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OVERVIEW

Franklin American Mortgage Company (FAMC) purchases loans that are in compliance with the requirements of the Truth in Lending Act for Loan Originator Compensation (TILA-LO Comp). TILA-LO Comp applies to all closed-end real estate secured transactions.

Prior to the original April 1, 2011 effective date, the National Association of Mortgage Brokers and National Association of Independent Housing Professionals filed a motion for emergency relief to delay the implementation of the TILA-LO Comp. The United States Court of Appeals for the District of Columbia denied the emergency motion.

Due to the delay caused by the motion for relief, the TILA-LO Comp is effective as follows:

- Applications dated between April 1, 2011 and April 5, 2011 (inclusive) could be under the prior or new compensation plan; and
- Applications dated on and after April 6, 2011 must be under the new compensation plan.

Additional requirements under TILA-LO Comp became effective January 1, 2014 and January 10, 2014.

BACKGROUND

On September 24, 2010 the Federal Reserve Board issued a final rule implementing changes to the Truth in Lending Act (TILA) for Loan Originator Compensation. The final rules protect mortgage borrowers from unfair, abusive, or deceptive lending practices that can arise from loan originator compensation practices. On January 20, 2013, the Consumer Finance Protection Bureau (CFPB) issued a new rule to implement amendments to the Truth in Lending Act made by the Dodd-Frank Act, implementing requirements and restrictions imposed by the Dodd-Frank Act on loan originator compensation. This rule was also revised on May 29, 2013 and September 13, 2013.
The rule applies to all persons who originate loans, including mortgage brokers and the companies that employ them, as well as mortgage loan officers employed by depository institutions and other lenders.

Loan Originator Definition

For purposes of TILA § 1026.36(a)(1), “Loan Originator” is defined as an organization or individual that for compensation or other monetary gain performs loan origination activities, such as

- Taking an application
- Arranging a credit transaction
- Assisting a consumer in applying for credit. Assisting a consumer in obtaining or applying for credit by advising on particular credit terms that are or maybe available to the consumer based on the consumer's financial characteristics.
- Offering or negotiating credit terms. Credit terms include fees and other costs.
- Making an extension of credit.
- Referring a consumer to a loan originator. Referring is an activity included under each of the activities of offering, arranging, or assisting a consumer in obtaining or applying to obtain an extension of credit.

- Advertising or communicating to the public that you can or will perform any loan origination services.

This regulation:

- Prohibits payments to the mortgage broker or loan originator that are based on the loan's interest rate or other terms as well as a proxy to the terms or conditions of a loan.
- Permits certain methods of compensating loan originators using bonuses, retirement plans, and other compensation plans that are based on mortgage-related profits.
- Prohibits mortgage brokers or loan originators in a transaction from being compensated by both the consumer and another person, such as a creditor.
- Prohibits a mortgage broker or loan officer from "steering" a consumer to a lender offering less favorable terms in order to increase the broker's or loan officer's compensation. Note that the provision does provide a safe harbor to facilitate compliance with the anti-steering rule if certain provisions are met. The safe harbor is met if:
    - The consumer is presented with loan offers for each type of transaction in which the consumer expresses an interest (that is, a fixed rate loan, adjustable rate loan, or a reverse mortgage); and
    - The loan options presented to the consumer include the following:
        - The lowest interest rate for which the consumer qualifies (note rate);
        - The lowest origination points or fees and discount points, and
        - The lowest rate for which the consumer qualifies for a loan with no risky features, such as a prepayment penalty, negative amortization, or a balloon payment in the first seven years.
- Imposes qualification rules for loan originators and mandates that the entity employing the loan originator ensure they are qualified and meet licensing and/or registration requirements.
- Requires the entity and loan officer NMLS ID on specific loan-related documents.

Compensation Overview

Compensation generally includes salaries, commissions, and any financial or similar incentive including bonuses, awards of merchandise, service, trips, or similar prizes.

Compensation may not be paid to or received by a loan originator if it is based on:

- A term of an individual transaction by the individual loan originator,
- The terms of multiple transactions by the individual loan originator,
- The terms of multiple transactions by multiple loan originators.

Additionally, the loan originator's compensation cannot be based in whole or in part of a factor that is a proxy for a term of the transaction. A proxy is a term of a transaction if:

- The loan originator has the ability (directly or indirectly) to add, drop, or change the factor in originating the transaction, and
- The factor consistently varies with that term over a significant number of transactions.

