DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Part 3500

[Docket No. FR–4173–P–01]

RIN 2502–AG88

Amendments to Real Estate Settlement Procedures Act Regulation: Exemption for Employer Payments to Employees Who Make Like-Provider Referrals and Other Amendments; Proposed Rule

AGENCY: Office of the Assistant Secretary for Housing-Federal Housing Commissioner, HUD.

ACTION: Proposed rule.

SUMMARY: In this proposed rule, the Department is seeking comments on a new exemption under Regulation X, its regulation implementing the Real Estate Settlement Procedures Act of 1974 (RESPA). The exemption would allow payments by an employer to its own *bona fide* employees for the referral of settlement service business to an affiliated settlement service provider, provided that the settlement service business that is referred is the same category of settlement service as provided by the employer of the employee making the referral, the employee makes the affiliated business arrangement disclosure as provided in 24 CFR 3500.15, and the employee making the referral does not perform any other category of settlement service in the same transaction.

This rule also proposes to implement two amendments to RESPA in recent legislation. One concerns referrals of settlement service business through telemarketing, in writing, or through electronic media. The other concerns mortgage servicing sales or transfers. The rule also describes additional technical corrections and clarifications the Department intends to make at a later date.

DATES: *Comment due date:* July 8, 1997.

ADDRESSES: Interested persons are invited to submit comments regarding this proposed rule to the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410–0500. Communications should refer to the above docket number and title. Facsimile (FAX) comments are not acceptable. A copy of each communication submitted will be available for public inspection and copying between 7:30 a.m. and 5:30 p.m. weekdays at the above address.

The Department also invites interested persons to submit comments on the proposed information collection requirements in § 3500.15(b) of this proposed rule. Comments should refer to the above docket number and title, and should be sent to the Office of Information and Regulatory Affairs, Office of Management and Budget, Attention: Desk Officer for HUD, Washington, DC 20503.

FOR FURTHER INFORMATION CONTACT: David R. Williamson, Director, Office of Consumer and Regulatory Affairs, Room 9146, telephone (202) 708–4560; or, for legal questions, Kenneth A. Markison, Assistant General Counsel for GSE/RESPA, Grant E. Mitchell, Senior Attorney for RESPA, or Richard S. Bennett, Attorney, Office of General Counsel, Room 9262, telephone (202) 708–1550. (The telephone numbers are not toll-free.) For hearing- and speech-impaired persons, these numbers may be accessed via TTY (text telephone) by calling the Federal Information Relay Service at 1–800–877–8339. The address for the above-listed persons is: Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410.

SUPPLEMENTARY INFORMATION:

I. Background

In the final rule published on June 7, 1996 (61 FR 29238) entitled ''Amendments to Regulation X, the Real Estate Settlement Procedures Act: Withdrawal of Employer-Employee and Computer Loan Origination Systems (CLOs) Exemptions,'' the Department withdrew a broad exemption for payments by employers to their own employees for any referral activities (24 CFR 3500.14(g)(1)(vii)). In its place, the rule established three narrower exemptions for employer payments to employees: (1) One for managerial employees (§ 3500.14(g)(1)(viii) of the June 7 rule); (2) One for employees who do not perform settlement services in any transaction (§ 3500.14(g)(1)(ix) of the June 7 rule); and (3) A provision clarifying that ''[a] payment by an employer to its own *bona fide* employee for generating business for that employer'' is permissible (§ 3500.14(g)(1)(vii) of the June 7 rule). The rule was to have become effective on October 7, 1996, 120 days from publication. (Note: The June 7 rule was corrected and revised on August 12, 1996 (61 FR 41944).)

Section 2103 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996, (Title II of the Omnibus Consolidated Appropriations Act, 1997) (Pub. L. 104–208; approved September 30, 1996) (the Act) was signed by the President on September 30, 1996. The Act delayed the effective date of the provisions of the Department's June 7, 1996 final RESPA rule concerning payments to employees by their employers to no earlier than July 31, 1997.

Although not required by the Act, on October 4, 1996 (61 FR 51782), the Department delayed temporarily the effective date of the entire June 7 final rule, as corrected and revised on August 12, 1996. The reason for the delay was to provide the Department with an opportunity to analyze the Act and develop an appropriate time schedule for establishing the effective dates of the various provisions of the June 7 rule, as revised August 12.

On November 4, 1996 (61 FR 56624), the Department published another notice in the **Federal Register** announcing that, consistent with the Act, the Department would shortly publish a revised final rule that would make effective those provisions of the June 7 final rule that are unaffected by the delay provisions of the legislation. On November 15, 1996 (61 FR 58472), the Department published a final rule in the **Federal Register** making effective certain portions of the June 7 final rule and August 12 technical revisions that were not delayed by the Act. The November 15, 1996 final rule put into effect those portions of the June 7 final rule dealing with Computer Loan Origination (CLO) Systems. The November 15 final rule thereby effectuated the withdrawal of the CLO exemption and the elimination of the CLO Fee Disclosure form. It also put into effect the revised Appendix D to part 3500 as published August 12, 1996. Further, it made several technical revisions and corrections to Regulation X.

This proposed rule furthers the plans indicated in the November 4, 1996 notice to move forward as expeditiously as possible, subject to the requirements of the Act, to establish new rules addressing employer payments to employees in lieu of the former broad exemption. It also proposes, in conjunction with putting into effect the revisions in the June 7 rule concerning employer payments to employees, to establish a new exemption. This exemption would allow payments by an employer to its own *bona fide* employees for the referral of settlement service business to an affiliated settlement service provider, under the following conditions: (1) The settlement service business that is referred is the same category of settlement service as provided by the employer of the employee making the referral; (2) The employee makes the affiliated business

arrangement disclosure in accordance with 24 CFR 3500.15; and (3) The employee does not perform any other category of settlement service in the same transaction. The Department anticipates that this new exemption will become effective at the same time as the Department makes the changes that were delayed by the Act (i.e., eliminating the exemption for payments by an employer to its employees for referral activities, currently codified as 24 CFR 3500.14(g)(1)(vii), and substituting the more limited exemptions that the June 7 rule would have codified as 24 CFR 3500.14(g)(1)(vii)-(ix))). The Act does not permit the Department to make those changes before July 31, 1997, or to announce an effective date for those provisions more than 180 days before the effective date.

