider:

A. **Risk Factors.** Different types of accounts pose different kinds of risk.

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[71] Pub. L. 111-319, 124 Stat. 3457

[72] https://www.ftc.gov/tips-advice/business-center/guidance/fighting-identity-theft-red-flags-rule-how-guide-business#how

For example, red flags for deposit accounts may differ from red flags for mortgage credit accounts, and those for consumer accounts may differ from those for business accounts. When identifying key red flags, think about the types of accounts offered; the ways to open covered accounts; how to provide access to those accounts; and what to know about identity theft in the mortgage business.

a. A covered account is generally:
    i. an account that a financial institution or creditor offers or maintains, primarily for personal, family, or household purposes, that involves or is designed to permit multiple payments or transactions; or
    ii. any other account that poses a reasonably foreseeable risk to customers of identity theft.

B. **Sources of Red Flags**. Consider other sources of information, including the experience of other members of the mortgage industry. Technology and criminal techniques change constantly. Mortgage professionals must stay informed and up-to-date on new threats.

C. **Categories of Common Red Flags.** Supplement A to the Red Flags Rule lists specific categories of warning signs to consider. The examples here are one way to think about relevant red flags in the context of daily mortgage lending activities.

a. **Alerts, Notifications, and Warnings from a Credit Reporting Company.** Changes in a credit report or a consumer's credit activity might signal identity theft:
- a fraud or active duty alert on a credit report
- a notice of credit freeze in response to a request for a credit report
- a notice of address discrepancy provided by a credit reporting company
- a credit report indicating a pattern inconsistent with the person's history
    - For example, an increase in the volume of inquiries or the use of credit; an unusual number of recently established credit relationships; or an account that was closed because of an abuse of account privileges.

b. **Suspicious Documents**. Documents can offer hints of identity theft:
- identification looks altered or forged
- the person presenting the identification doesn't look like the photo or match the physical description
- information on the identification differs from what the person with identification said verbally or doesn't match a signature on other available documents
- an application looks like it's been altered, forged, or torn up and reassembled

c. **Suspicious Personal Identifying Information**. Personal identifying information can indicate identity theft:

- inconsistencies with what is known.
    - For example, an address that doesn't match the credit report or the use of a Social Security number that's listed on the Social Security Administration Death Master File.
- inconsistencies in the information a customer has submitted
- an address, phone number, or other personal information already used on an account known to be fraudulent
- a bogus address, an address for a mail drop or prison, a phone number that's invalid, or one that's associated with a call center or answering service
- a Social Security number used by someone else obtaining a loan
- an address or telephone number used by several people obtaining a loan
- a person who omits required information on an application and doesn't respond to notices that the application is incomplete
- a person who can't provide authenticating information beyond what's generally available from a wallet or credit report.

d. **Account Activity.** How the account is being used can be a tip-off to identity theft:
- shortly after loan closing, the creditor is notified of a change of address
- a new account used in ways associated with fraud.
    - For example, the customer doesn't make the first payment, or makes only an initial payment; or most of the line of credit is used for cash advances for jewelry, electronics, or other merchandise easily convertible to cash.

e. **Notice from Other Sources**. A customer, a victim of identity theft, a law enforcement authority, or someone else notifies the creditor that an account has been opened or used fraudulently.

2. Detect Red Flags

Sometimes, using identity verification and authentication methods can help detect red flags. Consider whether the procedures should differ if an identity verification or authentication is taking place in person, by telephone, mail, or online.

A. **New accounts.** When verifying the identity of the person who is opening a new account or loan application, reasonable procedures may include getting a name, address, and identification number, and for in-person verification, checking a current government-issued identification card, like a driver's license or passport. Depending on the circumstances, a creditor may want to compare that to information found from other sources, like a credit reporting company, or third party verifications.

B. **Death Master File.** Asking questions based on information from other sources can be a helpful way to verify someone's identity.
   a. For example, a credit bureau provides a notice when the social security being used to obtain credit has been identified as that of a deceased person.

C. **Existing accounts.** To detect red flags for existing accounts, the creditor's program may include reasonable procedures to confirm the identity of the person, to monitor transactions, and to verify the validity of change-of-address requests.

For online authentication, consider the Federal Financial Institutions Examination Council's guidance on authentication. It explores the application of multi-factor authentication techniques in high-risk environments, including using passwords, PINs, smart cards, tokens, and biometric identification. Certain types of personal information like a Social Security number, date of birth, mother's maiden name, or mailing address are not considered reliable authenticators because they are easily accessible.

3. Prevent and Mitigate Identity Theft

When a red flag is spotted, an MLO must be prepared to respond appropriately, and follow its company's policies and procedures. The creditor's response will depend on the degree of risk posed. It may need to accommodate other legal obligations, like filing a Suspicious Activity Report (SAR), as required by the Bank Secrecy Act (BSA).

4. Update the Program

The Rule recognizes that new red flags emerge as technology changes or identity thieves change their schemes which requires periodic updates to a creditor's program. Updates to the program should factor in a creditor's own experience with identity theft; changes in how identity thieves operate; new methods available to detect, prevent, and mitigate identity theft; changes in the loans offered; and changes in creditor's business, like mergers, acquisitions, alliances, joint ventures, and arrangements with service providers.

Customer Identification Information

A Red Flag Rules Program should specify acceptable customer identifying information that will be required of each customer applying for a covered account. At a minimum, this should include:

- Name
- Date of birth, for an individual
- Address, which will be:
  - For an individual, a residential or business street address

    - For an individual who does not have a residential address, an Army Post Office or Fleet Post Office box number or the residential address of next of kin or
    - For a person other than an individual (such as a corporation, partnership or trust), a principal place of business, local office, or other physical location and identification number, which will be:
- For a U.S. person, a taxpayer identification number (such as a Social Security number) or for a non-U.S. person, one or more of the following:
    - A taxpayer identification number,
    - Passport number and country of issuance,
    - Alien identification card number, or
    - Number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard
  - Business and commercial customers should be required to provide a taxpayer identification number ("TIN").

Authenticating Customer's Identity

An Identity Theft Prevention Program should contain procedures for verifying the customer's identity, starting with the identifying information obtained from the customer and nondocumentary methods. These procedures should address customer verification through documents and third-party verifications.

- **Verification through documents.** An Identity Theft Prevention Program should contain procedures that set the documents a creditor will accept for identity verification purposes. These documents may include:
    - For an individual, unexpired government-issued identification evidencing nationality or residence and bearing a photograph or similar safeguard, such as a driver's license or passport, and
    - To the extent persons other than an individual (such as a corporation, partnership or trust), documents showing the existence of the entity, such as certified articles of incorporation, a government issued business license, a partnership agreement or trust instrument
- **Verification through nondocumentary methods**. Creditors that originate covered accounts for customers who are not physically present for the transaction, and who permit customer access to covered accounts remotely (for example, on the Internet), should include policies and procedures that describe the nondocumentary methods to be used in verifying the customer's identity:
    - These methods may include contacting a customer

    - Independently verifying the customer's identity through the comparison of information provided by the customer with information obtained from a consumer reporting agency, public database or other source
    - Checking references with other financial institutions
- The Identity Theft Prevention Program should address how it will handle situations where:
    - The customer is unable to present an unexpired government-issued identification document that bears a photograph or similar safeguard
    - The documents presented (for example, an out-of-state driver's license or a foreign passport) are unfamiliar to staff
    - The customer is not physically present during the account origination or access process
    - Other relevant circumstances where customer identity verification is not possible through use of documentation
- **Additional verification for certain customers.** An Identity Theft Prevention Program's policies and procedures should address situations involving business or commercial customers where it may be prudent to obtain information about individuals with authority or control over the financing transaction in order to verify the customer's identity.
    - This typically will include instances where customer identity verification is not possible through use of the financial institution's or creditor's normal verification methods.

The rule contains guidance with respect to what are "reasonable policies and procedures." For example, these reasonable policies include:

- Verifying the information in the consumer report with the consumer or
- Comparing the consumer report information to information
    - The user collects as part of its USA Patriot Act CIP (Consumer Identification Policy),
    - It maintains in its own files or
    - It obtains from third-party sources.

While there is no express requirement that CIP policies and procedures be in writing (unlike the Red Flags Rule), there is an implied expectation they should be in the wording of the legislation.

Duties Regarding Address Discrepancies

According to the United States Postal Service, more than 40 million Americans change their address annually, which creates obstacles in determining which addresses changes are legitimate and which are a fraud red flag. Financial institutions and creditors should be concerned about the validity of address information. Identity thieves have been known to intercept a victim's mail and change the address to obtain information to steal the consumer's identity or credit cards.[73]

For example, using the information one can obtain by diverting a consumer's mail to create new credit accounts with the new address may be a red flag to a creditor according to its Identity Theft Prevention Program.

The organization must develop policies and procedures designed to identify a notice of address discrepancy from a consumer reporting agency is a red flag and what appropriate action to take to investigate the information discrepancy. The notice should show the address used to order the report and given by the consumer and how differs from the address contained in the consumer report.

The organization may reasonably confirm that an address is accurate by any of the following means:

- Verification of the address with the consumer,
- Review of the organization's records,
- Verification of the address through third-party sources, or
- Other reasonable means.

If an accurate address is confirmed, the organization may furnish the consumer's address to the consumer reporting agency if:

1. The organization establishes a continuing relationship with the consumer, and
2. The organization, regularly and in the ordinary course of business, furnishes information to the consumer reporting agency.

Inconsistencies in the consumer's credit file are often a red flag the loan request contains misrepresentations.

For example, the credit report provides an address discrepancy warning on credit report, but the consumer noted on the loan application they have lived at their current address for 5 years.

The presence of one or two red flags in a loan file does not necessarily mean that there is fraudulent intent. However, if there are several red flags in a loan file may signal a fraudulent transaction that will trigger additional scrutiny in providing this consumer a mortgage.

Identity Theft Types

In 2018, the Federal Trade Commission processed 1.4 million fraud reports totaling $1.48 billion in losses. According to the FTC's "Consumer Sentinel Network Data Book," the most common

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[73] Section 114 of FACT Act

categories for fraud complaints were imposter scams, debt collection and identity theft.[74] It is important mortgage loan originators understand the different types of identity theft, be alert for the red flags, and act when discovered.

Synthetic identity theft is where some of the consumer's information is joined with information about others or made up information to form a totally synthetic identity. This type of ID theft combines real and fake personal information to create a new identity using sensitive data such as names, SSNs, and addresses that can be obtained on the dark web. According to the Federal Trade Commission (FTC), this was the most popular type of ID theft in 2018, and 2019 large company data security breaches exposed millions of consumers personal information fueling cybercrime with identity theft.

Sophisticated identity theft is a type of fingerless identity theft where hackers can be overseas and steal consumer information and then sell it remotely from the dark web. They are protected by the privacy veil of the dark internet, where they can sell ID theft information to another hacker who will use it fraudulently and steal from consumer accounts, max out credit cards, sell information to someone else who might impersonate the consumer, and put them in high financial risk.

Medical identity theft is used to provide medical treatments using someone's identity with no intention of paying the medical debt. It can lead to financial difficulties to the victim due to issues with debt collectors and credit issues as they follow the ID theft procedures. Patients can experience problems with their insurance copays and maximums because of fraudulent use.

Cyber-attack identity theft uses it for account takeover, mail identity theft, child/senior identity theft, information ransom, etc.

Credit card skimming and shimming increases as technology improves. While card skimming has been an issue for some time, shimming takes the crime to the next level with specific technology designed to record information from chip-enabled credit cards, which had previously been considered the more secure alternative to cards with magnetic strips.

Simplistic phone scams have remained popular, because modern technology enables effortless spoofing of legitimate phone numbers that belong to government agencies and other reputable organizations. Phone scams often use a combination of trust and urgency to convince victims to provide social security numbers or credit card account information.

Sim hijacking scam works when criminals call a cell phone carrier's tech support number pretending to be their target. They inform the call center employee that they have 'lost' their SIM card, and need their phone number to be transferred, or ported, to a new SIM card that the hackers themselves

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[74] https://www.consumeraffairs.com/finance/identity-theft-statistics.html

already own. This works via social engineering and maybe with other info they have sourced, be it on the dark web, such as a Social Security Number or home address (this info can be readily available due to the many data breaches that have happened in the last few years) the criminals convince the employee that they really are whom they claim to be, and the employee ports the phone number to the new SIM card.

Spoofing is used by scammers by using phone calls often with robocalls or scammers call personally using a technique called 'spoofing'. The scammers are able to manipulate their victim's Caller ID to make the call appear to be from a legitimate source, such as the IRS. They can then obtain the information they are seeking to steal the person's money.

Spear phishing is specifically targeted emails and text messages that uses information about consumers to tailor the messages in a manner, so the victim will trust the communications and click on links or attachments which result in malware or ransomware being downloaded.

Digital blackmailing is when a hacker steals an email list and sends messages that threaten to expose a person engaging in an illegal or unethical act. Some instances of digital blackmail don't involve lies about web surfing. A hacker can gain access to a webcam and capture intimate pictures and videos. The fraudster then uses the files to extort money from people.

Fraud Categories

Regulators identify two categories of fraud. **Fraud for housing** and fraud for profit. Fraud for housing is the least of the regulators worries. Fraud for housing happens when a borrower commits the fraud one time to obtain housing.

For example, A person purchases a home she states will be owner occupied, when in reality their sister will occupy the property. The sister could not qualify so the brother or sister purchases on her behalf.

Fraud for profit does the most damage as it's organized and out for the profit causing major losses for mortgage investors, and the biggest impact on the community where the fraud was committed.

For example, a real estate property investor purchases five homes in a community. He structures the sales of the homes to control the increasing values for the subsequent sales. He sales the inflated properties to straw buyers to increase the comparables used to determine his other property value. His property sales become the comparable sales in the neighborhood, and he can now sale the straw buyer homes in the higher market for the price he has set.

Red Flag Detection

The following lists is a summary of some of the red flags mortgage originators may find in their consumer files as they look for discrepancies, suspicious documents, or inconsistent information. Red flags that may warrant additional action and escalation as required by your company's Fraud Prevention Program. The consumer's loan request may be to fund fraudulent activities. Red flags do not state the loan must be declined, but it may require additional scrutiny if any of the following are identified or discovered, especially when the file contains multiple red flag warnings.

- Social Security number discrepancies within the loan file
- Address discrepancies within the loan file
- Verifications addressed to a specific party's attention
- Verifications completed on weekend or holiday
- Documentation that includes deletions, correction tape, or other alterations
- Numbers on the documentation appear to be "squeezed" due to alteration
- Different handwriting or type styles within a document

Mortgage Application Red Flags

- Significant or contradictory changes from initial to final application
- Employer's address shown as a post office box
- Information on the application differs from the information on the credit report
- Loan purpose is cash-out refinance on a recently acquired property
- Documentation shows buyer resides in subject property, but application shows different address while requesting nonowner occupied loan (For example, to avoid ability to repay rules as Dodd Frank Act put more restrictions on owner occupied loans than nonowner occupied)
- Same telephone number for applicant and employer
- Extreme payment shock may signal straw buyer
- Purchaser of investment property does not own primary residence

Sales Contract Red Flags

- Non-arm's length transaction: seller is real estate broker, relative, employer, etc.
- Seller is not currently reflected on title
- Purchaser is not the applicant
- Purchaser(s) deleted from/added to sales contract (assignment)
- No real estate agent is involved
- Power of attorney is used
- Second mortgage is indicated, but not disclosed on the application
- Earnest money deposit equals the entire down payment, or is an odd amount for local market

- Source of deposits are documented with multiple deposit checks with inconsistent dates. For example, Check #303 dated 10/1, Check #299 dated 11/1
- Name and/or address on earnest money deposit check differs from buyer's
- Real estate commission is excessive
- Contract is "boiler plate" with limited fill-in-the-blank terms, not reflective of a true negotiation or standard state real estate association approved form.

