Multistate Mortgage Committee (MMC)
STATE NONDEPOSITORY EXAMINER
GUIDELINES FOR REGULATION Z –
LOAN ORIGINATOR COMPENSATION RULE

I. INTRODUCTION

On August 26, 2009, the Federal Reserve Board (FRB) published a proposed rule in the Federal Register pertaining to closed-end credit under Regulation Z to the Truth in Lending Act. The proposed rule introduced loan originator compensation restrictions and included prohibitions against payments based on interest rates and steering activities intended to protect consumers against the unfairness, deception, and abuse that can arise with certain loan origination compensation practices. In a joint letter, CSBS, AARMR, and NACCA[1] supported the loan originator compensation restriction proposal, reasoning that:

> *Deceptive loan originator compensation practices have worked to create an unfair environment for consumers. Providing financial incentives to originators to provide nontraditional mortgage loan products has led to consumers taking on excessive risks in unsuitable mortgage loans.*

The Final Rule (the Rule) on loan originator compensation was published September 24, 2010[2], with an effective date of April 1, 2011. However, on March 31, 2011, an administrative stay was granted by the United States Court of Appeals for the District of Columbia Circuit delaying the effective date of the rule. The stay was lifted on April 5, 2011. The FRB published a final rule revising its official staff commentary to Regulation Z on July 2011 stating: "The administrative stay was in effect from April 1, 2011, until it was dissolved on April 5, 2011. Accordingly, the commentary is being revised to reflect that compliance with the final rule on loan originator compensation was not mandatory until April 6, 2011." <u>Therefore, these guidelines should be considered applicable for loans in which the creditor received an application on or after April 6, 2011.</u>

The Rule, as published in Regulation Z, including Supplement I to Part 226—Official Staff Interpretations, are provided as Appendix A to these guidelines for ease in examiner reference. However, since amendments to Regulation Z are expected under the Reform Act, examiners are advised to frequently check for amendments at http://ecfr.gpoaccess.gov/cgi/t/text/text-idx?c=ecfr&sid=635f26c4af3e2fe4327fd25ef4cb5638&tpl=/ecfrbrowse/Title12/12cfr226_main_02.tpl. [Note: Ctrl click the above address to launch the latest version of Regulation Z.]

The Task Force on Consumer Compliance of the Federal Financial Institutions Examination Council (FFIEC) has approved interagency examination procedures for Regulation Z - Truth in Lending, including the Rule. These revised procedures supersede the Regulation Z interagency examination procedures. Although limited, for uniformity and consistency, the interagency

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[1] Conference of State Bank Supervisors, American Association of Mortgage Regulators, and National Association of Consumer Credit Administrators.
[2] Found at http://edocket.access.gpo.gov/2010/pdf/2010-22161.pdf.

procedures are included within this document as Section IV. These MMC[3] guidelines supplement the interagency procedures and are intended to assist state regulators of nondepository[4] mortgage loan originators[5] and creditors in standardized and uniform reviews of the Rule.

II. BACKGROUND

The Rule is intended to protect consumers from unfair, abusive, or deceptive practices that can arise from loan originator compensation arrangements. The main provisions of the rule generally prohibit:

- Payments by creditors and other persons to loan originators based on loan terms and conditions.
- Dual compensation to loan originators by consumers and any other person.
- "Steering" consumers to loans to receive greater compensation, unless the loan is in the consumer's interest.

Each of the main provisions is discussed below. See section III for pertinent definitions.

<u>Compensation of Loan Originators on Covered Transactions</u>

The Rule regulates compensation to loan originators on "covered transactions" by prohibiting any compensation paid by any person other than the consumer based on loan terms or conditions. In general, terms or conditions include interest rate, annual percentage rate, loan to value ratio, and prepayment penalties. Terms or conditions do not include loan amount[6], overall loan volume, long-term loan performance, existing versus new customers, "pull through" rates, quality of loan files, legitimate business expenses, flat fee compensation, or compensation based on hourly rate.

<u>Dual Compensation</u>

The Rule prohibits loan originators from receiving compensation directly from the consumer while also receiving compensation on the same loan from any other person. Payments to the loan originator from loan proceeds are considered payments made directly by the consumer. Payments to the loan originator derived from the interest rate (e.g., YSP) are not considered payments received directly from the consumer. Points paid on the loan by the consumer to the creditor are not considered payments received directly from the consumer whether they are paid in cash or out of loan proceeds.

<u>Anti-Steering</u>

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[3] The Multistate Mortgage Committee (MMC) is the ten state representative body formed under the CSBS/AARMR Nationwide Cooperative Protocol and Agreement for Mortgage Supervision.
[4] Although these guidelines are developed and intended for use by nondepository mortgage regulators, the Rule applies equally to depository institutions, and examiners of those institutions may find these guidelines to be useful in reviewing compliance with the Rule as well.
[5] For the purposes of these guidelines, "loan originator" means "mortgage loan originator" throughout.
[6] Provided that payment is based on a fixed percentage (e.g., 1% of loan amount).

The rule prohibits loan originators from "steering"[7] consumers to a lender to receive greater compensation, unless the loan is in the consumer's interest.

III. DEFINITIONS[8]

Compensation – For purposes of §226.36(d) and (e), the term "compensation" includes salaries, commissions, and any financial or similar incentive provided to a loan originator that is based on any of the terms or conditions of the loan originator's transactions. See terms and conditions §36(d)(1)–3 in the Official Staff Interpretation (Appendix A of these guidelines) for examples of types of compensation that are or are not covered by §226.36(d) and (e).
Covered Transactions – Scope of coverage. Sections 226.36(b)[9] and (c) apply to closed-end consumer credit transactions secured by a consumer's principal dwelling. Sections 226.36(d) and (e) apply to closed-end consumer credit transactions secured by a dwelling. Sections 226.36(d) and (e) apply to closed-end loans secured by first or subordinate liens, and reverse mortgages that are not home-equity lines of credit under §226.5b. See §226.36(f) for additional restrictions on the scope of this section, and §§226.1(c) and 226.3(a) and corresponding commentary for further discussion of extensions of credit subject to Regulation Z.

Creditor – For purposes of §§226.36(d) and (e), a creditor means a creditor that is not deemed to be a loan originator on the transaction under this section. Thus, a person that closes a loan in its own name (but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation) is deemed a loan originator, not a creditor, for purposes of §226.36. However, that person is still a creditor for all other purposes of Regulation Z.

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 unit, cooperative unit, mobile home, and trailer, if it is used as a residence. [Source: Regulation Z, §226.2(a)(19)]

> Supplement I to Part 226—Official Staff Interpretations—2(a)(19) Dwelling .
> 1. Scope. A dwelling need not be the consumer's *principal* residence to fit the definition, and thus a vacation or second home could be a dwelling. However, for purposes of the definition of residential mortgage transaction and the right to rescind, a dwelling must be the principal residence of the consumer. (See the commentary to §§226.2(a)(24), 226.15, and 226.23.)
> 2. Use as a residence. Mobile homes, boats, and trailers are dwellings if they are in fact used as residences, just as are condominium and cooperative units. Recreational vehicles, campers, and the like not used as residences are not dwellings.

[7] Defined in Section III.
[8] Unless otherwise indicated definitions are taken directly from the Rule as filed in the Federal Register with no alterations or additional clarifications. Definitions taken from the Rule may appear differently in the Federal Register due to order and format.
[9] Note: §226.36(b) is currently reserved in Regulation Z pending additional rule writing under the Reform Act.

3. Relation to exemptions. Any transaction involving a security interest in a consumer's principal dwelling (as well as in any real property) remains subject to the regulation despite the general exemption in §226.3(b).

Loan Originator – Means with respect to a particular transaction, a person who for compensation or other monetary gain, or in expectation of compensation or other monetary gain, arranges, negotiates, or otherwise obtains an extension of consumer credit for another person. The term ‘‘loan originator’’ includes an employee of the creditor if the employee meets this definition. The term ‘‘loan originator’’ includes the creditor only if the creditor does not provide the funds for the transaction at consummation out of the creditor's own resources, including drawing on a *bona fide* warehouse line of credit, or out of deposits held by the creditor.

Managers and administrative staff – For purposes of §226.36, managers, administrative staff, and similar individuals who are employed by a creditor or loan originator but do not arrange, negotiate, or otherwise obtain an extension of credit for a consumer, and whose compensation is not based on whether any particular loan is originated, are not loan originators.

Mortgage broker – For purposes of §226.36, with respect to a particular transaction, the term ‘‘mortgage broker’’ refers to a loan originator who is not an employee of the creditor. Accordingly, the term ‘‘mortgage broker’’ includes companies that engage in the activities described in §226.36(a) and also includes employees of such companies that engage in these activities. Section 226.36(d) prohibits certain payments to a loan originator. These prohibitions apply to payments made to all loan originators, including payments made to mortgage brokers, and payments made by a company acting as a mortgage broker to its employees who are loan originators.

