

***MBA LEGAL ISSUES IN MORTGAGE TECHNOLOGY
ARIZONA BILTMORE RESORT & SPA
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***Legal Overview and Updates
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I. RESPA

A. Scope

1. RESPA applies to federally related mortgage loans.
2. The term “federally related mortgage loans” is broadly defined to include:
 - a. First lien purchase money loans.
 - b. First lien refinance loans.
 - c. Junior lien loans, including home equity credit lines.
 - i. Home equity credit lines are exempt from various RESPA requirements.

B. Disclosures

1. Time of application disclosures:
 - a. Good Faith Estimate of Settlement Costs.
 - i. Discloses estimates of settlement charges that the loan applicant is likely to incur in connection with the loan settlement.
 - ii. If the lender will require the use of certain settlement service providers selected by the lender, additional disclosures must be included.

- iii. Must be placed in the mail or delivered to the loan applicant within three business days after the application is received or prepared.
 - iv. A Good Faith Estimate is not required for home equity credit lines if the Truth in Lending Act home equity disclosures are provided.
 - v. Often a lender's loan processing system will use information on charges entered into the system to prepare a Good Faith Estimate to calculate the Truth in Lending Act disclosures.
- b. Special Information Booklet.
- i. A HUD issued booklet describing the home purchase, financing and settlement process.
 - ii. Must be placed in the mail or delivered to the loan applicant within three business days after the application is received or prepared.
 - iii. A Special Information Booklet is required only for first lien, purchase money loans.
- c. Servicing Disclosure Statement.
- i. A statement regarding the potential for the servicing of the loan to be transferred to another party.
 - ii. Delivery requirements vary based on how the application is taken.
 - A. For cases in which there is a "face-to-face" interview, the statement must be delivered at the time of application.
 - B. If there is no face-to-face interview, the statement must be placed in the mail within three business days from receipt of the application.
 - iii. The statement must be acknowledged by each applicant.
 - iv. A servicing disclosure statement is not required for home equity credit lines subject to the Truth in Lending Act or for junior lien loans.
 - v. RESPA requires only a simple statement of whether the servicing for the loan may be assigned, sold or transferred. Regulation X still reflects the prior RESPA requirement to provide much more detailed information. In 1997, HUD proposed amending

Regulation X to reflect RESPA, but has not finalized the amendment.

2. Definition of application:

- a. The submission of a borrower's financial information in anticipation of a credit decision, whether written or computer generated.
- b. If the submission does not state or identify a specific property, the submission is an application for a pre-qualification and not an application for a federally related mortgage loan.
- c. The federal Truth in Lending Act follows the RESPA definition of application for purposes of the requirement to provide an initial, estimated Truth In Lending disclosure statement in connection with an application for a loan to purchase or construct a consumer's primary residence.
 - i. Like the Good Faith Estimate under RESPA, the initial, estimated Truth in Lending disclosure statement must be delivered or placed in the mail not later than three business days after the creditor receives the consumer's written application.

3. Closing Disclosures.

- a. HUD-1 or HUD-1A Settlement Statement.
 - i. Discloses the actual settlement charges incurred in connection with the settlement, and any other charges incurred at settlement.
 - ii. The HUD-1A version may be used when there is only a borrower. The HUD-1 must be used when there is a buyer/borrower and a seller, and may be used when there is only a borrower.
 - iii. A Settlement Statement is not required for home equity lines of credit subject to the Truth in Lending Act.
 - iv. While the closing agent is responsible under RESPA to prepare the Settlement Statement, lenders have a significant interest in the preparation of the Statement.
 - A. Typically a lender's loan processing system will use information on charges to be disclosed in the Settlement Statement to calculate the final Truth in Lending Act disclosure items.

of your relationship with the affiliate, reflects that the consumer is not required to use the affiliate (except in certain cases), and summarizes the charges of the affiliate.

- b. The general delivery rule is that with a face-to-face referral or referral made in writing or by electronic media, the affiliated business arrangement notice must be provided at or before the time of the referral to the affiliate.
- c. A lender that makes a referral to an affiliate may provide the notice at the time that the lender provides the Good Faith Estimate.
- d. In the case of a referral made by telephone, (i) the consumer must be advised of the affiliation over the phone and informed that a written affiliated business arrangement notice will be provided, and (ii) a written notice must be provided within three business days.

C. Application to the Internet

- 1. For the most part, the Internet is a foreign concept in the RESPA world.
 - a. Other than the electronic media reference in connection with the affiliated business disclosure requirements, there are no express provisions regarding the delivery of the various RESPA disclosures electronically.
 - b. There are no Internet exceptions under RESPA.
 - c. There also is no special definition of an application for purposes of the Internet.
- 2. Both in the Internet environment, and outside of the Internet, companies struggle with the definition of an application with regard to the triggering of initial disclosures.
 - a. If a consumer submits financial information in anticipation of a credit decision, and the submission states or identifies a specific property, an application exists for RESPA purposes, and Truth in Lending Act purposes.
 - b. Current technology and consumer shopping practices team up to present issues.
 - i. When a consumer calls to ask about loan products and prices, by asking a few questions and using technology to instantly access consumer credit information, you can respond to the consumer

based on his or her credit position. But in obtaining the information, do you trigger the need to issue initial disclosures?

- ii. You can use a website to provide information about loan products and prices. If the website will provide more precise information if the consumer enters certain credit-related information, do you trigger the need to issue initial disclosures?
3. Look to ESIGN and UETA for authority to deliver disclosures electronically.

D. Section 8 Background

1. RESPA Section 8 prohibits the giving or receipt of any thing of value for the referral of settlement service business.
 - a. A settlement service includes various real estate transaction-related services, such as mortgage loan services, real estate brokerage services and title services.
 - b. A “referral” includes any oral or written action directed to a person that has the effect of affirmatively influencing the selection by any person of a settlement service provider.
 - c. A “thing of value” is broadly defined and no actual transfer of money is required for a thing of value to exist.
2. RESPA Section 8 also prohibits the splitting of a settlement service fee, other than for services provided.
3. RESPA Section 8 does not prohibit payments to any person that reflect the reasonable value of services, goods or facilities provided by the person.
4. HUD interprets the RESPA fee splitting prohibition to prohibit all unearned fees, including but not limited to cases in which:
 - a. Two or more persons split a fee for settlement services, any portion of which is unearned.
 - b. One settlement service provider marks-up the cost of services performed or goods provided by another settlement service provider without providing additional actual, necessary and distinct services, goods or facilities to justify the additional charge (HUD’s mark-ups position).
 - c. One service provider charges the consumer a fee where no, nominal or duplicative work is done, or the fee is in excess of the reasonable value of

goods or facilities provided or the services actually performed (HUD's overcharges position).