Credit Report Red Flags

- No credit history or "thin" credit files
- Invalid Social Security number or variance from other documents
- Duplicate Social Security number, additional user, or deceased notice warning for Social Security number on credit report
- Recently issued Social Security number
- Length of established credit is not consistent with applicant's age
- Credit patterns are inconsistent with income and lifestyle
- All tradelines opened at the same time
- Authorized user accounts have superior payment histories
- Numerous recent inquiries
- Employment discrepancies
- Social Security number or fraud alerts from credit bureau

Employment and Income Documentation Red Flags

- Employer's address is a post office box or applicant's current residence
- Applicant's residence is (will be) unreasonable distance from work
- Employer name is similar to a party to the transaction
    - For example, uses the applicant's initials
- Employer unable to be contacted or identified in cross directories or google search
- Year-to-date or past-year earnings are even dollar amounts
- Withholding not calculated correctly (check FICA tables)
- Withholding totals vary significantly from pay period to pay period
- Pay period dates overlap and/or do not correspond with other documentation
- Abnormalities in paycheck numbering
- Handwritten VOE, pay stubs, or W-2 forms
- Employer's identification number has a format other than 12-3456789
- Income appears to be out of line with type of employment
- Self-employed applicant does not make estimated tax payments

- Real estate taxes or mortgage interest claimed, but no ownership of real property disclosed
- High-income applicant without paid tax preparer
- Paid preparer signs taxpayer's copy of tax returns
- Interest and dividend income do not align with assets
- Applicant reports substantial income but has no cash in bank
- Large increase in housing expense
- Doesn't pass reasonableness test
  - For example, income appears to be out of line with type of employment, applicant age, education, and/or lifestyle

Asset Documentation Red Flags

- Down payment source is other than deposits (gift, sale of personal property)
- Applicant's salary does not support savings on deposit
- Applicant does not use traditional banking institutions
- Pattern of loyalty to financial institutions other than the subject lender
- Balances are greater than the FDIC insured limits
- Dates of bank statements are unusual or out of sequence
- Recently deposited funds without a plausible paper-trail or explanation
- Bank account ownership includes unknown parties
- Balances verified as even dollar amounts
- Two-month average balance is equal to present balance
- Source of earnest money is not apparent
- Earnest money is not reflected in account withdrawals
- Earnest money is from a bank or account with no relationship to the applicant
- Bank statements do not reflect deposits consistent with income
- Does not pass reasonableness test
  - For example, assets appear to be out of line with type of employment, applicant age, education, and/or lifestyle

Appraisal Red Flags

- Occupant shown to be tenant or unknown with owner occupied refinance
- Owner is someone other than seller shown on sales contract
- Appraisal indicates transaction is a refinance, but other documentation reflects a purchase
- Purchase price is substantially higher than predominant market value
- Purchase price is substantially lower than predominant market value
- Subject property obsolescence is minimized

    - For example, economic or social obsolescence decrease the property’s value due to these impacts; a big chain store builds a large facility on the vacant lot next to the property. With functional obsolescence the property would have a decrease in value due to the outdated design of the home since one upstairs bathroom for four bedrooms is less desirable in the current homebuyer’s market. With both examples, it would be a red flag if the appraiser did not make a price adjustment or use comparable properties that have similar impact in value allowing the subject property a higher valuation.
- Large positive adjustments made to comparable properties
- Comparable sales prices do not bracket the subject’s adjusted value
- Comparable sales are not similar in style, size, and amenity
- Dated sales used as comparable sales
- Uses new construction or condo conversion properties, when all comparable sales should be located in subject’s development
- Comparable properties are a significant distance from the subject, or located across neighborhood boundaries
    - For example, neighborhoods can vary when main arteries, highways or waterways separate the communities.
- Map scale distorts distance of comparable properties
- “For Rent” sign appears in photographs
- Photos appear to be taken from an awkward or unusual standpoint
- Address reflected in photos does not match property address
- Weather conditions in photos inconsistent with date of appraisal
- Appraisal dated before sales contract
- Significant appreciation in short period of time
- Prior sales are listed for subject and/or comparables without adequate explanation
- Title prepared for a party other than the lender
- Evidence of financial strain may indicate a compromised sale transaction
    - Financial strain may include:
        - Income tax, judgements, or similar liens recorded
        - Delinquent property taxes
        - Notice of default or modification agreement recorded
- Seller not on title
- Seller owned property for short time
- Buyer has pre-existing financial interest in the property

- Dates and amounts of existing encumbrances do not make sense
- Chain of title includes an interested party such as realtor or appraiser
- Buyer and seller have similar names, that if concealed is a non-arm's length transaction

Occupancy Transaction Red Flags

Purchase Transactions

- Real estate listed on application, yet applicant is a renter
- Applicant intends to lease current residence
- Significant or unrealistic commute distance to work
- Applicant is downsizing from a larger or more expensive house
- Sales contract is subject to an existing lease
- Occupancy affidavits reflect applicant does not intend to occupy
- New homeowner's insurance is a rental policy

Refinance Transactions

- Rental property listed on REO section of application is more expensive than subject property
- Different mailing address on applicant's bank statements, pay advices, etc.
- Different address reported on credit report
- Significant or unrealistic commute distance to work
- Appraisal reflects vacant or tenant occupancy
- Occupancy affidavits reflect applicant does not intend to occupy
- Homeowner's insurance is a rental policy (declarations page)
- Property search data provides discrepancies in information supplied

Closing Red Flags

- Borrower or seller names are different than sales contract and title
- Sales price is inconsistent with contract, loan approval, and/or appraisal
- Excessive earnest money or builder deposit
- Earnest money deposit is inconsistent with sales contract and/or application
- Payouts to unknown parties
- Refinance pays off undisclosed liens
- Excessive sales commissions
- Excessive fees and/or points
- Seller-paid closing costs, especially for purchaser with sufficient assets for down payment
- Cash proceeds to borrower are inconsistent with final application and loan approval

Identity Theft Actions Taken

The Red Flags Rule guidelines give examples of some appropriate responses, including:

- Following the company's Red Flag Rules or Identity Theft Prevention policies
- Contacting the customer to further document file
- Deny the request for credit
- Notify law enforcement
- Escalate the file to your company's Compliance Officer or BSA Officer as suspicious activity
    - The company's office would then determine if a SAR was warranted, or additional internal review
- Determining no response is warranted under its particular circumstances

The facts of a particular case may warrant using one of these options, several of them, or another response altogether. Consider whether any aggravating factors raise the risk of identity theft.

Stolen or Forged Document Examples

- A mortgage company contacted a brokerage to verify customer investment balances. The brokerage determined that the mortgage applicant had obtained a customer's account statement and was representing himself as the customer in order to secure a mortgage based on the victim customer's investment account balance, and presumably also intending to secure the mortgage in the customer's name.
- An applicant for a mortgage submitted a phony driver's license photograph copied from an official publication on identity document evaluation.
- An applicant provided a mortgage loan originator copies of banks statements that reflected sufficient funds to close and cover the reserves required. Upon closer inspection by the mortgage loan originator, it became apparent the fonts and spacing of the document looked altered. The borrower/fraudster had apparently cut and pasted the figures in the columns, but the totals did not add up to the amounts deposited and withdrawn.

Identity Theft Threat and Prevention

An estimated nine million Americans have their identities stolen each year. Identity thieves may drain accounts, damage credit, and even put medical treatment at risk. Identity theft leaves businesses with shocking large sums of unpaid bills by these scammers. Mortgage lenders and mortgage loan originators are an essential part of fraud prevention in the mortgage industry.

A mortgage company's identity theft prevention program or red flags rule program provides guidance and expectation for the front line defense to detect the "red flags" of identity theft and fraudulent transactions. At this point, mortgage companies can take the steps to mitigate risk and the damage caused by the fraud.

Current Fraud Scams

CFPB was worked hard to enforce federal laws including the Red Flag Rules. Lenders are dedicated to originating viable loans for their investors, and mandate annual training for their employees. Based on current statistics showing a decreasing trend in fraud, shows the measures taken by Dodd Frank Act, regulators, lenders and mortgage loan originators are working.

Undisclosed real estate debt fraud occurs when a loan applicant intentionally fails to disclose additional real estate debt or past foreclosures. According to the Core Logic's Fraud Report, during the second quarter of 2019, this type of fraud risk decreased 12.8% compared to the same quarter in 2018, although it's one of the most common issues discovered.

Property fraud occurs when information about the property or its value is intentionally misrepresented. From the second quarter of 2018 to the second quarter of 2019, property fraud risk decreased 9.9%.

Income fraud includes misrepresentation of the existence, continuance, source, or amount of income used to qualify. From the second quarter of 2018 to the second quarter of 2019, the income fraud risk indicator decreased 7.7%.

Transaction fraud occurs when the nature of the transaction is misrepresented, such as undisclosed agreements between parties and falsified down payments. The risk includes third party risk, non-arm's length transactions, and straw buyers. From the second quarter of 2018 to the second quarter of 2019, the transaction fraud risk indicator decreased 3.8%.

Identity theft fraud occurs when an applicant's identity and/or credit history is altered, a synthetic identity is created, or a stolen identity is used to obtain a mortgage. From the second quarter of 2018 to the second quarter of 2019, the Identity theft fraud risk indicator decreased 2.9%.

Occupancy fraud occurs when mortgage applicants deliberately misrepresent their intended use of a property (primary residence, secondary residence or investment). Programs, pricing, and underwriting guidelines are impacted by a property's intended occupancy. From the second quarter of 2018 to the second quarter of 2019, the Occupancy fraud risk indicator decreased 2.0%.

Additional Industry Findings

"Phantom employers" scheme of fake employers was identified by Fannie Mae and Freddie Mac. Some fake employers may appear legitimate and have valid phone numbers, addresses and websites, while others may not have viable information. This category includes false diplomas and college transcripts to supplement short tenure for younger borrowers. The most consistent red flag was the time with the current employer was typically less than one year. This short tenure avoids fraudulent income detection through IRS tax transcripts.

iBuyers Influence

iBuyers are changing housing market by offering an instant cash sale for qualified homes and flexibility for the home sellers, while avoiding open houses and contingencies in purchase agreements. The purchase and rapid resale of a property for a higher price (flipping) has traditionally been a red flag for potential mortgage fraud. Since the financial crisis, flipping has become more common and less concerning as more renovators take on the task of updating aged housing.

In the last two years, a growing portion of properties being purchased and quickly resold at a higher price are due to iBuyer activity. iBuyer price markups are modest, usually less than 10%. iBuyer transactions have proven to have lower fraud risk as there is a high level of transparency and standardization.

The industry is watching this piece of the market to identify if fraud increases if speculators cannot sell properties fast enough at an acceptable price. In a decreasing property value situation, it may motivate schemes where the property is sold to a straw buyer at an inflated price, similar to builder bailout scheme. A straw buyer normally has no intention of using or controlling the purchase of the home.

Module 4

Non-Traditional Mortgage Products –2 hours of Non-Traditional Mortgage Lending

ARM Loan Deep Dive and Reverse Mortgage Review

Module 4 Objective:

This module reviews in details two important non-traditional mortgage products, ARM loans and Reverse Mortgages. With these loan programs, is a review of the key terms needed to understand how these two types of loan programs function. The student will understand the function, adjustment and guidelines for adjustable rate mortgages and FHA home equity conversion mortgages and their intended uses.

Key Mortgage Terms

Adjustable Rate Mortgage (ARM) - A mortgage that permits the lender to periodically adjust the interest rate to reflect fluctuations in the cost of money.

Alt-A Loan - A type of loan in which the risk is greater than prime, but is just missed conforming loans. Its rates are still competitive, and less than Non-QM or Non-prime loans. The borrower may have a strong credit history, but the mortgage may have elements that increase risk. Risk issues could include higher loan-to-value, jumbo loan amount, higher debt-to-income ratios, or alternative documentation for the borrower's income.

Assumption – A loan assumption is a transaction in which one party (the "assumptor") obtains an ownership interest in real property from another party and accept responsibility for the terms, payment and obligation of that party's mortgage. Most loan programs require the assumptor to qualify for the assumed loan.

Like-kind property exchange in a transaction is the term frequently expressed concerning IRS Section 1031 exchanges. A 1031 exchange allows the investor to defer the tax gains or losses on a property because they do not physically receive the money, it's held in escrow and passes from one like-kind property to another.

Conforming Loan - A residential mortgage loan that meets the criteria necessary to be sold in the secondary market to Fannie Mae or Freddie Mac.

Conventional Loan - A residential mortgage loan with guidelines based on conforming market, and usually originated by a bank or institutional lender. The loan would not be insured or guaranteed by FHA, VA or USDA.

Conversion Option - An ARM loan option that gives a borrower the right to convert from an adjustable rate loan to a fixed-rate loan at a defined time during repayment of the debt and designated in the Promissory Note.

Cost of Funds Index (COFI) - A regional average of interest expenses incurred by financial institutions, which in turn is used as a base for calculating variable rate loans.

Fannie Mae – The Federal National Mortgage Association is the official name for FNMA or Fannie Mae. This government sponsored enterprise (GSE) buys loans from mortgage lenders, packages them together, and sells them as a mortgage-backed security to investors in the open market. It sets the standard guidelines for conforming loans to be sold to Fannie Mae to ensure the level of risk in the securities it guarantees. Its guidelines may vary from Freddie Mac, a competitor and contributor. Its purchase of loans provides a flow of fund for lenders to origination additional home loans and stimulate the economy.

Freddie Mac – The Federal Home Loan Mortgage Corporation is the official name for FHMLC or Freddie Mac. This government sponsored enterprise (GSE) buys loans from mortgage lenders, packages them together, and sells them as a mortgage-backed security to investors in the open market. It sets the standard guidelines for conforming loans to be sold to Freddie Mac to ensure the level of risk in the securities it guarantees. Its guidelines may vary from Fannie Mae, a competitor and contributor. Its purchase of loans provides a flow of fund for lenders to origination additional home loans and stimulate the economy.

Home Equity Loan - A loan secured by a mortgage on residential property that allows the homeowner access to the property's equity they must then repay.

Home Equity Line of Credit (HELOC) - An open-end residential home equity loan in which borrowers are granted a specific credit limit that allows a period of time the homeowner may draw on the available credit, then at the end of the period, the loan is amortized to pay off within the term of the loan. The homeowner may or may not pay only interest during the draw period, based on the terms of the loan. This can cause large payments due when the loan is in repayment.

Hybrid (ARM) – Mortgage loan with a stable interest rate for a fixed period of time, then starts to adjust regularly based on the ARM loan's index as set in the Promissory Note.

Land Contract - A real estate purchase installment agreement in which the buyer makes payments to the seller in exchange for the right to occupy and use the property, but no deed or title is transferred until all, or a specified portion of the payments have been made as agreed upon in the land contract.

Lease - A contract where one party pays the other rent in exchange for possession of real estate property. Mortgage lenders generally require the property to be a **leasehold property**. A leasehold estate allows temporary right to hold the land giving the lessee rights of real property by some form of title from the lessor. Leasehold estate is typically considered personal property.

Lease with Option to Purchase Contract in which a seller leases property to a person for a specific period of time with terms and option to buy the property at a predetermined purchase price during the lease term.

Lease Purchase Contract in which a seller leases property to a person for a specific period of time with terms and understanding the tenant will buy the property at a set purchase price during or at the end of the lease term.

Lien Release - A document in which a legal right to residential property is given up. The release must be recorded in the property county records to release the lien.

Nontraditional Mortgage loan as defined by the SAFE Act is any mortgage product other than a 30-year fixed-rate mortgage. The Interagency Guidance on Nontraditional Mortgage Product Risk definition allows a borrower to defer principal and sometimes interest with nontraditional mortgages.

Non-QM loans - A Non-Qualified Mortgage (Non-QM) is any home loan that doesn't comply with the Consumer Financial Protection Bureau's existing rules on Qualified Mortgages (QM). Usually this type of mortgage loan accommodates people who are not able to prove they are capable of making the mortgage payments, or exceed the QM thresholds.

Traditional Mortgage Product – as defined by SAFE Act, any 30-year fixed-rate loan.

ARM Loan Deep Dive

An adjustable rate mortgage (ARM) allows lenders freedom from being locked into a fixed-interest rate for the entire life of a loan as interest rates may adjust, according to the terms in the note, to reflect the current cost of money. Many lenders like ARMs because they can pass the risk of fluctuating interest rates on to borrowers. Lenders may offer multiple types of ARM programs.

ARM loan rates may be lower than a long term fixed rate when the short-term market is doing well. Although most borrowers prefer the security of a fixed rate and payment, ARMs have maintained a place in the market.

Terms, rate changes, and many other aspects of ARMs are prescribed guidelines by several agencies, depending on the loan program. Fannie Mae, Freddie Mac, FHA, and/or private mortgage insurers set their own rules on what they will accept regarding these types of loans, and creditors must also comply with TILA regulations regarding required ARM disclosures.

