BANKING
DEPARTMENT OF BANKING AND INSURANCE
DIVISION OF BANKING

Licensed Lenders: Mortgage Bankers; Correspondent Mortgage Bankers; Mortgage Brokers; Secondary Lenders; Consumer Lenders and Sales Finance Companies

Readoption with Amendments: N.J.A.C. 3:15

Recodification with Amendments: N.J.A.C. 3:15-2.3 as 2.4 and 2.4 as 2.3

Proposed: May 20, 2002 at 34 N.J.R. 1775(a)

Adopted: October 10, 2002 by Holly C. Bakke, Commissioner,
Department of Banking and Insurance

Filed: October 10, 2002 as R. 2002 d., **with technical changes** not requiring additional public notice and comment (see N.J.A.C. 1:30-6.3).

Authority: N.J.S.A. 17:1-8.1 and 15(e) and 17:11C-1 et seq.

Effective Date: October 10, 2002, Readoption
November 4, 2002, Recodification and Amendments

Expiration Date: October 10, 2007

Summary of Public Comments and Agency Responses:

The Department of Banking and Insurance ("Department") received written comments from James M. Demers, President, New England Financial Services Association, New York Consumer Finance Association and New Jersey Financial Services Association; W. Thomas Kelly, President, ISB Mortgage Company, LLC; Andrea Lee Negroni, Esq., Goodwin Procter, LLP; and Peter Bell, Executive Director, Innovative Mortgage Origination Council.

COMMENT: Several commenters supported the proposal.

RESPONSE: The Department notes and appreciates the support for the readoption with amendments.

COMMENT: One commenter stated that the proposed amendment to N.J.A.C. 3:15-1.4 appears to be far reaching and would require disclosing the trademark name of a lender, as well as the name of the licensed entity that is the actual lender. The commenter went on to note that he failed to see any consumer benefit and suggested that the section be amended to require listing the licensed entity only.

RESPONSE: The Department proposed the amendment to the rule to make it clear that licensed lenders must disclose to the Department, as part of their application process, all names they are authorized to use in conjunction with providing services to New Jersey consumers under the Licensed Lenders Act. The true name and the alternate or trade name that is used with the consumer in the transaction must be used in the closing documents. The Department disagrees with the commenter that there is no consumer benefit to this disclosure. Having licensed lenders disclose all the names to be used in their New Jersey business will assist the Department in handling consumer inquiries and complaints.

COMMENT: One commenter stated that the mortgage solicitor registration section, set forth at N.J.A.C. 3:15-2.13, was adopted well after 1983 and probably closer to 1993, and believes that the initial registration fee was $25.00. The commenter stated that he

had no problem with the proposed increase of the fee to $100.00 if in fact the Department will be able to monitor the movement of loan officers.

RESPONSE: The Department is unclear as to what the commenter meant by the term “loan officer,” but based on the context the Department believe he meant to refer to “mortgage solicitor.” The Department believes that the mortgage solicitor registration program has been successful in the past, and the Department anticipates that it will continue to achieve its purpose of monitoring the movement of mortgage solicitors. The Department agrees that the registration rule was not adopted in 1983, as mentioned in the Summary, but in 1993. The Department notes that the original $25.00 fee was increased to $50.00 in 1997.

COMMENT: One commenter stated that the doubling of the surety bond amounts and adding annual increases to those amounts will put an unnecessary burden on mortgage bankers/brokers, small and large.

RESPONSE: The increase in the surety bond requirements was a result of extensive discussions within the Department, and based upon a review of the fact that they had not been increased in five years. The amended rules do not require automatic annual increases from the new initial bond amount in the absence of a substantial increase the volume of the licensee’s business. As was the case under the prior rule, licensees are only required to increase the bond if there is a substantial increase in the closed loan volume for mortgage bankers, or in the number of applications taken for a mortgage broker. Conversely, should there be a decrease in the licensee’s volume of business sufficient to qualify that licensee to be secured by a bond in a lower amount than they

had posted for the preceding year, the licensee can, upon the submission of their annual report, decrease the amount of their bond in accordance with the ranges prescribed in the rule.

