



State of North Carolina

OFFICE OF THE COMMISSIONER OF BANKS

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GOVERNOR

JOSEPH A. SMITH, JR.
COMMISSIONER OF BANKS

April 5, 2010

William S. Bost, III
333 Six Forks Road, Suite 165
Raleigh, NC 27609

Re: Declaratory Ruling 2010-01 considering exemption of entities partially owned by depository institutions under G.S. § 53-244.050(d)(5)

Dear Mr. Bost:

You requested a declaratory ruling under G.S. § 150B-4 and 4 NCAC 3B.0105 as to whether the North Carolina Safe and Fair Enforcement Mortgage Licensing Act, G.S. § 53-244.010 et seq., Session Law 2009-374 ("NC SAFE" or "the Act"), affords an exemption for an entity that is owned in part by a wholly-owned subsidiary of a state-chartered non-member bank. Specifically, you have requested guidance as to what constitutes a "subsidiary that is owned and controlled by a depository institution and regulated by federal banking agency" under G.S. § 53-244.030(29)b., for purposes of the exemption of such entities under G.S. § 53-244.040(d)(5). As discussed below, we conclude that in order to qualify for such an exemption, an entity must demonstrate the following: (1) that it is a subsidiary of a depository institution; (2) that the entity is in fact "owned" by the depository institution; (3) that a depository institution maintains "control" over the subsidiary; and (4) that the subsidiary is regulated by a federal banking agency. As some of these factors require a careful and thorough analysis of facts and circumstances of the relationship between the depository institution, the entity, and other parties, the Office of the Commissioner of Banks ("NCCOB") will review each request for exemption on a case-by-case basis in order to confirm if an entity meets the standards set out in NC SAFE for an exemption.



Based on the limited facts and materials provided in your request, we are unable to reach a determination as to whether your client meets the requirements for exemption under NC SAFE. After reviewing this declaratory ruling, you may submit additional materials that would enable us to reach a final agency decision in regard to your client's request for an exemption.

This declaratory ruling is being issued in response to your inquiry pursuant to G.S. § 150B-4 and 4 NCAC 3B.0105. It is an interpretation of NC SAFE solely as it relates to the facts you have provided in your request. For the benefit of the public, a copy of this declaratory ruling will be made available on the NCCOB website. In addition, a copy of this ruling will be mailed to each holder of an active mortgage broker, mortgage lender, and mortgage servicer license issued by NCCOB.

Legislative History

The General Assembly enacted NC SAFE in order to bring North Carolina's mortgage lending laws into compliance with the federal Housing and Economic Recovery Act of 2008 (the "Federal SAFE Act"). Federal SAFE Act required each state to adopt certain minimum licensing standards for mortgage loan originators or risk losing the authority to regulate the mortgage loan originators operating in that state. North Carolina has had an existing mortgage licensing requirement for mortgage bankers, mortgage brokers, and loan officers since 2002, through Article 19A of Chapter 53 (the "Mortgage Lending Act" or "MLA"). However, the Federal SAFE Act contained minor variations and different nomenclature from the MLA. Therefore, in 2009, the General Assembly enacted NC SAFE which repealed and replaced the Mortgage Lending Act.

The terms of the Act are to be liberally construed to effect the purposes stated or clearly encompassed by the Article which are, in part:

[...] to protect consumers seeking mortgage loans and to ensure that the mortgage lending industry operates without unfair, deceptive, and fraudulent practices on the part of mortgage loan originators" and to "establish within this Article an effective system of supervision and enforcement of the mortgage lending industry by giving the Commissioner of Banks broad administrative authority to administer, interpret, and enforce [NC SAFE][...]

G.S. § 53-244.020.

Statutory Analysis

NC SAFE defines “engaging in the mortgage business” and establishes a system of licensure for mortgage lenders, mortgage brokers, mortgage servicers and mortgage loan originators. The Act exempts certain activities, individuals and entities from its licensure requirements under G.S. § 53-244.040(d). These include, inter alia, “registered mortgage loan originator” which is defined as an individual who meets the definition of mortgage loan originator, and, who:

- [...] is registered with, and maintains a unique identifier through the Nationwide Mortgage Licensing System and Registry and is an employee of:
- a. A depository institution;
 - b. A subsidiary that is owned and controlled by a depository institution and regulated by a federal banking agency; or
 - c. An institution regulated by the Farm Credit Administration.

G.S. §53-244.030(29).

“Depository institution” is defined as having “the same meaning as in section 3 of the Federal Deposit Insurance Act and includes any credit union whose share and deposit accounts are insured by the National Credit Union Administration under the Federal Credit Union Act.” G.S. § 53-244.030(8).