Components of ARMs

In this section we will review the components to an ARM loan:

- Index
- Margin
- Rate adjustment period
- Interest rate cap
- Interest rate floor
- Conversion option (if any)

Index

Once the initial interest rate for the loan is set, the rate of the loan is tied to a widely recognized and published index. The index is often referred to as the cost of money.

At the time a loan is made, the consumer may choose the loan program with the index that meets their financial goals. While in repayment the index will fluctuate based on market conditions. The index moves in line with other short-term interest rate debt instruments. At the time of adjustment, the index is added to the margin to determine the next period's interest rate.

Common adjustable rate mortgage indices include:

- Federal Cost of Funds (FedCofi)
- 11th District Cost of Funds Indexes (COFI)
- Constant Maturity Treasury (CMT)
  - One-year; Three-year; Five-year; Ten-year
- London Interbank Offered Rate (LIBOR)

FedCofi is a calculated formula of the monthly average interest rates for marketable Treasury bills and Treasury notes. It is used as a benchmark for some types of mortgage loans and securities. The FedCofi is published by Freddie Mac monthly.

COFI is the monthly cost-of-funds reflecting the weighted average interest rate paid by 11th Federal Home Loan Bank District savings institutions for savings and checking accounts. The 11th district covers Arizona, California and Nevada.

CMT is the weekly average yield on U.S. Treasury securities adjusted to a constant maturity of one year, three year, five year, or ten year (based on ARM term) as made available by the Federal Reserve Board.

LIBOR is the average rate for U.S. dollar-denominated deposits in the London market based on quotations of major banks.

For example, Fannie Mae uses a 1-year LIBOR index as published in the *Wall Street Journal*.[75] The index is subject to change over time and is, therefore, likely to be different each time there is an adjustment to the loan's interest rate. Indices generally with longer terms offer borrowers more protection from short-term fluctuations in the economy than indices with short terms.

Margin

A margin, which is sometimes referred to as a spread, remains fixed or constant for the duration of the loan. The margin is the number of percentage points added to the index and set by the loan program at time of rate lock. The margin never changes once locked and set out in the Note. The lower the margin the higher the initial interest rate and cost for the loan. The higher the margin the better the initial interest rate and costs on the loan. Having a high margin benefits the creditor when the loan adjusts, by allowing the lender to adjust upward quickly when the market has escalated.

The index plus the margin equals the adjusted interest rate also known as the **fully indexed rate.** This is the rate the loan would be if it were to adjust with the current index and margin today.

For Example, fully indexed rate:

4.25%	Current Index Value
+ 2.00%	Margin
6.25%	Fully Indexed Rate

Most loan programs require the borrower qualify at the fully indexed rate, but other loan programs may require the borrower qualify at the potential higher rate if the loan adjusted to its maximum amount. Check your loan program guidelines for which rate is required for the borrower to qualify.

Teaser Rates

When an ARM's initial rate, or start rate, is less than the fully indexed rate, it is considered a discounted rate or teaser rate. Lenders offer teaser rates to make ARMs more attractive for borrowers to use. Teaser rates may have a higher first payment adjustment cap which may cause a large bump in the payment in a rising market environment.

Rate Adjustment Period

The rate adjustment period is the length of time between ARM loan's interest rate adjustments.

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[75] https://www.fanniemae.com/content/guide/selling/b2/1.3/02.html#ARM.20Plan.20Indexes

Per Adjustment Rate Cap and Floor Interest Rate

Interest rate caps are used to limit the number of percentage points an interest rate increase during the term of a loan, helping to eliminate large fluctuations in mortgage payments and payment shock.

Rate caps are often displayed as two or three numbers. For example, a one year ARM loan may have 2/6 caps. This means:

- 2 – The first number indicates the maximum amount the interest rate can increase (or potentially decrease) from one adjustment period to the next.
- 6 – The second number indicates the maximum amount the interest rate can increase during the life of the loan.

For example, the start rate + the lifetime cap 6% = maximum interest rate for the life of the loan

For example, a Hybrid 5/1 ARM may have 3/2/6 caps. This means:

- 3 – maximum the loan may increase with the first adjustment after five years. When have hybrid with longer initial stable payment period, the lender may want to recoup loses with a larger increase for the first adjustment.
- 2 – maximum the loan may increase or decrease on all subsequent adjustments after the first adjustment
- 6 – maximum the loan may increase over the life of the loan

The **floor rate** is the minimum a loan may adjust down. Some loan programs will use the start rate as the floor rate, and others may allow the initial interest rate to decrease on the first and/or subsequent adjustments.

Conversion Option

Loan program allows the borrower to convert the adjustable rate mortgage to a fixed rate mortgage without the expense of a refinance or re-qualifying for a new loan or conversion. There is small window of time called the conversion period, and the borrower must exercise their option to convert during this period or loan will remain an ARM loan. The conversion is ‘optional’.

ARM Adjustment Example

If you see a rate cap described as 1/2/6, the interest rate cannot increase more than:

- 1% at the first adjustment
- 2% for subsequent adjustment periods
- 6% total over the life of the loan

These types of adjustment caps would be common with 6 month LIBOR type loan programs. The 1% per adjustment would translate to 2% per year.

How ARMs Work

To understand how an ARM works and how payments adjust, think of an ARM as a set of stair steps. The start rate is often the floor, or your first step where the ARM begins. This is the period of time subject to the initial, start, or teaser interest rate. To determine the adjusted rate is a three step process for the following one year ARM example.

1. With 2/6 caps, the maximum interest rate at the first and all subsequent adjustments is the current interest rate (For this example 3.00% at time of adjustment) + the adjustment rate cap (2%). This formula is used for each successive interest rate adjustment calculation. 3% + 2% = 5% This sets the maximum second year period rate at a maximum of 5.00%, or 5% is the cap for this adjustment.
   - As a sub-calculation of this portion – the maximum rate it may adjust over the life of the loan is 3% + 6% = 9% maximum life of loan interest rate capped
2. The second calculation is to identify the fully indexed rate. For this example, the current CMT index is 2.125% plus the margin is 2.25%. The fully indexed rate is the sum of these two figures or 4.375%.
3. The new adjusted interest rate for this 1 year CMT loan is the lesser of these two calculations or 4.375% the fully indexed rate. The adjustment did not hit the periodic cap of 5%.

Use the same concepts for calculation of the next year's interest rate adjustment. Again, remember the "steps."

1. The first calculation is the maximum interest rate, which is the current rate of 4.375% + the adjustment cap 2.00% = 6.375%.
2. Secondly, calculate the fully indexed rate. For the following year assume the market has risen and CMT is 5.50%. To calculate the fully indexed rate. The index 5.50% + the margin 2.25% = 7.75% the fully indexed rate.
3. Because of the escalating market, the lender is able to get more for their cost of funds, but the borrower is capped to keep from having their payment raise too fast. The 6.375% will be the interest rate for the next year due to the loan program caps. In this example, if the market continues to raise or stays the same in a year, the borrower can plan on having their payment raise again until it hits 9% lifetime cap. However, if the market improves, the borrower's rate and subsequent payment may decrease.

Hybrid ARM

A hybrid ARM is an ARM with an initial fixed-rate period longer than a one year period. That is, the loan has a stable initial rate for a specified number of years, and then the interest rate adjusts regularly for the remainder of the loan term, according to the terms of the note. TILA does not allow a lender to advertise a Hybrid ARM as a fixed rate loan. Be cautious how you advertise the initial stable rate period.

Hybrid ARMS have the initial stable rate period of 3 years, 5 years, 7 years or 10 years. At the end of the set initial period, the loan will adjust for every 6 months or annually depending on loan program chosen. Since TILA regulations set out qualified mortgage (QM) rules, 3/1 ARMs became a thing of the past for owner occupied loans. For a loan to be a QM loan, the lender must consider and qualify the borrower on the rate for the first five years of the loan.[76]

For example, a 5/1 hybrid CMT ARM has an introductory rate period or teaser rate for five years from the date the loan closed. The caps are 5/2/7. After the first adjustment, the loan will adjust annually based on the 1 year CMT. In this example, review the calculation for a first payment adjustment.

1. To find the first interest rate adjustment cap maximum, add the initial interest rate 3.50% to the initial rate adjustment cap 5.00% = 8.50% maximum adjustment cap. It is common for longer stable period loans to have a large first adjustment cap.
2. The fully indexed rate is then calculated. For this example, assume the CMT index is 5.50%. Add the index 5.50% + margin 2.25% = 7.75% fully indexed rate
3. The new rate is the lessor of the two calculations – 7.75% fully index rate will be the rate for the next period of time.

After the initial interest rate adjustment, the 2% caps are the subsequent adjustment cap for all future adjustments. The last number “7” is the life of loan cap. Initial rate 3.5% + 7% lifetime cap = 10.50% maximum rate the loan may adjust up to during the repayment of the loan.

ARM Disclosures

Lenders offering residential home financing, must comply with Truth-in-Lending Act Regulation Z requirements for disclosures of the loan terms to the borrowers (12 CFR §1026.19). For adjustable rate mortgages, TILA requires additional disclosures be provided on the Loan Estimate to inform consumers of the adjustable rate terms, and how the rate may change and impact their payment. In addition, TILA requires the lender provide the Consumer Handbook on Adjustable Rate Mortgages (CHARM booklet) to the borrower within three business days of loan application.

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[76] https://files.consumerfinance.gov/f/201401_cfpb_atr-qm_small-entity-compliance-guide.pdf

If the loan program is exempt from the LE and uses a Good Faith Estimate (GFE), then a separate ARM disclosure is required to be provided to the consumer within three business days of the loan application.

Reverse Mortgages

Another type of nontraditional mortgage is the reverse mortgage. A reverse mortgage may also be called a reverse equity mortgage or a reverse annuity mortgage. The most popular reverse mortgage program is FHA's Home Equity Conversion Mortgage or HECM.

The purpose of a reverse mortgage is to provide an elderly borrower who has substantial equity in a property to convert their accumulated equity into available cash without selling the property and without burdening the borrower with monthly payments to the lender. Seniors on a fixed income may not otherwise have access to much needed funds as they would not qualify with a mortgage payment. Only licensed and approved mortgage lenders may originate reverse mortgages to ensure they are properly trained to handle this loan program differences.

A reverse mortgage allows senior borrowers to use the equity in their home for any use, including, but not limited to start a small business, pay off personal debts, cover the cost of health care or medical expenses, or make home repairs and upkeep.

Conforming mortgage loans are termed "forward" loans or amortizing mortgage loans, where the loan balance decreases, and the equity increases through the repayment term. With a reverse mortgage, the balance of the loan rises as the borrower receives money from the lender and incurs interest to the outstanding loan balance. Since the borrower is not making any payments, when the reverse mortgage becomes due and payable, the borrower will have a higher loan balance from the start of the loan due to the accumulating interest and loan costs. For most reverse mortgages, the amount owed grows and the equity shrinks, which creates a "rising debt, falling equity" scenario.

Reverse Mortgage Myths and Deception

Common reverse mortgage myth is the loan may never be called due or foreclosed. If the borrower does not maintain residence in the property, doesn't maintain the property (the loan's collateral), or pay insurance and real estate property taxes; the lender may take the steps as necessary to maintain, collect, or satisfy its lien on the property. This loan is still a debt and the borrower must meet the terms of the note to maintain the loan and not have it called due and payable.

Next myth is there is no housing payment for a reverse mortgage. This statement may be misleading. There is no mortgage payment, but there are still housing payments to maintain the property's hazard insurance policy, property taxes, homeowner association fees, and any other fee required for the real estate property. It is not ‘free’ of costs to live in a residential property even when the property is paid in full with no mortgage lien, but is LESS expensive than many housing alternatives.

Next myth, senior borrowers will benefit the most if they use their equity early in retirement while still healthy enough to enjoy the benefits. Lender’s use celebrities in the advertisements that causes concern for regulators as seniors like to believe the celebrity understands and endorses the use of the product. Regulators were most concerned lenders were advertising using a reverse mortgage as a “lifestyle enhancement” as the primary use to travel and enrich their lifestyle when they are still young and healthy.

While the advertisement portrays an attractive light on aging, getting a reverse mortgage at 62 can be very risky and seniors may outlive their loan funds. Once the line of credit or equity is depleted, the funds may not be increased even if the home value increases. The available equity is set at the start of the loan and does not increase over the term of the loan. Refinancing is likely not an option as the loan balance increases over time with compounding mortgage interest.

If the senior borrower’s health fails and they are in need of funds to cover health care as they live into their 90’s, there is no equity to use. History now has shown borrowers that tapped into their home’s equity early in retirement jeopardized financial security later in life when the senior borrowers outlive their resources. [77]

Mortgage loan originators that work with reverse mortgage and senior borrowers need to be mindful of the statements in their advertisements. The Mortgage Acts and Practices (MAP Rule) with Regulation N prohibits deceptive acts and practices in the advertising of mortgage loan products and prohibits misrepresentation in any commercial communication concerning terms of a mortgage loan product. The Truth-in-Lending Act (TILA) prohibits acts or practices in advertisements for credit secured by a dwelling. The advertisement may not mislead by claiming there is no housing expense or misrepresent the loan is not a debt.[78]

CFPB has taken a closer look at misleading reverse mortgage advertisements. CFPB found statements not made in the advertisements would cause a reasonable consumer to believe the loans were being made by the government, when in reality they are made by lenders and insured by FHA; or require no repayment of the debt, when in reality this debt will continue to increase over time and require repayment and potentially foreclosure if the terms of the note are not met.[79]

FHA HECM Eligibility

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[77] https://files.consumerfinance.gov/f/201506_cfpb_a-closer-look-at-reverse-mortgage-advertising.pdf
[78] https://www.consumerfinance.gov/policy-compliance/rulemaking/regulations/1026/24/#i-2-ii
[79] https://www.federalregister.gov/documents/2011/12/16/2011-31731/mortgage-acts-and-practices-advertising-regulation-n-mortgage-assistance-relief-services-regulation

Although there are other reverse mortgage programs available, as FHA HECM is the most popular reverse mortgage program, this course will focus on FHA requirements. FHA reverse mortgages have some very specific requirements, besides the obvious 62 years of age requirement, that address the borrower's ability and willingness to continue to pay property expenses, and some less stringent requirements that make qualification for a Home Equity Conversion Mortgage more flexible than other options.

For example, there is no specific income documentation required, but the lender will evaluate the borrower's willingness and ability to meet their obligations and the mortgage requirements to pay property taxes, hazard insurance, flood insurance and other property expenses. There is no credit qualifying on a reverse mortgage, and no credit score requirement. The primary underwriting approval focus is the borrower's age, senior's ability to cover hazard insurance and property taxes, and the property's high equity position.

FHA qualifying considers the following factors:

- Age of the youngest homeowner
- Current value of the property
- Balance on existing mortgage loans
- Interest rates
- Occupy the property as their primary residence
- Not be delinquent on and federal debt
- Have financial resources to continue to make timely payments of ongoing property expense
- Participate in consumer information session given by HUD approved HECM counselor

Recent HECM Program Enhancements

FHA HECM had recent changes in 2019, and additional changes are in the works for approval and implementation as FHA continues to improve this HECM loan program and protect the consumers that use it. In 2019 the reverse mortgage program saw changes to the guidelines, loan limits, principal limit factors, and cost of HECM insurance premiums.

With the property's value a major factor and the most uncertain factor, FHA requires lenders to submit their reverse mortgage property appraisal to FHA for risk collateral assessment before loan consummation. FHA may require second appraisals in some cases with potential bias, with the use of the lessor of the two valuations for loan amount determination.

As with all loans, these loans have a loan limit. FHA allowed the HECM loan limit to increase for 2020 to $765,600, raising it more than $39,000 from $726,525 in 2019. If a home appraises for more than this amount, the $765,600 is the cap for the maximum amount of equity that can be considered for the reverse mortgage. FHA also allows higher loan amount limits in Freddie Mac's special exception areas, which include Alaska, Hawaii, Guam, and the Virgin Islands.