Prohibited compensation examples, include, but are not limited to:

- Compensation based on the loan's interest rate;
- Higher compensation for loans with a prepayment penalty; and
- Higher compensation if a certain number of loans have a higher interest rate.

The rule provides for seven safe harbor methods to compensate loan originators with respect to the payment of salary, commissions, and other compensation. Compensation paid or received using the following are not based on terms or proxies for transaction terms:

1. The loan originator's overall dollar volume (total amount of credit extended or total number of transactions originated).
2. The long-term performance of the loans.
3. An hourly rate based on the actual number of hours worked.
4. Loan made to new borrowers versus existing customers.
5. A payment that is fixed in advance for every loan the originator arranges for the creditor. (Example - $500 for every loan of $1000 for the first 100 loans and $500 for the next 50 loans.)
6. The percentage of the applications that close.
7. The quality of the loan files, which may include accuracy and completeness submitted to the creditor.

Note: This is not an all-inclusive list.
A loan originator generally may not receive compensation based on profits from a mortgage-related business but may receive compensation in the form of a bonus that is not based on profits. For example, a creditor may have a contract with the loan originator employee that guarantees a quarterly bonus if the monthly origination volume target is met. Additionally, an employer may structure retirement and bonus plans in ways that do not violate the requirements provided it is not based on the loan originator's transactions. Bonuses and other not per-loan compensation cannot exceed a 10% threshold of the loan originator's overall compensation.

Compensation Agreements

Three types of compensation agreements are necessary to meet the requirements of the rule:

1) Creditor/Retail Loan Officers. A creditor (lender with a warehouse line) must have an agreement with each employee loan officer it compensates;

2) Creditor/Broker (including a broker company.) The creditor must have an agreement with each broker whose compensation is paid by any party other than the borrower.

3) Broker/Broker Loan Officer. The broker must have an agreement with each loan officer attached to their license.

The compensation agreements include a compensation formula that must be followed whenever the agreements are required to be utilized. The compensation formula cannot be based on any of the terms of the loan, except loan amount.

Compensation Methods

There are two (2) types of compensation methods:

- Borrower paid
- Lender paid

Retail Transactions	Wholesale Transactions
The compensation method will always be lender paid.	The borrower and broker will discuss and determine if the method of compensation for the loan will be borrower paid or lender paid.

Borrower Paid Compensation Methods

The compensation is negotiated directly between the borrower and the loan originator or broker and no compensation will be paid to the broker from any other source.

The borrower must pay the broker in cash or by financing the amount into the loan; however, a Seller Contribution can be utilized to pay all or part of the negotiated broker compensation.

This fee will be documented as an origination fee, is considered an APR fee, and is included in the points and fees high costs calculation where applicable.

All loan feature and product price adjustments will be applied to the borrower premium pricing credit, if applicable. Any premium pricing credit given to the borrower based on the interest rate selected may not be used to pay the broker compensation but may be used for bona fide third party closing costs.

Bona fide closing costs are those costs typically associated with closing a loan paid to third parties which include but are not limited to:

- Appraisal
- Attorney
- Processing
- Settlement
- Title
- Prepaid Items (Escrow, insurance, etc.)

If the rate selected includes bona fide discount points, the borrower will pay those to the lender at closing. A Seller Contribution can be utilized to pay bona fide discount points.

Lender Paid Compensation Methods
The loan originator or broker receives compensation directly from the lender at a pre-determined level as outlined in an executed Compensation Agreement. A loan originator or broker may not credit any portion of their compensation to the borrower.

This will be documented as "Compensation" and is not considered an APR fee and is included in the points and fees high costs calculation where applicable.

All bona fide third party closing costs must be paid by the borrowers in cash, financed into the loan, or paid by the credit for premium pricing based on the interest rate chosen.

Bona fide closing costs are those costs typically associated with closing a loan paid to third parties which include but are not limited to:

- Appraisal
- Attorney
- Processing (must be a valid 3rd party fee)
- Settlement
- Title
- Prepaid Items (Escrow, insurance, etc.)

Fees cannot be collected from any other source.

Loan Originator Qualifications
The loan originator organization must obtain criminal background checks, credit reports, and information about administrative, civil or criminal findings by any government jurisdiction on individual loan originator employees.

Information on Loan Documents
For all covered loans, the loan originator and loan originator organization must include identification type information on certain loan documents, which include:

- The credit application (1003);
- The promissory note; and
- The Security Instrument.

The information must be provided whenever the loan document is provided to the consumer. The information includes:

- NMLS ID; and
- Name of the individual loan originator as provided in the NMLSRNML.