The Department also anticipates making the following technical clarifications and corrections to those provisions of the June 7 rule, as part of the final rule that will make those provisions effective subject to the requirements of the Act:

(1) A technical clarification indicating that under the managerial exemption (§ 3500.14(g)(1)(viii) of the June 7 rule), a manager not routinely performing settlement services may still receive compensation under the exemption if either: (1) The total value of the services provided by the manager does not exceed 5 percent of the annual income to the office or unit for which the manager is responsible attributable to RESPA-covered transactions, *or* (2) the manager performs settlement services in no more than three RESPA-covered transactions.

(2) A technical clarification indicating that in using the term ''in any transaction'' in the exemption for employees who do not perform settlement services (§ 3500.14(g)(1)(ix) of the June 7 rule), the Department did not intend that an employee who has stopped providing settlement services, an employee who changes jobs and no longer provides settlement services, or a new employee is forever prohibited from receiving compensation for referrals.

(3) A technical correction redesignating ''Controlled Business Arrangements'' as ''Affiliated Business Arrangements'' or ''AfBAs,'' reflecting the change in terminology in section 2103(c) of the Act.

(4) A technical correction relating to the timing of providing the AfBA disclosure, to conform the language of the regulation and Appendix B more closely to the statutory language as revised in section 2103(d) of the Act, to provide consistently that the AfBA disclosure statement must be provided in accordance with § 3500.15(b).

This proposed rule also proposes to implement amendments to RESPA contained in the Act. One amendment concerns referrals through telemarketing and electronic media. The other amendment concerns mortgage servicing sales, assignments, or transfers under section 6 of RESPA.

Finally, the proposed rule proposes some changes in response to section 2101 of the Act. In that section, Congress mandated that the Department and the Federal Reserve Board (the Board) work together to ''simplify and improve'' the disclosures given in a mortgage transaction subject to the Truth in Lending Act (TILA) and RESPA, and to create a unified format to satisfy the requirements of both statutes. On December 31, 1996, the Department and the Board published an Advance Notice of Proposed Rulemaking (ANPR) on Improvement of Disclosures Under RESPA and TILA (61 FR 69055), in order to solicit suggestions from the public regarding possible ways to simplify and improve disclosures required under the statutes. The Department received 82 comments from all sectors of the industry in response to the ANPR. The preamble of this rule describes how the Department proposes to incorporate some of the suggestions and recommendations generated by the ANPR into this proposed rule. The Department anticipates that other suggestions could be incorporated into subsequent rulemaking.

The Department believes, however, that significant simplification may only be possible through legislative changes and will work with the Board in making recommendations towards that end. Under the Act, Congress has required that the Department and the Board recommend any legislation that would be necessary to accomplish the objectives of simplifying and improving the disclosures subject to TILA and RESPA. Both agencies are currently considering several approaches to streamlining the disclosure requirements.

II. Proposed Exemption for Like-Provider Referrals

A. Description of Problem

The Department published a proposed rule on July 21, 1994 (59 FR 37360) to revise Regulation X. During the comment period on the Department's July 21, 1994 proposed rule, some commenters raised concern that the Department's proposed withdrawal of the broad exemption for employer payments to employees for referrals and its replacement with narrower exemptions would unduly restrict compensation of bank employees for making referrals to mortgage banking affiliates. A major trade association for the banking industry, for example, raised concern that while a banker could compensate its employee for the referral of mortgage loan business to a mortgage lending division within the bank, a banker would be prohibited from compensating an employee for the referral of a bank customer to a mortgage banking affiliate of the bank or a mortgage banking subsidiary of the parent holding company.

The trade association urged the Department to reconsider making such a distinction in its final rule, arguing that the distinction lacked justification or merit and, in essence, was solely based on the structure of the bank and the location of the mortgage lending function within the banking institution. The trade association explained that the proposed rule would penalize banks, their affiliates, holding companies, boards of directors, officers, and employees solely because of their corporate structures, which ''are specifically authorized by statute, implemented by state or Federal bank regulatory authorities and constantly monitored and examined for safety and soundness and compliance purposes.'' The trade association argued:

> From the consumer's perspective, the location of this mortgage lending activity within the banking institution's family of companies is irrelevant. The consumer's objective is to obtain a mortgage loan. To the consumer and the bank, this is the *business of banking* whether it takes place within the bank or as part of the banking institution's corporate family.

Since the Department's promulgation of its final rule on June 7, 1996, withdrawing the broader exemption and establishing more limited exemptions, similar concerns have been echoed by others. A mortgage lending subsidiary of a diversified financial services company indicated that for various business and regulatory reasons, it offers its services through more than one corporate entity. It argued that bank branch personnel should be able to receive compensation for referring customers who enter the branch and inquire about a first mortgage loan to the mortgage lending subsidiary. It pointed out that there is no danger of adverse steering since the customer is provided the controlled business disclosure (now referred to as the Affiliated Business Arrangement Disclosure Statement or AfBA Disclosure Statement), which alerts the

customer that he or she is dealing with the mortgage lending subsidiary; from the customer's perspective, the loan is still from the bank.

A major bank made essentially the same arguments. It faulted the June 7 rule for failing to accommodate the practice of referral of loan business by a lender to its affiliate. In a letter to the Department, the bank stated:

We believe that when a consumer comes to [the bank] to inquire about mortgage financing, whether to purchase a home or refinance an existing mortgage, the consumer has come to us because of our name and reputation. Whether contact is made in person at a branch office, by phone, or over the Internet, the consumer expects to learn about [bank] loan products that meet his or her financing needs, regardless of whether such loans are marketed, originated or serviced by different * * * legal entities. It makes little or no difference to our borrowers which * * * subsidiary originates their loans or whether their original contact was a loan officer employed by a different subsidiary. * * *

Without a change to the final rule, we will be forced into a costly reorganization to create a permissible compensation structure. We would either have to staff each branch with one or more mortgage lending division loan officers, or originate and book mortgage loans in each branch where the initial inquiry was made. In either case, any potential economies would be eliminated without adding value or convenience for our customers.