5. United States Circuit Courts of Appeal have rejected HUD's position on overcharges, but HUD's position regarding mark-ups has met with mixed results.

a. The Scorecard:

i. The Fourth, Seventh and Eighth Circuit Courts of Appeals have found that mark-ups do not violate the fee splitting prohibition.

ii. The Second and Third Circuit Courts of Appeals have found that the mark-ups violate the fee splitting prohibition, if not supported by services.

iii. The Eleventh Circuit, although ruling for the defendants in a case, noted that a single settlement service provider can violate the fee splitting prohibition and, thus, appeared to indicate that mark-ups violate the fee splitting prohibition if not supported by services.

iv. The Seventh Circuit also found that an impermissible fee split may exist when both the lender and the closing agent imposed a release fee on the borrower.

b. States Within The Jurisdiction of the Courts of Appeals:

i. Second Circuit: Connecticut, New York and Vermont.

ii. Third Circuit: Delaware, New Jersey, Pennsylvania and the Virgin Islands.

iii. Fourth Circuit: Maryland, North Carolina, South Carolina, Virginia and West Virginia.

iv. Seventh Circuit: Illinois, Indiana and Wisconsin.

v. Eighth Circuit: Arkansas, Iowa, Minnesota, Missouri, Nebraska, North Dakota and South Dakota.

vi. Eleventh Circuit: Alabama, Florida and Georgia.

6. Related TILA Issue.

a. Under the Truth in Lending Act and Regulation Z, in a mortgage loan transaction certain fees are excluded from the finance charge if they are bona fide and reasonable in amount.

- b. The fees include credit report fees, appraisal fees, loan-related document preparation fees and title examination fees.
 - c. If a party marks up one of the fees, does the entire fee still qualify for exclusion from the finance charge? Is the fee still reasonable?
7. Related State Law Issues.
- a. States typically limit the fees that may be imposed on a borrower, and various state regulators take the position that a mortgage company may pass on to a consumer only the actual charge imposed by a third party service provider.
 - b. States also have unfair and deceptive practice and related laws. Disclosing to a consumer that a third party charge is higher than the actual charge presents issues under such laws.
 - c. In September 2006 a California appellate court, in the case of *McKell v. Washington Mutual, Inc.*, addressed alleged mark-ups of third party fees by a lender.
 - i. The court determined that the borrowers properly alleged claims under the California Unfair Competition Law (UCL) in challenging the lender's imposition of charges for third party services that exceeded the actual cost of the services, with no indication to the borrowers of such mark-ups.
 - ii. Specifically, the court determined that the challenged conduct may constitute a deceptive practice within the meaning of the UCL, would be an unfair business practice under the UCL, and would be an unlawful business practice under the UCL.
 - iii. The unlawful business practice determination is based on the court's conclusion that the mark-up practice would violate RESPA. Thus, the California court sided with the federal appellate courts that believe mark-ups violate RESPA Section 8.

E. HUD Informal Advice on Lead Sale

- 1. Does compensating a party for providing leads constitute a payment for services or goods, or a referral fee or fee split?
- 2. HUD has advised informally that a settlement service provider can pay another party for leads.

- a. In a March 1994 informal interpretation, HUD advised that a settlement service provider could pay a party for a list of prospects, provided that the payment was for the use of the list, and not conditioned on the number of closed transactions or any other consideration, such as an endorsement of the provider's product by the seller of the list.
3. No HUD guidance specifically on Internet programs.
4. Enforcement action, with few facts.
 - a. A July 2003 settlement agreement with World Savings addressed a "For Services Rendered" program in which HUD alleged that World Savings compensated real estate agents for the online completion and submission of loan applications through a World Savings website. HUD alleged that the arrangement involved the compensation of real estate agents by World Savings for the referral of business in violation of the RESPA referral fee prohibition. World Savings denies any violation of RESPA Section 8.
 - b. The settlement agreement does not provide much detail regarding the specific services provided by the agents.
 - c. However, the settlement agreement provides that if World Savings desires to continue the program, it must do so consistent with RESPA, Regulation X, and HUD Policy Statements, and all compensation paid to agents must be reasonably related to the value of goods, facilities or services actually furnished or performed.
 - i. The Policy Statement reference reflects that HUD believes the program must comply with the 1999-1 and 2001-1 HUD Policy Statements on the compensation of mortgage brokers by lenders.
 - ii. Pursuant to the Policy Statements, which are addressed below, a mortgage broker must provide a minimum level of services, goods and facilities to receive any compensation from a lender, and the total compensation received by the mortgage broker must be reasonable in relation to the value of the services, goods and facilities provided by the broker, ignoring any referral value.

F. Basic Lead Sale Structure Points

1. A party can be paid a per name fee for a list of consumers, but the party should not also promote the purchaser of the list to the consumers.
2. Paying for a name only when a closed transaction results, or varying the fee paid for a name based on whether a closed transaction results, can be viewed as a referral fee or fee splitting arrangement, rather than a lead sale arrangement.

3. Be mindful of triggering mortgage brokerage requirements, both under RESPA and state law.
 - a. *RESPA*: Minimum service level required. See discussion of HUD Policy Statements below.
 - b. *State Law Requirements*: Include licensing requirements.

G. Lead Sales in the Context of the Internet

1. As noted above, there is no Internet version of RESPA, or special Internet exceptions under RESPA.
2. The list sale approach is used as a basis for click-through fee arrangements and similar arrangements on the Internet.
 - a. For example, a real estate broker can be paid a flat dollar amount on a per name basis when consumers who visit the broker's website transmit contact information to a lender by clicking-through to a lender's website.
3. At what point can a fee be earned/triggered for a lead?

H. Marketing in the Context of the Internet

1. As noted above, there is no Internet version of RESPA, or special Internet exceptions under RESPA.
2. With marketing, follow the traditional concept of payments for services, goods and facilities provided.
 - a. Banner ads.
 - b. Co-branded websites.

I. Mortgage Broker Compensation—HUD Policy Statements

1. *Two Basic Principles*: HUD has established two basic principles regarding the payment of compensation by lenders to mortgage brokers:
 - a. A lender may compensate a mortgage broker for services, goods and facilities provided by the broker, as long as the total compensation received by the broker from the lender, the consumer and any other party is within the range of the market value of the services, goods and facilities provided the broker.

- b. For a lender to pay any compensation to a mortgage broker, the broker must provide at least a minimum level of services, goods and facilities (for ease of reference, “services”).

2. *Minimum Level of Services:*

- a. *Background:* HUD first provided guidance on the minimum level of services in two informal interpretations (February 14 and June 20, 1995 letters by Nicolas Retsinas). HUD then formalized the guidance in Statement of Policy 1999-1, and reconfirmed the guidance in Statement of Policy 2001-1. HUD identifies specific services, and then addresses the minimum number of services that must be performed to justify the payment of any compensation by a lender to a mortgage broker.

- b. *Identified Services:*

- i. Taking information from the borrower and filling out the application, or performing a comparable activity, such as filling out a worksheet.
- ii. Analyzing the prospective borrower’s income and debt and pre-qualifying the prospective borrower to determine the maximum mortgage that the prospective borrower can afford.
- iii. Educating the prospective borrower in the home buying and financing process, advising the borrower about the different types of loan products available, and demonstrating how closing costs and monthly payments could vary under each product.
- iv. Collecting financial information (tax returns, bank statements) and other related documents that are part of the application process.
- v. Assisting the borrower in understanding and clearing credit problems.
- vi. Maintaining regular contact with the borrower, real estate broker/agent and lender between application and closing to apprise them of the status of the application and gathering any additional information as needed.
- vii. Initiating/ordering verifications of employment and verifications of deposit.
- viii. Initiating/ordering requests for mortgage and other loan verifications.

- ix. Initiating/ordering appraisals.
- x. Initiating/ordering inspections or engineering reports.
- xi. Providing disclosures (truth in lending, good faith estimate and others) to the borrower.
- xii. Ordering legal documents.
- xiii. Determining whether the property is located in a flood zone or ordering such service.
- xiv. Participating in the loan closing.

