

LENDERS UPDATE™

A MONTHLY SERVICE TO THE MORTGAGE LENDING INDUSTRY

AN ALT & ASSOCIATES NEWSLETTER

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SURPRISING TESTIMONY ON LOAN ORIGINATOR COMPENSATION

Over the last 6 months, as part of the introduction and implementation of the new Federal Reserve Board rule for payments of compensation to loan originators, one of the most controversial and it would seem, most difficult to understand, are the rules related to payments made to a broker's loan officer employees when the consumer has paid the broker its compensation, so called "borrower paid" compensation.

The commentary on the Loan Originator Compensation Rule states (for simplicity we paraphrase);

If any loan originator receives compensation directly from the consumer, no other person may provide any compensation to the loan originator, directly or indirectly in connection with that particular credit transaction. These restrictions 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 salary or hourly wage, which is not tied to a specific transaction, do not violate this restriction even if the consumer directly pays the loan originator a fee in connection with a specific credit transaction. If any loan originator receives compensation directly from the consumer in connection with a specific credit transaction, neither the mortgage broker company nor the employee of the mortgage broker company can receive compensation from the creditor in connection with that particular transaction.

Based on this commentary, the loan originator compensation rule has been construed to prohibit payments of commissions to loan officer employees of a mortgage broker when the consumer pays the broker's commission. In the Fed's own words, only salary and wages are permissible.

However, in the world of smoke and mirrors, sometimes things can change. As many of you know, the House of Representatives Sub-Committee on Insurance, Housing and Community Opportunity Committee on Financial Services, held hearings yesterday on mortgage origination regulations and the "impact of recent changes on homeowners and businesses". Sandra Braunstein, Director of Consumer and Community Affairs for the Board of Governors of the Federal Reserve System, testified and as part of that testimony she stated as follows:

"Second, for consumer-pay transactions, the final rule states that if the consumer directly compensates a loan originator, compensation may not be paid to a loan originator by any other person in connection with the transaction. This provision addresses the problem that loan originators were frequently compensated by both the consumer and the creditor in a manner that was not transparent to consumers and that could lead consumers to believe, wrongly, that by paying a loan originator directly, the loan originator would work on their behalf to find the most favorable loan. One consequence of this prohibition is that in consumer-pay transactions, a mortgage brokerage firm that is paid directly by the consumer may not pay a commission specific to that transaction to its loan officer. Because the restriction only covers payments that are specific to the particular transaction, a

brokerage firm that is paid by the consumer directly can still provide its loan officers with incentive compensation (in addition to salaries or hourly wages) without violating the rule.” [emphasis added]

This portion of the testimony contains a footnote that states:

“The Board believed it was necessary to prohibit a brokerage firm from sharing the consumer-paid compensation with its loan officer to prevent the loan officer from influencing whether the firm's compensation will be paid by the creditor or directly by the consumer and, therefore, potentially steering consumers to more expensive transactions. This could occur because in a "creditor-pay" transaction, the loan originator cannot be paid on the basis of the loan's rate or other terms (except the amount of the loan), so the amount of compensation the loan originator may receive is fixed in advance and not negotiated with the consumer. However, this limitation does not apply in a "consumer-pay" transaction, where a loan originator can negotiate any compensation amount that the consumer will accept. Under the Board's rule a loan officer does not receive a portion of the compensation paid directly by the consumer, which eliminates the incentive for steering consumers to a "consumer-pay" loan that is more expensive.”

An additional footnote states:

“For example, a brokerage firm could pay bonuses to loan officers who exceed a threshold number of loans within a specified period.”

What is the basis for this gratuitous comment? The Loan Originator Compensation Rule has now reached a new high in the art of reading tea leaves. You can't pay a commission to a loan officer in this situation but wait a few weeks or months, and then pay a commission and label it a volume bonus. Please!! For those of you familiar with “point banks” and the prohibition of them by the Fed, what is the distinction here?

Without further clarification or authority, we suggest caution in following Braunstein's comments .

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