B. Proposed Solution

Under the June 7 rule, if a bank customer asks a loan officer who provides settlement services in any transaction about a type of loan that the bank does not make, but which the bank's affiliate does make, the bank would have been precluded from compensating the loan officer for making the referral to the appropriate affiliate. However, the June 7 rule would have created an exemption to the prohibition against referral fees for employer payments to employees who do not perform settlement services in any transaction and who refer settlement service business to an affiliate, so long as the controlled business arrangement disclosure is provided. Thus, an employee of a bank could have referred a bank customer to a mortgage banking affiliate of the bank or a mortgage banking subsidiary of the parent holding company and could have received referral-based compensation. The only restrictions would have been that the controlled business arrangement disclosure would have to be provided, and, if the employee was to be compensated for the referral, the employee could not be one who performed settlement services in any residential real estate transaction covered by RESPA. (Part V(B) of this preamble discusses the meaning of ''in any transaction.'')

In light of certain of the expressed concerns, the Department is proposing to exercise its exemption authority under RESPA, to add a new exemption to section 8 of RESPA's prohibition against kickbacks and unearned fees. The Secretary has authority to create exemptions under section 19(a) of RESPA for classes of transactions as may be necessary to achieve the purposes of RESPA (12 U.S.C. 2617(a)). In addition, under section 8(c)(5) of RESPA, the Secretary may create regulatory exemptions for ''such other payments or classes of payments,'' after consulting with various Federal agencies (12 U.S.C. 2607(c)(5)). The exemption to be created under this proposed rule, like the exemptions promulgated June 7, would be issued pursuant to the Secretary's clear authority to create reasonable exemptions to further the purposes of RESPA.

Under the proposed exemption, § 3500.14(g)(1) would be amended by adding an exemption for a payment by an employer to its *bona fide* employee for referring settlement service business to a settlement service provider that has an affiliate relationship with the employer, or in which the employer has a direct or beneficial ownership interest of more than 1 percent, if the following conditions are met:

1. The settlement service business that is referred is the same category of settlement service that the employer of the employee making the referral provides;

2. The employee provides to the person being referred the affiliated business arrangement disclosure in accordance with § 3500.15(b); and

3. The employee making the referral does not perform any other category of settlement service in the same transaction.

The rule would specify that, for purposes of this exemption, each paragraph in the definition of ''settlement service'' provided in 24 CFR 3500.2(b) (excluding paragraphs (b)(15) and (b)(16) of that definition), as it is proposed to be revised, constitutes a separate ''category of settlement service.'' Some ''categories of settlement services'' to which this exemption might commonly apply would include originating mortgage loans, providing services involving hazard insurance, and providing title services.

While the rendering of services by a real estate agent or real estate broker is a settlement service (*see* paragraph (b)(15) of the definition of ''settlement service'' in § 3500.2 as proposed to be revised), referrals from one real estate agent or broker to another are generally exempt pursuant to section 8(c)(3) of RESPA (12 U.S.C. 2607(c)(3)) and 24 CFR 3500.14(g)(1)(v) of the RESPA regulations. Because the section 8(c)(3) exemption already exists, the referral of services by a real estate agent or real estate broker to another real estate agent or real estate broker is not included under the new exemption. In addition, real estate agents are usually independent contractors, and thus would not be considered ''employees'' eligible for this exemption for employer payments to employees.

In addition, paragraph (b)(16) of the definition of ''settlement service'' in § 3500.2 as proposed to be revised includes as a settlement service ''other services for which a settlement service provider requires a borrower or seller to pay.'' This catchall, however, is too open-ended to apply to the new exemption proposed. Commenters are encouraged to provide examples of other settlement services that would qualify under paragraph (b)(16). The Department will consider the examples submitted and possibly add them to the list of categories of settlement services enumerated in the definition so that referrals of such services may qualify for the new exemption proposed.

As with the exemptions contained in the June 7 rule, this additional exemption only pertains to *bona fide* employees. Individuals may not be hired on a part-time basis to make referrals because of their access to consumers as settlement service providers and then be compensated for such referrals. Sham employment arrangements are also prohibited. *See* 61 FR 29243 (column 3). Moreover, the exemption does not affect the prohibition in 24 CFR 3500.14(b) against the entity to which business is referred from compensating the affiliate or the employee of the affiliate making the referral.

It is anticipated that when the Department makes this proposed rule final, it will do so in a rule that will also make effective the changes to the exemptions for employer payments to employees as contained in the June 7 rule, subject to any further technical corrections or clarifications to such exemptions that the Department may announce. The language of the June 7 rule and the technical corrections and clarifications are not republished here, since the Department is not requesting comments on them.

C. Questions for Commenters

The Department is particularly interested in comments on the following issues:

1. What potential disadvantages or dangers, if any, would the exemption for employer payments to employees who make like-provider referrals pose for consumers? As summarized above, it has been argued by members of the settlement service industry that in the types of referrals covered by the proposed rule, there is little danger of adverse steering or adverse consequences to customers. However, the Department would like to hear from those with other views, including those with additional bases in support of such an exemption.