In addition to individual registered mortgage loan originators, the Act exempts those entities listed in G.S. § 53-244.030(29) a., b. and c. “*upon acceptance of the notice of exemption filed with the Commissioner as specified in G.S. §53-244.050(g).*” G.S. § 53-244.040(d)(5)(italics added). The Act further requires that such an entity “*shall notify the Commissioner in order to claim and confirm the exemption and to facilitate the referral of consumers that contact the Commissioner.*” G.S. § 53-244.050(g)(italics added). The Act requires such claims be submitted on a form “that shall contain: (1) the name of the exempt person; (2) the basis of the exempt status of the exempt person; (3) the principal business address and contact information for the exempt person; and (4) the state or federal regulatory authority responsible for the exempt person’s supervision, examination or regulation.” *Id.* Such a Claim of Exemption is required only for banking institutions exempted by G.S. § 53-244.040(d)(5). *Id.*

For an entity which is not itself a depository institution nor regulated by the Farm Credit Administration, exemption is available if the entity meets the parameters of G.S. § 53-244.030(29)b. *Id.* As your request notes, the language of G.S. § 53-244.030(29)b. differs somewhat from that of the MLA’s analogous provision for exemption of subsidiaries, which read:

Any person authorized to engage in business as a bank or a **wholly owned subsidiary of a bank**, a farm credit system, savings institution, or a **wholly owned subsidiary of a savings institution**, or credit union or a wholly owned subsidiary of a credit union, under the laws of the United States, this State, or any other state.

G.S. § 53-243.01(12)c. (repealed by S.L. 2009-374) (defining various entities and individuals as exempt from licensure)(emphasis added).

In general, North Carolina courts have narrowly interpreted exclusions or exceptions from a statutory scheme, especially where a broad interpretation may result in circumvention of the overriding statutory purpose. See Good Hope Hosp., Inc v. North Carolina Health and Human Services, 175 N.C. App. 309 (2006). In interpreting banking laws under its jurisdiction, NCCOB has narrowly construed exemptions where the overall statutory structure indicates the General Assembly's intention to maximize supervision and jurisdiction over entities operating in the State.

As noted above, the legislative history of NC SAFE indicates that the statute was enacted in order to comply with the Federal SAFE Act's minimum requirements and the language and terminology used in the Federal SAFE Act. NCCOB is unaware of any indication that the General Assembly considered the distinctions between "wholly owned" subsidiaries of depository institutions and subsidiaries "owned and controlled" by depository institutions.

In addition, the process for securing an exemption under NC SAFE reflects the General Assembly's intention for the Commissioner to conduct a thorough and searching review of an entity seeking exemption. NC SAFE requires an exemption claim to be (1) filed with the Commissioner, and (2) confirmed by the Commissioner. Thus, NCCOB believes it is appropriate to continue to narrowly construe requests for exemption under NC SAFE and to thoroughly review these requests in a fashion similar to the long-standing practice of NCCOB under the MLA.

With regard to the exemptions for entities listed under G.S. § 53-244.030(29)a., b. or c., NC SAFE Act requires an entity to demonstrate: (1) that it is a subsidiary of a depository institution; (2) that the entity is in fact "owned" by the depository institution; (3) that a depository institution maintains "control" over the subsidiary; and (4) that the subsidiary is regulated by a federal banking agency. We will further discuss these four criteria below.

(1) Subsidiary of a Depository Institution

NC SAFE does not define “subsidiary” of a depository institution. The Federal SAFE Act also fails to provide a definition. However, NC SAFE does define “depository institution” (as noted above) and “affiliate” by reference to federal banking laws. In the absence of a statutory definition for the meaning of the term “subsidiary” within NC SAFE, NCCOB believes it appropriate to look to the applicable law governing the depository institution’s formation and classification of subsidiaries and to common understanding of the term of “subsidiary.” Entities seeking exemption from NC SAFE should provide proof that the entity qualifies as a “subsidiary” of the depository institution under applicable banking law.

(2) “Owned” and (3) “controlled”

Neither NC SAFE nor the Federal SAFE Act define the terms “owned” or “controlled.”

NCCOB believes that the use of the additional terms “owned and controlled” after “subsidiary” demonstrates that the General Assembly intended for the Commissioner to look beyond the mere status of an entity as “subsidiary” and to review the level of ownership by the depository institution and the level of control maintained by that depository institution. Even assuming the General Assembly intended to reduce the MLA’s requirement that subsidiaries be “wholly owned,” NCCOB must also look to NC SAFE’s purposes of effective enforcement and supervision in interpreting “own and control.” NCCOB believes NC SAFE’s ownership requirement is best maintained through complete ownership of the subsidiary. However, NCCOB is willing to consider confirming exemptions for subsidiaries with less than 100% ownership if the entity can demonstrate that the depository institution maintains a majority ownership stake in the entity, controls the majority of voting shares in the entity, and the substance of the ownership structure ensures that the depository institution will maintain the majority economic interest in the entity. NCCOB will not confirm exemptions where a depository institution maintains only a minority ownership of the subsidiary.

Investigation into “control” has been a core principle central to NCCOB’s supervision of the mortgage industry since the inception of the MLA. Absent a clear indication from the General Assembly of an intention to change or diminish NCCOB’s close scrutiny of control for non-wholly-owned subsidiaries, NCCOB believes such an investigation is necessary to fulfill the legislative purposes of the Act and to avoid evasion of North Carolina’s regulatory supervision.