HUD considers the services identified in ii. through vi. to be counseling services.

HUD advises that if a mortgage broker takes the loan application information or performs a comparable function, and in addition performs at least five of the listed services, with at least one of the additional services not being a counseling service, then HUD generally will be satisfied that sufficient origination work was performed by the broker to justify compensation (but the compensation still must be reasonable in relation to the services provided).

If the only services rendered by a broker, other than taking the application or performing a comparable function, are counseling services, additional requirements apply to address the concern of HUD that meaningful counseling, and not steering, be performed. The additional requirements are that (a) the borrower has the opportunity to consider products from at least three different lenders, (b) the broker receives the same compensation regardless of which lender's products are selected, and (c) the payment to the broker must be based on the counseling services and may not be based on the amount of loan business referred to a particular lender.

II. MBA RESPA REFORM OPTIONS

A. RESPA Reform Round 2

1. HUD issued a RESPA reform proposal in July 2002 and withdrew the proposal in March 2004 in the face of opposition and comments from various fronts, including Congress, federal government agencies, industry groups and consumer groups.
2. HUD kicked off the second round of RESPA reform in June 2005 by announcing it would hold a series of roundtables.
3. MBA directly or through its members attended each of the seven roundtables.

4. MBA also formed the RESPA at Ready Task Force to address RESPA reform.

B. RESPA at Ready Task Force Proposals

1. Threshold determination: Should HUD elect to forgo reform at this time?
 - a. The market is evolving and reforming itself.
 - b. HUD may wish to consider allowing the market to continue to operate, innovate and simplify the mortgage process under the current rules.
 - c. Under the current rules, competition and innovation in the mortgage market are resulting in greater transparency and lower costs to consumers.
 - d. Regulatory changes will require significant and costly changes by the industry, and require consumer education.
 - i. The related costs ultimately will be borne by consumers.

B. If Reform is a Go

1. If HUD determines there is a need to revise the current rules, then three Options developed by the RESPA at Ready Task Force are available for consideration.
2. A central theme of the Options is that any reform should be accompanied by regulatory relief.
3. Option 1 focuses on revising the Good Faith Estimate and HUD-1.
4. Option 2 includes Option 1, and adds tolerances for lender and mortgage broker charges, along with limited Section 8 exemptions.
5. Option 3 includes Options 1 and 2, and adds tolerances for all major settlement charges, except government charges and prepaid charges, and includes an additional Section 8 exemption.

C. Option 1

1. Good Faith Estimate. The form would be revised to provide as follows:
 - a. At the top, the GFE would:
 - i. Include a brief statement describing the document.

- ii. Provide that the estimate is based on information provided by the consumer.
 - iii. Provide that additional information would be required to determine if the consumer and property qualify for the loan.
- b. The basic loan characteristics, such as the loan amount and term, would be set forth.
- c. The proposed interest rate, points, APR and monthly payment would be disclosed.
- d. The estimated charges would be disclosed in nine main categories instead of being itemized individually:
 - i. Lender charges.
 - ii. Mortgage broker charges.
 - iii. Credit report, property valuation and inspection charges.
 - iv. Title charges.
 - v. Government, recording and transfer charges.
 - vi. Interest and mortgage insurance charges.
 - vii. Taxes, flood and hazard insurance charges.
 - viii. Escrow charges and reserves.
 - ix. Other loan settlement charges, such as life of loan flood and tax services.
- e. The charges that are included in the APR calculation would be noted.
- f. The POC items would be shown as a lump-sum and deducted from the total charges to show the estimated amount due at closing.
- g. Consistent with the current rule, the GFE would disclose estimated compensation to be paid by the lender to the mortgage broker, but with an explanation.
 - i. You may recall that the FTC tested with consumers the method of disclosing lender-paid mortgage broker compensation that HUD included in its original reform proposal.

- ii. The FTC found that under the proposed disclosure method, consumers often could not determine whether a retail or wholesale loan was cheaper, and in various cases incorrectly concluded that the brokered loan was more expensive.
 - iii. Under Option 1, the GFE would state that brokers must disclose lender-paid compensation, and that to compare loans the consumer should focus on the interest rate, points and settlement charges, and not lender-paid broker compensation.
- 2. HUD-1.
 - a. Like the GFE, the HUD-1 would set forth the actual loan charges in nine main categories instead of itemizing each charge.
 - b. This would provide for an easy comparison of the estimated charges in the GFE and the actual charges in the HUD-1.
- 3. Other Matters:
 - a. The Special Information Booklet would be revised to reflect the new forms.
 - b. HUD would need to consult with the Federal Reserve Board for Truth in Lending Act coordination purposes.
 - c. The Option recommends that HUD preempt state laws that would conflict with the streamlined disclosure method.

D. Option 2

- 1. The Good Faith Estimate and HUD-1 would be the same as with Option 1.
- 2. Tolerances:
 - a. Tolerances would be added.
 - b. Except for discount points, the lender charges and the broker charges each could not vary by more than 2%, as long as:
 - i. The borrower and property qualify for the loan; and
 - ii. The borrower does not request a change in the loan described in the GFE.

3. The Good Faith Estimate would be open for acceptance for a minimum period of 5 calendar days.
4. Limited Section 8 Exemptions:
 - a. Lenders and mortgage brokers would be entitled to a limited Section 8 exception for average-cost pricing of their own charges and other categories of costs on the GFE, provided that:
 - i. The tolerances were not exceeded; and
 - ii. The charges for each of the cost categories are generally (that is, more than 80%) attributable to the sub-items of costs described in the category.
 - b. Lenders and mortgage brokers also would be entitled to an exemption from Section 8(b) with regard to mark-ups of third party costs, as long as the charges in each cost category are disclosed and the tolerances are not exceeded.
5. Non-Judicial Corrective Action
 - a. If the lender's or broker's charges exceeded the 2% tolerance, the lender or broker, as applicable, could take non-judicial corrective action by repaying any overage.
 - i. If the lender or broker did not repay the overage in a certain period of time, the amount required to correct the error would increase.

E. Option 3

1. Option 3 would include all the changes in Option 1 and Option 2.
2. Additional Tolerance:
 - a. There would be a 10% tolerance for a third-party costs and title costs, as long as:
 - i. The borrower and property qualify for the loan; and
 - ii. The borrower does not request a change in the loan described in the GFE.
 - b. Government charges and prepaid charges would not be included in the tolerance.

3. Additional Section 8 Exemption:
 - a. There would be a limited Section 8 exemption for lenders, mortgage brokers and other settlement service providers to permit volume discount arrangements.
 - i. As long as the charges in each cost category are within the tolerances, volume discounts would be permissible, whether or not the charges in the categories are greater than the volume costs negotiated.

III. RECENT RESPA ENFORCMENT ACTIONS

Please see the Appendix for a certain recent HUD settlement agreements.