Pull-Through Rate – According to Freddie Mac, "your pull-through rate is a percentage that measures the dollar volume of loans that you close versus the dollar volume of loans that you contract for using the Best Efforts offering. The more loans that you close and fund and deliver, the higher your pull-through percentage will be. Any loan that has expired or been withdrawn will adversely affect your pull-through rate. Freddie Mac will consider your pull-through rate, and its consistency in different market conditions, when determining your pricing." [Source: The Freddie Mac Selling System: Operating Principles www.FreddieMac.com/sell/secmktg/sellingloans.htm Page 1 of 3 Revised: April 8, 2004]

Residential Mortgage Loan – The term residential mortgage loan is not defined in Regulation Z or the Rule. The Rule applies to a "closed-end consumer credit transaction secured by a dwelling," however, neither Regulation Z nor the Rule provide a specific definition of a "closed-end consumer credit transaction secured by a dwelling." In general, examiners should consider generally understood terminology of "residential mortgage loan" to include closed-end loans secured by first or subordinate liens, and reverse mortgages that are not home-equity lines of credit under § 226.5b, that are secured by a dwelling (as defined above). The Rule excludes home-equity lines of credit (HELOCs) that are subject to § 226.5b and timeshare plans, as described in the Bankruptcy Code, 11 U.S.C. 101(53D).

Servicing – The definition of ''loan originator'' does not apply to a loan servicer when the servicer modifies an existing loan on behalf of the current owner of the loan. The rule only applies to extensions of consumer credit and does not apply if a modification of an existing obligation's terms does not constitute a refinancing under §226.20(a).

Steering – For purposes of §226.36(e), directing or ''steering'' a consumer to consummate a particular credit transaction means advising, counseling, or otherwise influencing a consumer to accept that transaction. For such actions to constitute steering, the consumer must actually consummate the transaction in question. Thus, §226.36(e)(1) does not address the actions of a loan originator if the consumer does not actually obtain a loan through that loan originator.

Table funding – Table funding occurs when the creditor does not provide the funds for the transaction at consummation[10] out of the creditor's own resources, including drawing on a bona fide warehouse line of credit, or out of deposits held by the creditor. Accordingly, a table-funded transaction is consummated with the debt obligation initially payable by its terms to one person, but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation. Although §226.2(a)(17)(i)(B) provides that a person to whom a debt obligation is initially payable on its face generally is a creditor, §226.36(a)(1) provides that, solely for the purposes of §226.36, such a person is also considered a loan originator. The creditor is not considered a loan originator unless table funding occurs. For example, if a person closes a loan in its own name but does not fund the loan from its own resources or deposits held by it because it assigns the loan at consummation, it is considered a creditor for purposes of Regulation Z and also a loan originator for purposes of §226.36. However, if a person closes a loan in its own name and draws on a bona fide warehouse line of credit to make the loan at consummation, it is considered a creditor, not a loan originator, for purposes of Regulation Z, including §226.36.

IV. REVISED INTERAGENCY EXAMINATION PROCEDURES

The following interagency procedures were implemented prior to the effective date of the Rule – See Appendix B.

Subpart E - Special Rules for Certain Home Mortgage Transactions
Prohibited Acts or Practices in Connection with Credit Secured by a Consumer's Dwelling
§226.36 – Loan Originator Compensation

> To protect borrowers in the residential mortgage market, certain unfair practices relating to compensation of mortgage brokers and other loan originators are prohibited. Loan originators include mortgage broker companies, including those companies that close loans in their own names in table-funded transactions, and loan officers and other employees of creditors that originate loans. Creditors are not considered to be loan

10 Supplement I to Part 226—Official Staff Interpretations. *State law governs.* When a contractual obligation on the consumer's part is created is a matter to be determined under applicable law; Regulation Z does not make this determination. A contractual commitment agreement, for example, that under applicable law binds the consumer to the credit terms would be consummation. Consummation, however, does not occur merely because the consumer has made some financial investment in the transaction (for example, by paying a nonrefundable fee) unless, of course, applicable law holds otherwise.

originators unless they use table funding or function as a mortgage broker in the transaction.

Loan originators cannot:

- Receive, and no person can pay directly or indirectly, compensation based on a loan's terms or conditions other than the loan amount (and then only provided that such compensation is based on a fixed percentage of the loan amount);
- Receive compensation, directly or indirectly, from a creditor or another party for a loan when a consumer directly pays the loan originator's compensation; or
- Direct or "steer" a consumer to a loan that is not in a consumer's interest to increase the loan originator's compensation.

A loan originator can obtain a "safe harbor" for compliance with the anti-steering requirement by obtaining loan options from a significant number of the creditors with which the loan originator regularly does business and, for each loan type in which the consumer has expressed interest, presenting the consumer with loan options for which the loan originator believes in good faith the consumer likely qualifies, that include:

1) The loan with the lowest interest rate;
2) The loan with the lowest interest rate without any risky features (such as prepayment penalties, negative amortization, or a balloon payment in the first seven years); and
3) The loan with the lowest total dollar amount for origination points or fees and discount points.

The loan originator compensation provisions do not apply to open-end home-equity lines of credit or to loans secured by a consumer's interest in a timeshare plan.

<u>Prohibited Payments to Loan Originators</u>

a. Determine that, in connection with a consumer credit transaction secured by a dwelling, no loan originator receives and no person pays to a loan originator, directly or indirectly, compensation that is based on any of the transaction's terms or conditions. (§226.36(d)(1)(i))
   Note: This prohibition does not apply if the loan originator receives compensation directly from a consumer in a consumer credit transaction secured by a dwelling. Additionally, the amount of credit extended is not deemed to be a transaction term or condition, provided compensation received by or paid to a loan originator, directly or indirectly, is based on a fixed percentage of the amount of credit extended. Such compensation may be subject to a minimum or maximum dollar amount.
b. If any loan originator receives compensation directly from a consumer in a consumer credit transaction secured by a dwelling, determine that (§226.36(d)(2)):
   1. No loan originator receives compensation, directly or indirectly, from any person other than the consumer in connection with the transaction (§226.36(d)(2)(i)); and

2. No person who knows or has reason to know of the consumer-paid compensation to the loan originator (other than the consumer) pays any compensation to a loan originator, directly or indirectly, in connection with the transaction. (§226.36(d)(2)(ii))

Prohibition on Steering

a. Determine that, in connection with a consumer credit transaction secured by a dwelling, a loan originator does not direct or ‘‘steer’’ a consumer to consummate a transaction based on the fact that the originator will receive greater compensation from the creditor in that transaction than in other transactions the originator offered or could have offered to the consumer, unless the consummated transaction is in the consumer's interest. (§226.36(e)(1))

Note: The rule provides a safe harbor to facilitate compliance with the prohibition on steering in §226.36(e)(1). The loan originator is deemed to comply with the anti-steering prohibition if the consumer is presented with loan options that meet all of the following conditions for each type of transaction in which the consumer expressed an interest:[11]

1. The loan originator obtains loan options from a significant number of the creditors with which the originator regularly does business and, for each type of transaction in which the consumer expressed an interest, presents the consumer with loan options that include (§226.36(e)(3)(i)):
   i. The loan with the lowest interest rate;
   ii. The loan with the lowest interest rate without negative amortization, a prepayment penalty, interest-only payments, a balloon payment in the first 7 years of the life of the loan, a demand feature, shared equity, or shared appreciation; or, in the case of a reverse mortgage, a loan without a prepayment penalty, or shared equity or shared appreciation; and
   iii. The loan with the lowest total dollar amount for origination points or fees and discount points.

2. The loan originator has a good faith belief that the options (presented to the consumer that are set forth, above) are loans for which the consumer likely qualifies. (§226.36(e)(3)(ii))

3. For each type of transaction, if the originator presents to the consumer more than three loans, the originator highlights the loans that satisfy options 1.i, 1.ii, and 1.iii above. (§226.36(e)(3)(iii))

Note: If the requirements set forth in §226.36(e) are met, the loan originator can, without steering, present fewer than three loans. (§226.36(e)(4))

[11] The term ‘‘type of transaction’’ refers to whether: (i) A loan has an APR that cannot increase after consummation; (ii) A loan has an APR that may increase after consummation; or (iii) A loan is a reverse mortgage. (§226.36(e)(2))

V. MMC GUIDELINES FOR EXAMINATION OF THE REGULATION Z LOAN ORIGINATOR COMPENSATION RULE

Disclaimer: These guidelines are intended to provide state examiners with a standard set of examination tools to determine institution compliance with certain "bright line" areas of the Rule. The actual Rule is both complex and nuanced and these guidelines are not intended, nor able to provide instruction for every scenario that may arise. The purpose of these guidelines is to provide the examiner with a standardized set of procedures for reviewing institutions for basic compliance with the Rule. The examiner should consider the facts of each unique situation and apply judgment appropriately.

Review Findings, Violations and Internal Control

When addressing examination findings, the examiner has a range of options from identification of internal control weaknesses to citation of violation. Each agency must make its own assessment of the nature and seriousness of the findings and these Guidelines should not be interpreted as any restriction on an agency's ability to take action under state law or Regulation Z.

NOTHING WITHIN THESE GUIDELINES IS INTENDED TO BE BINDING OR RESTRICTIVE ON A STATE'S AUTONOMOUS DETERMINATION AND SOVEREIGN AUTHORITY TO TAKE SUPERVISORY ACTION.

INSTRUCTIONS

Examiners[12] should review these guidelines and the Rule thoroughly before beginning the examination. The modules included in Section V are intended to be used for onsite and offsite review of the institution. Module 1 is to be completed by the examiner. Module 2 (Institution Information Request) and Module 3 (Institution Questionnaire) are to be completed by institution management.

