

OFFICE OF LEGISLATIVE RESEARCH
PUBLIC ACT SUMMARY



PA 12-96—sSB 67

Banks Committee

Government Administration and Elections Committee

AN ACT CONCERNING REVISIONS TO THE BANKING STATUTES

SUMMARY: This act broadens the banking commissioner’s investigatory powers, and enables him to order restitution and disgorgement for banking law violations without seeking a court order.

It makes several changes to mortgage licensing provisions. For example, it modifies the existing licensing exemption for “quasi-governmental agencies” to instead apply to “housing finance agencies.” It also exempts bona fide nonprofit organizations that promote affordable housing or provide home ownership education or similar services.

The act (1) requires qualified individuals and branch managers working for lenders or brokers to be licensed as mortgage loan originators and to complete any applicable continuing education requirements by November 1, 2012, (2) changes loan processor or underwriter licensing requirements, and (3) prohibits the commissioner from denying a mortgage licensing application on the basis of an expunged criminal conviction.

It requires each bank to (1) review a mortgage loan before excusing the borrower from amortization of the loan principal and (2) consider an obligor’s credit exposure arising from a derivative transaction when determining the obligor’s liability limitations.

The act removes a loan production office from the definition of “limited branch,” thereby exempting it from certain requirements.

The act prohibits non-bank entities, not just corporations, from acting as trustees without a license. It also eliminates the reciprocity requirement for an out-of-state bank, other than a foreign bank, to establish a de novo branch in Connecticut.

The act eliminates the requirement that public depositories provide collateral for deposits that are insured by the Federal Deposit Insurance Corporation (FDIC) or National Credit Union Administration (NCUA). It also makes changes to required collateral amounts, including the amount required for an institution that has received a memorandum of understanding, a cease and desist order, or other similar letter or order from a supervisory agency.

The act allows state chartered banks to satisfy certain notice requirements by providing the banking commissioner with a copy of the same notice the bank must provide to the FDIC under federal law. It also enables banks to use regional federal home loan banks other than the Federal Home Loan Bank of Boston to issue letters of credit.

Lastly, the act redefines the meaning of “influencing real estate appraisals” for

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residential property; makes a clarifying change regarding interest on residential security deposits; and adds and modifies several definitions and makes minor, technical, and conforming changes.

EFFECTIVE DATE: October 1, 2012, unless otherwise noted below.

BANKING ADMINISTRATION AND ENFORCEMENT

§ 4 — Investigations, Examinations, and Subpoena Power

By law, the banking commissioner may make public or private investigations or examinations in or outside of Connecticut, concerning any person subject to his jurisdiction, as he deems necessary to carry out his duties.

Additionally, the act authorizes the banking commissioner to:

1. require or permit a person to testify, produce a record, or file a statement in writing, under oath, or otherwise as he determines, about a matter relevant to an investigation or a pending proceeding and
2. publish information concerning statutory violations within his jurisdiction or any regulation or order adopted or issued under such statutes.

The act subjects the commissioner's investigations and examinations to FOIA and the confidentiality requirements for state banking records.

The law already authorizes the commissioner to administer oaths and affirmations, subpoena witnesses, compel attendance of witnesses, take evidence, require written statements, and require the production of records which he deems relevant or material for an investigation.

The act also authorizes the commissioner to issue subpoenas in Connecticut at the request of another state, as long as the (1) same actions would serve as a basis for an investigation or other proceeding if they had occurred in Connecticut and (2) other state has reciprocal legal authority to issue subpoenas in that state on behalf of the commissioner.

§ 5 — Enforcement Action

The act expands the commissioner's authority over a person found, as the result of an investigation, in violation of a banking law, regulation, rule, or order.

Existing law authorizes the commissioner to apply to the Hartford Superior Court for an order of restitution, plus interest, for money illegally obtained. The act gives him the option of ordering the person, without a court order, to make restitution plus interest for money illegally obtained. The act also allows him to order the person to disgorge any such money, or both. The person may request a hearing, in accordance with the Uniform Administrative Procedure Act, within 14 days of receiving the order. The commissioner already has this authority regarding securities violations.