IV. STATE LAW

A. Licensing

1. Most states have license requirements for mortgage loan-related activity, including brokering and lending.
 - a. States vary in their definition of what activity triggers a license requirement.
 - b. States also vary in their interpretation of what constitutes a triggering activity, which can lead to different results in states with similar definitions.
 - c. In particular, some states broadly interpret the activity that triggers the need for a mortgage broker license.
2. States increasingly are requiring the licensing of individual loan officers and loan solicitors.
 - a. Some states consider loan processors and wholesale account executives to be loan officers who must be licensed, even if they have no contact with the borrower.
3. For a company that holds mortgage loan-related licenses, states have requirements regarding advertisements that, among other things, provide for disclosures regarding the company's licenses in advertisements.
 - a. Internet websites are viewed as advertisements for purposes of the licensing disclosure requirements.

4. States also may restrict or require certain statements in advertisements. For example:
 - a. Many states require that a mortgage lender or broker licensee include its licensed name, address and license number on its advertisements/websites.
 - b. In addition to license numbers, states may require certain statements, such as “Licensed by the Department of Corporations under the California Residential Mortgage Lending Act” or “BROKER ONLY, NOT A LENDER” (for Connecticut brokers).
 - c. Potential conflicts can arise. For example, in California many entities hold both a Residential Mortgage Lender License and a Finance Lender License. The California regulator requires disclosure of licensing in advertisements under both licenses. However, the same regulator takes the position that an advertisement cannot state that an entity is doing business under both the Residential Mortgage Lender Act and the Finance Lender Act.
5. Additionally, states regulate and restrict the content of advertisements. For example:
 - a. Virginia recently revised its advertising regulations to prohibit, among other things, a lender or broker from publishing an advertisement that states or implies that a consumer has been or will be “preapproved” for a mortgage unless the advertisement discloses, in at least 14-point bold type that “THIS IS NOT A LOAN APPROVAL” and clearly and conspicuously discloses the conditions and/or qualifications associated with the preapproval.
 - b. Virginia is just one example of a growing number of states taking a hard look at advertising.
6. Certain state regulators require prior approval before a licensee may publish an advertisement.
 - a. For Mortgage Broker licensees, Nevada requires prior approval of advertisements, including company websites.
 - i. In Nevada, Mortgage Broker licensees may make or broker mortgage loans, and Mortgage Banker licensees may make mortgage loans. The Nevada regulator does not require prior approval of Mortgage Banker advertisements. Accordingly, if an entity makes mortgage loans in Nevada, it is important for the individuals in charge of the company website and advertisements

to know whether the entity is lending pursuant to a Mortgage Broker license or a Mortgage Banker license.

- b. California Finance Lender Licensees also must obtain prior approval of advertisements.
7. States also license other mortgage loan-related activities, including:
- a. Title agent services.
 - b. Other insurance agent services.
 - c. Settlement/escrow services.
 - d. Appraisal services.

B. Consumer Protection Laws

- 1. Although the consumer protection laws of the states vary, the laws often have common themes and can reach many aspects of transactions with consumers.
- 2. Often there are laws relating to, among other items:
 - a. Disclosures that must be provided to consumers.
 - b. Rates and fees that may be imposed on consumers.
 - c. Other terms of credit transactions with consumers.
- 3. Typically there are unfair and deceptive act and practice laws that can be broad in scope. For example,
 - a. Advertising, representations and offers to consumers, as well as terms of transactions with consumers, may be covered.
 - b. The marking-up of settlement service fees may present issues.

C. Unauthorized Practice of Law

- 1. State law must be assessed regarding whether preparing loan documents or conducting loan closings, with and without charging a fee, may constitute the unauthorized practice of law.

V. SARBANES-OXLEY ACT OF 2002 (“SOX”) (Public Law 107-204)

A. Background

1. A response to concerns over public company financial practices and reporting based on the Enron Corporation/Arthur Anderson “incident,” the bankruptcy of Global Crossing LLC (Arthur Anderson was the auditor) and restatements of earnings by prominent market participants.
2. Signed into law on July 30, 2002.

B. Certain Components

1. Establishes Public Company Accounting Oversight Board (Board) to oversee the audit of public companies subject to federal securities laws. (Title I.)
 - a. The Securities and Exchange Commission (SEC) has oversight and enforcement authority over the Board. (Section 107.)
 - b. A firm that desires to prepare, issue or participate in the preparation or issuance of any audit report of a securities issuer must be registered as a public accounting firm with the Board. (Section 102.)
 - c. The Board is directed to adopt auditing standards. (Section 103.)
 - d. The Board must conduct regular inspections of registered public accounting firms and associated persons regarding compliance with SOX. (Section 104.)
 - e. The Board also may investigate and discipline registered public accounting firms and associated persons. (Section 105.)
2. Imposes auditor independence requirements. (Title II.)
 - a. Prohibits auditors from providing certain non-audit services contemporaneously with an audit. (Section 201.)
 - i. Allows a company’s audit committee to approve in advance an auditor providing contemporaneous non-audit services that are not prohibited. (Sections 201 & 202.)
 - b. Requires a registered public accounting firm to change the lead audit partner for a company at least every five fiscal years. (Section 203.)
 - c. Prohibits a registered public accounting firm from performing an audit of an issuer if a chief executive officer, controller, chief financial officer,

chief accounting officer or person in an equivalent position of the issuer was employed by the accounting firm, and participated in the audit of the issuer, during the one-year period preceding the date of the initiation of the audit. (Section 206.)

3. Imposes corporate responsibility requirements. (Title III.)
 - a. Directs the SEC to adopt a rule requiring the principal executive officer(s) and principal financial officer(s) of public companies to provide specific certifications in connection with annual and quarterly reports filed under federal securities laws. (Section 302.) *See the Certifications section below.*
 - b. Prohibits improper influence of auditors. (Section 303.)
 - c. Provides for the forfeiture by an issuer's chief executive officer and chief financial officer of (a) any bonus or other incentive-based or equity-based compensation received during the 12-month period following the public issuance of or filing of a financial document with the SEC, and (b) any profits realized from the sale of securities of the issuer during that 12-month period, if the issuer must restate the financial document due to material noncompliance of the company, as a result of misconduct, with any financial reporting requirement under the securities laws. (Section 304.)
 - d. Prohibits directors and executive officers of an issuer of securities from trading in the issuer's securities during pension fund blackout periods. (Section 306.)
4. Provides for enhanced financial disclosures. (Title IV.)
 - a. Requires that financial statements filed with the SEC reflect all material correcting adjustments that have been identified by a registered public accounting firm. (Section 401.)
 - b. Requires that annual and quarterly financial reports filed with the SEC disclose all material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships of the issuer that may have a material current or future effect on financial condition, changes in financial condition, results of operations, liquidity, capital expenditures, capital resources or significant components of revenues or expenses. (Section 401.)
 - c. Prohibits personal loans to directors or executive officers. (Section 402.)
 - i. The prohibition started out as a disclosure requirement only.

