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March 5, 2010

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 7th Street, S.W., Room 10276
Washington, D.C. 20410-0500

Re: Proposed Changes to the Practice of Law Exemption to HUD Proposed Rule titled "SAFE Mortgage Licensing Act: HUD Responsibilities Under the SAFE Act," Docket No. FR-5271-P-01, 74 Fed. Reg. 66548 (December 15, 2009)

Dear Sir/Madam:

On behalf of the American Bar Association, which has nearly 400,000 members, I write to express our concerns over the above referenced proposed rule (the "Proposed Rule") to the extent that it would impose excessive new regulations on lawyers engaged in the practice of law. If adopted in its current form, the Proposed Rule could undermine both the confidential attorney-client relationship and the ability of state courts to supervise and discipline lawyers effectively. Therefore, the ABA urges HUD to modify the rule to expand its existing exclusion for licensed attorneys to cover all aspects of the attorneys' representation of clients in connection with the negotiation of a residential mortgage loan, not just those that are ancillary to the representation. Similarly, the ABA urges HUD to add a similar exclusion for licensed attorneys and those acting under their direction who provide mortgage loan modification services to clients.

The Limited Lawyer Exemption in the Proposed Rule

In its Proposed Rule, HUD seeks to clarify or interpret certain key statutory provisions in the Secure and Fair Enforcement Mortgage Licensing Act of 2008, P.L. 110-289, Title V (the "SAFE Act"), including the definition of "loan originator." Section 1503(3) of the SAFE Act defines "loan originator" to mean "an individual who (I) takes a residential mortgage loan application¹; and (II) offers

¹ The term "takes a residential mortgage loan application" is further defined in the Proposed Rule as "receiv[ing] a residential mortgage loan application for the purpose of deciding (or influencing or soliciting the decision of another) whether to extend an offer of residential mortgage loan terms to a borrower or prospective borrower (or to accept the terms offered by a borrower or prospective borrower in response to a solicitation), whether the application is received directly or indirectly from the borrower or prospective borrower." See Proposed Rule, Section 3400.103(c)(1), 74 Fed Reg. at 66557.

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or negotiates terms of a residential mortgage loan for compensation or gain.” The statutory definition also contains several other qualifications. *See* SAFE Act, Section 1503(3). In seeking to clarify and interpret the statutory definition of “loan originator,” HUD’s proposed rule broadens the wording of the original statutory definition² while adding certain exclusions, including a limited exclusion for the following type of lawyer:

“(6) A licensed attorney who only negotiates the terms of a residential mortgage loan on behalf of a client as an ancillary matter to the attorney’s representation of the client, unless the attorney is compensated by a lender, a mortgage broker, or other mortgage loan originator or by any agent of such lender, mortgage broker, or other mortgage loan originator;”

See Proposed Rule, Section 3400.104(e)(6), 74 Fed. Reg. at 66558.

In explaining its reasoning for including this limited attorney exemption in the proposed rule, HUD states as follows:

“In such cases, the attorney’s duties of loyalty to the client require the attorney to seek to further only the client’s interests, and the attorney does not negotiate *with* or make offers of loan terms *to* the client. Accordingly, such activities would not fall within the definition of “offers or negotiates” as proposed to be defined in §3400.103(c)(2) and discussed above, and would therefore not be engaging in the business of a loan originator. This rule would provide in §3400.103(e)(5) (sic) that such individuals are not subject to State licensing requirements.”

See Proposed Rule, 74 Fed. Reg. at 66552 (emphasis in original; second reference should be to §3400.103(e)(6) instead of §3400.103(e)(5)).

HUD’s Proposal to Include “Third-Party Loan Modification Specialists” Under the Rule

In the Proposed Rule, HUD also has stated its “inclination to require licensing, as loan originators under the SAFE Act, of individuals who perform loan modifications that involve offering or negotiating of loan terms that are materially different from the original loan. *See* Proposed Rule, 74 Fed. Reg. at 66553. As support for this view, HUD explains that “the activities of a loan servicer that result in modification of the terms of a residential mortgage loan can be virtually indistinguishable from the performance of a refinancing, which is unambiguously covered by the SAFE Act.” *Id.* HUD also notes in its Proposed Rule that it “has seen a substantial increase in the number of third-party actors (i.e., individuals other than lenders and loan servicers) offering their services as intermediaries to work putatively on behalf of borrowers to negotiate modifications of existing loan terms” and has proposed covering these so-called “third-party loan modification specialists” under the definition of loan originator under the SAFE Act. *Id.* at 66554. While HUD

²The Proposed Rule broadens the second element of the statutory definition of “loan originator” to include not just an individual who offers or negotiates terms of a residential mortgage loan for compensation or gain, but also an individual who “...represents to the public, through advertising or other means of communicating or providing information (including the use of business cards, stationary, brochures, signs, rate lists, or other promotional items), that such individual can or will provide any of the services or perform any of the activities described in paragraph (b)(1)(i) of this section...” *See* Proposed Rule, Section 3400.103(b)(1)(ii), 74 Fed. Reg. at 66557.

does not address the issue directly, the limited lawyer exemption included in the Proposed Rule's definition of loan originator discussed above presumably would also apply to those lawyers who provide residential loan modification services to clients as an ancillary matter to the lawyer's representation of the client.