Modules 2 and 3, as well as actual transaction testing and interviews by the examiner are necessary for full scope completion of Module 1. However, the guidelines are not intended to be a static method of examination. Examiners should use their best judgment in applying these guidelines. When deemed appropriate, the examiner may choose a full scope, limited scope or alternative scope examination approach. The following examination approaches are offered as examples:

1. Full Scope: Pre-exam completion of Modules 2 and 3 followed by completion of Module 1 through documentation review, onsite transaction testing, and interviews of institution staff or other parties.

[12] Although these guidelines have been developed for use by state examiners, institution management, internal control staff and outside auditors may find the guidelines useful in testing and monitoring compliance. When used by other than examiners, the reviewer should consider placing himself or herself in the role of examiner and apply the guidelines appropriately. Note: The guidelines are designed for testing of compliance with the Rule and are not intended as interpretation, clarification or supplement to the Rule.

2. Limited Scope: Completion of Module 1, excluding transaction testing and interviews, based on the institution's responses to Modules 2 and 3.
3. Limited Scope with offsite testing: Combine the Limited Scope approach with an offsite sampling of transaction documents and/or telephone interviews of institution staff or other parties.

Examiner in Charge note: Due to cross-over issues and similar documentation requests, an efficient use of resources may be to have the examiner(s) assigned to conduct review under the Rule also assigned to conduct the SAFE Examination Procedures review.

APPLICATION AND COVERAGE

The Rule applies to closed-end consumer credit transactions secured by a dwelling, including closed-end loans secured by first or subordinate liens, and reverse mortgages that are not home-equity lines of credit under § 226.5b. See §§ 226.1(c) and 226.3(a), and corresponding commentary, regarding extensions of consumer credit subject to TILA. The Rule excludes home-equity lines of credit (HELOCs) that are subject to § 226.5b and timeshare plans, as described in the Bankruptcy Code, 11 U.S.C. 101(53D). It also does not apply to loans secured by real property that does not include a dwelling. <u>Therefore, the these guidelines apply to residential mortgage loans, including reverse mortgage loans, but do not apply to home equity lines of credit (HELOCs), time-share transactions, or loans secured by real property if such property does not include a dwelling.</u>

Certain persons are excluded from coverage under the Rule, including persons and entities that originate loans but are also creditors that provide seller financing for properties that the originator owns. Also not covered are loan servicers that modify an existing loan on behalf of the current owner of the loan as long as the modification does not constitute a refinancing.

MODULE 1 – EXAMINER CHECKLIST

Module 1 consists of questions intended to guide the examiner for specific review. Much of the checklist can be completed from a thorough, off-site review of the institution's responses to Modules 2 and 3. Other sections will require transaction-level review and interviews of institution staff and others.

Specific Instructions for Completing Module 1: The following checklist is intended to be used in Word document form. Examiners ask each question of themselves and then check "yes" or "no" followed by completion of the Examiner Notes section. The Examiner Notes should be typed in the column box related to the question. There is no limitation on the amount of text that can be entered in the box (i.e. box will expand as you type). The checklist serves as both contemporaneous examination notes and an aid in drafting comments for the Report of Examination (ROE). If drafted with thought and care, portions of the Examiner Notes can be simply copied and pasted into the ROE, especially the answers drafted to questions A.2 and D.4.

A. REVIEW OF POLICIES AND PROCEDURES

	Examiner note: Obtain and thoroughly review all policies and procedures related to Loan Originator Compensation.	Y	N	Examiner Notes [Document supporting evidence and note determinations and findings made.]
A.1	Do written policies and procedures adequately cover (as applicable):			
A.1a	• Identification of loan originators as defined under the Rule?			
A.1b	• Description of compensation?			
A.1c	• Compensation agreements?			
A.1d	• Description of covered transactions?			
A.1e	• Payments by creditors and other persons to loan originators?			
A.1f	• Payments by consumers to loan originators?			
A.1g	• Compensation based on terms or conditions?			
A.1h	• Dual compensation?			
A.1i	• "Steering" by loan originators?			
A.1j	• Internal controls, monitoring and reporting?			
A.1k	• Compensation to managers and others not typically classified as loan originators?			
A.1l	• Compensation to mortgage brokers, independent contractors, affiliates and net branches?			
A.1m	• Handling of third party costs and seller contributions?			
A.1n	• Safe harbor? See Section C below.			
A.1o	• Records retention?			
A.2	Do institution policies and procedures provide adequate controls for compliance with the Rule? *Examiner note: It is not specifically required under the Rule that an institution develop and maintain policies and procedures in order to comply with the Rule. However, sound management practices and internal controls dictate adequate policies and procedures for the institution and its loan originators.*			

B. COMPENSATION

	Examiner note: Review responses to Modules 2 and 3, HR files, payroll records, general ledgers and HUD settlement statements.	Y	N	Examiner Notes [Document supporting evidence and note determinations and findings made.]
	LOAN COMPENSATION BASED ON TERMS OR CONDITIONS PAID BY ANY PERSON OTHER THAN THE BORROWER. *Examiner note: In this section you are attempting to identify situations in which payment to a loan originator by other than the borrower was based on terms or conditions of the mortgage loan. Keep in mind three basic tests: 1) Was payment based on rate, or other terms or conditions? 2) Was payment made by any person other than the borrower? 3) Was payment made to the loan originator (mortgage broker or individual)? A lender may not expressly pay and a loan originator may not receive compensation based on loan terms or conditions or that acts as a proxy for compensation based on loan terms or conditions. If there is a situation where a loan originator receives compensation that correlates to different loan terms or conditions, the lender must justify the distinction on other ground(s) such as differences in the level of work required of the originator to originate the loan. [Ctrl Click here for examples of compensation based on terms and conditions: 36(d)(1) Payments based on transaction terms and conditions.]*			
B.1	Does the institution have the ability to produce a list of all loans in which compensation to the loan originator was paid by any person other than the borrower (e.g. seller, creditor, third party)? If so, obtain this list and use it for loan sampling purposes.			
B.2	Is there any evidence that loan originators are compensated based on:			
B.2a	• Interest rate/Annual Percentage Rate? *Examiner note: Identify a sample of similar loan transactions for a given loan originator and determine if there is any compensation differential among loans in the sample based on higher interest rates, and if so, whether any compensation was paid to the loan originator from any person other than the borrower.*			

B.2b	• Loan to Value? *Examiner note: Identify a sample of similar loan transactions for a given loan originator and determine if there is any compensation differential in the sample based on higher or lower LTV, and if so, whether any compensation was paid to the loan originator from any person other than the borrower.*			
B.2c	• Prepayment Penalty? *Examiner note: Identify a sample of similar loan transactions for a given loan originator and determine if there is any compensation differential in the sample based on the existence of a prepayment penalty, and if so, whether any compensation was paid to the loan originator from any person other than the borrower.*			
B.2d	• Credit Score? *Examiner note: Identify a sample of similar loan transactions for a given loan originator and determine if there is any compensation differential in the sample based on credit score difference, and if so, whether any compensation was paid to the loan originator from any person other than the borrower. [Note: In order for a violation to occur the credit score differential must be a proxy for a term or condition where any difference in compensation is not justified on other grounds. For example, a lower credit score translates to a higher interest rate and higher loan originator compensation.]*			
B.2e	• Debt to Income? *Examiner note: Identify a sample of similar loan transactions for a given loan originator and determine if there is any compensation differential in the sample based on debt to income difference, and if so, whether any compensation was paid to the loan originator from any person other than the borrower. [Note: In order for a violation to occur the DTI ratio differential must be a proxy for a term or condition where any*			

	difference in compensation is not justified on other grounds. For example, a higher DTI ratio translates to a higher interest rate and higher loan originator compensation.]			
B.2f	• Amount of loan other than compensation based on a fixed percentage of loan amounts or volume of loans? *Examiner note: Identify a sample of similar loan transactions for a given loan originator and determine if there is any compensation differential based on loan amount other than compensation difference created by the actual amount of the loan or the volume of loans. [Example: Loan originator paid compensation of 1% of the loan amount for loans up to $500,000 and 2% of the loan amount for loans greater than $500,000.] If so, was any compensation paid to the loan originator from any person other than the borrower?*			
	UPCHARGING THIRD PARTY COSTS. *Examiner note: In this section you are determining whether the loan originator has retained any compensation that is the result of "upcharging" costs on third party services (e.g. charging $500 for a $400 appraisal and keeping the excess).*			
B.3	Comparing a sample of closing statements to the actual payment to third parties for services rendered, is there any evidence that the originator has retained fees in excess of the actual costs of the services?			
B.3a	• For those transactions in B.3 in which you answered "yes," is there evidence that the originator knew or should have known the actual amount of third party costs*? Examiner note: It is not a violation of the Rule for the originator to retain excess fees in situations in which the originator can show that the originator did not know the actual cost of the servicer (e.g. the originator uses multiple services each charging different amounts or ranges of amounts). However, such excess*			

	fees may be considered non bona fide and a violation of state law or Regulation X.			
B.4	Comparing a sample of closing statements and fees received, is there any evidence that the originator has received compensation for other services actually performed by the originator such as processing services or document preparation services? If so, determine whether the receipt of such compensation constitutes compensation based on loan terms or a proxy for such compensation that cannot be justified on other grounds..			
	MISCELLANEOUS COMPENSATION ISSUES			
B.5	Is there any evidence that exchanges between loan price and transaction costs (situations in which the creditor increases price to offset costs) has any bearing on loan originator compensation?			
B.6	Is there any evidence that loan originator compensation is reduced for a particular loan in order for the institution or originator to compete on loan terms? *[Example: ABC Mortgage offers rate of 7% and XYZ Mortgage offers rate of 6%. ABC lowers rate to 5.75% to compete with XYZ and reduces loan originator's compensation as an offset to reduction.]*			
B.7	Are loan originators able to deliver loans to more than one affiliate or subsidiary of a parent company? If so, are loan originators compensated the same by each affiliate or subsidiary? *Examiner note: Determine if there is any evidence that a loan originator is compensated more from one affiliate or subsidiary than another based on different terms or conditions.*			
B.8	Interview management, loan originators, underwriters, HR and accounting/payroll personnel. Ask each of the questions in B.2 through B.7. Document and investigate further any apparent compliance failures.			