COMMENT: One commenter stated that he wishes to know whether the Department has determined if the new required surety bond amount will be available and at what price.

RESPONSE: The Department notes that in Pennsylvania the initial bond amount is $100,000, the same as is now proposed for New Jersey licensees. In addition, the Department has not received any information suggesting existing difficulty in obtaining bonds at competitive rates in $100,000 to $150,000 amounts. The Department will monitor this situation and propose an amendment if necessary.

COMMENT: One commenter stated that the cost of insurance coverage in New Jersey is very high, that the cost of the current surety bond has increased each year and that the doubling of the surety bond amount will impose additional costs on the mortgage banker/broker industry which, combined with the liability that may be imposed by Assembly Bill A-75, will have the effect of putting certain mortgage lenders out of business.

RESPONSE: The Department recognizes the expense to be incurred by mortgage brokers and mortgage bankers for surety bonds. Mortgage bankers and brokers and secondary lenders are specifically required by the New Jersey Licensed Lenders Act to have such bonds. See N.J.S.A. 17:11C-13. The Commissioner of Banking and

Insurance determines the amount of the bond. The amount of the bond must strike a balance between the burden on the industry, and the need to protect consumers. Bonds were last increased in 1997. The Department notes that any consideration of possible changes in the industry as a result of the possible enactment of Assembly Bill A-75, which addresses issues of predatory lending, is purely speculative at this juncture. Further, the Department wishes the regulated community and consumers to note that the Department intends to promulgate rules regarding requirements to protect against predatory activities that may involve New Jersey licenses.

COMMENT: One commenter urged that the definition of “direct contact” in N.J.A.C. 3:15-1.2 should not include the use of the “Internet.” The commenter went on to note that many application forms on the Internet are displayed for the education and convenience of potential loan applicants and that this display should not be deemed to be a “direct contact.” The commenter stated that the Department should be concerned with receipt of application information from consumers, not the mere distribution or display of application forms. The commenter stated that no harm can come to consumers as a result of distribution and display of application forms on the Internet; that the more access consumers have to application forms of competing lenders, the more informed they will be about application requirements; and that it is when an application is submitted, rather than distributed, that consumers’ rights and interests are affected.

RESPONSE: The Department disagrees that the inclusion of a specific reference to the Internet within the definition of “direct contact” is inappropriate. The definition has

always included the terminology “or other electronic means” which included Internet activities. The addition of the specific word “Internet” was a further clarification. It should be noted that the pertinent language includes the distribution to or receipt from consumers of loan applications and does not state that both actions must occur or be available to constitute “direct contact.” The position of the Department is that any Internet site that permits an applicant to download an application for submission or to actually complete an application on-line and submit it on-line would be deemed to be “direct contact.” The Department disagrees with the commenter that it is only when an application is submitted that consumers are affected.

COMMENT: One commenter stated that the provision at N.J.A.C. 3:15-2.1(d) to permit lenders to pay real estate brokers and salespersons for providing mortgage related services is ill-advised and will ultimately lead to higher loan costs for consumers. In addition, the commenter noted that payment by lenders to real estate brokers encourages conflicts of interest. The commenter stated that brokers and salespersons usually provide some mortgage loan related services in order to qualify the proposed homebuyer for financing, and that it is in the real estate licensee’s interest to do so because if the buyer does not obtain financing, the sale would not be completed. The commenter stated that presumably the real estate licensee’s commission takes into account efforts in connection with loan origination activities and there is no need to expressly authorize additional fees from the lender. The commenter also stated that because the real estate licensee typically acts as the agent of the seller, he or she should not be earning a fee from the buyer’s mortgage lender because the interest of

the buyer and the seller are conflicting, and the real estate licensee should not put him or herself in the position of representing both the seller's and buyer's interests in the same transaction. The commenter went on to note that if lenders pay real estate brokers for loan origination services, those payments will ultimately be added to loan costs resulting in higher fees to consumers. The commenter went on to note that the Department of Banking and Insurance probably does not have the resources to monitor accurately the amount of reimbursements and whether those amounts "substantially exceed the average rate of regular (non-overtime) compensation of the real estate broker's support staff." The commenter stated that the reimbursement scheme sets up a mechanism, which cannot be easily monitored through existing regulatory resources and is therefore likely to lead to undetected abuses that will harm consumers.