2. The Department seeks comments on whether a potential danger is created for consumers that, through the design of compensation systems, the exemption could cause greater steering of consumers to products that are more profitable for the entity making or receiving the referral, but that are not necessarily in the consumer's best interest. For example, a loan officer of a lender that makes home equity loans might receive a $50 bonus for every home equity loan closed. In contrast, the same loan officer might receive a $100 bonus for referring a customer who inquires about a home equity loan to an affiliate of the lender that will refinance the primary mortgage, or $150 if he or she could originate the refinance of the primary mortgage in the name of the affiliate (and do only a minimum of work regarding origination of the loan). Please comment on whether this exemption would create a danger that consumers will be steered for reasons other than what is in their best interest, and if so, how this danger may be lessened or eliminated. Also comment on whether not creating this exemption would create different dangers for consumers, such as situations in which consumers who would benefit from referrals will not be referred because some employees who would be in a position to make referrals would not be compensated for doing so.

3. What are the advantages and disadvantages of limiting the exemption to those employees who do not perform any other category of settlement service in the same transaction, as proposed? Should the Department narrow the exemption by limiting it to those employees who do not perform any settlement service in the same transaction?

4. The Department recognizes that there could be some overlap among the 16 categories in the proposed rule. What refinements of the categories would ensure that the purposes of the exemption are fulfilled? Does the Department's proposal provide adequate guidance as to what is the ''same category of settlement service?'' How could this point be clarified further? What specific categories of settlement services would fall under paragraph (b)(16) of the definition of ''settlement service'' in § 3500.2 (''provision of any other services for which a settlement service provider requires a borrower or seller to pay''), as it is proposed to be revised?

5. Since the concerns which resulted in this proposed new exemption came mainly from lenders, should the Department narrow the scope of the exemption being proposed to apply only to lenders? What problems would other settlement service providers face if the exemption were limited in this fashion?

6. The exemption, as proposed, would not apply in situations in which a bank that does not originate any mortgage loans refers customers seeking mortgage loans to the bank's mortgage lending subsidiary. In such cases, the referring bank does not originate mortgage loans, and thus does not perform settlement service business in the same category as the business being referred. Should the exemption be expanded to allow compensation for such referrals?

III. Referrals Involving Telemarketing and Electronic Media

This proposed rule would revise § 3500.15(b)(1) of the RESPA regulations to conform to changes to RESPA made in section 2103(d) of the Act. Section 2103(d) of the Act primarily amended section 8(c)(4)(A) of RESPA (12 U.S.C. 2607(c)(4)(A)) to establish special procedures for disclosures of affiliated business arrangements in conjunction with referrals in which the telephone or electronic media are used in marketing. The proposed rule would set forth the new provisions regarding the timing of providing the disclosure, the methods of providing the disclosure, and the evidence needed to substantiate that the disclosure was provided.

The proposed rule would, consistent with the Department's prior rules, require that the Affiliated Business Arrangement Disclosure Statement be provided in writing on a separate piece of paper, and in the format set forth in Appendix D to part 3500. In proposing to revise § 3500.15(b)(1) to be consistent with the Act, the Department is also proposing to clarify the required elements of a proper affiliated business disclosure, as provided in Appendix D, which specifically includes the requirement that the disclosure contain an acknowledgement for the person being referred to sign. It also specifies that the person making the referral must request that the person being referred sign the disclosure promptly and return it to the affiliate making the referral or a designated addressee, and must provide information on where to send the signed disclosure.

Consistent with the Act, the proposed rule provides that, in the case of a face-to-face referral or a referral made in writing or by electronic media, the written disclosure must be provided at or before the time of the referral. In the case of a referral made by telephone, an abbreviated verbal disclosure also must be made during the telephone referral that, in clear and understandable language: (1) Specifies the nature of the relationship (explaining the ownership and financial interest) between the entity making the referral and the entity performing settlement services (or business incident thereto); (2) explains that because of this relationship, this referral may provide a financial or other benefit to the referring party; (3) states that the existence of this relationship does not require that the person being referred use the provider to whom he or she is being referred as a condition of settlement of the loan, or purchase, sale, or refinance of the property, as applicable; and (4) advises that a written disclosure will be provided within 3 business days. Different timing provisions for providing the written disclosure are contained in § 3500.15(b)(2) (iii)–(iv) of this proposed rule. These exceptions, which are simply a continuation of exceptions contained in prior rules regarding provision of such disclosure, involve referrals by a lender and situations involving an attorney or law firm that requires a client to use a particular title insurance agent or company.

Consistent with the Act, in all cases the person being referred must sign the disclosure. The person being referred should sign the disclosure at the time that the disclosure is provided. If the person being referred chooses not to sign the disclosure at the time that the disclosure is provided, the signature of the person being referred must be obtained at or before closing or settlement.

The proposed rule also provides that if a notation was made at the time that the disclosure was provided, in a written, electronic, or similar system of records maintained in the regular course of business, that notation may be used as evidence that the disclosure was provided at the time of the referral. Such a notation is to include a statement that the person being referred

chose not to sign the disclosure at the time that it was provided. The existence of such a notation, however, does not substitute for obtaining a signature at or before closing or settlement. In the case of a face-to-face referral, if the person being referred chooses not to sign the disclosure at the time that the disclosure is provided, such notation is mandatory.

IV. Sales or Transfers of Mortgage Servicing

This proposed rule also proposes to revise the RESPA regulations to reflect an amendment to section 6 of RESPA, set forth in section 2103(a) of the Act. Section 6(a), as amended, requires disclosure to applicants regarding the possibility of the assignment, sale, or transfer of the rights to service the applicant's federally related mortgage loan. Prior to the amendment, section 6 also provided that an applicant for a mortgage loan had to be provided a disclosure of the lender's historical practice in assigning, selling, and transferring servicing of loans, or, as an alternative to providing the historical data, a statement that the lender had previously sold servicing. A signed acknowledgment of receipt of the disclosure statement was also required in the applicant's loan file. The Act eliminates the historical data provisions and the acknowledgment requirement.

This proposed rule would implement the statutory amendment by striking language in § 3500.21 to make it consistent with the statutory amendment. The rule proposes to revise Appendix MS–1 to part 3500, the model Servicing Disclosure Statement format, to conform to the amendment. This proposed rule recognizes that certain entities do not undertake loan servicing and, therefore, transfer servicing before the first payment is due; the disclosure format may so state. The disclosure format in its revised form would be published in the Code of Federal Regulations for the convenience of compliance by affected parties. In response to comments received pursuant to the ANPR urging the Department to consolidate the Mortgage Servicing Disclosure with other RESPA forms, the proposed rule furthers section 2101 of the Act by proposing to clarify that the format language may also be included as part of the Good Faith Estimate.