MORTGAGE LICENSING

§§ 7-8 — Mortgage Loan Originator Definition and Exemptions

Existing law defines a mortgage loan originator, subject to certain exemptions, as someone who, for compensation or gain or the expectation of such, (1) takes a

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residential mortgage loan application or (2) offers or negotiates residential mortgage loan terms. The act specifies that this includes someone either acting for personal compensation or gain or for the compensation or gain of his or her employer or retainer.

The act also specifies that, for licensing purposes, an individual is acting as a mortgage loan originator, unless exempt, if he or she:

1. does so in connection with any residential mortgage loan on behalf of a licensee or person exempt from licensing as a mortgage lender, correspondent lender, or broker or
2. makes any representation to the public through advertising or other means of communication that he or she can or will act as a mortgage loan originator on behalf of a licensee or a person exempt from licensure.

The act exempts from mortgage loan originator licensing requirements:

1. an individual who takes residential mortgage applications or offers or negotiates residential mortgage terms while acting in his or her official capacity as an employee of a (a) federal, state, or local government agency; (b) housing finance agency exempt from licensure; or (c) bona fide nonprofit organization exempt from licensure (see § 9) and
2. an individual who offers or negotiates the terms of a residential mortgage loan secured by a dwelling that he or she owns but does not live in, unless he or she habitually or repetitively makes such offers or negotiations.

Existing law exempts from originator licensing requirements an individual who offered or negotiated the terms of a residential mortgage loan secured by a dwelling where the person lived. Under the act, this exemption does not apply if he or she habitually or repetitively makes such offers or negotiations.

§ 7 — Mortgage Broker Definition

The act modifies exclusions from the definition of a mortgage broker. Existing law defines a mortgage broker as a person who, for compensation or gain or the expectation of such, takes a residential mortgage loan application or offers or negotiates a residential mortgage loan's terms. The act adds the condition that the person not be the prospective source of the funds for the loan.

Prior law excluded from the definition someone who is sponsored by another mortgage lender, correspondent lender, or broker. The act instead excludes an individual (1) who is licensed and acting as a mortgage loan originator on behalf of his or her sponsoring mortgage lender, correspondent lender, broker, or exempt registrant or (2) exempt from mortgage loan originator licensure when acting within the scope of the exemption.

§ 9 — Mortgage Lender and Correspondent Lender Licensing Exemption

The act modifies the existing exemption from mortgage lender and mortgage correspondent lender licensure for "quasi-governmental agencies" to instead apply to "housing finance agencies." By law, these agencies are exempt when making residential loans under the specific authority of federal or any state's law.

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The act defines a housing finance agency as any authority (1) chartered by a state to help meet the affordable housing needs of the state's residents, (2) supervised directly or indirectly by the state government, (3) subject to audit and review by the state in which it operates, and (4) whose activities make it eligible to be a National Council of State Housing Agencies (NCSHA) member (The NCSHA is a nonprofit, nonpartisan organization created by the nation's state housing finance agencies to coordinate and leverage their federal advocacy efforts for affordable housing.)

Prior law exempted a person making a secondary mortgage loan to a person related to him or her by blood or marriage. The act narrows this exemption to a person making a secondary mortgage loan to an immediate family member.

§ 9 — *Bona Fide Nonprofit Organizations Licensure Exemption*

The act exempts a bona fide nonprofit organization from licensure as a mortgage broker when the organization brokers residential loans exclusively made by any (1) corporation or affiliate that makes residential mortgage loans exclusively for the benefit of its employees or agents or (2) insurance company or health care center, or its affiliate or subsidiary, that makes residential mortgage loans to promote home ownership in urban areas. (By law, these same organizations are also exempt from licensure as mortgage lenders or correspondent lenders.)

Prior law exempted from mortgage lender or correspondent lender licensing requirements any bona fide nonprofit corporation that makes residential mortgages promoting home ownership for the economically disadvantaged. The act extends this exemption to bona fide nonprofit organizations, not just corporations, meeting this standard.