With the higher maximum claim amount, brings increased principal limits for borrowers. The principal limit is the initial borrower limit of the reverse mortgage. To determine the principal limit, the lender considers:

1. The age of the youngest borrower on the reverse mortgage or property title
2. The interest rate of the reverse mortgage
3. The value of the property

The final change was an increase in the upfront cost of FHA HECM insurance fee premium, and a decrease to the ongoing monthly mortgage insurance premium (MIP). These fees are required for all HECM loans and may not be waived.

1. Upfront MIP costs: At closing, consumers pay 2% of the home's appraised value or the maximum lending limit of $765,600, whichever is less. Formerly, .5% upfront.
2. Ongoing MIP rates: As of 2019, consumers pay 0.5% of the outstanding reverse mortgage balance over the life of the loan. This ongoing MIP accrues annually and is paid when the loan matures. Formerly, 1.25% annually.

The change was done to benefit the borrower with a smaller monthly accruing MIP payment.[80]

Changes made in 2015 added a **Life Expectancy Set-Aside** (LESA) for the payment of property taxes, including special assessments levied by municipalities or state law; hazard insurance premiums; and applicable flood insurance premiums, as required for certain HECMs based on the financial assessment results. LESA are funds set aside from the senior borrower's line of credit and not made available to the borrower, but used by the servicer to pay taxes and insurance on behalf of the senior borrower when due. They are not borrowed funds until used, so do not accrue interest when not used.[81]

- The Fully-Funded Life Expectancy Set-Aside is available for both adjustable and fixed-interest-rate HECMs when required by the mortgagee based on the results of the financial assessment, or if the mortgagee does not require a Life Expectancy Set-Aside and the mortgagor elects to have one.

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[80] https://www.hud.gov/program_offices/housing/sfh/hecm
[81] https://www.law.cornell.edu/cfr/text/24/206.205

- The Partially-Funded Life Expectancy Set-Aside is only available for an adjustable interest rate HECM when required by the mortgagee based on the results of the financial assessment. (Mortgagee Letter 2014-21)

Payment Options

The homeowner who takes out a reverse mortgage generally gets to decide how to receive the proceeds. The payment options are:

- **Tenure** – equal monthly payments for as long as at least one borrower lives and continues to occupy the property as a principal residence
- **Term** – equal monthly payment for a fixed period of months selected
- **Line of Credit** – unscheduled payments or an installment at times and in an amount of the senior borrower's choosing until the line of credit is exhausted.
    - May be taken as a Lump Sum at any time
- **Modified tenure** – combination of line of credit and scheduled monthly payments for as long as the senior borrower remain in the home.
- **Modified term** - combination of line of credit plus monthly payments for a fixed period of months selected by the borrower.

Age Restrictions

To qualify for a reverse mortgage, all persons who have an ownership interest in the security property must be at least 62 years of age. If one of the owners does not satisfy this age requirement, the under aged owner must relinquish all ownership interests in the property.

Eligible Properties

Although the specific type of reverse mortgage may impose different standards, in general, single-family, one-unit dwellings are considered eligible properties for a reverse mortgage. Depending on the program, condominiums, planned unit developments (PUDs), and manufactured homes may be acceptable. Mobile home and cooperative units are not generally eligible.

Homeowners Insurance Requirement

As the property is the collateral for the Note, the lender requires the borrower maintains a homeowner's insurance policy that is sufficient to cover the replacement value of the collateral property. This protects the lender's interest in the event of damage that causes a loss of value, such as a fire, tornado, etc. The lender will require being named as the beneficiary for any claims to stay aware of the property condition.

The lender may also require a separate flood insurance policy if the property is located within the 100 year flood plain as required by FHA guidelines.

Ownership Interest

All borrowers on the title to the property with ownership interest must meet HECM guidelines which includes age restriction of 62 years of age. To be eligible for a reverse mortgage, the home must be the principal residence and any debt on the home must be paid off. A senior borrower is not prevented from getting a reverse mortgage if there is debt on the home since funds from the reverse mortgage may be used to pay off any remaining debt on the home, but the reverse mortgage created must be a first lien.

Homebuyer Counseling Requirement

HECM programs impose an additional condition on prospective borrowers by requiring them to participate in a consumer counseling session given by an approved HUD counselor before they can apply for the loan. The counselor will explain the costs of the loan and the financial implications as well as provide guidance and advice in selecting a program and/or a lender. A lender cannot submit an application for an FHA-insured reverse mortgage until the applicant provides proof that the required counseling session occurred. All housing counseling and education must be completed a minimum of 30 days, but no more than six months, prior to the borrower submitting an application to a lender.

This unbiased, independent counselor can help guide the borrower through what can be a confusing process and many difficult decisions. At the end of the session, the counselor must provide the required certification of counseling completion. A counselor may even point the homeowner to other programs or assistance that might be a better solution than a reverse mortgage.

In the event of a non-borrowing spouse, counselors are required to:

- Discuss the implications of marital status in states that recognize common law marriage or community property state rules.
- Inform prospective borrowers and non-borrowing spouses about the requirement that a non-borrowing spouse obtain ownership of the property or other legal right to remain upon the death of the last surviving mortgagor.
- Explain that failure to obtain ownership or other legal right to remain in the property will result in the HECM becoming due and payable and no deferral will be issued.

Accelerating Repayment

As with any mortgage situation, there are some circumstances that might cause the lender to require immediate repayment; for example:

- The homeowner fails to make necessary repairs to the property.
- The property is condemned.

- The homeowner does not pay the mandatory property taxes.
- The homeowner ceases to pay the appropriate homeowner’s insurance premiums.
- A government entity claims eminent domain over the property.
- The borrower ceases to live in the property, or it is discovered the property is no longer the borrower’s principal residence.

Non-Recourse Loans

A reverse mortgage is considered a “non-recourse” loan, so even in the rare instance that the amount of money distributed over the life of the reverse mortgage exceeds the value of the home, the borrower or the borrower’s heirs cannot owe more than fair market sale price of the home, minus reasonable sales expenses. The lender has no claims on any other assets that may be held by the borrower or the borrower’s heirs.

Successors in Interest to Property of a Deceased Borrower

The HECM guidelines require the home be sold and the reverse mortgage paid off if the senior borrower(s) are not able to occupy the secured home for twelve continuous months. Spouses who do not meet the criteria for HECM qualifying or chose not to be on the loan (non-borrowing spouses), may continue to occupy the secured home after the death of the senior borrower to the reverse mortgage if the following HUD’s requirements are met:

- Reverse mortgage loans issued on or before August 4, 2014, the rule states that when the senior borrowing spouse dies or permanently vacates the home for twelve months or more, the loan must be paid in full. The guidelines do not dictate how the heirs may pay off the reverse mortgage.
- Reverse mortgage loans issued after August 4, 2014 contain a statement to extend the deferral date of the due and payable status that occurs because of the death of the last surviving mortgagor, if a mortgagor was married at the time of closing. To retain occupancy of the home, the non-borrowing spouse must be identified at the time of closing and must be married to the mortgagor at the time of their death.

To defer the due and payable status of the HECM, the non-borrowing spouse must:

1. Have been the spouse of a HECM mortgagor at the time of closing and have remained the spouse of the mortgagor for the duration of the HECM mortgagor’s lifetime.
2. Have properly disclosed to the mortgagee at the origination and is specially named as a non-borrowing spouse in the HECM documents.
3. Have occupied and continue to occupy the property securing the HECM as the principal residence of the non-borrowing spouse.

If a surviving non-borrowing spouse fails to comply with the provisions of the deferral of the due and payable clause:

- The HECM will become immediately due and payable. The mortgagee is not required to obtain approval from HUD at the end of the deferral period to call a loan due and payable.
- The lender may not require immediate payment in full until the end of the deferral period.
- The mortgagor continues to maintain the ability to sell the property for at least the lesser of the sale price or appraised value. The estate always maintains the right to dispose of the property if legally entitled to.

If the HECM mortgagor predeceases the identified non-borrowing spouse and desires to continue to occupy the home, he must continue to satisfy the following conditions:

1. Establish legal ownership to the secured property within ninety days of the death of the mortgagor
2. Ensure all other conditions contained in the loan documents continue to be satisfied (payment of property taxes, maintaining property insurance, etc.)
3. Ensure that the HECM does not become eligible to be called due and payable for any other reason.

The terms of the HECM must continue to be met by the mortgagor's estate or the non-borrowing spouse, including the following;

1. The note will continue to accrue interest per the terms of the mortgage and loan agreement.
2. The monthly MIP must continue to be paid to HUD by the mortgagee.
3. The mortgagee may continue to collect servicing fees per the terms of the mortgage agreement.
4. The only additional disbursements under the agreement may be for Repair Set-Aside that was a part of the original mortgage documents.

Lenders are not required to verify the marital status of the mortgagor and non-borrowing spouse during the loan process, however:

- Both parties must sign a certification at loan closing verifying the truth and accuracy of the information provided in the application with respect to the mortgagor's marital status.
- Mortgagors who hold themselves out to be married with a non-borrowing spouse must submit a certification annually to the mortgagee.

After the death of the last surviving mortgagor, the mortgagee must obtain the Non-Borrowing Spouse certification within 30 days of receiving notice of the last surviving mortgagor's death and then every year thereafter.

In the event of a divorce between the parties during the term of the reverse mortgage, a mortgagee should obtain a copy of the divorce decree. If the parties are divorced at the time of the mortgagor's death, the protections of the deferral period are no longer available to the non-borrowing spouse.

For a married couple seeking a HECM, with one spouse choosing not to be a borrower on the loan, the loan originator should have them follow these guidelines to remain in the home after the principal borrower is no longer residing in the home:

1. Inform the lender that the couple is legally married, make sure the lender confirms the marriage, and file the required forms with HUD annually
2. Remain married to guard your interest in the home
3. Review the loan documents to make sure the non-borrowing spouse is named in the mortgage papers
4. Pay the property taxes and hazard insurance when due to preserve the deferral period for the surviving spouse
5. Continue to occupy the home as a primary residence
6. When the borrowing spouse ceases to be an owner occupant, file the appropriate paperwork to establish legal ownership within 90 days of their departure

Borrowers should always be advised to seek legal advice on such issues which could cause them to lose their home if not properly handled.

Module 5: Review of Georgia Mortgage Laws (Elective)

LEARNING OBJECTIVES

- Identify definitions and terms
  - Know those exempt from licensing
  - Have knowledge of the following:
  - Registration, financials and bonds, education, disclosures, annual fees, advertisements, renewal of licenses, record maintenance and applying for licenses
- Understand the automated licensing system

INTRODUCTION

- The contents of this lesson are provided through the Georgia Residential Mortgage Act and the Georgia Mortgage Division Rules.
- The full text of these statutes is available within the resources area of this lesson. Students are strongly encouraged to download and print a copy for further review.
- The Official Codes of Georgia Annotated will be referenced throughout this text as O.C.G.A.

DEFINITIONS [O.C.G.A. §7-1-1000]

Considering there is a lot of jargon when it comes to regulations in the lending industry, it is important to review how some of the terminology used is defined. Section 7-1-1000 of the Official Codes of Georgia Annotated defines the following terminology:

(1) 'Affiliate' or **'person affiliated with'** means, when used with reference to a specified person, a person who directly, indirectly, or through one or more intermediaries controls, is controlled by, or is under common control with the person specified. Any beneficial owner of 10 percent or more of the securities of a person or any executive officer, director, trustee, joint venturer, or general partner of a person is an affiliate of such person unless the shareholder, executive officer, director, trustee, joint venturer, or general partner shall prove that he or she in fact does not control, is not controlled by, or is not under common control with such person.

(2) 'Audited financial statement' means the product of the examination of financial statements in accordance with generally accepted auditing standards by an independent certified public accountant, which product consists of an opinion on the financial statements indicating their conformity with generally accepted accounting principles.

(3) 'Commissioner' means the commissioner of banking and finance.

(4) 'Commitment' or 'commitment agreement' means a statement by a lender required to be licensed or registered under this article that sets forth the terms and conditions upon which the lender is willing to make a particular mortgage loan to a particular borrower.

(5) 'Control,' including **'controlling,' 'controlled by,' and 'under common control with,'** means the direct or indirect possession of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting or nonvoting securities, by contract, or otherwise.

(6) 'Department' means the Department of Banking and Finance.

(7) 'Depository institution' has the same meaning as in Section 3 of the Federal Deposit Insurance Act, 12 U.S.C. Section 1813(c), and includes any credit union.

(8) 'Dwelling' means a residential structure that contains one to four units, whether or not that structure is attached to real property pursuant to Regulation Z Section 226.2(a)(19). The term includes an individual condominium unit, cooperative unit, mobile home, and trailer if it is used as a residence.

(9) **'Executive officer'** means the chief executive officer, the president, the principal financial officer, the principal operating officer, each vice president with responsibility involving policy-making functions for a significant aspect of a person's business, the secretary, the treasurer, or any other person performing similar managerial or supervisory functions with respect to any organization whether incorporated or unincorporated.

(10) **'Extortionate means'** means the use or the threat of violence or other criminal means to cause harm to the person, reputation of the person, or property of the person.

(11) **'Federal banking agencies'** means the Comptroller of the Currency, the Director of the Office of Thrift Supervision, the National Credit Union Administration, and the Federal Deposit Insurance Corporation. Such term shall also include the Board of Governors of the Federal Reserve System.

(12) **'Georgia Residential Mortgage Act'** means this article, which also includes certain provisions in order to implement the federal Secure and Fair Enforcement for Mortgage Licensing Act of 2008.

(13) '**Individual'** means a natural person.

(14) **'License'** means a license issued by the department under this article to act as a mortgage loan originator, mortgage lender, or mortgage broker.

(15) **'Loan processor or underwriter'** means an individual who performs clerical or support duties as an employee at the direction of and subject to the supervision and instruction of a person licensed or exempt from licensing. For purposes of this paragraph, 'clerical or support duties' may include, subsequent to the receipt of an application, the receipt, collection, distribution, and analysis of information common for the processing or underwriting of a residential mortgage loan; and communicating with a consumer to obtain the information necessary for the processing or underwriting of a loan, to the extent that such communication does not include offering or negotiating loan rates or terms or counseling consumers about residential mortgage loan rates or terms. An individual engaging solely in loan processor or underwriter activities shall not represent to the public, through advertising or other means of communicating or providing information, including the use of business cards, stationery, brochures, signs, rate lists, or other promotional items, that such individual can or will perform any of the activities of a mortgage loan originator.

(16) **'Lock-in agreement'** means a written agreement whereby a lender or a broker required to be licensed or registered under this article guarantees for a specified number of days or until a specified date the availability of a specified rate of interest for a mortgage loan, a specified formula by which the rate of interest will be determined, or a specific number of discount points if the mortgage loan is approved and closed within the stated period of time.

(17) **'Makes a mortgage loan'** means to advance funds, offer to advance funds, or make a commitment to advance funds to an applicant for a mortgage loan.

(18) **'Misrepresent**' means to make a false statement of a substantive fact. Misrepresent may also mean to intentionally engage in any conduct which leads to a false belief which is material to the transaction.

(19) **'Mortgage broker'** means any person who directly or indirectly solicits, processes, places, or negotiates mortgage loans for others, or offers to solicit, process, place, or negotiate mortgage loans for others or who closes mortgage loans which may be in the mortgage broker's own name with funds provided by others and which loans are assigned within 24 hours of the funding of the loans to the mortgage lenders providing the funding of such loans.

(20) **'Mortgage lender**' means any person who directly or indirectly makes, originates, underwrites, or purchases mortgage loans or who services mortgage loans.

(21) 'Mortgage loan' means a loan or agreement to extend credit made to a natural person, which loan is secured by a deed to secure debt, security deed, mortgage, security instrument, deed of trust, or other document representing a security interest or lien upon any interest in one-to-four family residential property located in Georgia, regardless of where made, including the renewal or refinancing of any such loan.

(22) 'Mortgage loan originator' means an individual who for compensation or gain or in the expectation of compensation or gain takes a residential mortgage loan application or offers or negotiates terms of a residential mortgage loan. Generally, this does not include an individual engaged solely as a loan processor or underwriter except as otherwise provided in paragraph (5) of subsection (a) of Code Section 7-1-1002; a person or entity that only performs real estate brokerage activities and is licensed or registered in accordance with Georgia law unless the person or entity is compensated by a mortgage lender, mortgage broker, or other mortgage loan originator or by any agent of such mortgage lender, mortgage broker, or other mortgage loan originator; and does not include a person or entity solely involved in extensions of credit relating to time-share plans, as that term is defined in 11 U.S.C. Section 101(53D).