The Department is interested in comments addressing alternative approaches to implementing the statutory language while protecting consumers. In connection with the report to Congress which the Department is developing pursuant to section 2101 of the Act, which will contain the Department's recommendations for statutory amendments, the Department is also considering whether the disclosure might be combined with other RESPA or Truth In Lending Act (TILA) disclosures, consistent with section 2101 of the Act. In addition, if commenters propose that the Department should continue to require more information in the disclosure than in the format proposed, they should address what the Department's authority to do so would be in light of the statutory amendment in section 2103(a) of the Act.

In a related matter, section 2103(e) establishes a 3-year limitation on the time aggrieved borrowers or classes of borrowers could bring actions under section 6 of RESPA. Inasmuch as this limitation is longer than the statute of limitations for other actions by individuals under RESPA (1 year), a new paragraph (f)(1)(iv) would be added to § 3500.21 of the regulations to highlight this provision.

V. Additional Technical Corrections and Clarifications Contemplated

In addition to the proposed revisions described in the preceding portions of this preamble, the Department intends that when it makes effective the provisions of the June 7 rule amending RESPA regulations concerning employer payments to employees, the Department will make further technical corrections and clarifications to the June 7 rule. While these technical corrections and clarifications are described below for informational purposes, the text is not published here, since the Department is not requesting comments on them.

A. Routine Dealing

The Department has been asked about language in the preamble and in Appendix B, ''Illustrations of the Requirements of RESPA,'' regarding the definition of a managerial employee as an ''employee * * * who does not routinely deal directly with consumers * * *.'' This definition applies to the exemption for employer payments to managerial employees (§ 3500.14(g)(1)(viii) of the June 7 rule). In the preamble to the Department's June 7, 1996 rule (61 FR 29245; bottom of middle column) the Department stated, ''HUD intends this phrase ('does not routinely') to allow a managerial employee who performs and is compensated for occasional settlement services (not more than three transactions a year) to be eligible for the exemption.'' The last sentence of Appendix B, illustration 12 of the June 7 rule also contained a statement referring to this three-transaction guideline.

Following publication of the June 7 rule, the Department has found that setting as a guide a fixed, maximum number of transactions for all managers under the Department's rule would unduly interfere with the functioning of offices. Roles and functions are not rigidly specified and because of departures, absences for illnesses, or other reasons, a manager may be called upon to complete transactions in process or otherwise become involved in troublesome transactions, in addition to any personal transactions the manager might otherwise undertake. Accordingly, the Department agrees that a manager who does not routinely deal with the public may perform greater than three transactions and still remain eligible for the managerial exemption. A more appropriate guideline is that a manager not routinely performing settlement services may still receive compensation under the exemption if either: (1) the total value of the services provided by the manager does not exceed 5 percent of the annual income to the office or unit for which the manager is responsible attributable to RESPA-covered transactions, *or* (2) the manager performs settlement services in no more than three RESPA-covered transactions.

In publishing the final rule, the Department will clarify this point.

B. In Any Transaction

The final rule will put into effect the exemption promulgated in the June 7 rule to the otherwise applicable prohibition against kickbacks and unearned fees. The exemption applies in affiliate relationships and allows payments made to employees who do not perform settlement services ''in any transaction'' and who provide the disclosure statement (24 CFR 3500.14(g)(1)(ix)). The use of the term ''in any transaction'' has created concern for some affiliated settlement service providers regarding the breadth of the restriction.

The Department sought to provide this exemption to those who were not currently involved in the provision of settlement services. Therefore, when the Department puts this exemption into effect in the final rule, it will clarify that it does not intend, by the use of the term ''in any transaction,'' that if an employee performs settlement services one time in his or her life, he or she shall forever lose the ability to receive payments pursuant to this exemption. Rather, in publishing the final rule the Department will clarify that it intends the ''in any transaction'' language to

allow an employee who has performed settlement services in the past to qualify for the exemption in any of the following types of circumstances:

1. *No longer providing settlement services.* This type of circumstance involves an employee who has not performed settlement services for his or her current employer (in the same job position) in any transaction for 1 year or more. *OR*

2. *An employee who changes jobs.* This type of circumstance involves an employee who performed settlement services for his or her employer in the past but, although still employed by the same employer, changes jobs so that he or she no longer holds the former position and does not perform settlement services in the new position. *OR*

3. *A new employee.* This type of circumstance involves an employee who performed settlement services for another employer on a past job, but no longer holds that job or works for that employer, and does not perform settlement services on his or her current job for the new employer.

In publishing the final rule the Department also will clarify that, as explained in the preamble to the June 7 rule (61 FR 29243), under all these circumstances, the employment relationship must be *bona fide* and not a sham designed to facilitate kickbacks among affiliated companies. Otherwise, the exemption will not apply.

C. ''Affiliated Business Arrangement''

The Department will make a technical correction required by an amendment to RESPA in section 2103(c) of the Act. That legislation redesignated ''Controlled Business Arrangements'' as ''Affiliated Business Arrangements'' or ''AfBAs.'' The final rule will incorporate into the RESPA rules the term ''affiliated business arrangement'' instead of the term ''controlled business arrangement'' used in the June 7 rule, completing the process of changing the terminology begun in the November 15, 1996 rule (61 FR 58472).