The act defines a bona fide nonprofit organization as an organization that has filed with the commissioner a written, certified submission in a form prescribed by the commissioner, along with other required documentation, demonstrating that the organization:

1. is a tax-exempt organization under IRS Code § 501(c)(3);
2. promotes affordable housing or provides home ownership education or similar services;
3. acts in a way that serves public or charitable, rather than commercial, purposes;
4. receives funding and revenue, charges fees, and compensates its employees in a way that does not incentivize it or its employees to act other than in the best interests of its clients;
5. provides or identifies for the borrower residential mortgage loans (a) with favorable terms to the borrower (i.e., terms consistent with loan origination in a public or charitable, and not commercial, context) and (b) comparable to mortgage loans and housing assistance provided under government housing assistance programs; and
6. meets any other standards the commissioner may by regulation require.

The act requires each bona fide nonprofit organization to submit, no later than

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December 31 of each year, a renewed certification and documentation with any updated information to the commissioner.

§ 8 — Loan Processors or Underwriters

Prior law required a loan processor or underwriter to be licensed if he or she was (1) an independent contractor or (2) employed by any person other than a licensed mortgage lender, correspondent lender, or broker or specified financial institution exempt from such licensure.

The act instead requires any individual engaged in loan processing or underwriting to be licensed, but provides an exemption for:

1. an employee of a licensed mortgage lender, correspondent lender, or broker who processes or underwrites residential mortgage loans originated or made by the licensee at the direction, and subject to the supervision, of a licensed mortgage loan originator;
2. an employee of a specified financial institution exempt from mortgage lender, correspondent lender, or broker licensing who processes or underwrites loans at the direction, and subject to the supervision, of either a licensed mortgage loan originator or a registered mortgage loan originator of the exempt entity; or
3. any individual engaged in loan processing or underwriting in connection with a residential mortgage loan originated by an individual not required to be licensed or registered as a mortgage loan originator.

Prior law required loan processors to register, and maintain a valid unique identifier, with the Nationwide Mortgage Licensing System and Registry (NMLSR) (see BACKGROUND). The act specifies that this requirement applies to licensed loan processors.

The act prohibits loan processor or underwriter licensees from being sponsored by more than one person at a time.

§ 7 — Employee and Independent Contractor Definitions

Existing mortgage licensing laws refer in various places to licensees or exempt registrants sponsoring someone, and define “sponsored” for this purpose as employed or retained as an independent contractor.

The act defines an “independent contractor” as an individual (1) retained on a basis where he or she is not the employee of anyone in connection with the services provided and (2) whose compensation is reported on an IRS Form 1099 (used by businesses to document non-employee payments larger than \$600 made to individuals or other businesses during the year) issued by the retaining person.

Various provisions in the mortgage licensing laws also refer to employees. The act defines an “employee” as an individual whose (1) work performance is subject to the right of control of, or is controlled by, a person and (2) compensation is reported on a W-2 form issued by the controlling person. For purposes of defining a “registered mortgage loan originator,” the term “employee” retains this meaning or any meaning the federal banking agencies issue in connection with the Secure and Fair Enforcement for Mortgage Licensing

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Act of 2008 (S.A.F.E. Act).

By law, a “registered mortgage loan originator” is any individual who (1) meets the definition of mortgage loan originator and is an employee of (a) a depository institution, (b) a subsidiary owned and controlled by a depository institution and regulated by a federal banking agency, or (c) an institution regulated by the Farm Credit Administration and (2) is registered with, and maintains a unique identifier through, NMLSR.

§§ 10 – 11 & 13 — Qualified Individual and Branch Manager Licensing Requirements

Existing law requires mortgage lenders, correspondent lenders, or brokers seeking licensure to have qualified individuals at the main office and branch managers at each branch office who meet certain experience, education, and testing requirements. The act requires that, effective November 1, 2012, qualified individuals and branch managers must also (1) be licensed as mortgage loan originators and (2) if seeking initial licensure as mortgage loan originators, have completed any continuing education requirements associated with their positions.

Under the act, a qualified individual or branch manager who held the position at a time prior to the implementation of the mortgage loan originator licensing requirements cannot hold such a position again before completing all continuing education requirements for the year in which he or she last held the position and, effective November 1, 2012, he or she must also obtain the required license before holding such a position again.

§§ 11 - 12 — Expunged Criminal Convictions and License Eligibility

The act prohibits the banking commissioner from denying a mortgage lender, correspondent lender, broker, loan originator, or loan processor or underwriter license on the basis of an expunged criminal conviction. The law already prohibits the banking commissioner from denying such licenses on the basis of a pardoned criminal conviction.