(23) 'Nationwide Mortgage Licensing System and Registry' means a mortgage licensing system developed and maintained by the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators for the licensing and registration of licensed mortgage loan originators, mortgage loan brokers, and mortgage loan lenders.

(24) 'Nontraditional mortgage product' means any mortgage product other than a 30 year fixed rate mortgage.

(25) 'Person' means any individual, sole proprietorship, corporation, limited liability company, partnership, trust, or any other group of individuals, however organized.

(26) 'Real estate brokerage activity' means any activity that involves offering or providing real estate brokerage services to the public, including acting as a real estate agent or real estate broker for a buyer, seller, lessor, or lessee of real property; bringing together parties interested in the sale, purchase, lease, rental, or exchange of real property; negotiating, on behalf of any party, any portion of a contract relating to the sale, purchase, lease, rental, or exchange of real property, other than in connection with providing financing with respect to any such transaction; engaging in any activity for which a person engaged in the activity is required to be registered or licensed as a real estate agent or real estate broker under any applicable law; and offering to engage in any activity or act in any capacity described herein.

(27) 'Registered mortgage loan originator' means any individual who meets the definition of mortgage loan originator, is registered with and maintains a unique identifier through the Nationwide Mortgage Licensing System and Registry, and is an employee of:

a. A depository institution;
b. A subsidiary that is:
    i. Owned and controlled by a depository institution; and
    ii. Regulated by a federal banking agency; or
c. An institution regulated by the Farm Credit Administration.

(28) 'Registrant' means any person required to register pursuant to Code Sections 7-1-1001 and 7-1-1003.2.

(29) 'Residential property' means improved real property used or occupied, or intended to be used or occupied, as the primary residence of a natural person. Such term does not include rental property or second homes. A natural person can have only one primary residence.

(30) 'Residential mortgage loan' means any loan primarily for personal, family, or household use that is secured by a mortgage, deed of trust, or other equivalent consensual security interest on a dwelling, as defined in Section 103(v) of the Truth in Lending Act, or residential real estate upon which is constructed or intended to be constructed a dwelling.

(31) 'Residential real estate' means any real property located in Georgia upon which is constructed or intended to be constructed a dwelling.

(32) 'Service a mortgage loan' means the collection or remittance for another or the right to collect or remit for another of payments of principal, interest, trust items such as insurance and taxes, and any other payments pursuant to a mortgage loan.

(33) 'Ultimate equitable owner' means a natural person who, directly or indirectly, owns or controls an ownership interest in a corporation or any other form of business organization, regardless of whether such natural person owns or controls such ownership interest through one or more natural persons or one or more proxies, powers of attorney, nominees, corporations, associations, limited liability companies, partnerships, trusts, joint-stock companies, other entities or devices, or any combination thereof.

(34) 'Unique identifier' means a number or other identifier assigned by protocols established by the Nationwide Mortgage Licensing System and Registry.

DEFINITIONS [O.C.G.A. §7-6A-2]

In addition, Section 7-6A-2 defines the following terminology:

(1) 'Acceleration' means a demand for immediate repayment of the entire balance of a home loan.

(2) 'Affiliate' means any company that controls, is controlled by, or is under common control with another company, as set forth in 12 U.S.C. Section 1841, et seq.

(3) 'Annual percentage rate' means the annual percentage rate for the loan calculated at closing according to the provisions of 15 U.S.C. Section 1606, the regulations promulgated thereunder by the Board of Governors of the Federal Reserve System, and the Official Staff Commentary on Regulation Z published by the Board of Governors of the Federal Reserve System.

(4) 'Bona fide discount points' means loan discount points knowingly paid by the borrower for the express purpose of reducing, and which in fact do result in a bona fide reduction of, the interest rate applicable to the home loan; provided, however, that the undiscounted interest rate for the home loan does not exceed by more than one percentage point the required net yield for a 90 day standard mandatory delivery commitment for a home loan with a reasonably comparable term from either the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation, whichever is greater.

(5) 'Borrower' means any natural person obligated to repay the loan including a co-borrower or cosigner.

(6) '**Creditor'** means a person who both regularly extends consumer credit that is subject to a finance charge or is payable by written agreement in more than four installments and is a person to whom the debt arising from the home loan transaction is initially payable. Creditor shall also mean any person brokering a home loan, which shall include any person who directly or indirectly for compensation solicits, processes, places, or negotiates home loans for others or offers to solicit, process, place, or negotiate home loans for others or who closes home loans which may be in the person's own name with funds provided by others and which loans are thereafter assigned to the person providing the funding of such loans, provided that creditor shall not include a person who is an attorney providing legal services in association with the closing of a home loan. A creditor shall not include: (A) a servicer; (B) an assignee; (C) a purchaser; or (D) any state or local housing finance agency or any other state or local governmental or quasi-governmental entity.

(7) 'High-cost home loan' means a home loan in which the terms of the loan meet or exceed one or more of the thresholds as defined in paragraph (17) of this Code section.

(8) **'Home loan'** means a loan, including an open-end credit plan where the principal amount does not exceed the conforming loan size limit for a single-family dwelling as established by the Federal National Mortgage Association and the loan is secured by a mortgage, security deed, or deed to secure debt on real estate located in this state upon which there is located or there is to be located a structure or structures, including a manufactured home, designed principally for occupancy of from one to four families and which is or will be occupied by a borrower as the borrower's principal dwelling, except that home loan shall not include:

A. A reverse mortgage transaction;

B. A loan that provides temporary financing for the acquisition of land by the borrower and initial construction of a borrower's dwelling thereon or the initial construction of a borrower's dwelling on land owned by the borrower;

C. A bridge loan made to a borrower pending the sale of the borrower's principal dwelling or a temporary loan made to a borrower and secured by the borrower's principal dwelling pending the borrower's obtaining permanent financing for such principal dwelling;

D. A loan secured by personal property including, but not limited to, a motor vehicle, motor home, boat, or watercraft and also secured by the borrower's principal dwelling to provide the borrower with potential income tax advantages when such personal property is the primary collateral for such loan;

E. A new loan secured by a borrower's principal dwelling as a result of a lien taken in connection with a debt previously contracted or incurred when the loan documents for such new loan do not include a mortgage, security deed, or deed to secure debt expressly securing such new loan; or

F. A loan primarily for business, agricultural, or commercial purposes.

(9) **'Make' or 'makes'** means to originate a loan or to engage in brokering of a home loan including the soliciting, processing, placing, or negotiating of a home loan made or offered by a person brokering a home loan.

(10) **'Manufactured home'** means a structure, transportable in one or more sections, which in the traveling mode is eight body feet or more in width or 40 body feet or more in length or, when erected on site is 320 or more square feet and which is built on a permanent chassis and designed to be used as a dwelling with a permanent foundation when erected on land secured in conjunction with the real property on which the manufactured home is located and connected to the required utilities and includes the plumbing, heating, air-conditioning, and electrical systems contained therein; except that such term shall include any structure which meets all the requirements of this paragraph except the size requirements and with respect to which the manufacturer voluntarily files a certification required by the secretary of the United States Department of Housing and Urban Development and complies with the standards established under the National Manufactured Housing Construction and Safety Standards Act of 1974, 42 U.S.C. Section 5401, et seq. Such term does not include rental property or second homes or manufactured homes when not secured in conjunction with the real property on which the manufactured home is located.

(11) **'Open-end credit plan' or 'open-end loan'** means a loan in which (A) a creditor reasonably contemplates repeated transactions; (B) the creditor may impose a finance charge from time to time on an outstanding balance; and (C) the amount of credit that may be extended to the borrower during the term of the loan, up to any limit set by the creditor, is generally made available to the extent that any outstanding balance is repaid.

(12) **'Points and fees'** means:

A. All items included in the definition of finance charge in 12 C.F.R. 226.4(a) and 12 C.F.R. 226.4(b) except interest or the time price differential. All items excluded under 12 C.F.R. 226.4(c) are excluded from points and fees, provided that for items under 12 C.F.R. 226.4(c)(7) the creditor does not receive direct or indirect compensation in connection with the charge and the charge is not paid to an affiliate of the creditor;

B. All compensation paid directly or indirectly to a mortgage broker from any source, including a broker that originates a loan in its own name in a table funded transaction, including but not limited to yield spread premiums, yield differentials, and service release fees, provided that the portion of any yield spread premium that is both disclosed to the borrower in writing and used to pay bona fide and reasonable fees to a person other than the creditor or an affiliate of the creditor for the following purposes is exempt from inclusion in points and fees: fees for tax payment services; fees for flood certification; fees for pest infestation and flood determination; appraisal fees; fees for inspection performed prior to closing; credit reports; surveys; attorneys' fees, if the borrower has the right to select the attorney from an approved list or otherwise; notary fees; escrow charges, so long as not otherwise included under subparagraph (A) of this paragraph; title insurance premiums; and fire and hazard insurance and flood insurance premiums, provided that the conditions set forth in 12 C.F.R. 226.4(d)(2) are met;

C. Premiums or other charges for credit life, credit accident, credit health, credit personal property, or credit loss-of-income insurance, debt suspension coverage or debt cancellation coverage, whether or not such coverage is insurance under applicable law, that provides for cancellation of all or part of a borrower's liability in the event of loss of life, health, personal property, or income or in the case of accident written in connection with a home loan and premiums or other charges for life, accident, health, or loss-of-income insurance without regard to the identity of the ultimate beneficiary of such insurance. In determining points and fees for the purposes of this paragraph, premiums or other charges shall only include those payable at or before loan closing and are included whether they are paid in cash or financed and whether the amount represents the entire premium for the coverage or an initial payment.

D. The maximum prepayment fees and penalties that may be charged or collected under the terms of the loan documents. Mortgage interest that may accrue in advance of payment in full of a loan made under a local, state, or federal government sponsored mortgage insurance or guaranty program, including a Federal Housing Administration program, shall not be considered to be a prepayment fee or penalty;

E. All prepayment fees or penalties that are charged to the borrower if the loan refinances a previous loan made or currently held by the same creditor or an affiliate of the creditor;

F. For open-end loans, points and fees are calculated in the same manner as for loans other than open-end loans, based on the minimum points and fees that a borrower would be required to pay in order to draw on the open-end loan an amount equal to the total credit line; and

G. Points and fees shall not include:

    i. Taxes, filing fees, recording, and other charges and fees paid or to be paid to public officials for determining the existence of or for perfecting, releasing, or satisfying a security interest;

    ii. Bona fide and reasonable fees paid to a person other than the creditor or an affiliate of the creditor for the following: fees for tax payment services; fees for flood certification; fees for pest infestation and flood determination; appraisal fees; fees for inspections performed prior to closing; credit reports; surveys; attorneys' fees, if the borrower has the right to select the attorney from an approved list or otherwise; notary fees; escrow charges, so long as not otherwise included under subparagraph (A) of this paragraph; title insurance premiums; and fire and hazard insurance and flood insurance premiums, provided that the conditions in 12 C.F.R. 226.4(d)(2) are met;

iii. Bona fide fees paid to a federal or state government agency that insures payment of some portion of a home loan, including, but not limited to, the Federal Housing Administration, the Department of Veterans Affairs, the United States Department of Agriculture for rural development loans, or the Georgia Housing and Finance Authority; and
iv. Notwithstanding any provision to the contrary in this chapter, compensation in the form of premiums, commissions, or similar charges paid to a creditor or any affiliate of a creditor for the sale of: (I) title insurance; or (II) insurance against loss of or damage to property or against liability arising out of the ownership or use of property, provided that the conditions in 12 C.F.R. 226.4(d)(2) are met.

(13) **'Process,' 'processes,' or 'processing'** means to act as a processor.
(14) **'Processor'** means any person that prepares paperwork necessary for or associated with the closing of a home loan, including but not limited to promissory notes, disclosures, deeds, and closing statements, provided that processor shall not include persons on the grounds that they are engaged in data processing or statement generation services for home loans.
(15) **'Servicer'** means the same as set forth in 24 C.F.R. 3500.2.
(16) **'Servicing'** means the same as set forth in 24 C.F.R. 3500.2.
(17) '**Threshold'** means:

A. Without regard to whether the loan transaction is or may be a 'residential mortgage transaction' as that term is defined in 12 C.F.R. 226.2(a)(24), the annual percentage rate of the loan is such that it equals or exceeds that set out in Section 152 of the Home Ownership and Equity Protection Act of 1994, 15 U.S.C. Section 1602(aa), and the regulations adopted pursuant thereto by the Federal Reserve Board, including Section 12 C.F.R. 226.32; or
B. The total points and fees payable in connection with the loan, excluding not more than two bona fide discount points, exceed: (i) 5 percent of the total loan amount if the total loan amount is $20,000.00 or more or (ii) the lesser of 8 percent of the total loan amount or $1,000.00 if the total loan amount is less than $20,000.00.

(18) **'Total loan amount'** means the amount calculated as set forth in 12 C.F.R. 226.32(a) and under the Official Staff Commentary of the Board of Governors of the Federal Reserve System. For open-end loans, the total loan amount shall be calculated using the total credit line available under the terms of the home loan as the amount financed.

Now that we have reviewed relevant terminology, we should move on to determine what the law specifically states regarding registration and licensing.

Exemptions; Registration Requirements [O.C.G.A. §7-1-1001]

According to the law, the following persons shall not be required to obtain a mortgage loan originator, broker, or mortgage lender license. However, they may be subject to registration requirements, unless otherwise stated:

1. Any lender authorized to engage in business as a bank, credit card bank, savings institution, building and loan association, or credit union under the laws of the United States, any state or territory of the United States, or the District of Columbia, the deposits of which are federally insured;
2. Any wholly owned subsidiary of any lender described in paragraph (1) of this Code section. Any subsidiary that violates any applicable law of this article may be subject to a cease and desist order as provided for in Code Section 7-1-1018; Any wholly owned subsidiary of any bank holding company; provided, however, that such subsidiary shall be subject to registration requirements in order to facilitate the department's handling of consumer inquiries. Such requirements are contained in Code Section 7-1-1003.3;

3. Registered mortgage loan originators, when acting for an entity described in paragraphs (1) or (2) of this Code section. To qualify for this exemption, an individual shall be registered with and maintain a unique identifier through registration with the Nationwide Mortgage Licensing System and Registry;
4. Any individual who offers or negotiates terms of a residential mortgage loan with or on behalf of an immediate family member of such individual. For purposes of this exemption, the term 'immediate family member' means a spouse, child, sibling, parent, grandparent, or grandchild. Immediate family members shall include stepparents, stepchildren, stepsiblings, and adoptive relationships;
5. A licensed attorney who negotiates the terms of a residential mortgage loan on behalf of a client as an ancillary matter to the attorney's representation of the client, unless the attorney is compensated by a lender, a mortgage broker, or other mortgage loan originator or by any agent of such lender, mortgage broker, or other mortgage loan originator;
6. A Georgia licensed real estate broker or real estate salesperson not actively engaged in the business of negotiating mortgage loans; however, a real estate broker or real estate salesperson who directly or indirectly negotiates, places, or finds a mortgage for others shall not be exempt from the provisions of this article;
7. Any person performing any act relating to mortgage loans under order of any court;
8. Any natural person or the estate of or trust created by a natural person making a mortgage loan with his or her own funds for his or her own investment, including those natural persons or the estates of or trusts created by such natural persons who make a purchase money mortgage for financing sales of their own property;
9. The United States of America, the State of Georgia or any other state, and any agency, division, or corporate instrumentality of any governmental entity, including without limitation: the Georgia Housing and Finance Authority, the Georgia Development Authority, the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC), the Government National Mortgage Association (GNMA), the United States Department of Housing and Urban Development (HUD), the Federal Housing Administration (FHA), the Department of Veterans Affairs (VA), the Farmers Home Administration (FmHA), and the Farm Credit Administration and its chartered agricultural credit associations;
10. Any individual who offers or negotiates terms of a residential mortgage loan secured by a dwelling that serves as the individual's residence;
11. Any person who makes a mortgage loan to an employee of such person as an employment benefit;
12. Any licensee under Chapter 3 of this title, the "Georgia Industrial Loan Act," provided that any mortgage loan made by such licensee is for $3,000.00 or less;
13. Nonprofit corporations making mortgage loans to promote home ownership or improvements for the disadvantaged.
14. A natural person employed by a licensed or registered mortgage broker, a licensed or registered mortgage lender, or any person exempted from the mortgage broker or mortgage lender licensing requirements of this article when acting within the scope of employment and under the supervision of the mortgage broker or mortgage lender or exempted person as an employee and not as an independent contractor, except those natural persons exempt from licensure as a mortgage broker or mortgage lender under paragraph (17) of this Code section. To be exempt from licensure as a mortgage broker or mortgage lender, a natural person shall be employed by only one such employer and shall be at all times eligible for employment in compliance with the provisions and prohibitions of Code Section 7-1-1004. Such natural person, who meets the definition of mortgage loan originator provided in paragraph (22) of Code Section 7-1-1000, shall be

subject to mortgage loan originator licensing requirements. A natural person against whom a cease and desist order has become final shall not qualify for this exemption while under the employment time restrictions of subsection (o) of Code Section 7-1-1004 if such order was based on a violation of Code Section 7-1-1002 or 7-1-1013 or whose license was revoked within five years of the date such person was hired;

15. Any person who purchases mortgage loans from a mortgage broker or mortgage lender solely as an investment and who is not in the business of brokering, making, purchasing, or servicing mortgage loans;
16. Any natural person who makes five or fewer mortgage loans in any one calendar year. A person other than a natural person who makes five or fewer mortgage loans in any one calendar year shall not be exempt from the licensing requirements of this article; or
17. (A) A natural person otherwise required to be licensed as a mortgage lender or mortgage broker, who is under an exclusive written independent contractor agreement with any person that is a wholly owned subsidiary of a financial holding company or bank holding company, savings bank holding company, or thrift holding company, which subsidiary also meets the following requirements, subject to the review and approval of the department:
    i. The subsidiary has provided an undertaking of accountability supported by a surety bond equal to the lesser of $1 million or $50,000.00 per exempt person, to cover all of its persons exempted by this paragraph, that includes full and direct financial responsibility for the mortgage broker activities of each such exempted person, and also provides for the education of the exempt persons, the handling of consumer complaints related to the exempt persons, and the supervision of the mortgage broker activities of the exempt persons;
    ii. The subsidiary has applied for and been granted a mortgage broker or mortgage lender license, consistent with the provisions of this article and renewable annually; and
    iii. The subsidiary has paid applicable fees for this license, which license fees shall be the lesser of one-half of the sum of the cost of the individual licenses or $100,000.00.