RESPONSE: The Department notes that there is a statutory exemption from the licensing requirements imposed by the Licensed Lenders Act for a real estate broker or salesperson who is not engaged in the business of a mortgage banker or mortgage broker. This section of the rules identifies the limitations that the Department applies for that licensing exemption to have application. It must also be noted that the section of the rules expressing a dollar limitation and stating that the payment must represent reimbursement for services actually rendered in connection with a mortgage loan application has been in existence for a substantial period of years with few reports of problems. The provision specifically limits the reimbursable amount to $250.00 and requires that the real estate broker provide a written itemized statement of the specific services and their costs. The only amendment put forward in the proposal is the clarification that prescribes the criteria that must be met before reimbursement can be

made for the time spent by the individual real estate salesperson or broker involved in the transaction. The Department believes that the constraints imposed by this section do effectively protect consumers.

COMMENT: One commenter stated that the proposal in N.J.A.C. 3:15-2.6(c) to require the submission of an initial application for licensure and of initial licensure fees as required by N.J.A.C. 3:15-4 if a renewal application is submitted more than 90 days after the license has expired will lead to additional and unnecessary work for the Department and unreasonable burdens for licensees. The commenter stated that late fees are an appropriate means to encourage timely license renewals and the requirement to begin the licensure process anew if a renewal application is more than 90 days late is not warranted. The commenter noted that mitigating circumstances might justify late renewals, yet there is no administrative discretion built into the rule for such circumstances. The commenter noted that if a natural or man-made physical disaster made the office of the licensed lender uninhabitable, a renewal application could justifiably be delayed more than 90 days. The commenter went on to note that if a new application must be made for the license, the lender has no control over the processing and approval time for the new application and, presumably, would not be authorized to continue its business during the interim. The commenter stated that this penalty is unnecessarily harsh for the relatively innocuous violation of a late renewal. The commenter stated that in various parts of the proposal, the Department made reference to its lack of resources; requiring existing licensees to “start over” and barring them from conducting business in the meantime would add to the Department’s

workload with no apparent benefit to New Jersey consumers. The proposed rule also does not indicate the recommended disposition of loan applications that are “in process” during the time the late renewing licensee is applying for relicensure. The commenter went on the note that if the licensee could not continue its business uninterrupted during the renewal (reapplication) process, consumers with loan applications in process could be significantly harmed.

RESPONSE: The Department disagrees that the requirement that a licensee that submits a renewal application later than 90 days following the expiration of its license must file a new application and be treated as a new applicant is unnecessarily “burdensome.” The Department mails license renewal application materials to all licensees eligible to renew for a biennial licensing period 90 days prior to the expiration date of the licenses. The proposal sets out a series of time frames after license expiration during which a licensee who failed to do so on a timely basis may renew with the payment of a penalty for late filing, or with a reinstatement application and the payment of a reinstatement fee. It is only those licensees who fail to file for renewal within 90 days after the license has expired that must make a new filing. The Department believes that its time frames are appropriate and that a 180 day notice period for renewal (90 days prior to expiration and 90 days post expiration) is sufficient. The Department notes that any “new” business conducted by a person after the expiration date of its license without having received a new license or other written authorization to continue the conduct of licensed business from the Department would be a violation. In the event of a natural or man-made disaster, the Commissioner has general regulatory authority to extend the expiration date of licenses.

COMMENT: One commenter stated that the proposal at N.J.A.C. 3:15-2.14 regarding notice of change in control requires more advance notice to the Department of Banking and Insurance than many companies can provide. The commenter stated that she has been involved in numerous transactions in which the final terms of an acquisition, a merger, or another change of control was not finalized until days before the closing of the transaction. The commenter noted that the rule requires 60 days advance notice to the Department, including the submission of a copy of a fully executed stock purchase agreement, which requirements are inconsistent with business and legal realities in the mergers and acquisitions marketplace for financial service companies. In addition, the proposal does not specify whether or when the request for change of control will be processed and approved by the Department. The commenter suggested that the rule include a deemer provision, so that requests for change of control that are not approved within a reasonably prompt period, such as 30 days, are deemed approved. The commenter further stated that it would also be desirable if the rule provided for expedited processing for changes of control of existing licensees provided there are no significant outstanding regulatory violations on the part of the licensee or any proposed controlling persons.