The act also specifies that the level of criminal offense and the status of any conviction, pardon, or expungement will be determined based on the law of the jurisdiction where the case was prosecuted.

§ 13 – Testing Requirements

By law, an applicant for a mortgage lender, originator, or broker license must, among other requirements, pass a written test developed by NMLSR and administered by an NMLSR-approved test provider. The act decreases, from four to three, the number of consecutive times an applicant may retake the written test, with each consecutive test occurring at least 30 days after the previous test, before he or she must wait at least six months to retake the test.

The act makes other minor and conforming changes related to education and testing requirements.

§§ 8 & 14 — Banking Commissioner Enforcement Action

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The act allows the commissioner to bring an enforcement action or issue a cease and desist order if it appears to him that someone is violating or would violate the mortgage licensing statutes or regulations due to an act or omission the person knew or should have known would contribute to the violation.

The law already allows the commissioner to bring an enforcement action or issue a cease and desist order if it appears to him that (1) someone has violated, is violating, or is about to violate the mortgage licensing statutes or regulations or (2) a licensee has failed to perform an agreement with a borrower, committed any fraud, misappropriated funds, or misrepresented, concealed, suppressed, intentionally omitted, or otherwise intentionally failed to disclose any material particulars of any residential mortgage loan transaction to anyone entitled to such information.

Existing law also allows the commissioner to suspend, revoke, or refuse to renew any mortgage lender, correspondent lender, or broker license for any reason that would be sufficient to deny a license application, or if he finds that a licensee, the licensee's control person, the qualified individual or branch manager with supervisory authority, trustee, employee, or agent of the licensee has:

1. made any material misstatement in the license application;
2. committed any fraud; misappropriated funds; or misrepresented, concealed, suppressed, intentionally omitted, or otherwise intentionally failed to disclose any of the material particulars of any residential mortgage loan transaction;
3. violated any of the licensing provisions or laws or regulations applicable to the conduct of its business; or
4. failed to perform any agreement with a licensee or a borrower.

The act specifies that the term "agent," when used in reference to individuals under the banking commissioner's jurisdiction, includes any settlement agent used by the licensee. The act also defines a "settlement agent" as a person specified in a HUD-1 settlement statement (a statement of actual settlement costs which the U.S. Department of Housing and Urban Development (HUD) furnishes to the homeowner) who was selected by the licensee. Any settlement agent appearing on the licensee's list of approved settlement agents is deemed selected by the licensee even if the borrower selects the name from the list.

By law, each residential mortgage loan negotiated, solicited, arranged, placed, found, or made without a license constitutes a separate violation for purposes of the commissioner's general enforcement authority. Under the act, this also applies to each such loan taken, offered, processed, or underwritten without a license.

§ 16 — Reporting Requirements

By law, each licensed mortgage lender, correspondent lender, broker, loan originator, and loan processor or underwriter must submit reports of condition (including financial data and residential mortgage loan activity data) to the NMLSR. The act extends this requirement to entities registered with NMLSR but exempt from licensure, and requires the reports to be accurate and submitted in a timely manner. A licensee's or exempt registrant's failure to submit a timely and

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accurate report of condition constitutes a violation of this provision.

Additionally, the act makes an exempt registrant's failure to submit a report of condition timely and accurately a basis to inactivate the licenses of all mortgage loan originators, loan processors, or underwriters it sponsors. To the extent NMLSR does not require individual mortgage loan originators or loan processors or underwriter licensees to submit reports of condition, the act requires licensees to timely and accurately report all required information in their possession to their sponsor for the sponsor's reporting obligation. Failure to do so constitutes a violation of this provision.

§§ 18 – 21 & 31 — LOAN PRODUCTION OFFICE

The act defines a "loan production office" as an office of a Connecticut bank or out-of-state bank, other than a foreign bank, whose activities are limited to loan production and solicitation. The act enables Connecticut banks and out-of-state banks other than foreign banks, with the approval of the banking commissioner, to establish loan production offices in the state.