    (B) To maintain the exemption, a natural person shall:
    i. Solicit, process, place, or negotiate a mortgage loan to be made only by the licensed subsidiary or its affiliate; and
    ii. Be at all times in compliance with the provisions and prohibitions of Code Section 7-1-1013 and the provisions and prohibitions applicable to employees under Code Section 7-1-1004.

    (C) For purposes of this paragraph, the term "financial holding company" means a financial holding company as defined in the Bank Holding Company Act of 1956, as amended.

    (D) The commissioner shall provide by rule or regulation for the implementation of this paragraph.
18. (A) An employee of a bona fide nonprofit corporation who acts as a mortgage loan originator only with respect to his or her work duties with the bona fide nonprofit corporation and who acts as a mortgage loan originator only with respect to mortgage loans with terms that are favorable to the borrower shall be exempt from obtaining a mortgage loan originator license. In order for a corporation to be considered a bona fide nonprofit corporation under this paragraph, the department shall determine, under criteria and pursuant to processes established by the department, that the nonprofit corporation:

i. Has the status of a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code of 1986;
ii. Promotes affordable housing;
iii. Conducts its activities in a manner that serves public or charitable purposes, rather than commercial purposes;
iv. Receives funding and revenue and charges fees in a manner that does not incentivize it or its employees to act other than in the best interests of its clients;
v. Compensates its employees in a manner that does not incentivize employees to act other than in the best interests of its clients;
vi. Provides or identifies for the borrower mortgage loans with terms favorable to the borrower and comparable to mortgage loans and housing assistance provided under government housing assistance programs. In order for mortgage loans to have terms that are favorable to the borrower, the department shall determine that the terms are consistent with loan origination in a public or charitable context, rather than in a commercial context; and
vii. Satisfies the exemption from licensure set forth in paragraph (13) of this subsection.

(B) The department shall periodically examine the books and activities of an organization it has previously identified as a bona fide nonprofit corporation for purposes of this paragraph in order to determine if it continues to meet the criteria for such status under subparagraph (A) of this paragraph. In conducting such an examination, the department shall have all of the powers set forth in Code Section 7-1-1009. In the event the nonprofit corporation no longer qualifies for such status, then the employee exemption from having a mortgage loan originator license shall no longer be applicable.

The above lists the type of people that are not legally required to obtain a license in order to do conduct their actives. Let's now turn to those which the law imposes a license requirement.

Requirements for MLO License [O.C.G.A. §7-1-1001.1]

To comply with the federal requirements contained in the Secure and Fair Enforcement for Mortgage Licensing Act of 2008, also known as the S.A.F.E. Mortgage Licensing Act of 2008, it is now prohibited for any person to engage in the activities of a mortgage loan originator without first obtaining and maintaining a mortgage loan originator license.

The department has the broad administrative authority to administer, interpret, and enforce the SAFE Mortgage Licensing Act of 2008, and promulgate rules and regulations implementing it. The provisions in the SAFE Act apply to the activities of retail sellers of manufactured homes to the extent determined by the United States Department of Housing and Urban Development through written guidelines, rules, regulations, or interpretive letters.

Therefore, since one must be licensed in order to conduct mortgage loan originator duties, it is no surprise that the law goes on to state the following:

a. It shall be prohibited for any person to transact business in this state directly or indirectly as a mortgage broker, a mortgage lender, or a mortgage loan originator unless such person:
    1. Is licensed or registered as such by the department utilizing the Nationwide Mortgage Licensing System and Registry;
    2. Is a person exempted from the licensing or registration requirements pursuant to Code Section 7-1-1001;

3. In the case of an employee of a mortgage broker or mortgage lender, such person has qualified to be relieved of the necessity for a license under the employee exemption in paragraph (11) of subsection (a) of Code Section 7-1-1001;
4. In the case of a mortgage loan originator, such person is supervised by a mortgage broker, mortgage lender, or exemptee on a daily basis while performing mortgage functions; is employed by and works exclusively for only one mortgage broker, mortgage lender, or exemptee; and is paid on a W-2 basis by the employing mortgage broker, mortgage lender, or exemptee, except those natural persons exempt from licensure as a mortgage broker or mortgage lender under paragraph (17) of subsection (a) of Code Section 7-1-1001. Each licensed mortgage loan originator shall register with and maintain a valid unique identifier issued by the Nationwide Mortgage Licensing System and Registry. For the purposes of implementing an orderly and efficient mortgage loan originator process, the department may establish licensing rules or regulations and interim procedures for licensing and acceptance of applications; or

b. A loan processor or underwriter who is an independent contractor shall not engage in the activities of a loan processor or underwriter unless such independent contractor loan processor or underwriter obtains and maintains a mortgage broker or mortgage lender license. Each independent contractor loan processor or underwriter licensed as a mortgage broker or mortgage lender shall have and maintain a valid unique identifier issued by the Nationwide Mortgage Licensing System and Registry.
c. It shall be prohibited for any person, as defined in Code Section 7-1-1000, to purchase, sell, or transfer one or more mortgage loans or loan applications from or to a mortgage loan originator, mortgage broker, or mortgage lender who is neither licensed nor exempt from the licensing or registration provisions of this article. Such a purchase shall not affect the obligation of the borrower under the terms of the mortgage loan. The department shall provide for distribution or availability of information regarding approved or revoked licenses.
d. Every person who directly or indirectly controls a person who violates subsection (a) or (b) of this Code section, every general partner, executive officer, joint venturer, or director of such person, and every person occupying a similar status or performing similar functions as such person violates with and to the same extent as such person, unless the person whose violation arises under this subsection sustains the burden of proof that he or she did not know and, in the exercise of reasonable care, could not have known of the existence of the facts by reason of which the original violation is alleged to exist.

As you can see, the law is very specific regarding who must be licensed and who is exempted from this requirement. It is crucial that a person understand what mortgage loan originator activities are in order to determine whether they must be licensed or registered to continue conducting certain activities or whether they are not required to be licensed or registered in order to continue doing what they are doing. If a person is caught conducting mortgage loan originator activities without a license, that person will subject to punishment by law.

Application for Licenses [O.C.G.A. §7-1-1003]

As mentioned previously, the department has authority to prescribe licenses. As such, they are responsible for reviewing applications. The law states that applications for licensure must include the following:

1. The legal name and address of the applicant and, if the applicant is a partnership, association, corporation, or other business entity, of every member, officer, and director thereof;
2. All names, including, but not limited to, website domain names (URLs), under which the applicant will conduct business in Georgia;
3. For mortgage brokers and mortgage lenders, the address of the main office or principal place of business where books and records are located and any other locations at which the applicant will engage in any business activity covered by the provisions of this article, together with the mailing address where the department shall send all correspondence, orders, or notices. Any changes in this mailing address shall be delivered in writing to the department before the change is effective;
4. For mortgage brokers and mortgage lenders, the complete name and address of the applicant's initial registered agent and registered office for service of process in Georgia. If the applicant is a Georgia corporation, this registered agent shall be the same as the agent recorded with the Secretary of State. Any changes in the registered agent or registered office shall be delivered in writing to the department and the Secretary of State, if applicable, before the change is effective. The registered agent may, but is not required to, be an officer of the applicant, and the registered office shall be a Georgia location where the registered agent may be served;
5. For mortgage brokers and mortgage lenders, the general plan and character of the business;
6. For mortgage brokers and mortgage lenders, a financial statement of the applicant;
7. For mortgage brokers and mortgage lenders, such other data, financial statements, and pertinent information as the department may require with respect to the applicant, its directors, trustees, officers, members, agents, or ultimate equitable owners of 10 percent or more of the applicant; and
8. For mortgage brokers and mortgage loan originators, evidence of satisfaction of experience or education requirements, as required by regulations of the department.

b. All applications filed under this Code section shall be filed together with:
    1. Investigation and supervision fees established by regulation;
    2. The items required by Code Section 7-1-1003.2;
    3. Other information as may be required by the department.

Physical Place of Business [O.C.G.A. §7-1-1003.1]

Generally, applicants for licensure are persons with a physical place of business in Georgia, but what happens if an applicant does not have a physical place of business in Georgia?

If the applicant for a mortgage broker license or a renewal of such license does not have a physical place of business in Georgia, a license or renewal shall only be issued if the applicant's home state does not require that in order to be licensed a mortgage broker shall have a physical place of business in such home state. In either case, an applicant shall have a registered agent and a registered office in this state.

Financial Requirements: Bond Requirements [O.C.G.A. §7-1-1003.2]

The law imposes certain financial requirements on those that want to become licensed. The law states the following:

a. Each licensed or registered mortgage broker shall provide the department with a bond. The bond for a mortgage broker shall be in the principal sum of $150,000.00 or such greater sum as the department may require as set forth by regulation based on an amount that reflects the dollar amount of loans originated, and the bond shall meet the other requirements of subsection (d) of this Code section.
b. Except as otherwise provided in subsection (d) of this Code section, the department shall not license or register any mortgage lender unless the applicant or registrant provides the department with a bond. The bond for a mortgage lender shall be in the principal sum of $250,000.00 or such greater sum as the department may require as set forth by regulation based on an amount that reflects the dollar amount of loans originated, and which bond shall meet the other requirements of subsection (d) of this Code section.
c. Each mortgage loan originator shall be covered by a surety bond of his or her sponsoring licensed or registered mortgage broker or lender. In the event that the mortgage loan originator is an employee of a licensed or registered mortgage broker or lender or under an exclusive written independent contractor agreement as described in paragraph (17) of Code Section 7-1- 1001, the surety bond of such licensed or registered mortgage broker or lender may be used in lieu of the mortgage loan originator's surety bond requirement.
d. General bond requirements:
    1. The bond requirements for mortgage loan originators, mortgage brokers, and mortgage lenders are continuous in nature and shall be maintained at all times as a condition of licensure;
    2. The corporate surety bond shall be for a term and in a form satisfactory to the department, shall be issued by a bonding company or insurance company authorized to do business in this state and approved by the department, and shall run to the State of Georgia for the benefit of any person damaged by noncompliance of a licensee with this article, the 'Georgia Residential Mortgage Act,' or with any condition of such bond. Damages under the bond shall include moneys owed to the department for fees, fines, or penalties. Such bond shall be continuously maintained thereafter in full force. Such bond shall be conditioned upon the applicant or the licensee conducting his or her licensed business in conformity with this article and all applicable laws;
    3. When an action is commenced on a licensee's bond, the department may require the filing of a new bond; and
    4. Immediately upon recovery of any action on the bond, the licensee shall file a new bond.
e. Any person including the department who may be damaged by noncompliance of a licensee with any condition of a bond or this article, the 'Georgia Residential Mortgage Act,' may proceed on such bond against the principal or surety thereon, or both, to recover damages.

Application for Registration [O.C.G.A. §7-1-1003.3]

According to law, any application to register as a mortgage lender or broker must be made annually in writing, under oath, and on a form provided by the department. The application is subject to requirements specified by rules and regulations of the department.

Therefore, if you are already registered, you must apply to be registered yearly.

This process is different for those applying for licensure as mortgage loan originators, mortgage brokers, and mortgage lenders.

We will discuss the application and renewal process for mortgage loan originators, brokers, and lenders later. We will next review the extent of the authority given to the department by law with regards to licensing.

<u>Automated Licensing System for MLOs, Mortgage Brokers and Mortgage Lenders</u>

[O.C.G.A. §7-1-1003.5]

The law states that the department is authorized to do all of the following:

1. Participate in a Nation-wide Multistate Licensing System and Registry established to facilitate the sharing of information and standardization of the licensing and application processes for mortgage loan originators, mortgage brokers, and mortgage lenders by electronic or other means;
2. Enter into operating agreements, information sharing agreements, interstate cooperative agreements, and other contracts necessary for the department's participation in the Nation-wide Multistate Licensing System and Registry;
3. Request that the Nation-wide Multistate Licensing System and Registry adopts an appropriate privacy, data security, and security breach notification policy that is in full compliance with existing state and federal law;
4. Disclose or cause to be disclosed without liability via the Nationwide Mortgage Licensing System and Registry applicant and licensee information, including, but not limited to, violations of this article and enforcement actions, via the Nation-wide Multistate Licensing System and Registry to facilitate regulatory oversight of mortgage loan originators, mortgage brokers, and mortgage lenders across state jurisdictional lines;
5. Establish and adopt, by rule or regulation, requirements for participation by applicants and licensees in the Nation-wide Multistate Licensing System and Registry upon the department's determination that each new or amended requirement is consistent with both the public interest and the purposes of this article; and
6. Pay all fees received from licensees and applicants related to applications, licenses, and renewals to the Office of Treasury and Fiscal Services; provided, however, that the department may net such fees to recover the cost of participation in the Nationwide Mortgage Licensing System and Registry; and

As you can see, the department has a lot of power when it comes to the licensing of mortgage loan originators, brokers, and lenders. In fact, the law also makes clear how much power the department has by stating that regardless of the department's participation in NMLS&R, it retains full and exclusive determinations whether to grant, renew, suspend, or revoke licenses issued to mortgage loan originators, mortgage brokers, and mortgage lenders. Nothing in this section of Georgia law can reduce this authority.