RESPONSE: The Department disagrees that the required 60 days notice is too long a time period. The Department believes that “due diligence” research would be required for a substantial period of time before a business entity entered into an acquisition, merger or change of control of a licensed lender. The Department will continue to proceed expeditiously when such applications are submitted.

The suggestion that the change of control application be deemed approved after 30 days is already established at N.J.S.A. 17:11C-12.

COMMENT: One commenter stated that the disclosures required by N.J.A.C. 3:15-2.16 are numerous. The commenter suggested that many disclosures make sense, but minor items such as failure to pass an insurance license exam by an individual may be difficult for some large entities to track and report. The commenter suggested that the proposal be amended to reduce the number of items about which licensed lenders have to notify the Department.

RESPONSE: The Department disagrees that any of the required disclosure items are "minor items." The Department conducted a thorough review of items that it believes necessary for its on-going monitoring and regulation of licensed lenders. The items listed in the proposal have been identified as important by the Department, and although there may be a certain burden on licensed lenders in a larger entity to provide this information, the Department believes that the consumer benefit outweighs this burden. Lastly, the Department notes that the rule does not require notification upon the failure to pass an insurance license exam.

COMMENT: Several commenters stated that the proposal at N.J.A.C. 3:15-2.16 that licensees notify the Department about various events is too broad. One commenter maintained that the requirement to notify the Department of any arrest, indictment or conviction of the licensee or its principals or substantial stockholders may create an impossible standard for compliance. The commenter noted that the licensee would

have to be aware of all such situations, which is unlikely in the case of a large company with numerous principals and stockholders. In addition, the commenter stated that the breadth of the requirement, covering even minor offenses, is too broad. The commenter suggested that the charge of disturbing the peace is a misdemeanor and if a 10 percent stockholder of a licensed lender is convicted of that offense, the conviction may be unknown to the licensee and irrelevant to the licensee's ability to lawfully conduct the business of a licensed lender.

The commenter stated that a better approach would be a requirement that the licensee notify the Department of a conviction of any of its principals if the conduct involved any financial business or involved fraud or financial crimes. One commenter further stated that if the Department of Banking and Insurance adopts the rules set forth in N.J.A.C. 3:15-2.16 regarding notification, it will be duty bound to investigate compliance with the rules, which will add to its already substantial administrative and supervisory burdens. The commenter stated that the Department will have to review and process what could be hundreds or thousands of notices each year. Further, the commenter stated that the proposal did not indicate for what purposes these notices might be used, or whether the notices are publicly available through the Freedom of Information Act or other requesting mechanism. The commenter also stated that the rule proposal does not demonstrate or claim that these notice requirements protect New Jersey's consumers or that the substance of these notices is relevant to the conduct of the business of licensed lenders.

RESPONSE: The Department disagrees that the notification requirement concerning the arrest, indictment or conviction of a licensee or of its principals or stockholders is too

broad. The language in the notification requirement mirrors the question on the subject of arrests, indictments or convictions that appears on every initial application to be a licensed lender, as well as on every renewal application. Further, it calls for information already on the public record. The addition of this reporting requirement is to ensure that the Department has current knowledge of any such occurrence between the initial license application and each succeeding license renewal. The Department has found that on renewal applications, licensees report events that have occurred well before the actual date of the renewal application. The Department believes that arrests, indictments or convictions directly related to lending or financial activities do represent a more serious level of concern. However, the Department believes that it is entirely appropriate to require the reporting of the information set forth in the proposal, since financial crimes are not the only matters that may impact upon a licensee's character and general fitness for continued licensure.