- ii. Certain loans are excluded from the prohibition, including consumer credit under the Truth in Lending Act if the loan:
 - A. Is made in the ordinary course of the consumer credit business of the issuer;
 - B. Is of a type that is generally made available by the issuer to the public; and
 - C. Is made on market terms, or terms that are no more favorable than those offered by the issuer to the general public for such extensions of credit.
 - iii. Loans made by FDIC-insured institutions that are subject to the lending restrictions of Federal Reserve Act Section 22 (h) also are excepted from the prohibitions.
- d. Directs the SEC to adopt rules regarding internal control over financing reporting. (Section 404.) *See the Internal Control Over Financial Reporting Section below.*
- e. Directs the SEC to adopt rules to require an issuer to disclose, with its periodic reports, (i) whether or not the issuer has adopted a code of ethics for senior financial officers, and (ii) if the issuer has not adopted such a code of ethics, the reasons for not doing so. (Section 406.)
- i. For purposes of the requirement, a “code of ethics” means such standards as are reasonably necessary to promote:
 - A. Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional relationships.
 - B. Full, fair, accurate, timely and understandable disclosure in the periodic reports required to be filed by the issuer.
 - C. Compliance with applicable governmental rules and regulations.
5. Directs the SEC to adopt rules to require an issuer to disclose, with its periodic reports, (a) whether or not the audit committee of the issuer has at least one member who is a financial expert, and (b) if not, the reasons why the audit committee does not have at least one member who is a financial expert. (Section 407.)
6. Provides whistleblower protection. (Section 806.)
- a. Prohibits a publicly traded company, or an officer, employee, contractor, subcontractor or agent of the company, from discharging, demoting,

suspending, threatening, harassing, or in any other manner discriminating against an employee in the terms and conditions of employment because of any lawful act done by the employee:

- i To provide information, cause information to be provided or otherwise assist in an investigation regarding any conduct that the employee reasonably believes violates certain federal anti-fraud laws, any rule of the SEC, or any other federal law relating to fraud against shareholders that is conducted by any federal agency, Congress, a person with supervisory authority over the employee or any other person who works for the employer and has authority to investigate, discover or terminate misconduct.
 - ii. To file, cause to be filed, testify, participate in, or otherwise assist in a proceeding filed or about to be filed relating to an alleged violation of any such laws or rules.
- 7. Amends the federal criminal statutes to require periodic reports filed by issuers with the SEC that contain financial statements to be accompanied by a written statement by the chief executive officer and chief financial officer, or equivalent, of the issuer. (Section 906.)
 - a. The written statement must certify that the public report containing financial statements fully complies with applicable federal securities laws, and that the information contained in the report fairly presents, in all material respects, the financial condition and results of operation of the issuer.
 - b. Anyone who makes the required certification knowing that the periodic report does not comply with the applicable requirements is subject to a fine of up to \$1 million, imprisonment for up to 10 years, or both.
 - c. Anyone who willfully makes the required certification knowing that the periodic report does not comply with the applicable requirements is subject to a fine of up to \$5 million, imprisonment for up to 20 years, or both.

C. Certifications

- 1. As noted above, SOX requires certain certifications:
 - a. The SEC is directed to require by rule that principal executive officer(s) and principal financial officer(s) of public companies provide specific certifications in connection with annual and quarterly reports filed under federal securities laws. (Section 302.)

- b. The federal criminal statutes were amended to require periodic reports filed by issuers with the SEC that contain financial statements to be accompanied by a written statement by the chief executive officer and chief financial officer, or equivalent, of the issuer certifying that the public report containing financial statements fully complies with applicable federal securities laws, and that the information contained in the report fairly presents, in all material respects, the financial condition and results of operation of the issuer.
2. Form of Section 302 certification adopted by the SEC:

*Certifications** I, [identify the certifying individual], certify that:

1. I have reviewed this [specify report] of [identify registrant];
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the

effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date:

[Signature]

[Title]

*Provide a separate certification for each principal executive officer and principal financial officer of the registrant. See Rules 13a-14(a) and 15d-14(a).

D. Internal Control Over Financial Reporting

1. As noted above, SOX requires the SEC to adopt rules regarding internal control over financing reporting. Specifically, the SEC is directed to adopt rules that require annual reports of an issuer to contain an internal control report that (a) states the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting, and (b)

contains an assessment of the effectiveness of the internal control structure and procedures of the issuer. (Section 404.)

2. The SEC adopted rules to implement the Section 404 requirement, including a rule requiring that management provide the following in annual reports on internal control over financial reporting:
 - a. A statement of management's responsibility for establishing and maintaining adequate internal control over financial reporting for the company.
 - b. A statement identifying the framework used by management to evaluate the effectiveness of the company's internal control over financial reporting as required by SEC rules.
 - c. Management's assessment of the effectiveness of the company's internal control over financial reporting as of the end of the company's most recent fiscal year, including a statement as to whether or not internal control over financial reporting is effective.
 - i. The discussion must include disclosure of any material weaknesses in the company's internal control over financial reporting identified by management.
 - ii. Management is not permitted to conclude that the company's internal control over financial reporting is effective if there are one or more material weaknesses in the company's internal control over financial reporting.
 - d. A statement that the registered public accounting firm that audited the financial statements included in the annual report containing the required disclosure has issued an attestation report on management's assessment of the company's internal control over financial reporting.

(17 CFR Section 229.308.)

3. Based on feedback regarding the limited nature and extent of guidance to management, the SEC plans to provide additional guidance on the assessment by management of the effectiveness of internal control over financial reporting.
 - a. The SEC issued a concept release in July 2006 seeking input to develop the additional guidance, and comments were due by September 18, 2006.
 - b. The SEC expressly addresses information technology in the release. The SEC notes that:

- i. Companies are having difficulty in completing their assessment of internal control over financial reporting with regard to information technology, and
 - ii. One example of this is concerns regarding the extent to which information technology processes should be included in the scope of an assessment.
- c. The SEC expressly seeks comment on:
- i. Whether guidance is needed about documentation for information technology controls.
 - ii. If so, whether guidance is needed for both documentation of the controls and documentation of testing for the assessment.

E. REFORM TO SOX

- 1. On September 19, 2006, the House Financial Services Committee held hearings regarding SOX.
 - a. Testimony included successes and problems with SOX.
 - b. SEC Chairman discussed guidance and proposed regulatory reform with respect to the Section 404 internal control reporting requirements, particularly with regard to auditor requirements. (SEC July 2006 concept release is part of the effort.)
 - c. PCAOB discussed plan to improve implementation of the Section 404 audit of internal control reporting requirements, particularly with regard to auditor requirements.

VI. REGULATION AB

A. Background

- 1. Disclosure and reporting requirements under federal securities laws traditionally focused on operating companies that issue securities. The Securities and Exchange Commission (SEC) believed that the requirements did not elicit relevant information for most asset-backed securities transactions, such as securities backed by a pool of mortgage loans.
 - a. For example, disclosure requirements provide for a discussion of the business and management of a securities issuer. With an asset-backed security, there generally is no business or management to describe.

Rather, the transaction structure, characteristics and quality of the asset pool and servicing often are what is important to an investor.

2. Through no-action letters and other staff positions the SEC developed a framework to fit asset-backed securities into the disclosure and reporting rules, but there was no separate rule specifically designed for such securities.
3. The SEC adopted new and amended rules and forms, that include Regulation AB (17 C.F.R. Subpart 229.1100), to specifically address disclosure and reporting requirements for asset-backed securities under the Securities Act of 1933 and the Securities Exchange Act of 1934. The new and amended rules and forms were published in the *Federal Register* on January 7, 2005.
4. The new requirements generally apply to initial securities offerings made after December 31, 2005.

B. Definition

1. An asset-backed security is defined in part as a security that is primarily serviced by the cash flows of a discrete pool of receivables or other financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distributions of proceeds to the security holders. The basic definition was first adopted by the SEC in 1992. (Section 229.1101(c).)
2. The SEC desired to use a “principles-based” definition to allow broad flexibility as to assets types and structures that are subject to the alternative disclosure and regulatory regime for asset-backed securities.