<u>Investigations: Education and Other Requirements</u> [O.C.G.A. §7-1-1004]

The law also specifically provides the department with the authority to establish any requirements it deems necessary for the application for license or registration:

a. Upon receipt of an application for license or registration, the department shall conduct such investigation as it deems necessary to determine that the mortgage broker and mortgage lender applicant and the individuals who direct the affairs or establish policy for the mortgage broker and mortgage lender applicant, including the officers, directors, or the equivalent, are of good character and ethical reputation; that the mortgage broker and mortgage lender applicant is not disqualified for licensure as a result of adverse administrative civil or criminal findings in any jurisdiction; that the mortgage broker and mortgage lender applicant and such persons meet the requirements of subsection (h) of this Code section; that the mortgage broker and mortgage lender applicant and such persons demonstrate reasonable financial responsibility; that the mortgage broker and mortgage lender applicant has reasonable policies and procedures to receive and process customer grievances and inquiries promptly and fairly; and that the mortgage broker and mortgage lender applicant has and maintains a registered agent for service in this state.

b. The department shall not license or register any mortgage broker and mortgage lender applicant unless it is satisfied that the mortgage broker and mortgage lender applicant may be expected to operate its mortgage lending or brokerage activities in compliance with the laws of this state and in a manner which protects the contractual and property rights of the citizens of this state.
c. The department may establish by rule or regulation minimum education or experience requirements for an applicant for a mortgage broker license or renewal of such a license.
d. To this end, the law provides that the department must do whatever is necessary to determine that the applicant has completed all requirements for licensure. Once an application for a mortgage loan originator license is submitted, the department must make sure that the applicant:
   1. Has never had a mortgage loan originator license revoked in any governmental jurisdiction, except that a subsequent formal vacation of such revocation shall not be deemed a revocation;
   2. Has not been convicted of, or pled guilty or nolo contendere to, a felony in a domestic, foreign, or military court; provided, however, that any pardon of a conviction shall not be a conviction for purposes of this subsection;
   3. Has demonstrated financial responsibility, character, and general fitness such as to command the confidence of the community and to warrant a determination that the mortgage loan originator will operate honestly, fairly, and efficiently within the purposes of this article;
   4. Has completed the pre-licensing education requirement described in subsection (e) of this Code section;
   5. Has passed a written test that meets the test requirement described in subsection (f) of this Code section; and
e. (1) An individual shall complete at least 20 hours of pre-licensing education courses reviewed and approved by the Nationwide Mortgage Licensing System and Registry based upon reasonable standards. Review and approval of a pre-licensing education course shall include review and approval of the course provider. The 20 hours of pre-licensing education shall include at least:
      A. Three hours of federal law and regulations;
      B. Three hours of ethics, which shall include instruction on fraud, consumer protection, and fair lending issues; and
      C. Two hours of training related to lending standards for the nontraditional mortgage product marketplace.
   2. Nothing in this subsection shall preclude any pre-licensing education course, as approved by the Nationwide Mortgage Licensing System and Registry, that is provided by the employer of the mortgage loan originator applicant or an entity which is affiliated with the applicant by an agency contract, or any subsidiary or affiliate of such employer or entity.

3. Pre-licensing education may be offered either in a classroom, online, or by any other means approved by the Nationwide Mortgage Licensing System and Registry.
4. The pre-licensing education requirements approved by the Nationwide Mortgage Licensing System and Registry in paragraph (1) of this Code section for any state shall be accepted as credit towards completion of pre-licensing education requirements in Georgia.
5. A person previously licensed under this article subsequent to January 1, 2010, applying to be licensed again shall prove that they have completed all of the continuing education requirements for the year in which the license was last held.
6. The department is authorized to enact rules and regulations related to the expiration of pre-licensing education

f.

1. In order to meet the written test requirement referred to in subsection (d) of this Code section for mortgage loan originators, an individual shall pass, in accordance with the standards established under this subsection, a qualified written test developed by the Nationwide Mortgage Licensing System and Registry and administered by a test provider approved by the Nationwide Mortgage Licensing System and Registry based upon reasonable standards.
2. A written test shall not be treated as a qualified written test for purposes of this subsection unless the test adequately measures the applicant's knowledge and comprehension in appropriate subject areas, including:
    - A. Ethics;
    - B. Federal law and regulation pertaining to mortgage origination;
    - C. State law and regulation pertaining to mortgage origination; and
    - D. Federal and state law and regulation, including instruction on fraud, consumer protection, the nontraditional mortgage marketplace, and fair lending issues.
3. Nothing in this subsection shall prohibit a test provider approved by the Nationwide Mortgage Licensing System and Registry from providing a test at the location of the employer of the applicant or the location of any subsidiary or affiliate of the employer of the applicant or the location of any entity with which the applicant holds an exclusive arrangement to conduct the business of a mortgage loan originator.
4. (A) An individual shall not be considered to have passed a qualified written test unless the individual achieves a test score of not less than 75 percent correct answers to questions.
    - B. An individual may retake a test three consecutive times with each consecutive taking occurring at least 30 days after the preceding test.
    - C. After failing three consecutive tests, an individual shall wait at least six months before taking the test again.
    - D. A licensed mortgage loan originator who fails to maintain a valid license for a period of five years or longer shall retake the test, not taking into account any time during which such individual is a registered mortgage loan originator.

Uniform State Test (UST)

- The Uniform State Test (UST)
    - This is a section within the National Test
    - Georgia has a UST state test with only one exam for licensing

- Will include 25 questions
  - National Test with UST will contain 125 questions total
  - Grade is a total of all questions
- This material will test an applicant's knowledge of state-related content and CSBS/AARMR Model State Law (MSL)
- Replaces the state-specific test section for those states choosing to implement it
- A person who passes the National Test with UST content or the Stand-alone UST will have satisfied requirements for a license in that state

Points "d," "e," and "f"" list the requirements necessary in order to obtain a mortgage loan originator license. If the department finds that any of these requirements have not been met, then the department reserves the right to deny the application for licensure.

This section of the law also provides the requirements necessary to renew a license after having obtained one.

g. (1) In order to meet the annual continuing education requirements referred to in paragraph (2) of subsection (e) of Code Section 7-1-1005, a licensed mortgage loan originator shall complete at least eight hours of education approved in accordance with paragraph (2) of this subsection which shall include at least:
   - A. Three hours of federal law and regulations;
   - B. Two hours of ethics, which shall include instruction on fraud, consumer protection, and fair lending issues; and
   - C. Two hours of training related to lending standards for the nontraditional mortgage product marketplace.

   2. For purposes of paragraph (1) of this subsection, continuing education courses shall be reviewed and approved by the Nation-wide Multistate Licensing System and Registry based upon reasonable standards. Review and approval of a continuing education course shall include review and approval of the course provider.
   3. Nothing in this subsection shall preclude any education course from approval by the Nation-wide Multistate Licensing System and Registry that is provided by the employer of the mortgage loan originator or any entity which is affiliated with the mortgage loan originator by an agency contact, or any subsidiary or affiliate of such employer or entity.
   4. Continuing education may be offered either in a classroom, online, or by any other means approved by the Nationwide Mortgage Licensing System and Registry.
   5. A licensed mortgage loan originator, except for as provided for in paragraph (9) of this subsection and subsection (f) of Code Section 7-1-1005, shall only receive credit for a continuing education course in the year in which the course is taken and shall not take the same approved course in the same or successive years to meet the annual requirements for continuing education.
   6. A licensed mortgage loan originator who is an approved instructor of an approved continuing education course may receive credit for the licensed mortgage loan originator's own annual continuing education requirement at the rate of two hours of credit for every one hour taught.
   7. An individual having successfully completed the education requirements approved by the Nationwide Mortgage Licensing System and Registry in paragraph (1) of this subsection for any state shall be accepted as credit towards completion of continuing education requirements in Georgia.

8. A licensed mortgage loan originator who subsequently becomes unlicensed shall complete the continuing education requirements for the last year in which the license was held prior to issuance of a new or renewed license.
9. An individual meeting the requirements of subsection (e) of Code Section 7-1-1005 may make up any deficiency in continuing education as established by rule or regulation of the department.

h. The department shall not issue or may revoke a license or registration if it finds that the mortgage loan originator, mortgage broker, or mortgage lender applicant or licensee, or any person who is a director, officer, partner, agent, employee, or ultimate equitable owner of 10 percent or more of the mortgage broker or mortgage lender applicant, registrant, or licensee or any individual who directs the affairs or establishes policy for the mortgage broker or mortgage lender applicant, registrant, or licensee, has been convicted of a felony in any jurisdiction or of a crime which, if committed within this state, would constitute a felony under the laws of this state.

i. Fees for background checks that the department administers shall be sent to the department by applicants and licensees together with the fingerprints. Mortgage broker and mortgage lender applicants, licensees, and registrants shall have the primary responsibility for obtaining background checks of covered employees which are defined as employees who work in this state and also have the authority to enter, delete, or verify any information on any mortgage loan application form or document. The department shall, however, retain the right to obtain conviction data on covered employees.

j. In connection with an application for licensing with respect to any mortgage loan originator applicant, mortgage broker, or lender applicant, at the direction of the department, the applicant shall at a minimum, furnish to the Nationwide Mortgage Licensing System and Registry information concerning the applicant's identity, including:
    1. Fingerprints for submission to the Federal Bureau of Investigation, and any governmental agency or entity authorized to receive such information for a state, national, and international criminal history background check; and
    2. Personal history and experience in a form prescribed by the Nationwide Mortgage Licensing System and Registry, including the submission of authorization for the Nationwide Mortgage Licensing System and Registry and the department to obtain;
        A. An independent credit report obtained from a consumer reporting agency described in section 603(p) of the Fair Credit Reporting Act, 15 U.S.C. Section 1681a(f); and
        B. Information related to any administrative, civil, or criminal findings by any governmental jurisdiction.
    3. For the purposes set forth in this subsection and in order to reduce the points of contact which the Federal Bureau of Investigation may have to maintain for purposes of such section, the department may use the Nationwide Multistate Licensing System and Registry as a channeling agent for requesting information from and distributing information to the Department of Justice or any governmental agency; and
    4. For the purposes of this subsection and in order to reduce the points of contact which the department may have to maintain for purposes of such subsection, the department may use the Nationwide Multistate Licensing System and Registry as a channeling agent for requesting and distributing information to and from any source so directed by the department.

k. Every mortgage broker and mortgage lender licensee, registrant, and applicant shall be authorized and required to obtain background checks on covered employees. Such background checks shall be handled by the Georgia Crime Information Center pursuant to Code Section 35-3-34 and the rules and regulations of the Georgia Crime Information Center. Licensees, registrants, and applicants shall be responsible for any applicable fees charged by the center. A background check shall be initiated for a person in the employ of a licensee, registrant, or applicant within ten days of the date of initial hire and be completed with satisfactory results within the first 90 days of employment. This provision shall not apply to directors, officers, partners, agents, or ultimate equitable owners of 10 percent or more or to persons who direct the company's affairs or establish policy, whose background shall have been investigated through the department before taking office, beginning employment, or securing ownership. Upon receipt of information from the Georgia Crime Information Center that is incomplete or that indicates an employee has a criminal record in any state other than Georgia, the employer shall submit to the department two complete sets of fingerprints of such person, together with the applicable fees and any other required information. The department shall submit such fingerprints as provided in subsection (i) of this Code section.

l. Upon receipt of fingerprints, fees, and other required information, the Georgia Crime Information Center shall promptly transmit one set of fingerprints to the Federal Bureau of Investigation for a search of bureau records and an appropriate report and shall retain the other set and promptly conduct a search of its own records and records to which it has access. The Georgia Crime Information Center shall notify the department in writing of any derogatory finding, including, but not limited to, any conviction data regarding the fingerprint records check, or if there is no such finding. All conviction data received by the department or by the applicant, registrant, or licensee shall be used by the party requesting such data for the exclusive purpose of carrying out the responsibilities of this article, shall not be a public record, shall be privileged, and shall not be disclosed to any other person or agency except to any person or agency which otherwise has a legal right to inspect the file. The department shall be entitled to review any applicant's, registrant's, or licensee's files to determine whether the required background checks have been run and whether all covered employees are qualified. The department shall be authorized to discuss the status of employee background checks with licensees. All such records shall be maintained by the department and the applicant or licensee or registrant pursuant to laws regarding such records and the rules and regulations of the Federal Bureau of Investigation and the Georgia Crime Information Center, as applicable. As used in this subsection, "conviction data" means a record of a finding, verdict, or plea of guilty or plea of nolo contendere with regard to any crime, regardless of whether an appeal of the conviction has been sought, subject to the conditions set forth in subsection (h) of this Code section. Violation of this Code section may subject a licensee or registrant to the revocation of its license or registration.
m. In connection with an application for licensing or registration under this Code section, the department may use the Nation-wide Multistate Licensing System and Registry, when such service is available, as a channeling agent for the submission of fingerprints to the Federal Bureau of Investigation and any governmental agency or entity authorized to receive such information for a state, national, and international criminal history background check. The department is authorized to set forth rules and regulations in order to implement the provisions of this subsection.
n. The department may deny or revoke a license or registration or otherwise restrict a license or registration if it finds that the mortgage broker or mortgage lender applicant or any person who is a director, officer, partner, or ultimate equitable owner of 10 percent or more or person who directs the company's affairs or who establishes policy of the applicant has been in one or more of these roles as a mortgage lender, broker, or registrant whose license or registration has been denied, revoked, or suspended within five years of the date of the application.
o. The department shall not issue a license or registration to and may revoke a license or registration from a mortgage broker or mortgage lender applicant, licensee, or registrant if such person:
    1. Has been the recipient of a final cease and desist order issued within the preceding five

years if such order was based on a violation of subsection (h) of this Code section or Code Section 7-1-1002 or 7-1-1013;

2. Employs any other person against whom a final cease and desist order has been issued within the preceding five years if such order was based on a violation of subsection (h) of this Code section or Code Section 7-1-1002 or 7-1-1013; or
3. Has had his or her license revoked within five years of the date such person was hired or employs any other person who has had his or her license revoked within five years of the date such person was hired.

p. Each mortgage broker and mortgage lender applicant, licensee, and registrant shall, before hiring an employee, examine the department's public records to determine that such employee is not subject to the type of cease and desist order described of this Code section.

q. Within 90 days after receipt of a completed application and payment of licensing fees prescribed by this article, the department shall either grant or deny the request for license or registration.

r. A person shall not be indemnified for any act covered by this article or for any fine or penalty incurred pursuant to this article as a result of any violation of the law or regulations contained in this article, due to the legal form, corporate structure, or choice of organization of such person, including, but not limited to, a limited liability company.

So there you have it, folks! What we just went over spells out the specific requirements to obtain a license and retain one as a mortgage loan originator, mortgage broker, or mortgage lender. For the purposes of doing so, the department is granted full authority in the decision making of granting, renewing, or revoking licensure.

Of course, the Nationwide Mortgage Licensing System and Registry is in place for a reason and the law does place responsibilities on borkers and lenders to provide certain thing to the NMLS&R. For example, the law requires that Each mortgage broker and mortgage lender shall submit to the Nationwide Mortgage Licensing System and Registry reports of condition, which shall be in such form and shall contain such information as the department and the Nationwide Mortgage Licensing System and Registry may require. **[O.C.G.A. §7-1-1004.1]**

The law also places responsibility on the department to establish a process whereby licensees may challenge information that is entered in the Nationwide Mortgage Licensing System and Registry by the department. **[O.C.G.A. §7-1-1004.2]**

For the purposes of ensuring that accountability is met and in order to make the NMLS&R function as it is intended, it is important that the unique identifier of any person originating a residential mortgage loan shall be clearly shown on all residential mortgage loan application forms, solicitations, or advertisements, including business cards, websites, and any other documents as established by rule, regulation, or order of the department. **[O.C.G.A. §7-1-1004.3]**

We already discussed some of the requirements purported by law for the renewal of a license or registration. However, the law does pose additional requirements regarding the timeframe for renewal. We will review this next.

<u>Renewal of Licenses and Registrations</u> [O.C.G.A. 7-1-1005]

a. All licenses and registrations issued pursuant to this article shall expire on December 31 of each year, and application for renewal shall be made annually on or before December

1 of each year.

b. Any licensee or registrant making proper application on or before December 1 for the renewal of a license or registration for the following calendar year shall be permitted to continue to operate pending final approval or disapproval of the application if the application for the license or registration is not acted upon prior to January 1. For purposes of this subsection, a 'proper application' shall include a requirement that all documentation requesting a renewal has been completed, the requisite continuing education has been successfully obtained, and payment has been made of all outstanding fines and applicable fees required by this article.
c. No investigation fee shall be payable in connection with the renewal application, but an annual license or registration fee established by regulation of the department to defray the cost of supervision shall be paid with each renewal application, which fee shall not be refunded.
d. Any person holding a license or registration pursuant to this article who fails to file a proper application for a license or registration renewal for the following license year, including the proper fee accompanying the application, on or before December 1 and who files an application after December 1 may be required to pay, in addition to the license or registration fees, a fine in an amount to be established by regulations promulgated by the department.
e. The minimum standards for license renewal for mortgage loan originators shall include:
    1. The mortgage loan originator continues to meet the minimum standards for license issuance;
    2. The mortgage loan originator has satisfied the annual continuing education requirements; and
    3. The mortgage loan originator has paid all required fees for renewal of the license;
    4. The mortgage loan originator is in compliance with any and all written orders issued by the department.
f. The department may adopt procedures for the reinstatement of expired licenses consistent with the standards established by the Nationwide Mortgage Licensing System and Registry.

