

# Nationwide Mortgage Licensing System

August 11, 2010  
Costas A. Avrakotos

[www.klgates.com](http://www.klgates.com)

## Nationwide Mortgage Licensing System

“The goal of the Nationwide Mortgage Licensing System is to improve mortgage industry supervision, heighten communication across states, **increase consistency in licensing requirements** and automate processes to the greatest degree possible.”

NMLS Policy Guidebook, January 25, 2010 edition

## ONE SIZE FITS ALL

- One Goal of the NMLS has been to promote Uniformity in the licensing process among the states.
- Uniformity has 3 components.
  - Uniformity in the information required to license an entity through the NMLS;
  - Uniformity in the manner in which the states will apply the requirements of the NMLS;
  - Uniformity in the manner in which licensees satisfy the requirements of the NMLS.
- Information to license an entity will not be the same in each state, so jurisdiction-specific information can be submitted outside the system.
- States are veering away from applying the NMLS requirements uniformly. Will we have uniform system that will be applied in 50+ different ways?



## SPINNING OUT OF CONTROL?

- The NMLS defines control and control person, with the definition of control incorporated into many state licensing laws.
- **CONTROL** = The power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. Any person that (i) is a general partner or executive officer, including Chief Executive Officer, Chief Financial Officer, Chief Operations Officer, Chief Legal Officer, Chief Credit Officer, Chief Compliance Officer, director, and individuals occupying similar positions or performing similar functions; (ii) directly or indirectly has the right to vote 10% or more of a class of a voting security or has the power to sell or direct the sale of 10% or more of a class of voting securities; (iii) in the case of an LLC, Managing Member; or (iv) in the case of a partnership, has the right to receive upon dissolution, or has contributed, 10% or more of the capital is presumed to control that company.
- **CONTROL PERSON** = An individual (natural person) named that directly or indirectly exercises **control** over the applicant.
- Yet, there are multiple uses for the term control, and multiple and inconsistent ways in which state regulators may see or apply the term control.

## CONTROL PERSONS GONE WILD

- State A = Principals of the applicant are considered “control persons.” Principals includes “**management level employees**” and certain contact persons...in addition to officers, directors and direct and indirect owners. Management level employees include **assistant vice presidents** or higher.
- State B = A Control Person is defined to include any person who: (i) is a director, officer, partner, agent, **employee**, or ultimate equitable owner of 10% or more of the applicant or licensee or ii) any individual who directs the affairs or establishes policy for the applicant or licensee.
- State C
  - In one paragraph, State C provides a Control Person is any person who **directly or indirectly** has the right to vote **10%** or more of a class of voting securities or has the power to sell or direct the sale of **10%** or more of a class of voting securities.
  - But in another paragraph, State C states that Natural Persons identified on Form MU1 Schedule B who **indirectly own 25%** or more of the applicant meet the definition of “Control Persons”.

- An applicant cannot move forward through the NMLS with its submission unless a company owner that owns 10% or more of the applicant is listed as a control person.
- Some states insist that company owners of an applicant or licensee be marked as control persons despite written guidance that only natural persons are control persons.
- A couple of states recently have insisted that the Contact Employee be a Control Person. Different Contact Employees cannot be identified for different states. The Guidebook provides that the Contact Employee does not need to be a decision maker.

- Some states require the Qualified Individual to be identified as a Control Person.
- States impose inconsistent requirements as to the current employer of Control Persons.
- Often Directors of licensees meet the definition of Control Person, yet are not employees of the licensee.
- In completing the employment history of Form MU2, the majority of the states have the Control Person identify the current employer, while the person's involvement with the licensee is entered in the Other Business section.
- Some states, however, want the name of the licensee be entered as the current employer of such Control Person, despite being incorrect.

## CHANGE IN OFFICERS = CHANGE IN CONTROL

- As set forth above, control is defined to include a general partner, certain titled executive officers, or directors.
- One state has taken the position that, given the definition of control, a mere change in officers or directors requires the licensee to make the licensing statute's formal change of control filing.
- Will other states be following this lead?