An indication of the importance of “control” in North Carolina’s mortgage regulation is found in the first declaratory ruling issued under the MLA. As we have no indication that the General Assembly intended to alter this approach, the interpretations of the MLA provide guidance as to the purpose of North Carolina’s licensing structure. In Declaratory Ruling 2003-01, addressing “net branching” the Commissioner explained the intent of the MLA:

Based upon the plain meaning of its provisions, the Act clearly requires:

1. Personal responsibility on the part of licensed loan officers for their behavior in the conduct of mortgage lending.
2. Personal accountability and potential liability on the part of branch managers and managing principals who supervise licensed loan officers in the conduct of the mortgage business.
3. Responsibility of licensed firms to supervise and manage the behavior of all individuals in the firm's employ who are engaged in the mortgage business, with potential liability of the firm for any breaches of that duty.

Declaratory Ruling 2003-1 at 2 – 3 (November 6, 2003).

The basic statutory structure of the MLA underpinning the Commissioner's ruling has been maintained through NC SAFE. The MLA required that an individual engaged in the mortgage business be supervised and controlled by an entity that maintains adequate supervision. This same conceptual structure informs the meaning of "owned and controlled" under NC SAFE. Although the term's conformance with the Federal SAFE Act now permits less than wholly owned subsidiaries to claim an exemption in certain circumstances, it would be counter to the purposes of NC SAFE to permit entities with only a tenuous relationship with a depository institution to evade State regulation.

Therefore, with regard to the definition of the meaning "subsidiary owned and controlled" in G.S. § 53-244.030(29)b, the Commissioner will look to the specific facts and circumstances related to the entity's ownership and control to determine if sufficient indicia of both ownership and control exist to justify exemption from NC SAFE's licensure requirements. Where an entity is clearly the wholly-owned subsidiary of a depository institution, NCCOB will not require further inquiry other than confirmation of the appropriate federal banking agency's oversight of the subsidiary. Where an entity is less than wholly-owned, the inquiry must go further into the relationship between the depository institution and the entity. Some facts and circumstances related to this deeper inquiry would include, without limitation, the following:

1. The depository institution parent of the entity claiming an exemption holds at least a 51% majority ownership and control of a majority of voting shares in the entity;
2. Employees of the entity will be subject to the same supervision and control as other employees of the depository institution parent;
3. Recognition in the organizational agreements that the management responsibilities of the depository institution parent are non-delegable.
4. An undertaking by the depository institution that it will stand behind all acts of the entity claiming the exemption if it loan origination process and compliance with federal and state laws applicable to the entity's mortgage business
5. Acknowledgement that the entity will ensure that all mortgage loan originators acting on its behalf will register with the National Mortgage Licensing System.

(4) Regulation by a Federal Banking Agency

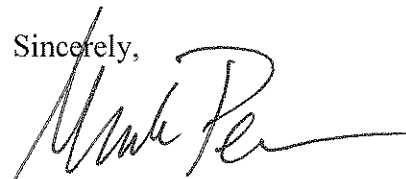
Exemption through G.S. § 53-244.030(29)b. requires the subsidiary (not merely the depository institution itself) be regulated by a Federal Banking Agency. The Act defines "Federal Banking Agencies" to mean "the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the National Credit Union Administration, and the Federal Deposit Insurance Corporation." G.S. § 53-244(12). The combined intention of NC SAFE and the Federal SAFE Act is to ensure a comprehensive scheme of licensure for mortgage loan originators, who are subject to the regulation of either a state or federal regulatory authority, and in some cases subject to both federal and state regulation. In order to avoid potential gaps in regulatory supervision, NCCOB will require a letter from the applicable federal banking agency that indicates that the federal banking agency supervises the subsidiary requesting exemption from NC SAFE. In the past, federal banking agencies have held varying interpretations of their regulatory authority over subsidiaries and affiliates of depository institutions, and this process will promote the primary goal of "an effective enforcement system of supervision and enforcement of the mortgage lending industry."

Conclusion

In conclusion, the Commissioner will make a determination of the claim of exemption on a case by case basis through an investigation into the criteria and factors described in this declaratory ruling. Until the Commissioner has received and confirmed the exemption, such an entity faces significant risk in operating a mortgage business in North Carolina. With regard to a subsidiary that is wholly-owned by a depository institution, proper filing of a claim of exemption claim required by G.S. § 53-244.050(g) and proof of notice to the appropriate federal regulatory authority is all that is required to obtain such confirmation. With regard to any entity which is partially owned by a depository institution, the Commissioner will review the claim of exemption and other information provided by the applicant upon request of NCCOB staff to determine if there exists sufficient indicia of ownership and control to ensure that the entity meets the definition of G.S. § 53-244.030(29)b. including, but not limited to those indicia outlined above.

I trust this is responsive to your inquiry. If you have additional questions regarding this matter, please contact to Will Corbett, Staff Attorney in the Non-Depository Division.

Sincerely,



Mark Pearce
Chief Deputy Commissioner of Banks