C. Certain Restrictions

1. The SEC imposed restrictions on the parties that may use the new requirements for asset-backed securities. In particular:
 - a. The party that issues the asset-backed securities (commonly called the “issuing entity”), and the party that deposits the assets that will back the securities issued by the issuing entity, may not be investment companies under the Investment Company Act, or become investment companies as a result of the asset-backed securities transaction.
 - b. An issuing entity must be passive in nature. Its activities must be restricted to the asset-backed securities transaction (passively owning or holding the pool of assets, issuing the asset-backed securities, and other activities reasonably incidental thereto).

- c. The pool of assets cannot include as of the cut-off date or other measurement date any non-performing assets, and the amount of delinquent assets may not equal, on a dollar basis, 50% or more of the pool of assets.
 - i. A non-performing asset is any asset that would be treated as being wholly or partially charged-off under:
 - A. The transaction agreements;
 - B. The charge-off policies of the sponsor, an affiliate of the sponsor that originates the asset, or the servicer; or
 - C. The charge-off policies established by the primary safety and soundness regulator of any of the parties listed in B., or the program or regulatory entity that oversees the program under which the pool asset was originated.
 - ii. A delinquent asset is any asset that is more than 30 or 31 days, or a single payment cycle, as applicable, past due from the contractual due date, as determined in accordance with any of the following:
 - A. The transaction agreements;
 - B. The delinquency recognition policies of the sponsor, an affiliate of the sponsor that originates the asset, or the servicer; or
 - C. The delinquency recognition policies established by the primary safety and soundness regulator of any of the parties listed in B, or the program or regulatory entity that oversees the program under which the pool asset was originated.
 - iii. SEC guidance regarding the identification of a non-performing asset and a delinquent asset based on the standards set forth in i. and ii.:
 - A. Most restrictive of A., B. or C. applies in each case.
 - B. With regard to the alternatives in B., the use of the most restrictive is not required.

(Section 229.1101(c), (d), (g); SEC Manual of Publicly Available Telephone Interpretations.)

D. Principles-Based Approach

- 1. With regard to the disclosure that is required by Regulation AB, the SEC adopted a principles-based approach that focuses on disclosure concepts or objectives, with illustrations, in lieu of detailed disclosure guides for each securitized asset.

2. Pursuant to the approach, the application of a particular concept or objective needs to be tailored in preparing and presenting a disclosure to the information that is material to the particular transaction and asset type involved.
3. The MBA supported the adoption of a principles-based approach.
4. Good news, bad news situation.
 - a. The good news is that the principles based approach provides for flexibility in dealing with different types of securitized assets and the varying terms and details of transactions.
 - b. The bad news is that this flexibility has resulted in differing views on what disclosures are required.
 - c. The MBA is continuing its efforts to seek guidance for the mortgage industry on the interpretation and implementation of Regulation AB.

E. Disclosures

1. The SEC advised that it believed the existing disclosure standards did not adequately capture certain categories of information regarding asset-backed securities transactions, such as the background, experience, performance and roles of various transaction parties, including the sponsor, servicer and the trustee, that may be material and should be disclosed when they are material. As a result, the new disclosure requirements are designed to elicit additional information regarding these matters, to the extent material.
2. Among other items, required disclosures include:
 - a. A summary of the asset-backed securities transaction and risk factors. (Section 229.1103.)
 - b. Information regarding the:
 - i. Sponsor. (The sponsor is the party who organizes and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuing entity). (Section 229.1104.)
 - ii. Depositor, if the sponsor is not the depositor. (The depositor is the party who receives or purchases the pool assets, and transfers or sells the assets to the issuing entity.) (Section 229.1106.)
 - iii. Issuing entity. (The issuing entity is the trust or other entity created at the direction of the sponsor or depositor that owns or

holds the pool assets and in whose name the asset-backed securities supported or serviced by the pool assets are issued.) (Section 229.1107.)

- iv. Servicer(s), except for any unaffiliated servicer that services less than 10% of the pool assets. (Section 229.1108.)
- v. Trustee. (The trustee may be, for example, the trustee of the trust that is the issuing entity.) (Section 229.1109.)
- vi. Originators, other than the sponsor or its affiliates, that originated or expected to originate 20% or more of the pool assets. (Originators that originated or are expected to originate 10% or more of the pool assets must be identified.) (Section 229.1110.)
- vii. Significant obligors of pool assets. In particular, selected financial information must be provided for obligors of 10% or more of the pool assets, and financial statements must be provided for obligors of 20% or more of the pool assets. (Section 229.1112.)

c. Static pool information.

- i. For an amortizing asset pool, this includes, to the extent material, information generally for a five-year period regarding delinquencies, cumulative losses and prepayments for prior securitized pools of the sponsor for the asset type. (If the sponsor has less than three years of experience securitizing the particular assets, Regulation AB provides that the sponsor should consider providing this information, to the extent material, by vintage origination years with regard to originations or purchases by the sponsor for the asset type. Based on the concept of a wine's vintage, a vintage origination year refers to assets originated during the same year.)
- ii. For a revolving asset master trust, this includes, to the extent material, information regarding delinquencies, cumulative losses, prepayments, payment rate, yield and standardized credit scores or other applicable measure of obligor credit quality in separate increments based on the date of origination of the pool assets. Regulation AB notes that while material increments may vary, you should consider presenting data at a minimum in 12-month increments for the first five years of the account's life.

(Section 229.1105.)

- d. A description of the pool assets. The general categories of information include:
 - i. General information regarding pool asset types and selection criteria.
 - ii. Pool characteristics.
 - iii. Delinquency and loss information.
 - iv. Sources of pool cash flow.
 - v. Representations and warranties and repurchase obligations regarding pool assets.
 - vi. Claims on pool assets.
 - vii. Revolving periods, prefunding accounts and other changes to the asset pool.

(Section 229.1111.)

- e. Structure of the transaction. (Section 229.1113.)

- f. Compliance with applicable servicing criteria.

- i. A compliance certification from each servicer is required (except for unaffiliated servicers that service less than 10% of the pool assets).

(Section 229.1122.)

- g. Credit enhancement or other support mechanisms for the pool assets or asset-backed securities. (Section 229.1114.)

- h. Derivative instruments that are used to alter the payment characteristics of the cash flows from the issuing entity and whose primary purpose is not to provide credit enhancement related to the pool assets or asset-backed securities. (Section 229.1115.)

- i. Affiliations and certain relationships and related transactions. (Section 229.1119.)

- j. Ratings. (Section 229.1120.)

- k. Distributions and pool performance. (Section 229.1121.)