The ABA's Concerns Regarding the Narrow Lawyer Exemption in the Proposed Rule

While the ABA supports the partial lawyer exclusion contained in Section 3400.103(e)(6) of the Proposed Rule as far as it goes and concurs with HUD's reasoning for the exemption stated above, the ABA believes that the exemption is too narrow and should not be limited only to those situations where the attorney is negotiating the terms of a residential mortgage loan as an "ancillary" matter to the attorney's representation of the client. A lawyer who is retained by a client to negotiate a residential mortgage loan owes the same fiduciary duties to the client, including duties of loyalty, regardless of whether the lawyer's negotiation services are central or ancillary to the representation. Therefore, the exemption in the Proposed Rule should not be limited just to those situations where the lawyer is helping the client to negotiate the residential mortgage loan terms as an "ancillary matter" to the lawyer's representation of the client.

The ABA also is very concerned that unless the attorney exemption to the Proposed Rule's definition of "loan originator" is substantially broadened to include both ancillary and non-ancillary residential mortgage loan and mortgage modification matters, the Proposed Rule will adversely affect many lawyers and their ability to represent their clients effectively. The rule would make many lawyers who represent clients in the negotiation of original residential mortgage loans—or the subsequent modification of such loans—subject to the many substantive regulatory provisions of the SAFE Act, and the Proposed Rule would require the lawyers to be licensed and fully regulated by HUD and the states as "loan originators" just as if they were a mortgage lender, broker, or servicer. In addition, the rule could be read to require the lawyers' employees, agents, and other individuals working under the lawyers' direction to be licensed and regulated by HUD and the states as well.³

In the absence of a broader attorney exemption, the expansive definition of "loan originator" in the Proposed Rule would allow HUD and state agencies to regulate core aspects of the confidential attorney-client relationship. In particular, because "loan originator" is broadly defined to include an individual who "...negotiates terms of a residential mortgage loan for compensation or gain" or "represents to the public, through advertising or other means of communicating or providing information...that such individual can or will provide..." such services⁴, the definition would allow

³ Although Section 3400.103(b)(2) of the Proposed Rule states that "an individual does not engage in the business of a loan originator merely by performing administrative or clerical tasks," Section 3400.23 defines the term "clerical or support duties" to "not include...taking a residential mortgage loan application...or offering or negotiating terms of a residential mortgage loan." See Proposed Rule, 74 Fed. Reg. at 66556-66557. Therefore, it is unclear whether a lawyer's employees, agents and others working under the lawyer's direction would be covered by the existing "licensed attorney" or "administrative or clerical tasks" exemptions or whether such individuals would be subject to the licensing, registration and other regulatory requirements of the Proposed Rule.

⁴ See the proposed definition of an individual who "engages in the business of a loan originator". Proposed Rule, Section 3400.103(b)(1), 74 Fed. Reg. at 66557; See also footnote 2, *supra*.

HUD and state agencies to regulate the legal advice and other core legal services that real estate lawyers, general practitioners, and many other lawyers routinely provide to their clients. *See* Section 3400.103(b)-(c), 74 Fed. Reg. at 66557.

In addition, HUD's proposal to further expand the definition of "loan originator" to include so-called "third-party loan modification specialists," i.e., individuals other than lenders and loan servicers who work on behalf of borrowers to negotiate modifications of existing loan terms, would allow HUD and the state agencies to regulate the legal advice and other core legal services that bankruptcy lawyers, consumer debtor lawyers, general practitioners, and other types of lawyers routinely provide to their clients in connection with residential mortgage modifications.