D. Timing of Affiliated Business Arrangement Disclosure

The Department will make a technical correction relating to the timing of providing the AfBA disclosure. The June 7 rule used inconsistent language to describe when the disclosure was to be provided. (*See* 24 CFR 3500.14(g)(1)(ix)(A)(2) (''before the referral''); 24 CFR 3500.15(b)(1) (''prior to the referral,'' ''no later than the time of each referral,''); Appendix B, illustration 11 (''at or before the time that the referral is made''); Appendix B, illustration 12 (''at the time of the referral''.) The Department will conform the language of the regulation and Appendix B more closely to the statutory language as revised in section 2103(d) of the Act, to provide consistently that the AfBA disclosure statement must be provided in accordance with § 3500.15(b).

Section 3500.15(b) sets forth the applicable time frames for providing the disclosure. This provision requires, in the case of a face-to-face referral or a referral made in writing or by electronic media, providing a written disclosure at or before the time of the referral, except in cases of a referral by a lender or situations involving an attorney or law firm that requires a client to use a particular title insurance agent. In the case of a telephone referral, a written disclosure must be provided within 3 business days after the referral by telephone and an abbreviated verbal disclosure must be made during the telephone referral. The change that will be included in the final rule will eliminate the use of inconsistent terminology and will conform the description of the timing for providing the disclosure to be consistent with section 8(c)(4) of RESPA, as amended by section 2103(d) of the Act.

Findings and Certifications

Executive Order 12866

The Office of Management and Budget (OMB) reviewed this proposed rule under Executive Order 12866, *Regulatory Planning and Review*, issued by the President on September 30, 1993. OMB determined that this rule is a ''significant regulatory action,'' as defined in section 3(f) of the Order (although not economically significant, as provided in section 3(f)(1) of the Order). Any changes made in this rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection between 7:30 a.m. and 5:30 p.m. weekdays in the Office of the Rules Docket Clerk, Office of General Counsel, Room 10276, Department of Housing and Urban Development, 451 Seventh Street, SW, Washington, DC.

Paperwork Reduction Act

The information collection requirements contained in § 3500.15(b) prior to this proposed rule have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520), and assigned OMB control number 2502–0516. In securing that approval, the Department had estimated that the annual reporting and recordkeeping hour burden would be 240,000 hours (2.4 million annual responses at 6 minutes per response). The provisions of § 3500.15(b) of this proposed rule regarding the Affiliated Business Arrangement Disclosure would simply clarify the timing and the methods of providing the disclosure, and the evidence needed to substantiate that the disclosure was provided, in circumstances in which the referral is made over the telephone or through electronic media. The Department does not anticipate that the provisions of § 3500.15(b) of this proposed rule will increase the number of annual burden hours described above. The Department has, however, submitted the information collection requirements in § 3500.15(b) of this proposed rule to OMB for review under the Paperwork Reduction Act and the procedures set forth in 5 CFR part 1320. As required by the Paperwork Reduction Act, interested persons are invited to submit comments according to the instructions in the **DATES** and **ADDRESSES** sections in the preamble of this proposed rule. The Department specifically requests comments on the following:

(1) Whether the proposed collection of information is necessary for the proper performance of the functions of the Department, including whether the information will have practical utility;

(2) The accuracy of the Department's estimate of the burden of the proposed collection of information;

(3) How to enhance the quality, utility, and clarity of the information to be collected; and

(4) How to minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

The information collection requirements in § 3500.21 of this proposed rule also have been approved by OMB, and assigned OMB control number 2502–0458. The rule does not propose to make changes to the information collection requirements set forth in § 3500.21. The rule proposes to make changes to the Servicing Disclosure Statement format described in this section, but this format is a model format and is not required to be used. The OMB approval number for this section is also in the process of being renewed in accordance with the procedures set forth in OMB's regulations implementing the Paperwork Reduction Act of 1995 and codified at 5 CFR part 1320.

Environmental Impact

In accordance with 24 CFR 50.19(c)(1) of the Department's regulations, published in a final rule on September 27, 1996 (61 FR 50914), this proposed rule does not direct, provide for assistance or loan and mortgage insurance for, or otherwise govern or regulate property acquisition, disposition, lease, rehabilitation, alteration, demolition, or new construction, or set out or provide for standards for construction or construction materials, manufactured housing, or occupancy. Therefore, this proposed rule is categorically excluded from the requirements of the National Environmental Policy Act.

Regulatory Flexibility Act

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), has reviewed this proposed rule before publication and by approving it certifies that this rule would not have a significant economic impact on a substantial number of small entities, other than those impacts specifically required to be applied universally by the RESPA statute. In this proposed rule, the Department strives to provide flexible requirements in order to reduce any burden on small entities.

Executive Order 12612, Federalism

The General Counsel, as the Designated Official under section 6(a) of Executive Order 12612, *Federalism*, has determined that the policies contained in this proposed rule would not have substantial direct effects on States or their political subdivisions, or the relationship between the Federal Government and the States, or on the distribution of power and responsibilities among the various levels of government. As a result, the proposed rule is not subject to review under the Order.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104–4; approved March 22, 1995) (UMRA) establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments, and the private sector. This rule does not impose any Federal mandates on any State, local, or tribal governments, or on the private sector, within the meaning of the UMRA.

List of Subjects in 24 CFR Part 3500

Condominiums, Consumer protection, Housing, Mortgages, Mortgage servicing, Reporting and recordkeeping requirements.

Accordingly, for the reasons set out in the preamble, part 3500 of Title 24 of the Code of Federal Regulations is proposed to be amended as follows:

PART 3500—REAL ESTATE SETTLEMENT PROCEDURES ACT

1. The authority citation for 24 CFR part 3500 continues to read as follows:

Authority: 12 U.S.C. 2601 *et seq.*; 42 U.S.C. 3535(d).

2. In § 3500.2, paragraph (b) is amended by revising the definition of ''*Settlement service*'' to read as follows:

§ 3500.2 Definitions.