1. Tax matters, legal proceedings, and reports and additional information. (Sections 229.1116 to 229.1118.)

F. Certifications and Related Items

1. Asset backed securities issuers currently must provide a Section 302 certification under SOX in connection with annual reports filed under the federal securities laws. The SEC already had developed a specific form of certification for asset-backed issuers. The rules and forms adopted along with Regulation AB contain a modified form of the previously developed form of certification:

*Certifications*¹ I, [identify the certifying individual], certify that:

1. I have reviewed this report on Form 10-K and all reports on Form 10-D required to be filed in respect of the period covered by this report on Form 10-K of [identify the issuing entity] (the “Exchange Act periodic reports”);

2. Based on my knowledge, the Exchange Act periodic reports, taken as a whole, do not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, all of the distribution, servicing and other information required to be provided under Form 10-D for the period covered by this report is included in the Exchange Act periodic reports;

4. [I am responsible for reviewing the activities performed by the servicer(s) and based on my knowledge and the compliance review(s) conducted in preparing the servicer compliance statement(s) required in this report under Item 1123 of Regulation AB, and except as disclosed in the Exchange Act periodic reports, the servicer(s) [has/have] fulfilled [its/their] obligations under the servicing agreement(s); and]

[Based on my knowledge and the servicer compliance statement(s) required in this report under Item 1123 of Regulation AB, and except as disclosed in the Exchange Act periodic reports, the servicer(s) [has/have] fulfilled [its/their] obligations under the servicing agreement(s); and]²

5. All of the reports on assessment of compliance with servicing criteria for asset-backed securities and their related attestation reports on assessment of compliance with servicing criteria for asset-backed securities required to be included in this report in accordance with Item 1122 of Regulation AB and Exchange Act Rules 13a-18 and 15d-18 have been included as an exhibit to this report, except as

otherwise disclosed in this report. Any material instances of noncompliance described in such reports have been disclosed in this report on Form 10-K.³

[In giving the certifications above, I have reasonably relied on information provided to me by the following unaffiliated parties [name of servicer, sub-servicer, co-servicer, depositor or trustee].]⁴

Date: _____

[Signature]

[Title]

¹ With respect to asset-backed issuers, the certification must be signed by either: (1) The senior officer in charge of securitization of the depositor if the depositor is signing the report on Form 10-K; or (2) The senior officer in charge of the servicing function of the servicer if the servicer is signing the report on Form 10-K on behalf of the issuing entity. See Rules 13a-14(e) and 15d-14(e) (§§240.13a-14(e) and 240.15d-14(e)). If multiple servicers are involved in servicing the pool assets, the senior officer in charge of the servicing function of the master servicer (or entity performing the equivalent function) must sign if a representative of the servicer is to sign the certification. If there is a master servicer and one or more underlying servicers, the references in the certification relate to the master servicer. A natural person must sign the certification in his or her individual capacity, although the title of that person in the organization of which he or she is an officer may be included under the signature.

² The first version of paragraph 4 is to be used when the servicer is signing the report on behalf of the issuing entity. The second version of paragraph 4 is to be used when the depositor is signing the report.

³ The certification refers to the reports prepared by parties participating in the servicing function that are required to be included as an exhibit to the Form 10-K. See Item 1122 of Regulation AB (§229.1122) and Rules 13a-18 and 15d-18 (§§240.13a-18 and 240.15d-18 of this chapter). If a report that is otherwise required to be included is not attached, disclosure that the report is not included and an associated explanation must be provided in the Form 10-K report.

⁴ Because the signer of the certification must rely in certain circumstances on information provided by unaffiliated parties outside of the signer's control, this paragraph must be included if the signer is reasonably relying on information that unaffiliated trustees, depositors, servicers, sub-servicers or co-servicers have provided.

(Section 229.601(b)(31)(ii).)

2. Servicers (except for unaffiliated servicers that service less than 10% of the pool assets) must provide a written statement signed by an authorized officer to the effect that:
 - a. A review of the servicer's activities during the reporting period and of its performance under the applicable servicing agreement has been made under the officer's supervision.
 - b. To the best of such officer's knowledge, based on such review, the servicer has fulfilled all of its obligations under the agreement in all material respects throughout the reporting period or, if there has been a failure to fulfill any such obligation in any material respect, specifying each such failure known to such officer and the nature and status thereof.

(Section 229.1123.)

3. Parties that perform servicing functions with respect to more than five percent of the pool assets must conduct assessments of, and provide assertions of, compliance with servicing requirements.
 - a. The SEC used the Uniform Single Attestation Program (USAP) developed by the MBA as a starting point, but noted limitations with the USAP with regard to assets other than mortgage loans.
 - b. A platform level assessment and attestation, rather than a deal-specific assessment and attestation is required. Thus, for a particular deal, a party will address asset-backed securities transactions taken as a whole that involve the party participating in the servicing function and are backed by the same asset type backing the class of asset-backed securities in the deal.
 - c. See the SEC Manual of Publicly Available Telephone Interpretations for guidance on the calculation of the five percent threshold, and regarding flexibility in determining the servicing platform that is the basis for the assessment and attestation.

(Sections 240.13a-18 and 240.15d-18.)

4. Based on an exemption adopted by the SEC, asset-backed securities issuers do not have to comply with SOX Section 404 requirements regarding reporting on internal control over financial reporting. (Sections 240.13a-15 and 240.15d-15.)

APPENDIX

Certain Recent HUD Settlement Agreements Under RESPA.

- A. August 2005 Settlement With Coldwell Banker Residential Real Estate, Inc. (CBREE).
1. CBREE provides real estate brokerage services in the greater Atlanta, Georgia area.
 2. HUD alleges that CBREE gave things of value to its sales agents for referrals to settlement service providers, including (a) giving higher sales commission splits to agents who referred business to a related title company, (b) requiring agents to refer business to the title company in order to receive referrals of relocation business, (c) allowing only those agents who referred business to the title company to be paid their commission at settlement, and (d) giving prizes and other benefits to those agents who referred business to the title company.
 3. HUD asserts that the alleged practices violate RESPA. Although not stated in the settlement agreement, HUD must have taken the position that the sale agents were not employees of CBREE.
 4. CBREE denies that its conduct violated RESPA and asserts that HUD's allegations do not accurately portray CBREE's conduct.
 5. CBREE also asserts that in some instances prior to HUD's investigation and since the start of HUD's investigation CBREE ceased any of the practices alleged by HUD.
 6. CBREE agreed to pay \$250,000 to the United States and to provide written notice of the requirements of RESPA to all its sales associates.
- B. August 2005 Settlement With Prudential Locations LLC (Prudential).
1. Prudential provides real estate brokerage services in the Honolulu, Hawaii area.
 2. HUD alleges that Prudential is affiliated with and has a financial interest in Wells Fargo Home Mortgage Hawaii, LLC, and that Prudential:
 - a. Organized, promoted, executed and paid for the "First Annual Wells Fargo Friends Party" in January 2003, and only real estate agents who referred over \$1 million in business to the affiliated lender were invited to attend.
 - b. Paid for and gave real estate agents the *opportunity to win* a three year lease of a Mercedes-Benz and other prizes at the "First Annual Wells Fargo Friends Party" in return for referrals of business to the lender.

- c. Paid for and gave a particular real estate agent a three-year lease of a Mercedes-Benz when the agent won a drawing that was open only to agents who referred business to the lender.
- d. Paid for and gave real estate agents trips to Thailand, Las Vegas and San Francisco for their referrals of business to the lender.
- e. Paid for and gave real estate agents the *opportunity to win* restaurant gift certificates in October 2003 for their referrals of business to the lender.
- f. Paid for and gave real estate agents restaurant gift certificates in October 2003 in return for referrals of business to the lender.
- g. HUD asserts that the brokerage firm violated RESPA, and/or aided and abetted others in violation of RESPA, with respect to the alleged practices.
- h. The settlement agreement provides that the entry into the agreement does not constitute an admission of liability or wrongdoing by the brokerage firm.
- i. Among other terms, the brokerage firm agreed to:
 - A. Pay \$48,000 to the United States.
 - B. Abide by RESPA, and such compliance includes, without limitation, not organizing or paying for parties, trips, automobile leases, gift certificates or other things of value in return for the referral of settlement services.
 - C. Prepare a memorandum explaining RESPA's requirements, subject to HUD approval, and distribute the memorandum to the firm's employees, agents, all those who attended the "First Annual Wells Fargo Friends Party" and those agents who received restaurant gift certificates.