	DUAL COMPENSATION. *Examiner note: In this section you are trying to determine whether any person, in addition to the borrower, has paid compensation to the loan originator. Keep in mind two basic tests: 1) Has the borrower paid any compensation to the loan originator? 2) If the answer to 1 is "yes," has any person, in addition to the borrower, paid any compensation to the loan originator?*			
B.9	Is there any evidence that loan originator compensation has been paid by the borrower AND any other person? Consider the following:			
B.9a	• A sample of HUD settlement statements. Are fees paid to the loan originator by the borrower and another person on the same transaction? If so, investigate further.			
B.9b	• A sample of loans in which the borrower has paid fees to both the creditor and the originator. On the same transaction, are fees paid by the creditor to the originator in addition to fees paid by the borrower to the originator?			
B.9c	• A sample of loans in which yield spread premiums (YSP) have been paid or received. On the same transaction, are fees paid by the creditor to the originator in addition to fees paid by the borrower to the originator?			
B.9d	• Review a sample of payroll records and disbursements and cross-reference with loan transactions to identify any payments on loans where the borrower also paid compensation to the originator.			
B.10	Interview management, loan originators, underwriters, HR, and accounting/payroll personnel. Ask specifically whether loan originators are ever paid by the borrower and any other person on the same transaction.			

C. STEERING

		Y	N	
	Examiner note: In this section you are attempting to determine whether borrowers have been steered to a loan in order for the loan originator to receive greater compensation and, if so, whether the loan is in the consumer's interest. Keep in mind 2 basic tests: 1)) Did the loan originator make greater compensation than would have been made (all other things being equal)? 2) If the answer to 1 is yes, is the loan not in the borrower's interest. Both tests must be satisfied for possible violation. Moreover, assuming both tests appear to have been met, the examiner must determine if the loan originator complied with the Safe Harbor provisions. If so, there is no violation. Finally note, a creditor is not liable for violation of these provisions unless it is acting as a mortgage broker. See Commentary at 226.36 (e)(1). This section prohibits an originator, particularly a mortgage broker or mortgage broker loan originator, from directing or steering a consumer to consummate a transaction based on the fact that the loan originator would receive greater compensation for that transaction as compared to other transactions, unless the transaction is in the consumer's interest. By its terms, the section does not apply to creditors nor make them liable for originator/mortgage broker steering unless they are acting as mortgage brokers for the particular transaction. Additionally, employee loan originators of creditors, when their employer is acting as a creditor, satisfy the anti-steering provisions as long as they are not compensated based on rate or terms of a loan.			Examiner Notes [Document supporting evidence and note determinations and findings made.]
C.1	Reviewing a sample of similar loans originated by the same loan originator:			
C.1a	• Is there any evidence that the loan originator was paid greater compensation? *Example: Borrower A is similar in characteristics to borrower B. Borrower B receives a rate 1% higher than borrower A. The loan originator*			

	is compensated 1% of the loan amount on borrower A and 1.5% of the loan amount on borrower B.			
C.1b	• Of the loans in C.1.a for which you answered "yes," is there any evidence that loans were made that were not in the consumer's interest? *Example: Borrowers with similar credit scores and other characteristics during the same time period are offered or provided loans with different terms or conditions.*			
C.1c	• Of the loans in C.1b for which you answered "yes," did the loan originator follow the Safe Harbor provision?			
	TESTING THE SAFE HARBOR PROVISION FOR MORTGAGE BROKERS AND LOAN ORIGINATORS OF MORTGAGE BROKERS. *Examiner note: In this section you are attempting to determine whether the loan originator's anti-steering /Safe Harbor procedure is sufficient, and whether the loan originator has complied with either the anti-steering or Safe Harbor provisions in each situation where required. Using the Safe Harbor is not required provided the loan originator can show that the borrower has not been steered to a loan that was not in their interest. The Safe Harbor provision is not necessary for creditors or the loan originator employees of creditors as long as the creditor's payments to its employees are not based on loan terms or conditions. However, when the creditor acts as a broker, both that creditor and its loan originator employees must comply with the anti-steering requirements.*			
C.2	Does the loan originator have written policies for complying with the Safe Harbor provision? Document and retain. *Examiner note: It is not specifically required under the Rule that an institution develop and maintain policies and procedures in order to comply with the Rule. However, sound management practices and internal controls dictate adequate policies and procedures for*			

	the institution and its loan originators.			
C.3	Do the written policies require that loan offer options be obtained from a "significant number" of creditors with which the loan originator regularly does business?			
C.3a	• If the loan originator regularly does business with three or more creditors, are at least three creditor options required to be offered to the consumer?			
C.3b	• If the loan originator regularly does business with less than three creditors, are all creditor options required to be offered to the consumer?			
C.4	Do the written policies govern what constitutes "regularly does business"? [See details under §226.36(e)(3)2.]			
C.5	Do the written policies require the following options to be presented to the consumer in writing for each type of loan (fixed or adjustable) in which the consumer expressed an interest? *Examiner note: The Rule does not dictate a specific time in which the written options must be given. Ascertain whether the options were provided no later than a point in time when the options could have been useful to the consumer in making an informed decision to choose a specific option.*			
C.5a	• Option with the lowest rate?			
C.5b	• Option with the lowest rate without higher risk features? High risk features include: Negative amortization; a prepayment penalty; a balloon payment in the first 7 years; a demand feature; shared equity; or shared appreciation.			
C.5c	• Option with the lowest total dollar amount for origination points or fees and discount points?			
C.6	Special Safe Harbor provision for reverse mortgage loans: Do written policies require the following options to be provided to the consumer in writing for a reverse mortgage loan?			
C.6a	• Loan with the lowest rate?			

C.6b	• Loan without a prepayment penalty, or shared equity or shared appreciation?			
C.6c	• Loan with the lowest total dollar amount for origination points or fees and discount points?			
C.7	Do written policies require that the loan originator have a good faith belief that the options presented are loans for which the consumer likely qualifies? How is such good faith belief documented?			
C.8	Reviewing a sample of loan transaction documents, is it apparent that the originator is in compliance with policies and procedures related to steering and the Safe Harbor provision?			
C.9	In situations where the originator lacks policies governing the Safe Harbor provision, is there any evidence that the originator has failed to comply with the Safe Harbor provision requirements under the Rule?			
C.10	In situations where the loan originator does not use the Safe Harbor provision, does the institution document that the loan is in the consumer's interest? Obtain any such documentation.			
	The following questions cover sound creditor practices in maintaining relationships with third party loan originators.			
C.11	For creditors: Does the creditor have written policies requiring that loan originators using the Safe Harbor provision have written policies or procedures in place? What steps does the creditor take to assure that the loan originator has adequate written policies?			
C.12	Does the creditor review and monitor third party originator compliance with the Safe Harbor provision?			
C.12a	• How does the creditor conduct such review and monitoring?			
C.12b	• What action does the creditor take if it finds discrepancies in third party originator compliance under the Rule?			

D. OPERATIONAL MANAGEMENT

		Y	N	Examiner Notes [Document supporting evidence and note determinations and findings made.]
	RECORDS RETENTION. This section applies to creditors and others who compensate loan originators. *Examiner note: The Rule does not preempt your state law or regulation on records retention.*			
D.1	Are records relating to loan originator compensation, including records necessary to prove or disprove any prohibitions or requirements in the Rule, maintained for a period of at least two years from the date of loan consummation?			
D.1a	• Specifically, does the creditor retain for at least two years a record of the compensation agreement with the loan originator that was in effect on the date the transaction's rate was set?			
D.1b	• Specifically, does the creditor retain for at least two years a record of the actual amount of compensation it paid to a loan originator in connection with each covered transaction?			
D.2	Does the institution avoid incentive plans for originators that promote the sale of loans based on terms or conditions?			
D.3	Does the institution avoid incentive plans for originators that promote the sale of loans that are not in the consumer's interest?			
D.4	Based on the foregoing, does management have a clear understanding of its responsibilities under the Rule? *Examiner note: Consider response to questionnaire, policies and procedures, and management oversight. Examiners should conduct interviews of management and staff where appropriate, and conduct actual review of compensation practices.*			

MODULE 2 – INSTITUTION INFORMATION REQUEST

Note: It is not necessary to provide information prior to April 6, 2011.