## **DOES CONTROL OF A SUBSIDIARY MAKE IT AN OWNED AND CONTROLLED SUBSIDIARY?**

- Some states provide an exemption from mortgage lender or broker licensing for a subsidiary that is owned and controlled by a depository institution.
- Over 40 states provide an exemption from mortgage loan originator licensing for an employee of an owned and controlled subsidiary of a depository institution who is registered through the NMLS.
- State statutes do not define “owned and controlled” for purposes of identifying this subsidiary.
- Is a licensee that is controlled by company as defined in the NMLS and under many state laws, an owned and controlled subsidiary?

## DEFICIENT UNTIL PROVEN INNOCENT

- There is no uniformity in the manner in which states use the deficiency features.
- The deficiency feature is used in a manner that is not intended to process a new or renewal license application.
- For example:
  - States post deficiency items to "provide information from the checklist" before the 5 day window to submit the documentation has expired;
  - States place a licensee or applicant in deficient status without listing deficiencies;
  - States do not clear deficiency items, or update them often;
  - States do not use the deficiency list in NMLS, but rather mail a letter to licensees to request outstanding documentation;
  - States do not provide contact information to clear a deficiency;
  - States use the deficiency list to post notice of consumer complaints.

## I ATTEST

The NMLS provides that for “Choosing Your Account Administrators,” the Primary Account Administrator is a person of the company’s choosing that will have full access to the company’s record on the NMLS and will be able to fill out and submit a complete company record to any state mortgage regulator. The Primary Account Administrator does not need to be an officer, but may be an employee of your company.

- Many licensees appoint the licensing manager who facilitates the initial application, renewal, annual report filings and any change notifications for all licenses and registrations maintained by an entity as the Primary Account Administrator.

Recently, a few states are requiring the individual who attests to the NMLS filing to be a control person and submit an MU2.

- Submission of an MU2 subjects individuals who are not control persons to personal disclosure filings in states in which they would not be subject to a filing.
- Enforcing the requirement that a control person submit filings severely limits the ability of the licensing manager to perform the tasks for which he or she was hired.

## I CANNOT ATTEST

- The corporate attestation that must be submitted with every change in a licensee's NMLS record provides, among other certifications, that "to the extent any information previously submitted is not amended, such information remains accurate and complete."
- Given the inconsistent manner in which defined terms are applied by the states, undoubtedly some of the attestations being made are not accurate.
- There are certain circumstances when a change in an NMLS record is required, and such an attestation cannot be made in good faith.

## WELCOME TO OZ

### -- Limited Transparency In The Making Of Policy And Practice Decisions

- An underlying and ongoing concern is the issue of transparency in the manner in which policy is established and decisions are made in the NMLS.
- Industry participates in monthly IDWG conference calls with CSBS representatives, and states may have their weekly calls.
- However, ultimately policy and decisions affecting the entire system and all the states are made by a small Working Group of regulators.
- Industry can communicate their concerns to CSBS and IDWG, which supposedly reaches this Working Group, but industry cannot voice their concerns directly to the Great Oz behind the screen.
- State regulators who are advocating certain positions, and the manner in which decisions are being made should be made public.

## RULES TO LIVE BY

- There is no record of the policy decisions and rules that have been implemented over the years.
- The requirements have changed from what had been agreed when the NMLS was first being developed and from earlier versions of the Guidebook.
- There should be a reasoned basis as to why a change in existing requirements or established practices is warranted, and it should be discussed with the industry
- States refer to the Guidebook when convenient, or provide that we cannot rely on the information in the Guidebook when convenient.

## **FOLLOW THIS PATH**

### **-- Reliance On The Direction Provided By CSBS**

- Users have relied on the helpful direction provided by CSBS as to what information is required, how to answer certain NMLS questions, or how to apply provisions in the Guidebook.
- Some state regulators refuse to accept the answer or guidance of CSBS.
- Licensees need to know that when they obtain direction from the administrators of the NMLS, they can rely on that information.
- The Ombudsman role has been created to handle certain situations, but a question cannot be posed to the Ombudsman each time it requires a simple interpretative answer or clarification of a policy.
- If a question has broader policy implications that need to be considered by the state regulators working group, then industry should be able to voice its concerns directly to the working group.