COMMENT: One commenter stated that the notification requirement at N.J.A.C. 3:15-2.16 with regard to any action against a professional license or other right to engage in business is too broad. The commenter stated that the notice requirement should be limited to actions against licensees or their principals that have some bearing on the lending business or on financial activities.

RESPONSE: The Department disagrees. Any action against a professional license or right to engage in business is serious, and to properly discharge its statutory duties the Department needs to be aware of such information. Allowing licensees to determine what action has "some bearing on the lending business or on financial activities" is not a

clear standard. In certain cases, the Department may not take action with regard to a situation about which it receives notice. However, in all such cases, it is necessary for the Department to assess the facts and determine whether the action affects the operation of the licensee's business and/or its eligibility for continued licensure.

COMMENT: One commenter stated that the visual advertisement regulation at N.J.A.C. 3:15-8.2 that requires that a statement indicating whether it is an advertisement for a first mortgage loan, second mortgage loan, consumer loan, retail installment contract, or retail charge account appear for the entire time that the advertisement is broadcast or disseminated is extremely cumbersome in a 30-second television spot, particularly in light of the many other Federal and State requirements that may apply. The commenter stated that the required statement may distract the consumer from other equally important disclosures that need not be displayed for this duration. The commenter recommended the substitution of the requirement that the disclosure be "clear and conspicuous." The commenter stated that the change would conform the New Jersey regulation to Federal Reserve Board Regulation Z, 12 CFR §§ 226.5(a)(1) and 226.17(a)(1).

RESPONSE: Since its adoption in 1997, the Department has had no reports of problems with compliance with this subchapter. The Department believes that the readoption of these rules continues a valuable level of notice to New Jersey consumers.

COMMENT: One commenter stated that the proposal at N.J.A.C. 3:15-2.3 regarding a branch office not being a separate business entity does not address asset acquisitions,

but only addresses purchases or mergers. The commenter suggested that the section be revised to address asset acquisitions, and to provide that the entity that sells its assets to another lender will be permitted to retain its branch office license in a “non-active” status. The commenter went on to note that providing this flexibility to the selling entity to re-enter the marketplace if the business relationship established with the acquiring entity is terminated would provide flexibility to the selling entity.

RESPONSE: The Department considers an asset acquisition to fall under the rule for purchases. The suggestion for the creation of “non-active status” for licensees is beyond the scope of the proposal.

COMMENT: One commenter supported the concept that a lender’s branch office should not pay its own core operating expenses as set forth in N.J.S.A. 3:15-2.3(f)2. The commenter went on to suggest that the proposal be amended to permit branch office staff to pay for certain expenses such as cell phones, car expenses and advertising.

RESPONSE: The Department appreciates the expression of support for the subchapter. If expenses represent operating costs of the office in conducting the licensed business, the position of the Department is that they must be paid for by the licensed entity.

COMMENT: One commenter agreed with the proposal at N.J.A.C. 3:15-2.3(f)3 that a branch office shall not maintain a bank account or an account for the payment of expenses that is separate from the account of the licensee.

RESPONSE: The Department appreciates the expression of support for the amendment.

COMMENT: One commenter endorsed the changes proposed at N.J.A.C. 3:15-2.3(f)4 and 5.

RESPONSE: The Department appreciates the expression of support for the amendment.

COMMENT: One commenter stated that the prohibition in N.J.A.C. 3:15-2.3(f)6 regarding indemnification of the lender against damages caused by branch office staff is overly broad.

RESPONSE: The Department disagrees. The rule makes it clear that a branch office is to be treated in the same way as the principal office.

COMMENT: One commenter suggested that N.J.A.C. 3:15-2.3(f)6 be amended to permit a lender to seek indemnification from branch employees for losses and expenses both during and after the period of employment with the lender.

RESPONSE: The Department believes its current position prohibiting indemnification by branches is sound and notes it is in accordance with HUD's mortgagee letter 00-15 dated May 1, 2000 prohibiting such indemnification.

COMMENT: One commenter stated that N.J.A.C. 3:15-2.3(f)6 should be amended to make a distinction between the calculation of profit and loss for purposes of calculating

commission payments to a branch manager and indemnification of losses attributable to fraud or malfeasance from the personal funds of the employee.