* * * * *

(b) * * *

Settlement service means any service provided in connection with a prospective or actual settlement, including any one or more of the following:

(1) Origination of a federally related mortgage loan (including, but not limited to, the taking of loan applications, loan processing, and the underwriting and funding of such loans), or rendering of services by a mortgage broker (including counseling, taking of applications, obtaining verifications and appraisals, and other loan processing and origination services, and communicating with the borrower and lender);

(2) Provision of title services, including title searches, title examinations, abstract preparation, insurability determinations, and the issuance of title commitments and title insurance policies;

(3) Rendering of services by an attorney;

(4) Preparation of documents, including notarization, delivery, and recordation;

(5) Rendering of credit reports;

(6) Rendering of appraisals;

(7) Rendering of inspections, including inspections required by applicable law or any inspections required by the sales contract or mortgage documents prior to transfer of title;

(8) Conducting of settlement by a settlement agent and any related services;

(9) Provision of services involving mortgage insurance;

(10) Provision of services involving hazard or other casualty insurance;

(11) Provision of services involving flood insurance;

(12) Provision of services involving homeowner's warranties;

(13) Provision of services involving mortgage life, disability, or similar insurance designed to pay a mortgage loan upon disability or death of a borrower, but only if such insurance is required by the lender as a condition of the loan;

(14) Provision of services involving real property taxes or any other assessments or charges on the real property;

(15) Rendering of services by a real estate agent or real estate broker; and

(16) Provision of any other services for which a settlement service provider requires a borrower or seller to pay.

* * * * *

3. Section 3500.14 is amended by adding and reserving new paragraphs (g)(1)(viii) and (g)(1)(ix), and by adding a new paragraph (g)(1)(x), to read as follows:

§ 3500.14 Prohibition against kickbacks and unearned fees.

* * * * *

(g) * * *

(1) * * *

(viii) [Reserved]

(ix) [Reserved]

(x)(A) A payment by an employer to its *bona fide* employee for the referral of settlement service business to a settlement service provider that has an affiliate relationship with the employer or in which the employer has a direct or beneficial ownership interest of more than 1 percent, if the following conditions are met:

(*1*) The settlement service business that is referred is the same category of settlement service that the employer of the employee making the referral provides;

(*2*) The employee provides to the person being referred the affiliated business arrangement disclosure in accordance with § 3500.15; and

(*3*) The employee making the referral does not perform any other category of settlement service (including a service described by paragraph (b)(15) or (b)(16) of the definition of ''*Settlement service*'' in § 3500.2(b)) in the same transaction.

(B) For purposes of this paragraph (g)(1)(x), each service described in the definition of ''*Settlement service*'' in § 3500.2 (b)(1) through (b)(15) constitutes a different category of settlement service that may qualify for this exemption.

* * * * *

4. Section 3500.15 is amended by revising paragraph (b)(1); by redesignating paragraphs (b)(2) and (b)(3) as paragraphs (b)(5) and (b)(6), respectively; and by adding new paragraphs (b)(2) through (b)(4); to read as follows:

§ 3500.15 Affiliated business arrangements.

* * * * *

(b) * * *

(1) The person making a referral provides to each person being referred a written disclosure on a separate piece of paper, in the format of the Affiliated Business Arrangement Disclosure Statement set forth in Appendix D to this part. The person making the referral must request that the person being referred sign the disclosure promptly and return it to the affiliate making the referral or a designated addressee, and must provide information on where to send the signed disclosure. The disclosure shall:

(i) Specify the nature of the relationship (explaining the ownership and financial interest) between the person performing settlement services (or business incident thereto) and the person making the referral;

(ii) Describe the estimated charge or range of charges (using the same terminology, as far as practical, as Section L of the HUD–1 or HUD–1A settlement statement) generally made by the provider of settlement services; and

(iii) Include an acknowledgement for the person being referred to sign.

(2) The person making the referral shall provide the disclosure in accordance with the following timetable:

(i) In the case of a face-to-face referral or a referral made in writing or by electronic media, at or before the time of the referral, except as provided in paragraph (b)(2)(iii) or (b)(2)(iv) of this section;

(ii) In the case of a referral made by telephone, within 3 business days after the referral by telephone, except as provided in paragraph (b)(2)(iii) or (b)(2)(iv) of this section. In the case of a referral made by telephone, an abbreviated verbal disclosure also must be made during the telephone referral that, in clear and understandable language:

(A) Specifies the nature of the relationship (explaining the ownership and financial interest) between the entity making the referral and the entity performing settlement services (or business incident thereto);

(B) Explains that because of this relationship, this referral may provide a financial or other benefit to the referring party;

(C) States that the existence of this relationship does not mean that the person being referred must use the provider to whom he or she is being referred as a condition of settlement of the loan, or purchase, sale, or refinance of the property, as applicable; and

(D) Advises that a written disclosure will be provided within 3 business days.

(iii) In the case of a referral by a lender (including a referral by a lender to an affiliated lender) the disclosure may be provided at the time that the good faith estimate required under section 5(c) of RESPA (12 U.S.C. 2604) is provided.

(iv) In the case of an attorney or law firm that requires a client to use a particular title insurance agent, the attorney or law firm shall provide the written disclosure no later than the time the attorney or law firm is engaged by the client.

(3)(i) *Signature.* In all cases, the person being referred must sign the disclosure. The person being referred should sign the disclosure at the time that the disclosure is provided. If the person being referred chooses not to sign the disclosure at the time that the disclosure is provided, the signature of the person being referred must be obtained at or before closing or settlement.

(ii) *Other evidence of compliance.* The existence of a notation having been made, at the time that the disclosure was provided, in a written, electronic, or similar system of records maintained in the regular course of business, which includes a notation of the fact that the person being referred chose not to sign the disclosure at the time that it was provided, may be used as evidence that the disclosure was provided at the time of the referral, but does not substitute for obtaining a signature in accordance with paragraph (b)(3)(i) of this section. In the case of a face-to-face referral, if the person being referred chooses not to sign the disclosure at the time that the disclosure is provided, such notation is mandatory.

