February 28, 2011

The Honorable Ben S. Bernanke
Chairman
Board of Governors of the Federal
Reserve System
20th Street and Constitution Avenue N.W.
Washington, D.C. 20551

Ms. Sandra F. Braunstein
Director, Consumer and Community Affairs
Division
Board of Governors of the Federal Reserve
System
1709 New York Avenue N.W.
Room 8201
Washington, D.C. 20006

Re: Final Rule Regarding Loan Originator Compensation

Dear Chairman Bernanke and Director Braunstein:

The undersigned trade associations are writing because of our concern about interpretations that the Board of Governors of the Federal Reserve System (the Board) may adopt with respect to the terms "affiliate" and "third party charges" used in the Board's final rule regarding loan originator compensation practices (75 Fed. Reg. 58,509 (Sept. 24, 2010)), which is scheduled to take effect on April 1, 2011. We believe these interpretations not only would be unnecessary but would cause irreparable injury to the various members of our associations, to competition in the marketplace, and to consumers if they are adopted. Accordingly, we seek your review of the consequences of these interpretations and your consideration of clarifications to the rule to prevent them.

The Final Rule and the Staff's Problematic Interpretation

As you know, the Board's loan officer compensation rule contains two major prohibitions. First, it prohibits payment to originators based on loan terms or conditions or proxies for them. Second, it prohibits so-called dual compensation of loan originators by consumers and other parties, including those who often pay compensation (or at least ensure that brokers obtain some form of compensation) for brokering loans to them.

The potential problem as we see it originates with the Board's definition of "affiliate" *as a single person* for the purposes of the loan originator compensation rule set forth in Regulation Z (12 C.F.R. Part 226.36(d)). In its rule, the Board has indicated that its interpretation of "affiliate" is "necessary to prevent circumvention of the final rule." The Board provides the following illustration:

> [T]he rule would be circumvented, for example, if a parent company that has two mortgage lending subsidiaries could arrange to pay a loan originator greater compensation on higher rate loans offered by subsidiary A than the compensation it would pay the same originator for a lower rate loan made by subsidiary "B". To address this issue, the Board treats such subsidiaries of the parent company as a single person so that if a loan originator is able to deliver loan to both subsidiaries, they must compensate the loan originator in the same manner. Accordingly, if a loan originator delivers a loan to subsidiary B and the interest rate is 8 percent, the originator must receive the same compensation that would have been paid by subsidiary A for a loan with a rate of either 7 or 8 percent. (75 Fed. Reg. at 58,526).

Board staff has informed more than one of the undersigned trade associations that they not only would consider all lending affiliates of an originator as one person as stated in the rule, but that they also would consider fees paid to a mortgage company's affiliated real estate brokerage and title/settlement service companies as one person, meaning that fees paid for the fair market value of services performed by these affiliated companies could be considered as loan compensation.

For brokered loans, this would, in effect, prohibit -- for no justifiable reason -- the use of a successful and long-established affiliated business model employed by many members of the undersigned associations that offers consumers one-stop shopping, which Congress had expressly authorized in a 1983 amendment to the Real Estate Settlement Procedures Act (RESPA). According to the independent real estate research firm REALTrends, Inc., 285 of the nation's 500 largest residential real estate brokerage firms -- which were involved in 30% of all home purchase transactions in 2007 -- offer mortgages, and 240 of the top 500 firms offer title, closing or escrow services. According to a 2010 survey of home buyers by Harris Interactive, the parent of Harris Poll, 29% of recent home buyers used a one-stop shopping service in 2010 compared to 20% in 2002 – an increase of 45%.

Under the staff's interpretation, bona fide and reasonable compensation paid by a seller/buyer for real estate brokerage services to that firm would be considered by the Board as direct compensation paid to the mortgage company, which would mean that the real estate broker's affiliated mortgage company could not broker any loans and be paid for such brokerage activity by the lender without violating the dual source compensation prohibition.

This could not have been the intended result. Indeed, Section 1401 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. (2010) expressly exempts real estate brokers from the definition of loan originator**.** *See* 15 U.S.C. § 1602(cc)(2)(D) ("mortgage originator does not include a person or entity that only performs real estate brokerage activities and is licensed or registered in accordance with applicable State law, unless such a person is compensated by a lender a mortgage broker, or other mortgage originator, or by any agent of such lender, mortgage broker or other mortgage originator.")

Similarly, mortgage companies often have title agency affiliates. Under the Board staff interpretation, if a buyer uses the mortgage company's title affiliate and if either the borrower or the seller pays part of the title or closing costs to the title affiliate, the lender with whom the title agent is

affiliated could not broker any loans for payment by the lender without violating the rule's dual source compensation prohibition.

We do not believe that this interpretation is consistent with the Board's goals in this rulemaking. First, title insurance rates in forty-four states are set by the states, approved by the states, or are filed with the states The established, approved, and/or filed rates are the rates that have to be charged. Two additional states do not recognize title insurance. Thus, for the overwhelming majority of transactions, there is no risk that an affiliated lender could circumvent the final rule by inflating the title rates.