RESPONSE: The current rule makes it clear that a branch office is not a separate business entity. The concept of calculation of profit and loss for purposes of calculating commission payments to a branch manager may be an internal accounting function of a licensed lender but is not required to be made by this rule and the Department does not believe that it is appropriate to requires such a calculation. Likewise, the Department does not believe it is appropriate to make a distinction between such an internal accounting calculation done by a licensed lender and indemnification of losses attributable both to fraud or malfeasance between the personal funds of the employee as suggested by the commenter. Further, the Department has made it clear that indemnification agreements by branches is prohibited, and notes that any indemnification from the personal funds of an employee would also be prohibited.

COMMENT: One commenter stated that N.J.A.C. 3:15-2.3(f)6 should be amended to permit a lender to seek indemnification from a branch employee for any losses attributable to negligent acts by the employee. The commenter stated that it was his understanding that such indemnification occurs as a matter of business practice in the mortgage industry. The commenter stated that Federal and State agencies that regulate mortgage lenders hold the lender accountable for proper business practices, and that based on fundamental fairness, the lender should be permitted to hold its employees responsible for their conduct.

RESPONSE: The Department believes its current position prohibiting indemnification by branches is sound and notes it is in accordance with HUD's mortgagee letter 00-15 dated May 1, 2000 prohibiting such indemnification.

COMMENT: One commenter stated she believed that there was a technical error in N.J.A.C. 3:15-2.16(a)5 and that several words are missing. The commenter stated that the words "in any activity which" should be included before the phrase "may have a substantial impact."

RESPONSE: The Department agrees and will make the change upon adoption.

Summary of Changes upon Adoption:

The agency is making the following technical changes to the proposal upon adoption:

1. At N.J.A.C. 3:15-1.5(2)3, the rule's effective date is added.

2. The reference to N.J.A.C. 3:15-2.7(b) should be to N.J.A.C. 3:152.7(c) in N.J.A.C. 3:15-2.7(d).

3. Words added to N.J.A.C. 3:15-2.16(a)5 as set forth in the last Comment above.

Federal Standards Statement

The readopted rules with amendments do not contain any standards or requirements that exceed the standards or requirements imposed by Federal law. The readopted rules with amendments continue to apply certain Federal standards to New Jersey licensed lenders. The Federal standards involved are: The Real Estate

Settlement and Procedures Act, 12 U.S.C. § 2607, and the Depository Institutions Deregulation and Monetary Control Act of 1980, P.L. 96-221.

Full text of the readoption can be found in the New Jersey Administrative Code at N.J.A.C. 3:15.

Full text of the adopted recodification and amendments follows (additions to proposal indicated in boldface with asterisks ***thus*;** deletions from proposal indicated in brackets with asterisks * [thus] *):

3:!5-1.5 License names permitted

(a) The number of alternate or trade names that may be used by a licensee in this State shall not exceed three, unless:

1. – 2. (No change from proposal.)

3. The licensee has, prior to *(effective date of this rule)* ***November 4, 2002***, has been approved to use four or more alternate or trade names, in which case, the licensee may continue to use those names, but shall not be approved to use an additional alternate or trade name until the total number of alternate or trade names being used by that licensee is two or fewer, unless a larger number is permitted pursuant to (a)1 or 2 above.

3:15-2.7 Inactive license status; fee

(a) - (c) (No change from proposal.)

(d) A person who holds an inactive individual license may reactivate the individual license by submitting an individual license reactivation form as prescribed by the Commissioner to the Department including the payment of the appropriate license fee as set forth in N.J.A.C. 3:15-4.3, a $200.00 reactivation fee and proof of continuous employment as defined in *[(b)]* ***(c)*** above.

3:15-2.16 Licensee notification requirements

(a) A licensee shall notify the Department in writing within 15 days of the occurrence of any of the following:

1. - 4. (No change from proposal.)

5. Upon the involvement of the licensee, or any officer, director, partner, member, owner or substantial stockholder of the licensee, or any affiliate thereof, ***in any activity that*** may have a substantial impact on the ability of a licensee to engage in the licensed activity in a prudent or worthy manner.