(4) Failure to comply with the disclosure requirements of this section may be overcome if the person making a referral can prove by a preponderance of the evidence that procedures reasonably adopted to result in compliance with these conditions have been maintained and that any failure to comply with these conditions was unintentional and the result of a *bona fide* error. An error of legal judgment with respect to a person's obligations under RESPA is not a *bona fide* error. Administrative and judicial interpretations of section 130(c) of the Truth in Lending Act (15 U.S.C. 1640(c)) shall not be binding interpretations of the preceding sentence or section 8(d)(3) of RESPA (12 U.S.C. 2607(d)(3)).

* * * * *

5. Section 3500.21 is amended by revising paragraphs (b) and (c); and by adding a new paragraph (f)(1)(iv); to read as follows:

§ 3500.21 Mortgage servicing transfers.

* * * * *

(b) *Servicing Disclosure Statement; Requirements.* (1) At the time an application for a mortgage servicing loan is submitted, or within 3 business days after submission of the application, the lender, mortgage broker who anticipates using table funding, or dealer who anticipates a first lien dealer loan shall provide to each person who applies for such a loan a Servicing Disclosure Statement. A format for the Servicing Disclosure Statement appears as Appendix MS–1 to this part. The specific language of the Servicing Disclosure Statement is not required to be used, and the statement may be included in the Good Faith Estimate required under § 3500.7(a), so long as the title ''SERVICING DISCLOSURE STATEMENT'' is used. The information set forth in ''Instructions to Preparer'' on the Servicing Disclosure Statement need not be included with the information given to applicants, and material in square brackets is optional or alternative language. The model format may be annotated with additional information that clarifies or enhances the model language. The lender, table funding mortgage broker, or dealer should use the language that best describes the particular circumstances.

(2) The Servicing Disclosure Statement must indicate whether the servicing of the loan may be assigned, sold, or transferred to any other person at any time while the loan is outstanding. If the lender, table funding mortgage broker, or dealer in a first lien dealer loan does not engage in the servicing of any mortgage loans, the disclosure may consist of a statement that such entity intends to assign, sell, or transfer servicing of the loan before the first loan payment is due.

(c) *Servicing Disclosure Statement; Delivery.* The lender, table funding mortgage broker, or dealer that anticipates a first lien dealer loan shall deliver Servicing Disclosure Statements to each applicant for a mortgage servicing loan at the time of application, or by placing it in the mail with prepaid first-class postage within 3 business days from receipt of the application. In the event the borrower is denied credit within the 3-business day period, no servicing disclosure statement is required to be delivered. If co-applicants indicate the same address on their application, one copy delivered to that address is sufficient. If different addresses are shown by co-applicants on the application, a copy must be delivered to each of the co-applicants.

* * * * *

(f) * * *

(1) * * *

(iv) *Limitation on time of action.* Any action pursuant to this section must be brought within 3 years from the date of the occurrence of the violation.

* * * * *

6. Appendix B to part 3500 is amended by adding a new illustration 15 at the end of the appendix, to read as follows:

Appendix B to Part 3500—Illustrations of Requirements of RESPA

* * * * *

15. *Facts:* A, a bank, is affiliated with, B, a mortgage banking company. A customer walks into the bank, A, and asks F, A's loan officer, about getting a mortgage loan to purchase a house. While A makes home equity loans, A does not make first mortgage loans. Thus, F refers the customer to B, the mortgage banking affiliate, takes an application, and provides the customer with the affiliated business arrangement disclosure statement. F receives a payment from his employer, A, for making the referral. F does not perform any other category of settlement service in this transaction.

Comments: Under § 3500.14(g)(1)(x), employers may pay their own *bona fide* employees for the referral of settlement service business to a settlement service provider that has an affiliate relationship with the employer or in which the employer has a direct or beneficial ownership interest of more than 1 percent, if the following conditions are met:

(1) The settlement service business that is referred is the same category of settlement service that the employer of the employee making the referral provides;

(2) The employee provides to the person being referred the affiliated business arrangement disclosure in accordance with § 3500.15; and

(3) The employee making the referral does not perform any other category of settlement service in the same transaction.

Employees who perform settlement services in other transactions may still qualify for the exemption.

In this case, the settlement service business that is referred is originating a mortgage loan, and the business entity for which the employee works also provides this service. Thus, the same category of settlement service is being referred as is performed by the employer of the employee making the referral. (Categories of settlement services that may qualify for this exemption are listed in the definition of ''*Settlement services*'' in § 3500.2 (b)(1) through (b)(15).) Also, the employee provides the affiliated business disclosure in accordance with § 3500.15. While this particular employee takes an application, he does not perform any other category of settlement service in this transaction.

Thus, in the circumstances described, the employee may receive the referral fee for making the referral without violating RESPA.

7. Appendix MS–1 to part 3500 is revised to read as follows:

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APPENDIX MS-1 TO PART 3500

[Sample language; use business stationery or similar heading]

[Date]

SERVICING DISCLOSURE STATEMENT

NOTICE TO FIRST LIEN MORTGAGE LOAN APPLICANTS: THE RIGHT TO COLLECT YOUR MORTGAGE LOAN PAYMENTS MAY BE TRANSFERRED.

You are applying for a mortgage loan covered by the Real Estate Settlement Procedures Act (RESPA) (12 U.S.C. Sec. 2601 et seq.). RESPA gives you certain rights under Federal law. This statement tells you what the chances are that the servicing for this loan may be transferred to a different loan servicer. "Servicing" refers to collecting your principal, interest and escrow account payments, if any. You will be given advance notice before a transfer occurs.

Servicing Transfer Information

[We may assign, sell or transfer the servicing of your loan while the loans is outstanding.]

[or]

[We do not service mortgage loans. We intend to assign, sell or transfer the servicing of your mortgage loan before the first payment is due.]

[INSTRUCTIONS TO PREPARER: Insert the date and select the appropriate language under "Servicing Transfer Information." The model format may be annotated with further information that clarifies or enhances the model language.]

Dated: February 13, 1997.

Nicolas P. Retsinas,

Assistant Secretary for Housing—Federal Housing Commissioner.

[FR Doc. 97–12081 Filed 5–8–97; 8:45 am]

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