The broad definition of "loan originator" in the Proposed Rule would make lawyers (and perhaps those individuals working under the lawyers' direction) subject to licensing, registration, and the general supervision and disciplinary authority of HUD and the individual state agencies regulating loan originators if they merely help their clients to negotiate the original terms of their residential mortgage loans—or a modification of those loan terms—and their legal services are not ancillary to their representation of the client. By granting HUD and the state agencies sweeping powers to regulate these lawyers, the lawyer's employees and agents, and the legal services that they provide to their clients, the Proposed Rule could erode the confidential relationship between lawyers and their clients, including the attorney-client privilege, and therefore could undermine the client's right to effective counsel.⁵

By vesting HUD and the state agencies with expansive new powers to regulate lawyers providing non-ancillary mortgage loan negotiation and modification services to clients, the Proposed Rule also threatens to undermine the ability of state courts to effectively supervise and discipline lawyers. For centuries, lawyers have been primarily regulated by the highest court of the state in which the lawyer is licensed. During that time, the courts have developed extensive regulations governing all aspects of the practice of law, including strict ethical codes and disciplinary rules. By granting HUD and the state agencies expansive new powers to regulate many lawyers, the legislation will likely result in federal and state agency rules that could conflict with and undermine the state supreme courts' traditional supervision and regulation of lawyers. This overlapping federal-state regulation (and state agency-state supreme court regulation) could also cause confusion over the standards that lawyers must follow in dealing with their clients.

Finally, additional HUD and state agency regulation of lawyers in this area is simply not needed in order to protect consumers seeking to negotiate residential mortgage loans or modifications of those loans. The primary reason to license and regulate mortgage loan originators is to keep them honest and ensure proper government oversight over them. But because lawyers already have substantial fiduciary duties to their clients that are strictly enforced by the state supreme courts and state bars

⁵ Generally speaking, "agents and subordinates working under the direct supervision and control of the attorney are included within the scope of the attorney-client privilege." *See* 1 Edna Selan Epstein, *The Attorney-Client Privilege and the Work Product Doctrine* 211 (5th ed. 2007). In addition, "the privilege also extends to summer associates, paralegals, investigators, and secretaries who are acting in the capacity of and presented to a client as an 'agent' of the attorney." *Id.*

that license and oversee the lawyers, this rationale for licensing the loan originators simply does not apply to lawyers who are already licensed by their state courts and bars.⁶

The ABA's Proposed Amendments

To remedy these problems arising from the Proposed Rule, the ABA respectfully urges HUD to adopt several proposed amendments to the rule. In particular, the ABA recommends that HUD amend the current attorney exemption contained in Section 3400.104(e)(6) to eliminate the ancillary limitation and replace it with the following broader language:

“(6) A licensed attorney or individual acting under the direction of the attorney who negotiates the terms of a residential mortgage loan on behalf of a client, or who provides other legal services to the client in connection with the loan, unless the attorney is compensated by a lender, a mortgage broker, or other mortgage loan originator or by any agent of such lender, mortgage broker, or other mortgage loan originator;”

Similarly, if HUD decides to proceed with its proposal to include so-called third-party loan modification specialists under the definition of loan originator and thereby cover them by the licensing requirements of the SAFE Act (*See* Proposed Rule at 66554), the ABA urges HUD to add a new corresponding exemption for attorneys helping their clients to renegotiate or modify existing residential mortgage loans—and those acting under the attorneys' direction—that is not limited to “ancillary” matters. In particular, the ABA urges HUD to add the following new exemption to any new Proposed Rule that seeks to cover third-party loan modification specialists:

“(x) A licensed attorney or individual acting under the direction of the attorney who negotiates the terms of a residential loan modification on behalf of a client, or who provides other legal services to the client in connection with the loan modification, unless the attorney is compensated by a lender, a mortgage broker, or other mortgage loan originator or by any agent of such lender, mortgage broker, or other mortgage loan originator;”

If adopted, these amendments to HUD's Proposed Rule would allow licensed attorneys and those acting under their direction to continue to provide effective legal representation to their clients in connection with the negotiation or modification of residential mortgage loans, regardless of whether those legal services are ancillary or central to the representation.

⁶ According to the official Commentary to the ABA Model Rules of Professional Conduct, which have been adopted in some form by almost all state supreme courts, a lawyer's non-attorney assistants such as secretaries, paralegals, investigators, and law student interns “act for the lawyer in rendition of the lawyer's professional services... (and the lawyer must give such assistants appropriate instruction and supervision concerning the ethical aspects of their employment...)” *See* ABA Model Rule 5.3, Comment 1. The ABA Model Rules further provide that a lawyer having direct supervisory authority over a nonlawyer assistant “shall make reasonable efforts to ensure that the person's conduct is compatible with the professional obligations of the lawyer.” *See* ABA Model Rule 5.3(b). Therefore, because those individuals working under the direction of a licensed attorney are already effectively subject to the same professional standards as the attorney, additional HUD and state agency regulation of these individuals is not necessary to protect consumers.

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Thank you for considering the views of the ABA on these important issues. If you have any questions regarding the ABA's position on the Proposed Rule or our suggested amendments, please contact me at (202) 662-1765 or ABA Senior Legislative Counsel Larson Frisby at (202) 662-1098.

Sincerely,

A handwritten signature in black ink, appearing to read "Thomas M. Susman", with a long horizontal flourish extending to the right.

Thomas M. Susman