1. Licensees and examined institutions must complete Module 3 – Institution Questionnaire.

2. Please provide copies of all policies, procedures, standards and guidelines established for maintaining compliance with the Loan Originator Compensation Rule (the Rule). Policies should include identification of loan originators; descriptions of compensation, covered transactions, terms and conditions, and “steering”; requirements of compensation agreements; procedures for complying with the Rule; procedures for internal monitoring and reporting, as well as monitoring of third-party originators (e.g. mortgage brokers); employee training; and records retention. Include the effective date for all policies, procedures, standards and guidelines.

3. Describe what human resources records and payroll records are available to the Examiner in Charge for each employee or independent contractor conducting the business of a mortgage loan originator (e.g. job descriptions, employment contracts, compensation agreements, paystubs, payroll ledgers, W2s/W9s, etc.).

4. For creditors: Describe what third party originator records are available to the Examiner in Charge for each mortgage broker or other originator from whom you receive loan submissions.

5. Provide a list of all employees or independent contractors who have received compensation as a loan originator during the examination period. Include full name, title, date of hire, location of employment, NMLS Unique Identifier, and any date of termination, resignation or transfer of each individual.

6. For creditors: Provide a list of all third party originators that have submitted loan originations to the institution during the examination period.

7. Provide a list of any other person receiving compensation for loan originations not included in 5 or 6 above.

8. Provide example copies of any reports produced for monitoring compliance with the Rule. Make available to the Examiner in Charge all reports covering the date of the examination.

9. Provide a list of compensation situations that required an exception to written policies.

10. Provide a list of all institutions with whom you regularly do business that originate or make residential mortgage loans, along with the estimated percentage of activity conducted with each. In other words, if you are an originator, the list should include each lender you have originated residential mortgage loans for. If you are a lender, the list should include each originator you have accepted residential mortgage loan submissions from.

11. Provide all third party service cost sheets from which the institution priced services during the examination period (e.g. appraiser rates, title costs, credit report costs, etc.).

12. Make available loan transaction documentation as requested by the Examiner in Charge.

MODULE 3 – INSTITUTION QUESTIONNAIRE

The following questionnaire is intended to save time and resources for both the institution and the examination team. Unless instructed otherwise, this questionnaire is to be completed and returned as instructed in the examination entry letter. Please answer all questions thoroughly. Simple Yes/No answers are not sufficient for most questions. Please provide further explanation as needed to assist in clarifying the institution's response and aid the examiner in understanding your practices.

The following questions pertain to consummated residential mortgage loans, excluding open-end home-equity lines of credit or loans secured by a consumer's interest in a timeshare plan, originated during the examination period, but no earlier than April 6, 2011.

INSTITUTION QUESTIONNAIRE

1. How are loan originators compensated? Provide details of all compensation procedures and calculations.

2. What incentive plans are offered to loan originators? Provide details.

3. Are loan originators ever compensated based on:

    a. The interest rate or Annual Percentage Rate obtained on a loan?
    b. The loan to value obtained on a loan?
    c. Originating a loan with a prepayment penalty?
    d. The amount of loan fees paid to the institution or creditor?

4. Are credit scores a determining factor in the amount of compensation earned by a loan originator? Explain.

5. Is debt to income a determining factor in the amount of compensation earned by a loan originator? Explain.

6. Are loan originators allowed to receive reimbursement for third party costs (e.g. appraisal, credit report, etc.)?

7. Are loan originators allowed to charge more for third party costs than the actual cost of the service and retain such costs as compensation? Explain.

8. Are loan originators allowed to charge for services other than loan origination services that are performed by the originator? For example: loan processing, document preparation, inspection fees, etc.

9. Is the loan originator compensated any differently when price is increased by the creditor or employer to offset loan costs?

10. Is loan originator compensation ever reduced in order for the institution to compete on loan terms? For example: The institution reduces its rate by 50 basis points to induce a shopping consumer to stay with the institution, and the loan originator's compensation is reduced accordingly.

11. Are loan originators able to deliver loans to more than one affiliate or subsidiary of the institution's parent company? If so, are loan originators compensated differently based on which affiliate the loans are delivered to?

12. Are loan originators allowed to receive compensation (including yield spread premium or similar) from both the consumer and any other person on the same transaction?

Questions 13 through 18 address both mortgage broker loan originators originating loans and creditor institutions receiving brokered loans.

13. Does the institution allow loan originators to "steer" consumers to transactions where the loan originator receives more compensation and the loan is not in the consumer's interest? Explain.

14. Does the institution require or use the steering Safe Harbor provision under the Rule? [See §226.36(e)(1)]

15. During the examination period, in how many transactions has the institution required or used the steering Safe Harbor provision under the Rule? Institution may answer with a number or the percentage of total loans originated.

16. Does the institution require third party originators to use the steering Safe Harbor provision?

17. If a creditor, what action does the institution take to monitor third party compliance with the steering Safe Harbor provision?

18. If the institution does not require or use the steering Safe Harbor provision what methods does it use to determine that steering has not and will not occur?

19. How long does the institution retain compensation agreements?

20. How long does the institution retain records of actual compensation?

21. How long does the institution retain records that support the options offered under the steering Safe Harbor provision?

APPENDIX A
to the
STATE NONDEPOSITORY EXAMINER
GUIDELINES FOR REGULATION Z –
LOAN ORIGINATOR COMPENSATION RULE

Title 12: Banks and Banking
PART 226—TRUTH IN LENDING (REGULATION Z)
Subpart E—Special Rules for Certain Home Mortgage Transactions

§ 226.36 Prohibited acts or practices in connection with credit secured by a dwelling.

Link to an amendment published at 75 FR 66580, Oct. 28, 2010.

(a) *Loan originator and mortgage broker defined.* (1) *Loan originator.* For purposes of this section, the term "loan originator" means with respect to a particular transaction, a person who for compensation or other monetary gain, or in expectation of compensation or other monetary gain, arranges, negotiates, or otherwise obtains an extension of consumer credit for another person. The term "loan originator" includes an employee of the creditor if the employee meets this definition. The term "loan originator" includes the creditor only if the creditor does not provide the funds for the transaction at consummation out of the creditor's own resources, including drawing on a *bona fide* warehouse line of credit, or out of deposits held by the creditor.

(2) *Mortgage broker.* For purposes of this section, a mortgage broker with respect to a particular transaction is any loan originator that is not an employee of the creditor.

(b) [Reserved]

(c) *Servicing practices* . [Note: This section intentionally left out as not pertaining directly to the Rule.]

(d) *Prohibited payments to loan originators.* (1) *Payments based on transaction terms or conditions.* (i) In connection with a consumer credit transaction secured by a dwelling, no loan originator shall receive and no person shall pay to a loan originator, directly or indirectly, compensation in an amount that is based on any of the transaction's terms or conditions.

(ii) For purposes of this paragraph (d)(1), the amount of credit extended is not deemed to be a transaction term or condition, provided compensation received by or paid to a loan originator, directly or indirectly, is based on a fixed percentage of the amount of credit extended; however, such compensation may be subject to a minimum or maximum dollar amount.

(iii) This paragraph (d)(1) shall not apply to any transaction in which paragraph (d)(2) of this section applies.

(2) *Payments by persons other than consumer.* If any loan originator receives compensation directly from a consumer in a consumer credit transaction secured by a dwelling:

(i) No loan originator shall receive compensation, directly or indirectly, from any person other than the consumer in connection with the transaction; and

(ii) No person who knows or has reason to know of the consumer-paid compensation to the loan originator (other than the consumer) shall pay any compensation to a loan originator, directly or indirectly, in connection with the transaction.

(3) *Affiliates.* For purposes of this paragraph (d), affiliates shall be treated as a single "person."

(e) *Prohibition on steering.* (1) *General.* In connection with a consumer credit transaction secured by a dwelling, a loan originator shall not direct or "steer" a consumer to consummate a transaction based on the fact that the originator will receive greater compensation from the creditor in that transaction than in other transactions the originator offered or could have offered to the consumer, unless the consummated transaction is in the consumer's interest.

(2) *Permissible transactions.* A transaction does not violate paragraph (e)(1) of this section if the consumer is presented with loan options that meet the conditions in paragraph (e)(3) of this section for each type of transaction in which the consumer expressed an interest. For purposes of paragraph (e) of this section, the term "type of transaction" refers to whether:

(i) A loan has an annual percentage rate that cannot increase after consummation;

(ii) A loan has an annual percentage rate that may increase after consummation; or

(iii) A loan is a reverse mortgage.

(3) *Loan options presented.* A transaction satisfies paragraph (e)(2) of this section only if the loan originator presents the loan options required by that paragraph and all of the following conditions are met:

(i) The loan originator must obtain loan options from a significant number of the creditors with which the originator regularly does business and, for each type of transaction in which the consumer expressed an interest, must present the consumer with loan options that include:

(A) The loan with the lowest interest rate;

(B) The loan with the lowest interest rate without negative amortization, a prepayment penalty, interest-only payments, a balloon payment in the first 7 years of the life of the loan, a demand feature, shared equity, or shared appreciation; or, in the case of a reverse mortgage, a loan without a prepayment penalty, or shared equity or shared appreciation; and

(C) The loan with the lowest total dollar amount for origination points or fees and discount points.

(ii) The loan originator must have a good faith belief that the options presented to the consumer pursuant to paragraph (e)(3)(i) of this section are loans for which the consumer likely qualifies.