We now know the necessary requirements for license renewal. Let's move on to discussing some of the responsibilities licensees have once they have obtained their license.

Contents of License; Posting of License; etc. [O.C.G.A. §7-1-1006]

All licenses must have the name of the person who possesses the license. Once obtained, the licensee must do the following:

a. A licensee shall post a copy of such license in a conspicuous place in each place of business of the licensee.
b. A license shall not be transferred or assigned.
c. No licensee shall transact business under any name or names other than those designated in the records of the department.
d. For mortgage brokers and mortgage lenders, each licensee shall notify the department in writing of any change in the address of the principal place of business or of any additional location of business in Georgia, any change in registered agent or registered office, any change of executive officer, contact person for consumer complaints, or ultimate equitable owner of 10 percent or more of any corporation or other entity licensed under this article, or of any material change in the licensee's financial statement. Notice of changes shall be received by the department no later than 30 business days after the change is effective.
e. No mortgage broker or mortgage lender shall open a new additional office in Georgia without

prior approval of the department. Applications for such additional office shall be made in writing on a form prescribed by the department and shall be accompanied by payment of a $350.00 nonrefundable application fee. The application shall be approved unless the department finds that the applicant has not conducted business under this article efficiently, fairly, in the public interest, and in accordance with law. The application shall be deemed approved if notice to the contrary has not been mailed by the department to the applicant within 45 days of the date the application is received by the department.

f. All branch managers in Georgia shall be approved by the department. A mortgage broker or mortgage lender may place a new branch manager subject to the department's approval but shall file for approval within 15 days of the placement and shall remove the person immediately should the department deny approval.

<u>Licensee To Give Notice of Certain Actions</u> [O.C.G.A. §7-1-1007]

Additionally, the law requires licensees to provide notice to the department of certain actions For example, a licensee must give the department notice to via registered or certified mail or statutory overnight delivery of any action which may be brought against it by any creditor or borrower where such action is brought under this article, involves a claim against the bond filed with the department for the purposes of compliance with Code Section 7-1-1003.2 or 7-1-1004, or involves a claim for damages in excess of $25,000.00 for a mortgage broker or mortgage loan originator and $250,000.00 for a lender and of any judgment which may be entered against it by any creditor or any borrower or prospective borrower, with details sufficient to identify the action or judgment, within 30 days after the commencement of any such action or the entry of any such judgment.

The same is the case for a corporate surety. A corporate surety shall, within ten days after it pays any claim to any claimant, give notice to the department by registered or certified mail or statutory overnight delivery of such payment with details sufficient to identify the claimant and the claim or judgment so paid. Whenever the principal sum of such bond is reduced by one or more recoveries or payments thereon, the mortgage loan originator, mortgage broker, or mortgage lender shall furnish a new or additional bond so that the total or aggregate principal sum of such bond or bonds shall equal the sum required under Code Section 7-1-1003.2 or 7-1-1004 or shall furnish an endorsement duly executed by the corporate surety reinstating the bond to the required principal sum thereof.

Also, if a bond filed must be canceled by either the mortgage loan originator, mortgage broker, or mortgage lender or the corporate surety, the department must be notified before doing so. The department must be notified by registered or certified mail, statutory overnight delivery with return receipt requested, or electronically through the Nationwide Multistate Licensing System and Registry, the cancellation to be effective not less than 30 days after receipt by the department of such notice and only with respect to any breach of condition occurring after the effective date of such cancellation.

Additionally, the law states that:

a. A licensee or registrant shall, within ten days after knowledge of the event, report in writing to the department:
    1. Any knowledge or discovery of an act prohibited by Code Section 7-1-1013;
    2. The discharge of any employee for dishonest or fraudulent acts; and

3. Any administrative, civil, or criminal action initiated against the licensee, registrant, or any of its control persons by any government entity.

Any person reporting such an event shall be protected from civil liability as provided in Code Section 7-1-1009.

<u>Record Maintenance</u> [O.C.G.A. §7-1-1009]

As you know, there are certain record keeping requirements for licensees. This section of the law states the following regarding record maintenance:

a. Mortgage brokers and mortgage lenders required to be licensed or registered under this article shall maintain at their offices or such other location as the department shall permit such books, accounts, and records as the department may reasonably require in order to determine whether such mortgage brokers and mortgage lenders are complying with the provisions of this article and rules and regulations adopted in furtherance thereof. Such books, accounts, and records shall be maintained separately and distinctly from any other personal or unrelated business matters in which the mortgage brokers and mortgage lenders are involved.
b. The department may, by its designated officers and employees, as often as it deems necessary, but at least once every 24 months, investigate and examine the affairs, business, premises, and records of any mortgage broker or mortgage lender required to be licensed or registered under this article insofar as such affairs, business, premises, and records pertain to any business for which a license or registration is required by this article. Notwithstanding the provisions of this subsection, the department has the discretion to examine a mortgage broker or mortgage lender less frequently, provided that its record of complaints, comments, or other information demonstrates that mortgage broker's or mortgage lender's ability to meet the standards of Code Sections 7-1-1003, 7-1-1003.2, and 7-1-1004. In the case of registrants, the department shall not be required to conduct such examinations if it determines that the registrant has been adequately examined by another bank regulatory agency. In order to avoid unnecessary duplication of examinations, the department may accept examination reports performed and produced by other state or federal agencies, unless the department determines that the examinations are not available or do not provide information necessary to fulfill the responsibilities of the department under this article.
c. In addition to any authority allowed under this article, the department shall be authorized to conduct investigations and examinations of mortgage loan originators as follows:
    1. For purposes of initial licensing, license renewal, license suspension, license conditioning, license revocation or termination, or general or specific inquiry or investigation to determine compliance with this article, the department shall have the authority to access, receive, and use any books, accounts, records, files, documents, information, or evidence, including, but not limited to:
        A. Criminal, civil, and administrative history information, including nonconviction data;
        B. Personal history and experience information, including independent credit reports obtained from a consumer reporting agency described in section 603(p) of the Fair Credit Reporting Act, 15 U.S.C. Section 1681a(f); and
        C. Any other documents, information, or evidence the department deems relevant to the inquiry or investigation regardless of the location, possession, control, or custody of such documents, information, or evidence;
    2. For the purposes of investigating violations or complaints, or for the purposes of examination, the department may review, investigate, or examine any mortgage loan originator licensee, individual, or person subject to this article as often as necessary in

order to carry out the purposes of this article. The department may direct, subpoena, or order the attendance of and examine under oath all persons whose testimony may be required about the loans or the business or subject matter of any such examination or investigation and may direct, subpoena, or order such person to produce books, accounts, records, files, and any other documents the department deems relevant to the inquiry;

3. Each mortgage loan originator licensee, individual, or person subject to this article shall make available to the department upon request the books and records relating to the activities of a mortgage loan originator;
4. Each mortgage loan originator subject to this article shall make or compile reports or prepare other information as directed by the commissioner in order to carry out the purposes of this subsection, including, but not limited to:
    - A. Accounting compilations;
    - B. Information lists and data concerning loan transactions in a format prescribed by the department; or
    - C. Use, hire, contract, or employ public or privately available analytical systems, methods, or software to examine or investigate a mortgage loan originator;
5. In making any examination or investigation authorized by this article, the department may control access to any documents and records of the licensee or person under investigation. In order to carry out the purposes of this Code section, the department may:
    - A. Enter into agreements or relationships with other government officials or regulatory associations in order to improve efficiencies and reduce regulatory burden by sharing resources, standardized or uniform methods or procedures, and documents, records, information, or evidence obtained under this Code section;
    - B. Accept and rely on examination or investigation reports made by other government officials, within or without this state; and
    - C. Accept audit reports made by an independent certified public accountant for the licensee, individual, or person subject to this article in the course of that part of the examination covering the same general subject matter as the audit and may incorporate the audit report in the report of examination, report of investigation, or other writing of the department;
6. The authority to investigate provided for in this subsection shall remain in effect whether such licensee, individual, or person subject to this article acts or claims to act under any licensing or registration law of this state or claims to act without such authority; and
7. No mortgage loan originator licensee, individual, or person subject to investigation or examination under this article shall knowingly withhold, abstract, remove, mutilate, destroy, or secrete any books, records, computer records, or other information.

Annual Financial Statements [O.C.G.A. §7-1-1010]

In addition to having to keep certain records in case of investigation, certain records must be created and kept for delivery to the department.

For example:

a. If a mortgage broker is a United States Department of Housing and Urban Development loan correspondent, such broker shall also submit to the department the audit that is required for the United States Department of Housing and Urban Development. The department may require the mortgage broker to have made an audit of the books and affairs of the licensed or registered business and submit to the department an audited financial statement if the department finds that such an audit is necessary to determine whether the mortgage broker is complying with the provisions of this article and the rules and regulations adopted in furtherance of this article.

b. Each mortgage lender licensed or registered under this article shall at least once each year have made an audit of the books and affairs of the licensed or registered business and submit to the department at renewal an audited financial statement, except that a mortgage lender licensed or registered under this article which is a subsidiary shall comply with this provision by annually providing a consolidated audited financial statement of its parent company and a financial statement, which may be unaudited, of the licensee or registrant which is prepared in

accordance with generally accepted accounting principles. A lender who utilizes a bond in lieu of an audit need not supply such audit, unless specially required by the department. An audit shall be less than 15 months old to be acceptable. The department may by regulation establish additional minimum standards for audits and reports under this Code section.

Annual Fees [O.C.G.A. §7-1-1011]

As with everything, obtaining, retaining, and using a license does come with certain financial obligations.

The law enables the department to prescribe annual fees to be paid by licensees and registrants, which fees shall be set at levels necessary to defray costs and expenses incurred by the state in providing the examinations and supervision required by this article and its federally mandated participation in the Nationwide Mortgage Licensing System and Registry.

The law also imposes certain fees to the borrower instead of the mortgage loan originator, broker, or lender:

The law imposes a fee on the borrower during the closing of every mortgage loan subject to regulation under this article which, as defined in Code Section 7-1-1000, includes all mortgage loans, whether or not closed by a mortgage broker or mortgage lender licensee or registrant, a fee of
$10.00. The fee shall be paid by the borrower to the collecting agent at the time of closing of the mortgage loan transaction. The collecting agent shall remit the fee to the department at the time and in the manner specified by regulation of the department. Revenue collected by the department pursuant to this subsection shall be deposited in the general fund of the state.

- As used in this subsection, the term "collecting agent" means the person listed as the secured party on a security deed or other loan document that establishes a lien on the residential real property taken as collateral at the time of the closing of the mortgage loan transaction.
- The fee mentioned above included in the closing of a loan is meant to be a debt from the borrower to the collecting agent until such assessment is paid and shall be recoverable at law in the same manner as authorized for the recovery of other debts. Any collecting agent who neglects, fails, or refuses to collect the fee imposed by this subsection shall be liable for the payment of the fee.

Disclosure Requirements [O.C.G.A. §7-1-1014]

Aside from other rules, regulations, and policies that the department may promulgate to effectuate the purpose of this article, the department can also promulgate regulations governing the disclosures that must be provided for applicants for mortgage loans, including the following requirements:

1. Any person required to be licensed or registered under this article shall provide to each applicant for a mortgage loan prior to accepting an application fee or any third-party fee such as a property appraisal fee, credit report fee, or any other similar fee a disclosure of the fees payable and the conditions under which such fees may be refundable;
2. Any mortgage lender required to be licensed or registered under this article shall make available to each applicant for a mortgage loan at or before the time a commitment to make a mortgage loan is given a written disclosure of the fees to be paid in connection with the commitment and the loan, or the manner in which such fees shall be determined and the conditions under which such fees may be refundable; and
3. Any mortgage lender required to be licensed or registered under this article shall disclose to each borrower of a mortgage loan that failure to meet every condition of the mortgage loan may result in the loss of the borrower's property through foreclosure. The borrower shall be required to sign the disclosure at or before the time of the closing of the mortgage loan.

The department may prescribe standards regarding the accuracy of required disclosures and may provide for applicable administrative or civil penalties or fines for failure to provide the disclosures or to meet the prescribed standards.

Regulations Relative to Advertising [O.C.G.A. §7-1-1016]

There are also specific provisions regarding advertising that the department has the authority to create and enforce. The department shall prescribe regulations governing the advertising of mortgage loans, including, without limitation, the following requirements:

1. (A) Advertisements for loans regulated under this article shall not be false, misleading, or deceptive. No person whose activities are regulated under this article shall advertise in any manner so as to indicate or imply that its interest rates or charges for loans are in any way recommended,' 'approved,' 'set,' or 'established' by the state or this article.
   B. An advertisement shall not include an individual's loan number, loan amount, or other publicly available information unless it is clearly and conspicuously stated in boldface type at the beginning of the advertisement that the person disseminating it is not authorized by, in sponsorship with, or otherwise affiliated with the individual's lender, which shall be identified by name. Such an advertisement shall also state that the loan information contained therein was not provided by the recipient's lender;
2. All advertisements, including websites, disseminated by a licensee or a registrant in this state by any means shall contain the name, license number, Nationwide Mortgage Licensing System and Registry unique identifier, and an office address of such licensee or registrant, which shall conform to a name and address on record with the department; and
3. No mortgage broker or mortgage lender licensee shall advertise its services in Georgia in any media disseminated in this state, whether print or electronic, without the words 'Georgia Residential Mortgage Licensee' or, for those advertisers licensed in more than one state, a listing of Georgia as a state in which the advertiser is licensed.

Advertising Requirements

[Georgia Department of Banking and Finance-Mortgage Division Rules 80-11-1-.02]

There is a lot of advertising involved in the lending industry, therefore making it crucial for proper consumer protection laws to be available and easily enforced. These provisions exist on the federal level. With regards to provisions in the state of Georgia, the following provisions are in place in an effort to protect the consumer:

a. Advertisements for mortgage loans shall not be false, misleading, or deceptive.
b. Advertisements for mortgage loans shall not indicate in any manner that the interest rates or charges for loans are in any way recommended, approved, set or established by the state or by any law of the state.
c. All solicitations or advertisements, including business cards and websites, for mortgage loans disseminated in this state by persons required to be licensed or registered under O.C.G.A. Title 7, Chapter 1, Article 13 shall contain the name, license number, valid unique Nationwide Multistate Licensing System and Registry (NMLSR) identifier, and an office address of the licensee or registrant advertising the mortgage loan, which name, address, and license number shall conform with the name, license number, valid unique NMLSR identifier and office address on record with the Department of Banking and Finance.
d. All advertisements disseminated in this state by persons required to be licensed under O.C.G.A. Title 7, Chapter 1, Article 13 in any media, whether print or electronic, shall contain the words "Georgia Residential Mortgage Licensee" or, if an entity is licensed in more than one state, the licensee's advertisement may list Georgia as a state in which the licensee is licensed.
e. All advertisements for mortgage loans shall comply with all applicable federal and state laws.
f. For purposes of this Rule, "advertisement" means material used or intended to be used to induce the public to apply for a mortgage loan. Such term shall include any printed or published material, audio or visual material, website, or descriptive literature concerning a mortgage loan subject to regulation under O.C.G.A. Title 7, Chapter 1, Article 13 whether disseminated by direct mail, newspaper, magazine, radio or television broadcast, electronic, billboard or similar display. The term advertisement shall not include promotional materials containing fifteen words or fewer relating to the mortgage business of the entity which material does not contain references to a specific rate or product, such as balloons, hats, pencils or pens, and calendars.
g. Every mortgage broker or mortgage lender required to be licensed or registered shall maintain a record of samples of its advertisements (including commercial scripts of all radio and television broadcasts) for examination by the Department of Banking and Finance.
h. An advertisement shall not include an individual’s loan number, loan amount, or other publicly available information unless it is clearly and conspicuously stated in bold-faced type at the beginning of the advertisement that the person disseminating it is not authorized by, acting on behalf of, or otherwise affiliated with the individual’s lender, which shall be identified by name. Such an advertisement shall also state that the loan information contained therein was not provided by the recipient’s lender.