- C. November 2005 Settlement With 1-800 East-West Mortgage Company (East-West), with the FDIC as a signatory to the Settlement.
 - 1. East-West is a wholly-owned subsidiary of Commerce Bank & Trust Co. in Worcester, Massachusetts, and provides mortgage loan services in or about Massachusetts and the greater New England area.
 - 2. HUD and FDIC allege that East-West received, requested and/or was reimbursed for:
 - a. Tickets and premium seating to Boston Red Sox baseball games from settlement service providers in exchange for the referral of business.

- b. Tickets and premium seating to New England Patriots football games from settlement service providers in exchange for the referral of business.
 - c. Restaurant gift certificates from settlement service providers in exchange for the referral of business.
 - d. Payment for charitable galas and other special events with the New England Patriots from settlement service providers in exchange for the referral of business.
 - e. Payment for luxury suites at musical concerts from settlement service providers in exchange for the referral of business.
3. HUD and FDIC also allege that East-West violated RESPA, and/or aided and abetted others in violation of RESPA, with respect to the alleged practices.
 4. East-West denies that any payments or things of value it or its employees received were pursuant to any agreement or understanding that business would be referred.
 5. East-West agreed to pay \$150,000 to the United States.
 6. East-West also agreed to cooperate with any HUD and/or FDIC investigation of any settlement service providers who provided kickbacks or other things of value to East-West

D. June 2006 Settlement Agreement With Grasso Appraisal Services, Inc. (Grasso).

1. Relates to November 2005 Settlement With 1-800 East-West Mortgage Company (East-West).
2. East-West provides mortgage loan services in or about Massachusetts and the greater New England area, and Grasso performed property appraisals for East-West.
3. HUD alleges that Grasso paid for and/or subsidized the purchase of restaurant gift certificates for East-West in return for the referral of business, and that Grasso violated RESPA with respect to the alleged practices.
4. Grasso denies that any payments or things of value provided to East-West were pursuant to any agreement or understanding that business would be referred.
5. Grasso agreed to pay \$4,000 to the United States.
6. Grasso agreed to cooperate with any HUD investigations of any settlement service providers who provided kickbacks or other things of value to East-West.

- E. June 2006 Settlement Agreement With R. Norman Peters and his law firm Peters & Sowydra (collectively “Peters”).
1. Relates to November 2005 Settlement With 1-800 East-West Mortgage Company (East-West).
 2. East-West provides mortgage loan services in or about Massachusetts and the greater New England area, and Peters served as a closing attorney for East-West.
 3. HUD alleges that Peters paid for and/or subsidized the purchase of tickets and premium seating to Boston Red Sox baseball games, tickets to a special event with the New England Patriots, and restaurant gift certificates for East-West, and lunch for all East-West employees, in return for the referral of business.
 4. HUD also alleges that Peters violated RESPA and/or aided and abetted others in violation of RESPA with respect to the alleged practices.
 5. Peters denies that any payments or things of value provided to East-West were pursuant to any agreement or understanding that business would be referred.
 6. Peters agreed to pay \$7,500 to the United States.
 7. Peters agreed to cooperate with any HUD investigations of any settlement service providers who provided kickbacks or other things of value to East-West.
- F. So far this year HUD has entered into six separate settlement agreements in which HUD alleged that captive reinsurance companies were formed by parties in a position to refer title insurance business, and that title underwriters reinsured title insurance policies with the captive companies as a means to impermissibly provide a thing of value in return for the referral of title insurance business.
1. The settlement agreements are with:
 - a. AHT Reinsurance, Inc. and M.D.C. Holdings, Inc. (April 2006).
 - b. Chesapeake Title Reinsurance Company, Inc. and CitiMortgage, Inc. (July 2006).
 - c. WL Homes LLC, dba John Laing Homes (July 2006).
 - d. Shea Homes Limited Partnership and related entities and Shea Insurance Services, Inc. (September 2006).
 - e. William Lyon Homes and Duxford Title Reinsurance, Inc. (September 2006).

- f. Fulton Homes Corporation and Fulton Homes Sales Corporation (October 2006)
2. The settlement agreements are similar in nature, and provide for payments by the parties ranging from \$150,000 to \$950,000.
3. By way of example, the settlement agreement with Fulton Homes Corporation and Fulton Homes Sales Corporation (collectively “Fulton Homes”) provides as follows:
 - a. Fulton Homes builds homes in Arizona. HUD alleges that Fulton Homes refers homebuyers to certain companies for title insurance. HUD also alleges that on or about February 1, 2004, Fulton Homes joined as a participant in First American Homebuilders Reinsurance Company (FAHRC), a captive title reinsurance company that reinsures certain title insurance business.
 - b. HUD states its position that (i) it is a violation of RESPA Section 8(a) to accept a thing of value in the form of any opportunity to participate in money-making captive title reinsurance arrangements in return for the referral of settlement service business to primary title insurance companies, and (ii) any captive title reinsurance arrangements in which payments to the reinsurer are not bona fide and exceed the value of the reinsurance would violate RESPA Section 8.
 - c. HUD further states that (i) in its view there is almost never any bona fide need or business purpose for title reinsurance on a single family residence, especially from an entity or an affiliate of an entity that is in a position to refer business to the primary title insurer, and (ii) when there is a history of little or no claims paid or the premium payments to the captive reinsurer far exceed the risk borne by the reinsurer, there is strong evidence that there is an arrangement constructed for the purpose of payment of referral fees or other things of value in violation of RESPA Section 8.
 - d. Fulton Homes states its position that (i) it participated in a captive title reinsurance program through FAHRC in good faith reliance on HUD’s regulations, guidelines and interpretations of RESPA, including its 1997 and 2004 letters regarding reinsurance, and in compliance with applicable law, and (ii) its participation was in compliance with applicable law and that its share of premiums received did not exceed the value of reinsurance provided and risk assumed.
 - e. Fulton Homes represents that (i) title reinsurance was only extended in Arizona and (ii) no new title reinsurance business was written after January 31, 2005.

- f. HUD made no finding of RESPA violations and noted that Fulton Homes cooperated with HUD.
- g. Fulton Homes agreed not to enter into any future captive title reinsurance arrangements, and to cease writing new captive title reinsurance business, but is not prohibited from conduct permitted by any changes to RESPA law or new HUD policy statements. Fulton Homes also agreed to pay \$150,000 to the United States.
- h. The agreement may not be construed as preventing Fulton Homes from unwinding the captive title reinsurance arrangements, including without limitation the ceding of risk and/or premium to one or more third parties under terms and conditions that differ from the terms and conditions under which such risk and/or premium was obtained. Additionally, HUD will not consider such unwinding undertaken in conjunction with the agreement to be in violation of RESPA, provided that the unwinding does not involve an agreement or understanding for the referral of future settlement service business.

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