(iii) For each type of transaction, if the originator presents to the consumer more than three loans, the originator must highlight the loans that satisfy the criteria specified in paragraph (e)(3)(i) of this section.

(4) *Number of loan options presented.* The loan originator can present fewer than three loans and satisfy paragraphs (e)(2) and (e)(3)(i) of this section if the loan(s) presented to the consumer satisfy the criteria of the options in paragraph (e)(3)(i) of this section and the provisions of paragraph (e)(3) of this section are otherwise met.

(f) This section does not apply to a home-equity line of credit subject to §226.5b. Section 226.36(d) and (e) do not apply to a loan that is secured by a consumer's interest in a timeshare plan described in 11 U.S.C. 101(53D).

[73 FR 44604, July 30, 2008, as amended at 75 FR 58533, Sept. 24, 2010]

Supplement I to Part 226—Official Staff Interpretations *Section 226.36—Prohibited Acts or Practices in Connection with Credit Secured by a Dwelling*

1. *Scope of coverage.* Sections 226.36(b) and (c) apply to closed-end consumer credit transactions secured by a consumer's principal dwelling. Sections 226.36(d) and (e) apply to closed-end consumer credit transactions secured by a dwelling. Sections 226.36(d) and (e) apply to closed-end loans secured by first or subordinate liens, and reverse mortgages that are not home-equity lines of credit under §226.5b. *See* §226.36(f) for additional restrictions on the scope of this section, and §§226.1(c) and 226.3(a) and corresponding commentary for further discussion of extensions of credit subject to Regulation Z.

2. *Mandatory compliance date for §§226.36(d) and (e).* The final rules on loan originator compensation in §226.36 apply to transactions for which the creditor receives an application on or after the effective date. For example, assume a mortgage broker takes an application on March 10, 2011, which the creditor receives on March 25, 2011. This transaction is not covered. If, however, the creditor does not receive the application until April 8, 2011, the transaction is covered.

3. *Effective date.* For guidance on the applicability of the rules in §226.36, see comment 1(d)(5)–1.

36(a) Loan originator and mortgage broker defined.

1. *Meaning of loan originator.* i. *General.* Section 226.36(a) provides that a loan originator is any person who for compensation or other monetary gain arranges, negotiates, or otherwise obtains an extension of consumer credit for another person. Thus, the term “loan originator” includes employees of a creditor as well as employees of a mortgage broker that satisfy this definition. In addition, the definition of loan originator expressly includes any creditor that

satisfies the definition of loan originator but makes use of "table funding" by a third party. *See* comment 36(a)–1.ii below discussing table funding. Although consumers may sometimes arrange, negotiate, or otherwise obtain extensions of consumer credit on their own behalf, in such cases they do not do so for another person or for compensation or other monetary gain, and therefore are not loan originators under this section. (Under §226.2(a)(22), the term "person" means a natural person or an organization.)

ii. *Table funding.* Table funding occurs when the creditor does not provide the funds for the transaction at consummation out of the creditor's own resources, including drawing on a *bona fide* warehouse line of credit, or out of deposits held by the creditor. Accordingly, a table-funded transaction is consummated with the debt obligation initially payable by its terms to one person, but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation. Although §226.2(a)(17)(i)(B) provides that a person to whom a debt obligation is initially payable on its face generally is a creditor, §226.36(a)(1) provides that, solely for the purposes of §226.36, such a person is also considered a loan originator. The creditor is not considered a loan originator unless table funding occurs. For example, if a person closes a loan in its own name but does not fund the loan from its own resources or deposits held by it because it assigns the loan at consummation, it is considered a creditor for purposes of Regulation Z and also a loan originator for purposes of §226.36. However, if a person closes a loan in its own name and draws on a *bona fide* warehouse line of credit to make the loan at consummation, it is considered a creditor, not a loan originator, for purposes of Regulation Z, including §226.36.

iii. *Servicing.* The definition of "loan originator" does not apply to a loan servicer when the servicer modifies an existing loan on behalf of the current owner of the loan. The rule only applies to extensions of consumer credit and does not apply if a modification of an existing obligation's terms does not constitute a refinancing under §226.20(a).

2. *Meaning of mortgage broker.* For purposes of §226.36, with respect to a particular transaction, the term "mortgage broker" refers to a loan originator who is not an employee of the creditor. Accordingly, the term "mortgage broker" includes companies that engage in the activities described in §226.36(a) and also includes employees of such companies that engage in these activities. Section 226.36(d) prohibits certain payments to a loan originator. These prohibitions apply to payments made to all loan originators, including payments made to mortgage brokers, and payments made by a company acting as a mortgage broker to its employees who are loan originators.

3. *Meaning of creditor.* For purposes of §226.36(d) and (e), a creditor means a creditor that is not deemed to be a loan originator on the transaction under this section. Thus, a person that closes a loan in its own name (but another person provides the funds for the transaction at consummation and receives an immediate assignment of the note, loan contract, or other evidence of the debt obligation) is deemed a loan originator, not a creditor, for purposes of §226.36. However, that person is still a creditor for all other purposes of Regulation Z.

4. *Managers and administrative staff.* For purposes of §226.36, managers, administrative staff, and similar individuals who are employed by a creditor or loan originator but do not arrange,

negotiate, or otherwise obtain an extension of credit for a consumer, and whose compensation is not based on whether any particular loan is originated, are not loan originators.

36(c) Servicing practices. [Note: This section intentionally left out as not pertaining directly to the Rule.]

36(d) Prohibited payments to loan originators.

1. *Persons covered.* Section 226.36(d) prohibits any person (including the creditor) from paying compensation to a loan originator in connection with a covered credit transaction, if the amount of the payment is based on any of the transaction's terms or conditions. For example, a person that purchases a loan from the creditor may not compensate the loan originator in a manner that violates §226.36(d).

2. *Mortgage brokers.* The payments made by a company acting as a mortgage broker to its employees who are loan originators are subject to the section's prohibitions. For example, a mortgage broker may not pay its employee more for a transaction with a 7 percent interest rate than for a transaction with a 6 percent interest rate.

36(d)(1) Payments based on transaction terms and conditions.

1. *Compensation.* i. *General.* For purposes of §226.36(d) and (e), the term "compensation" includes salaries, commissions, and any financial or similar incentive provided to a loan originator that is based on any of the terms or conditions of the loan originator's transactions. See comment 36(d)(1)–3 for examples of types of compensation that are not covered by §226.36(d) and (e). For example, the term "compensation" includes:

A. An annual or other periodic bonus; or

B. Awards of merchandise, services, trips, or similar prizes.

ii. *Name of fee.* Compensation includes amounts the loan originator retains and is not dependent on the label or name of any fee imposed in connection with the transaction. For example, if a loan originator imposes a "processing fee" in connection with the transaction and retains such fee, it is deemed compensation for purposes of §226.36(d) and (e), whether the originator expends the time to process the consumer's application or uses the fee for other expenses, such as overhead.

iii. *Amounts for third-party charges.* Compensation includes amounts the loan originator retains, but does not include amounts the originator receives as payment for *bona fide* and reasonable third-party charges, such as title insurance or appraisals. In some cases, amounts received for payment for third-party charges may exceed the actual charge because, for example, the originator cannot determine with accuracy what the actual charge will be before consummation. In such a case, the difference retained by the originator is not deemed compensation if the third-party charge imposed on the consumer was *bona fide* and reasonable, and also complies with state and other applicable law. On the other hand, if the originator marks up a third-party charge

(a practice known as “upcharging”), and the originator retains the difference between the actual charge and the marked-up charge, the amount retained is compensation for purposes of §226.36(d) and (e). For example:

A. Assume a loan originator charges the consumer a $400 application fee that includes $50 for a credit report and $350 for an appraisal. Assume that $50 is the amount the creditor pays for the credit report. At the time the loan originator imposes the application fee on the consumer, the loan originator is uncertain of the cost of the appraisal because the originator may choose from appraisers that charge between $300 to $350 for appraisals. Later, the cost for the appraisal is determined to be $300 for this consumer's transaction. In this case, the $50 difference between the $400 application fee imposed on the consumer and the actual $350 cost for the credit report and appraisal is not deemed compensation for purposes of §226.36(d) and (e), even though the $50 is retained by the loan originator.

B. Using the same example in comment 36(d)(1)–1.iii.A above, the $50 difference would be compensation for purposes of §226.36(d) and (e) if the appraisers from whom the originator chooses charge fees between $250 and $300.

2. *Examples of compensation that is based on transaction terms or conditions.* Section 226.36(d)(1) prohibits loan originator compensation that is based on the terms or conditions of the loan originator's transactions. For example, the rule prohibits compensation to a loan originator for a transaction based on that transaction's interest rate, annual percentage rate, loan-to-value ratio, or the existence of a prepayment penalty. The rule also prohibits compensation based on a factor that is a proxy for a transaction's terms or conditions. For example, a consumer's credit score or similar representation of credit risk, such as the consumer's debt-to-income ratio, is not one of the transaction's terms or conditions. However, if a loan originator's compensation varies in whole or in part with a factor that serves as a proxy for loan terms or conditions, then the originator's compensation is based on a transaction's terms or conditions. To illustrate, assume that consumer A and consumer B receive loans from the same loan originator and the same creditor. Consumer A has a credit score of 650, and consumer B has a credit score of 800. Consumer A's loan has a 7 percent interest rate, and consumer B's loan has a 61/2percent interest rate because of the consumers' different credit scores. If the creditor pays the loan originator $1,500 in compensation for consumer A's loan and $1,000 in compensation for consumer B's loan because the creditor varies compensation payments in whole or in part with a consumer's credit score, the originator's compensation would be based on the transactions' terms or conditions.