Second, to address comments and concerns regarding third party charges, the Board revised comment 36(d)(1)-1 to its rule regarding loan originator compensation practices "to clarify that for purposes of §§ 226.36(d) and (e), the term "compensation" includes amounts retained by the loan originator, but does not include amounts that the loan originator receives as payments for bona fide, third party charges, such as title insurance. . . ." 75 Fed. Reg. at 58,521. However, under the Board's current interpretation, an "affiliate" does not qualify as a third party pursuant to this exemption. Thus, even though in about 90% of transactions the title fees of independent companies and affiliated companies are restricted or filed as a matter of state law, the Board has adopted an interpretation that in effect would preclude mortgage companies from brokering loans when the consumer uses an affiliated title company but permits it when the consumer uses a non-affiliated company that charges the exact same filed rate. Put another way, the Board would refuse to exempt bona fide reasonable title charges of title affiliates, even if they are the same as bona fide reasonable charges of unaffiliated title companies. There is no logical rationale for this distinction.

This interpretation of the term "affiliate" would result in other even more illogical consequences. For example, some real estate brokerage firms or title companies are part of corporate holding companies that may own other businesses such as utilities and insurance companies. If, at closing, it is discovered that a consumer has paid a fee to one of these insurance companies or utilities (which fall within the Dodd-Frank Wall Street Reform Act's broad "common control" definition of "affiliate"), the Board's interpretation would prevent the mortgage company from receiving a fee from the lender to whom it brokered the loan since the consumer's fee to the insurance company or utility also would count as loan originator compensation.

The Reasons Provided for Not Modifying this Interpretation Are Not Persuasive

The reasons we have been given for the staff's interpretation is that (1) no comments were received on this point when the rule was proposed; and (2) the Dodd-Frank Wall Street Reform Act treats affiliates in a manner similar to what is articulated in the Board's final rule. However, neither reason is persuasive.

With respect to the first point, no comments were submitted regarding this issue because it was not reasonably anticipated that the term "affiliate" – which the Board states was designed to stop two affiliated mortgage subsidiaries from circumventing the prohibition against compensating loan officers on loan terms -- would ever be interpreted so broadly as to essentially treat bona fide real estate brokerage commissions, filed title fees, insurance premiums and utility fees as loan origination compensation. Likewise, it was not reasonably anticipated that when "third party" bona fide

reasonable charges were declared to be exempt, affiliates, by definition, would be excluded from treatment as a "third party" because of a common ownership interest with the creditor/originator. Indeed, another part of the rule requires "any third party charge the loan originator imposes on the consumer [to] comply with state and other applicable law to be deemed bona fide and reasonable." 75 Fed. Reg.at 58,522. Yet, even the fees of affiliates that comply with state and other applicable laws needlessly would be counted as loan originator compensation.

With respect to the second point, the staff's interpretation of "affiliate" goes far beyond the Dodd-Frank Wall Street Reform Act when it considers real estate brokerage fees to be loan originator compensation because the Act specifically exempts real estate brokers from being considered a loan originator. To the extent the Act treated title agencies in a manner similar to that contained in the Board's the final rule, the Act permits exemptions from these statutory rules, and one is certainly warranted in this case.. We believe that for the reasons stated above, the differential treatment of title fees depending on whether a title agency is an affiliate justifies an exemption or some other relief.

Two Proposed Solutions

Accordingly, we urge the Board not to adopt the interpretations suggested by the Board's staff and to instead adopt one of two reasonable solutions to the problems discussed above. One solution would be for the Board to continue to define an "affiliate" as one person but to interpret the term "third party" to include affiliates so that the fees of third party title companies, appraisal companies, real estate brokers, etc. (whether affiliated with the originator or not) may be exempted from loan originator compensation so long as they are bona fide and reasonable. A second solution might be to limit the definition of "affiliate" to include mortgage lending and mortgage brokering businesses as specifically stated in the rule but not to include non- mortgage providers in that definition.

Without any solution, however, the Board would be adopting a rule that would reduce competition and consumer choice in the mortgage marketplace.

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We appreciate your consideration of this serious matter and would be pleased to discuss this further if it would be helpful. We look forward to hearing from you since the April 1, 2011 deadline rapidly approaches and we need to find a way to resolve this matter before that time.

Respectfully yours,

The **Community Mortgage Banking Project (CMBP)**: A public policy organization representing the interests of independent mortgage bankers. For decades, the community-based mortgage banker has delivered value and choice to consumers by leveraging local market expertise, quality service, and lower costs for borrowers. The CMBP supports financial market reforms that promote consumer access, borrower and investor transparency, and local competition and choice.

The **Consumer Mortgage Coalition (CMC):** A trade association of national mortgage lenders, servicers, and service providers.

The **National Association of Homebuilders (NAHB):** A trade association that helps promote the policies that make housing a national priority. Since 1942, NAHB has been serving its members, the housing industry, and the public at large.

The **National Association of Mortgage Brokers (NAMB):** The only national trade association that represents the mortgage broker industry. Since 1973, NAMB has represented the interests of more than 70,000 mortgage originator professionals located in all 50 states and the District of Columbia.

The National Association of REALTORS®: "The Voice for Real Estate," America's largest trade association, representing 1.1 million members involved in all aspects of the residential and commercial real estate industries.

The Real Estate Services Providers Council, Inc. (RESPRO®): A national non-profit trade association of providers from all segments of the residential home buying and financing industry, including real estate broker-owners, mortgage lenders, title agents/underwriters, homebuilders, and financial institutions. They all offer a diversified menu of services for home buyers and home owners through wholly-owned subsidiaries or through joint ventures with other providers, both of which are designated under the Real Estate Settlement Procedures Act (RESPA) as "affiliated business arrangements."

The Realty Alliance: A network of the largest full-service residential real estate firms in North America, all of which offer consumers the benefits they ask for in the form of one-stop shopping for services related to their real estate transaction. The Realty Alliance represents more than 100,000 professionals in real estate, mortgage, title, insurance and similar businesses.