Existing law defines a "limited branch" to mean any office at a fixed location of a Connecticut bank at which banking business is conducted other than the main office, branch, or mobile branch. The act excludes loan production offices from the definition of limited branch, thus exempting loan production offices from certain requirements that apply to limited branches (e.g., notice requirements for branch closures).

The act imposes a \$1,000 application fee to establish a loan production office. By law, the fee to establish a limited branch is \$1,500.

EFFECTIVE DATE: Upon passage

LOANS

§ 22 — *Mortgage Amortization*

Prior law allowed a Connecticut bank, at its discretion, to excuse a mortgage loan borrower from amortization of the loan principal. The act requires the bank's governing board, or a management committee or board committee it designates, to first review the mortgage loan and determine that excusing the borrower from amortization would be prudent under the circumstances.

EFFECTIVE DATE: Upon passage

§ 23 — *Derivative Transactions*

The act requires a bank to consider an obligor's credit exposure arising from a derivative transaction when determining the obligor's liability limitations. It gives the commissioner the authority to establish a method for determining credit exposure and the extent to which the credit exposure will be taken into account and allows him to adopt regulations for this purpose.

"Derivative transaction" includes any transaction that is (1) a contract, agreement, swap, warrant, note, or option and (2) based, in whole or part, on the value of any interest in, or any quantitative measure of, or the occurrence of any

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event leading to, one or more commodities, securities, currencies, interest, or other rates, indices, or other assets.

§§ 24 - 29 — FIDUCIARY POWERS OF CORPORATIONS OTHER THAN BANKING INSTITUTIONS

Existing law generally prohibits corporations, other than banks, from receiving any money, securities, or other personal property or real estate in trust, to manage on someone else's behalf, unless the corporation is specifically allowed to do so by state statute or a special act of the General Assembly. If the law allows the corporation to act as trustee, it must first obtain a license from the banking commissioner.

The act broadens the prohibition to apply to other nonbank entities instead of just corporations. It defines an "entity" as a corporation, joint stock company, association, partnership, limited partnership, unincorporated organization, limited liability company, or similar organization, excluding those of which the majority of shares are owned by the United States or any state. The act also expands the trustee licensing requirements and exemptions to apply to all such nonbank entities instead of only to corporations, and makes other conforming changes.

§ 30 — DE NOVO BRANCHES OF OUT-OF-STATE BANKS

Under existing law, an out-of-state bank, other than a foreign bank, may, with the banking commissioner's approval, establish a de novo (new) branch in Connecticut as long as the bank's state allows Connecticut-based institutions to do the same there, among other requirements. Prior law allowed the commissioner to waive this reciprocity requirement in limited circumstances. The act eliminates this reciprocity requirement altogether.

EFFECTIVE DATE: Upon passage

§ 32 — RENTAL SECURITY DEPOSITS

PA 11-94 eliminated the requirement that landlords pay a minimum 1.5% interest rate on residential security deposits. The act clarifies that this change does not affect security deposits before January 1, 2012 (PA 11-94's effective date).

EFFECTIVE DATE: Upon passage

§§ 35 – 42 – UNINSURED PUBLIC DEPOSITS

Collateral Requirements for Public Deposits (§§ 36 – 39 & 41 – 42)

The act decreases collateral requirements for banking institutions allowed to hold public funds (i.e., qualified public depositories).

By law, public deposits are funds:

1. received or held in a qualified public depository from (a) the state or any of its political subdivisions; (b) a commission, committee, board, or officer of the state or its political subdivisions; (c) a housing authority; or (d) a Connecticut court or
2. held by the Judicial Department in a fiduciary capacity.

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Prior law required qualified public depositories that received or held public deposits to maintain collateral equal to a specified percentage of their public deposits. The act instead ties the collateral amount to the institution's percentage of uninsured public deposits, thus decreasing the amount of collateral that it must maintain. The act defines an "uninsured public deposit" as the portion of a public deposit not insured or guaranteed by FDIC or NCUA.

As under prior law, an institution's collateral requirement depends on its risk-based capital ratio, which is a measure of its financial strength.