3. *Examples of compensation not based on transaction terms or conditions.* The following are only illustrative examples of compensation methods that are permissible (unless otherwise prohibited by applicable law), and not an exhaustive list. Compensation is not based on the transaction's terms or conditions if it is based on, for example:

i. The loan originator's overall loan volume (*i.e.,* total dollar amount of credit extended or total number of loans originated), delivered to the creditor.

ii. The long-term performance of the originator's loans.

iii. An hourly rate of pay to compensate the originator for the actual number of hours worked.

iv. Whether the consumer is an existing customer of the creditor or a new customer.

v. A payment that is fixed in advance for every loan the originator arranges for the creditor (*e.g.,* $600 for every loan arranged for the creditor, or $1,000 for the first 1,000 loans arranged and $500 for each additional loan arranged).

vi. The percentage of applications submitted by the loan originator to the creditor that result in consummated transactions.

vii. The quality of the loan originator's loan files (*e.g.,* accuracy and completeness of the loan documentation) submitted to the creditor.

viii. A legitimate business expense, such as fixed overhead costs.

ix. Compensation that is based on the amount of credit extended, as permitted by §226.36(d)(1)(ii). *See* comment 36(d)(1)–9 discussing compensation based on the amount of credit extended.

4. *Creditor's flexibility in setting loan terms.* Section 226.36(d)(1) does not limit a creditor's ability to offer a higher interest rate in a transaction as a means for the consumer to finance the payment of the loan originator's compensation or other costs that the consumer would otherwise be required to pay directly (either in cash or out of the loan proceeds). Thus, a creditor may charge a higher interest rate to a consumer who will pay fewer of the costs of the transaction directly, or it may offer the consumer a lower rate if the consumer pays more of the costs directly. For example, if the consumer pays half of the transaction costs directly, a creditor may charge an interest rate of 6 percent but, if the consumer pays none of the transaction costs directly, the creditor may charge an interest rate of 6.5 percent. Section 226.36(d)(1) also does not limit a creditor from offering or providing different loan terms to the consumer based on the creditor's assessment of the credit and other transactional risks involved. A creditor could also offer different consumers varying interest rates that include a constant interest rate premium to recoup the loan originator's compensation through increased interest paid by the consumer (such as by adding a constant 0.25 percent to the interest rate on each loan).

5. *Effect of modification of loan terms.* Under §226.36(d)(1), a loan originator's compensation may not vary based on any of a credit transaction's terms or conditions. Thus, a creditor and originator may not agree to set the originator's compensation at a certain level and then subsequently lower it in selective cases (such as where the consumer is able to obtain a lower rate from another creditor). When the creditor offers to extend a loan with specified terms and conditions (such as the rate and points), the amount of the originator's compensation for that transaction is not subject to change (increase or decrease) based on whether different loan terms are negotiated. For example, if the creditor agrees to lower the rate that was initially offered, the new offer may not be accompanied by a reduction in the loan originator's compensation.

6. *Periodic changes in loan originator compensation and transactions' terms and conditions.* This section does not limit a creditor or other person from periodically revising the compensation it agrees to pay a loan originator. However, the revised compensation arrangement must result in payments to the loan originator that do not vary based on the terms or conditions of a credit transaction. A creditor or other person might periodically review factors such as loan performance, transaction volume, as well as current market conditions for originator compensation, and prospectively revise the compensation it agrees to pay to a loan originator. For example, assume that during the first 6 months of the year, a creditor pays $3,000 to a particular loan originator for each loan delivered, regardless of the loan terms or conditions. After considering the volume of business produced by that originator, the creditor could decide that as of July 1, it will pay $3,250 for each loan delivered by that particular originator, regardless of the loan terms or conditions. No violation occurs even if the loans made by the creditor after July 1 generally carry a higher interest rate than loans made before that date, to reflect the higher compensation.

7. *Compensation received directly from the consumer.* The prohibition in §226.36(d)(1) does not apply to transactions in which any loan originator receives compensation directly from the consumer, in which case no other person may provide any compensation to a loan originator, directly or indirectly, in connection with that particular transaction pursuant to §226.36(d)(2). Payments to a loan originator made out of loan proceeds are considered compensation received directly from the consumer, while payments derived from an increased interest rate are not considered compensation received directly from the consumer. However, points paid on the loan by the consumer to the creditor are not considered payments received directly from the consumer whether they are paid in cash or out of the loan proceeds. That is, if the consumer pays origination points to the creditor and the creditor compensates the loan originator, the loan originator may not also receive compensation directly from the consumer. Compensation includes amounts retained by the loan originator, but does not include amounts the loan originator receives as payment for *bona fide* and reasonable third-party charges, such as title insurance or appraisals. *See* comment 36(d)(1)–1.

8. *Record retention.* See comment 25(a)–5 for guidance on complying with the record retention requirements of §226.25(a) as they apply to §226.36(d)(1).

9. *Amount of credit extended.* A loan originator's compensation may be based on the amount of credit extended, subject to certain conditions. Section 226.36(d)(1) does not prohibit an arrangement under which a loan originator is paid compensation based on a percentage of the amount of credit extended, provided the percentage is fixed and does not vary with the amount of credit extended. However, compensation that is based on a fixed percentage of the amount of credit extended may be subject to a minimum and/or maximum dollar amount, as long as the minimum and maximum dollar amounts do not vary with each credit transaction. For example:

i. A creditor may offer a loan originator 1 percent of the amount of credit extended for all loans the originator arranges for the creditor, but not less than $1,000 or greater than $5,000 for each loan.

ii. A creditor may *not* offer a loan originator 1 percent of the amount of credit extended for loans of $300,000 or more, 2 percent of the amount of credit extended for loans between $200,000 and $300,000, and 3 percent of the amount of credit extended for loans of $200,000 or less.

36(d)(2) Payments by persons other than consumer.

1. *Compensation in connection with a particular transaction.* Under §226.36(d)(2), if any loan originator receives compensation directly from a consumer in a transaction, no other person may provide any compensation to a loan originator, directly or indirectly, in connection with that particular credit transaction. *See* comment 36(d)(1)–7 discussing compensation received directly from the consumer. The restrictions imposed under §226.36(d)(2) relate only to payments, such as commissions, that are specific to, and paid solely in connection with, the transaction in which the consumer has paid compensation directly to a loan originator. Thus, payments by a mortgage broker company to an employee in the form of a salary or hourly wage, which is not tied to a specific transaction, do not violate §226.36(d)(2) even if the consumer directly pays a loan originator a fee in connection with a specific credit transaction. However, if any loan originator receives compensation directly from the consumer in connection with a specific credit transaction, neither the mortgage broker company nor an employee of the mortgage broker company can receive compensation from the creditor in connection with that particular credit transaction.

2. *Compensation received directly from a consumer.* Under Regulation X, which implements the Real Estate Settlement Procedures Act (RESPA), a yield spread premium paid by a creditor to the loan originator may be characterized on the RESPA disclosures as a “credit” that will be applied to reduce the consumer's settlement charges, including origination fees. A yield spread premium disclosed in this manner is not considered to be received by the loan originator directly from the consumer for purposes of §226.36(d)(2).

36(d)(3) Affiliates.

1. For purposes of §226.36(d), affiliates are treated as a single “person.” The term “affiliate” is defined in §226.32(b)(2). For example, assume a parent company has two mortgage lending subsidiaries. Under §226.36(d)(1), subsidiary “A” could not pay a loan originator greater compensation for a loan with an interest rate of 8 percent than it would pay for a loan with an interest rate of 7 percent. If the loan originator may deliver loans to both subsidiaries, they must compensate the loan originator in the same manner. Accordingly, if the loan originator delivers the 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.

36(e) Prohibition on steering.

1. *Compensation.* See comment 36(d)(1)–1 for guidance on compensation that is subject to §226.36(e).

Paragraph 36(e)(1).

1. *Steering.* For purposes of §226.36(e), directing or “steering” a consumer to consummate a particular credit transaction means advising, counseling, or otherwise influencing a consumer to accept that transaction. For such actions to constitute steering, the consumer must actually consummate the transaction in question. Thus, §226.36(e)(1) does not address the actions of a loan originator if the consumer does not actually obtain a loan through that loan originator.

2. *Prohibited conduct.* Under §226.36(e)(1), 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.

i. 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. Possible loan offers are available through the loan originator if they could be obtained from a creditor with which the loan originator regularly does business. Section 226.36(e)(1) does not require a loan originator to establish a business relationship with any creditor with which the loan originator does not already do business. To be considered a possible loan offer available through the loan originator, an offer need not be extended by the creditor; it 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 its current rate sheets or other similar means of communicating its current credit terms to the loan originator. An 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.

ii. Section 226.36(e)(1) 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 §226.36(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, §226.36(e)(1) 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 §226.36(d)(1), and compliance with that provision by such a loan originator also satisfies the requirements of §226.36(e)(1) for that transaction with the creditor. 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 §226.36(e)(1) if the originator is compensated for arranging the loan with the other creditor.

iii. See the commentary under §226.36(e)(3) for additional guidance on what constitutes a "significant number of creditors with which a loan originator regularly does business" and guidance on the determination about transactions for which "the consumer likely qualifies."