NOTE: If the loan originator changes prior to close, new documents reflecting the revised information must appear.
Additionally, state-specific documents may require the NMLS information to be included as well.

FAMC CORRESPONDENT REQUIREMENTS - ALL CORRESPONDENTS

Covered Transactions

This requirement will apply to all real estate secured transactions including investment properties.

Yearly TILA-LO Compensation Attestation and Certification

On a yearly basis, each approved Correspondent will review the FAMC Correspondent TILA-LO Compensation chapter, have the applicable officer sign the Yearly Compliance Attestation & Certification stating they have read and understood the requirement and trained their staff accordingly, and an attestation affirming they are following all applicable requirements of FAMC and their own internal policies and procedures.

FAMC will not initially require policy and procedure documentation from the Correspondent but will reserve the right to request and review the policies and procedures that a lender follows to ensure compliance with loans originated and sold to FAMC. Upon written request and as outlined in the Correspondent Lending Agreement, the lender must provide the information in a timely manner. Failure to adhere to this request could result in termination.

FAMC CORRESPONDENT REQUIREMENTS – WHOLESALE TRANSACTIONS

Required Loan Specific Disclosure

- Broker Compensation Acknowledgement & Agreement – This form must be signed and dated by broker and borrower. Borrower must clearly identify if they chose a Borrower Paid or Lender Paid option. Correspondents can use a different version of the document provided it contains a clearly defined compensation method chosen by the borrower and the form is signed and dated by the borrower and broker.
- Anti – Steering / Safe Harbor Disclosure – This form is required on broker originated loans in which the loan officer is being paid by the lender (Lender Paid option) and must be signed and dated by the broker and borrower. The form must contain loan options for the products the borrower has expressed interest in. FAMC will not allow the same loan option to be disclosed to the borrower in order to meet the requirements of the Anti-Steering Disclosure. Disclosing only one option to the borrower could equate to steering and thus nullify the Safe Harbor. The options must include a loan:
  - With the lowest note interest rate,
  - With the lowest interest rate and which does not contain negative amortization, a prepayment penalty, an "interest only" feature, a balloon payment in the first 7 years, a demand feature, shared equity/appreciation; or, for a reverse mortgage, a loan without a prepayment penalty or shared equity/appreciation, and
  - The lowest total dollar amount of origination points/fees and discount points.

  Correspondents can use a different version of the document provided it contains the same information outlined above and the form is signed and dated by the borrower.

Required File Documentation

In addition to loan level disclosures, additional file documentation is required. The loan file will be reviewed to ensure the compensation is structured properly based on the selection method:

Borrower Paid	Lender Paid
• Documented on the fee sheet as origination, processing, etc. • Paid by the borrower in cash or financed into the loan amount on a refinance transaction. Compensation cannot be from premium pricing. • If there are Seller Paid Concessions, it must be clearly documented that Seller is paying all or part of the broker compensation. • Is included in the APR • Is included in any high cost calculations (where applicable)	• Documented as broker compensation on the fee sheet. • Is not included in the APR • Is included in any high cost calculations (where applicable)

Also, third party fees will be reviewed based on the compensation method:

Borrower Paid	Lender Paid
• Processing fee may be charged by the broker without an invoice. • Fees can be charged by an affiliate of the broker as listed on the Affiliated Business Arrangement Disclosure.	• Processing fee must be a valid 3rd party with appropriate invoice. • No third party fee may be charged by an affiliate of the broker as listed on the Affiliated Business Arrangement Disclosure.

NOTE: All fees charged must be in compliance with FAMC TILA.

Excess Premium Pricing

After all applicable and allowable fees have been paid any remaining premium pricing cannot cause a regulatory violation and must be in compliance with current product and underwriting guidelines.

On a borrower paid transaction, remaining premium pricing cannot exceed product or underwriting guidelines.

On a lender paid transaction any remaining premium would be a violation and the loan cannot be purchased.

Switching Compensation Methods

Compensation methods can be changed if the borrower decides to switch their selected compensation method. The switch must be based on a valid changed circumstance under TRID and still comply with the rule.

FAMC CORRESPONDENT REQUIREMENTS – RETAIL TRANSACTIONS

For retail transactions, the FAMC Correspondent division will review the Closing Disclosure and any other necessary documents to ensure there is no evidence of the borrower paying the Loan Originator directly instead of the Loan Originator's company. Retail transactions in which the borrower paid the Loan Originator directly will not be eligible for purchase.