Prior law also required public depositories to determine the minimum market value of eligible collateral (see BACKGROUND) by applying a collateral ratio, calculated as the market value of the eligible collateral pledged divided by the public deposit plus accrued interest. The act changes the calculation of the collateral ratio to equal the value of the eligible collateral pledged divided by the uninsured public deposit plus accrued interest.

The act also makes conforming changes.

Depositories Subject to Certain Orders (§§ 37 & 39)

Prior law required a public depository that was subject to a cease and desist order, or that entered into a stipulation and agreement or letter of understanding and agreement with a bank or credit union supervisor, to maintain as collateral, apart from its other assets, 120% of all public deposits it held, unless the depository and the public depositor agreed on a greater percentage.

The act changes the collateral requirement to 120% of the public depository's uninsured public deposits. The public depository may have a collateral requirement of 100% of all its uninsured public deposits if the depository has a risk-based capital ratio of 12% or greater and it satisfies the following conditions, to the extent applicable:

1. the depository may not pledge mortgage pass-through or participation certificates or similar securities as eligible collateral unless they have been issued or guaranteed by the Federal National Mortgage Association or Federal Home Loan Mortgage Corporation and for which prices are quoted;
2. the depository may not pledge as eligible collateral issues of Government National Mortgage Association pass-through or participation certificates or similar securities for which prices are not quoted;
3. if the depository pledges one- to four-family residential mortgages as eligible collateral, the mortgage collateral ratio must be 150%; and
4. if the depository pledges state and municipal bonds as eligible collateral, the bonds must be rated in the three highest rating categories by a rating service recognized by the commissioners.

The depository may pledge any other eligible collateral not limited above.

EFFECTIVE DATE: Upon passage

Letters of Credit (§ 40)

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Under prior law, a public depository could secure a public deposit with an irrevocable letter of credit, in lieu of eligible collateral, from the Federal Home Loan Bank of Boston.

The act expands the public depository's options by allowing it to supply a letter of credit as collateral support for its uninsured public deposits from a federal home loan bank that:

1. has the highest rating from a rating service recognized by the banking commissioner or
2. the banking commissioner deems acceptable for such purposes, provided the letter of credit amount, when combined with any eligible collateral pledged by the depository, as a percentage of uninsured public deposit, meets the depository's minimum eligible collateral requirement.

EFFECTIVE DATE: Upon passage

Reporting Requirement (§ 42)

Prior law required a public depository to regularly report to the banking commissioner, among other things, the total amount of public deposits it held.

The act modifies the reporting requirement to apply to the depository's public deposits other than those that have been redeposited into the depository by another insured depository institution according to a reciprocal deposit arrangement that makes such funds eligible for FDIC or NCUA insurance coverage.

EFFECTIVE DATE: Upon passage

§ 34 – INFLUENCING REAL ESTATE APPRAISALS

The law prohibits any person from influencing real estate appraisals of residential property. The act redefines the meaning of such influence.

Prior law defined "influencing residential real estate appraisals" as to directly or indirectly coerce, influence, or otherwise encourage an appraiser to misstate or misrepresent the value of residential property including refusing, or intentionally failing, to (1) pay an appraiser for an appraisal that reflects a fair market value estimate that is less than the sale contract price or (2) use, or encourage other mortgage brokers not to use, an appraiser based solely on the fact that the appraiser provided an appraisal reflecting a fair market value estimate that was less than the contract price.

The act defines "influencing real estate appraisals" as directly or indirectly causing or attempting to cause, through coercion, extortion, inducement, bribery, intimidation, compensation, instruction, or collusion, the value assigned to the residential property to be based on any factor other than the appraiser's independent judgment.

EFFECTIVE DATE: Upon passage

BACKGROUND

Eligible Collateral for Public Depositories

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The law defines eligible collateral as:

1. U.S. Treasury bills, notes, and bonds,
2. U.S. government agency securities,
3. U.S. agency variable rate securities,
4. mortgage pass-through or participation certificates or similar securities,
5. one-to-four family residential mortgages that meet certain criteria, and
6. state and municipal bonds (CGS § 36a-330).

Nationwide Mortgage Licensing System and Registry (NMLSR)

NMLSR was implemented pursuant to a uniform mortgage licensing project under the auspices of the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators for the licensing and registration of mortgage lenders, correspondent lenders, brokers, and loan originators.

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