## MY WAY OR NO WAY

### -- Authority Of A State To Compel A Licensee To Enter Information In The NMLS When Other States Do Not Impose The Requirement

- In an increasing number of situations, one state is insistent that certain information be entered into the NMLS when other states do not require such.
- This has arisen when a state has required:
  - A less than 10% indirect owner to be disclosed
  - A person to be identified as a control person
  - An enforcement matter to be disclosed.
- Complying with the demands of one state to enter something into a licensee's NMLS record would trigger notices and explanations to other states.
- Industry has been instructed that if one state requires a filing, it can be handled like other jurisdiction specific information, and be submitted outside the system.
- If there is to be a uniform mechanism for licensing companies, one state should not be permitted to impose its will as to what must be submitted in the NMLS over that which has been found by the other states as generally acceptable.

## TRUE CONFESSIONS

### -- Sanctions Reporting

- Uncertainty exists and an inordinate amount of time is spent, in trying to determine when different sanctions or administrative actions need to be reported through the NMLS. The definitions of certain terms help in understanding when certain matters need to be disclosed, but other terms are left open to speculation.
- Some licensees will spend the time parsing out the language to determine if a matter needs to be disclosed, others may disclose every regulatory issue that arises in an exercise of caution.
- Licensees who make a reasoned determination that a matter does not need to be reported should not be subject to sanctions by a state regulator who subsequently decides that an issue needs to be reported.
- For the system to be uniform, then the NMLS reporting obligations for sanctions or administrative actions should govern, and state laws and regulations that separately impose reporting obligations for sanctions or administrative action should not apply.
- There should be a materiality standard as to what sanctions or administrative actions must be reported.

## ONCE SHOULD BE ENOUGH

### -- Duplicative NMLS and State Filing Obligations

- As a matter of state law, certain annual or license maintenance filings are required, which filings are also required or will be required through the NMLS. If an entity satisfies the NMLS filing obligation, the statutory/regulatory filing should be satisfied.
  - If a licensee meets the sanctions and litigation reporting obligations of the NMLS, the licensee should not be subject to a separate state filing obligation.
  - If the NMLS adopts a company-level call report requirement, containing the loan level information in the proposed call report requirement, then the licensee should not be subject to separate state annual loan level reporting obligations that ask for the same information.

## LOST BETWEEN TWO WORLDS

### -- Licensing Of Individuals Who Are NOT Required To Register As MLOs, Or Who Cannot Yet Register Under The Rules Of The Federal Banking Agencies

- Federal banking agencies having adopted rules to provide for the registration of the mortgage loan originator employees of FDIC-insured depository institutions, and of their owned and controlled subsidiaries.
- Registration cannot begin until next year, which for most states is after the effective date of the state's mortgage loan originator licensing obligation.
- Employees of banking agency regulated institutions engaged in loan modification activities will not be required to register as MLOs.
- The federal banking agencies have indicated that employees of their regulated institutions for SAFE Act purposes are subject to the banking agencies MLO registration rules and are not subject to state licensing.
- States should not seek to assert authority over, and require mortgage loan originator licensing of, the employees of these institutions subject to the banking agencies rules.

## LICENSING EXEMPT ENTITIES

- Exempt Entities should not be compelled to file in the same manner as licensees through the NMLS, so as to be listed or registered on the NMLS and/or to sponsor their mortgage loan originators who may need to be licensed.
- Entities not subject to licensing, such as mortgage loan servicers in some states, should not be subject to licensing through the NMLS to sponsor employees who need to be licensed as mortgage loan originators in the state to conduct loan modification activities.



**Costas A. Avrakotos**  
**K&L Gates LLP**  
**1601 K Street NW**  
**Washington, DC 20006-1600**  
**(202) 778-9015 Telephone**  
**(202) 778-9100 Facsimile**  
[Costas.avrakotos@klgates.com](mailto:Costas.avrakotos@klgates.com)  
[www.klgates.com](http://www.klgates.com)