3. *Examples.* Assume a loan originator determines that a consumer likely qualifies for a loan from Creditor A that has a fixed interest rate of 7 percent, but the loan originator directs the consumer to a loan from Creditor B having a rate of 7.5 percent. 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 §226.36(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.

36(e)(2) Permissible transactions.

1. *Safe harbors.* A loan originator that satisfies §226.36(e)(2) is deemed to comply with §226.36(e)(1). A loan originator that does not satisfy §226.36(e)(2) is not subject to any presumption regarding the originator's compliance or noncompliance with §226.36(e)(1).

2. *Minimum number of loan options.* To obtain the safe harbor, §226.36(e)(2) requires that the loan originator present loan options that meet the criteria in §226.36(e)(3)(i) for each type of transaction in which the consumer expressed an interest. As required by §226.36(e)(3)(ii), the loan originator must have a good faith belief that the options presented are loans for which the consumer likely qualifies. If the loan originator is not able to form such a good faith belief for loan options that meet the criteria in §226.36(e)(3)(i) for a given type of transaction, the loan originator may satisfy §226.36(e)(2) by presenting all loans for which the consumer likely qualifies and that meet the other requirements in §226.36(e)(3) for that given type of transaction. A loan originator may present to the consumer any number of loan options, but presenting a consumer more than four loan options for each type of transaction in which the consumer expressed an interest and for which the consumer likely qualifies would not likely help the consumer make a meaningful choice.

36(e)(3) Loan options presented.

1. *Significant number of creditors.* A significant number of the creditors with which a loan originator regularly does business is three or more of those creditors. If the loan originator regularly does business with fewer than three creditors, the originator is deemed to comply by obtaining loan options from all the creditors with which it regularly does business. Under §226.36(e)(3)(i), the loan originator must obtain loan options from a significant number of creditors with which the loan originator regularly does business, but the loan originator need not present loan options from all such creditors to the consumer. For example, if three loans available from one of the creditors with which the loan originator regularly does business satisfy the criteria in §226.36(e)(3)(i), presenting those and no options from any other creditor satisfies that section.

2. *Creditors with which loan originator regularly does business.* To qualify for the safe harbor in §226.36(e)(2), the loan originator must obtain and review loan options from a significant number of the creditors with which the loan originator regularly does business. For this purpose, a loan originator regularly does business with a creditor if:

i. There is a written agreement between the originator and the creditor governing the originator's submission of mortgage loan applications to the creditor;

ii. The creditor has extended credit secured by a dwelling to one or more consumers during the current or previous calendar month based on an application submitted by the loan originator; or

iii. The creditor has extended credit secured by a dwelling twenty-five or more times during the previous twelve calendar months based on applications submitted by the loan originator. For this purpose, the previous twelve calendar months begin with the calendar month that precedes the month in which the loan originator accepted the consumer's application.

3. *Lowest interest rate.* To qualify under the safe harbor in §226.36(e)(2), for each type of transaction in which the consumer has expressed an interest, the loan originator must present the consumer with loan options that meet the criteria in §226.36(e)(3)(i). The criteria are: The loan with the lowest interest rate; the loan with the lowest total dollar amount for discount points and origination points or fees; and a loan with the lowest interest rate without negative amortization, a prepayment penalty, a balloon payment in the first seven years of the loan term, shared equity, or shared appreciation, or, in the case of a reverse mortgage, a loan without a prepayment penalty, shared equity, or shared appreciation. To identify the loan with the lowest interest rate, for any loan that has an initial rate that is fixed for at least five years, the loan originator shall use the initial rate that would be in effect at consummation. For a loan with an initial rate that is not fixed for at least five years:

i. If the interest rate varies based on changes to an index, the originator shall use the fully-indexed rate that would be in effect at consummation without regard to any initial discount or premium.

ii. For a step-rate loan, the originator shall use the highest rate that would apply during the first five years.

4. *Transactions for which the consumer likely qualifies.* To qualify under the safe harbor in §226.36(e)(2), the loan originator must have a good faith belief that the loan options presented to the consumer pursuant to §226.36(e)(3) are transactions for which the consumer likely qualifies. The loan originator's belief that the consumer likely qualifies should be based on information reasonably available to the loan originator at the time the loan options are presented. In making this determination, the loan originator may rely on information provided by the consumer, even if it subsequently is determined to be inaccurate. For purposes of §226.36(e)(3), a loan originator is not expected to know all aspects of each creditor's underwriting criteria. But pricing or other information that is routinely communicated by creditors to loan originators is considered to be reasonably available to the loan originator, for example, rate sheets showing creditors' current pricing and the required minimum credit score or other eligibility criteria.

Subpart D—Miscellaneous

§226.25 Record retention.

(a) *General rule.* A creditor shall retain evidence of compliance with this regulation (other than advertising requirements under §§226.16 and 226.24) for 2 years after the date disclosures are required to be made or action is required to be taken. The administrative agencies responsible for enforcing the regulation may require creditors under their jurisdictions to retain records for a longer period if necessary to carry out their enforcement responsibilities under section 108 of the act.

(b) *Inspection of records.* A creditor shall permit the agency responsible for enforcing this regulation with respect to that creditor to inspect its relevant records for compliance.

Supplement I to Part 226—Official Staff Interpretations *Section 226.25—Record Retention*

25(a) General rule.

1. *Evidence of required actions.* The creditor must retain evidence that it performed the required actions as well as made the required disclosures. This includes, for example, evidence that the creditor properly handled adverse credit reports in connection with amounts subject to a billing dispute under §226.13, and properly handled the refunding of credit balances under §§226.11 and 226.21.

2. *Methods of retaining evidence.* Adequate evidence of compliance does not necessarily mean actual paper copies of disclosure statements or other business records. The evidence may be retained on microfilm, microfiche, or by any other method that reproduces records accurately (including computer programs). The creditor need retain only enough information to reconstruct the required disclosures or other records. Thus, for example, the creditor need not retain each open-end periodic statement, so long as the specific information on each statement can be retrieved.

3. *Certain variable-rate transactions.* In variable-rate transactions that are subject to the disclosure requirements of §226.19(b), written procedures for compliance with those requirements as well as a sample disclosure form for each loan program represent adequate evidence of compliance. (See comment 25(a)–2 pertaining to permissible methods of retaining the required disclosures.)

4. *Home equity plans.* In home equity plans that are subject to the requirements of §226.5b, written procedures for compliance with those requirements as well as a sample disclosure form and contract for each home equity program represent adequate evidence of compliance. (See comment 25(a)–2 pertaining to permissible methods of retaining the required disclosures.)

5. *Prohibited payments to loan originators.* For each transaction subject to the loan originator compensation provisions in §226.36(d)(1), a creditor should maintain records of the compensation it provided to the loan originator for the transaction as well as the compensation

agreement in effect on the date the interest rate was set for the transaction. See §226.35(a) and comment 35(a)(2)(iii)–3 for additional guidance on when a transaction's rate is set. For example, where a loan originator is a mortgage broker, a disclosure of compensation or other broker agreement required by applicable state law that complies with §226.25 would be presumed to be a record of the amount actually paid to the loan originator in connection with the transaction.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

DIVISION OF CONSUMER
AND COMMUNITY
AFFAIRS

CA 11-3

March 18, 2011

TO THE OFFICERS AND MANAGERS IN CHARGE OF CONSUMER AFFAIRS SECTIONS

SUBJECT: Revised Interagency Examination Procedures for Regulation Z

The Task Force on Consumer Compliance of the Federal Financial Institutions Examination Council recently approved the attached interagency examination procedures for Regulation Z - Truth in Lending. These revised procedures supersede the Regulation Z interagency examination procedures transmitted with CA Letter 11-1.

The attached examination procedures primarily reflect recent revisions to Regulation Z, which implements the Truth in Lending Act. The revisions reflect recently issued final rules that prohibit certain practices related to loan originator compensation. The final rules prohibit loan originators from receiving compensation that is based on the interest rate or other loan terms except the amount of credit extended. The final rules also prohibit a loan originator that receives compensation directly from the consumer from also receiving compensation from the lender or another party. Additionally, loan originators are prohibited from directing or "steering" a consumer to accept a mortgage loan that is not in the consumer's interest in order to increase the originator's compensation.

Another revision in the examination procedures reflects amendments to Regulation Z that implement the appraisal independence provision in the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd Frank Act). These amendments also require that fee appraisers receive customary and reasonable compensation for their services. Finally, the revised procedures implement regulatory amendments that increase the annual percentage rate threshold

used to determine whether a mortgage lender is required to establish an escrow account for first-lien, "jumbo" mortgage loans. This change was also mandated by the Dodd-Frank Act. The above requirements become effective on April 1, 2011.

If you have any questions, please contact David Evans, Senior Supervisory Consumer Financial Services Analyst at (202) 452-2093, or Paul Robin, Manager, Oversight and Policy, at (202) 452-3140.

Sincerely,
(signed)

Sandra F. Braunstein
Director
Division of Consumer and Community Affairs