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ARKANSAS SECURITIES DEPARTMENT

October 29, 1999

Stephen F.J. Ornstein
THACHER, PROFFITT & WOOD
1700 Pennsylvania Avenue, N.W.
Washington, DC 20006

RE: Arkansas Mortgage Loan Company and Loan Broker Act
Request for interpretative Opinion No. 99-013

Dear Mr. Ornstein:

Your letter of September 9, 1999 (a copy of which is enclosed for reference), requesting advice pertaining to the registration provisions of the Arkansas Loan Company and Loan Brokers Act has been forwarded to me for response. In your letter you set forth six different scenarios and request advice as to whether or not the registration provisions would be applicable. I will address the different scenarios in the same order as you have presented them in your letter. Please be advised that the following discussion is for discussion purposes only and is not to be relied upon without supplementation. Prior to rendering either a legal opinion or a "no action" position upon which reliance can be placed, the Department requires more specific information regarding the parties involved and the particulars of the contemplated transaction. With that proviso, I will offer you my thoughts on the fact situations that you have posed.

1. Purchase and Sale of Mortgage Loans on a Secondary Market Basis.

Without discussion, it is my opinion that you have reached the correct conclusion, i.e., that registration of the LLC would be required because of the purchase and sale of the mortgage loans.

2. "Warehouse" Lending.

Likewise, under the second scenario you present, I agree that "a warehouse lender would not be deemed a 'mortgage loan company' within the meaning of the Act merely because it takes a pledge of the loans made by the originating lender as security for the granting of the warehouse line of credit." However, I disagree with your interpretation to the extent that you state that "the registration, bond and net worth requirements of the Act would not apply to a warehouse lender" due to the fact that, under the facts presented, the LLC becomes the owner of the loans upon default of the originating lender, and will proceed to sell the loans in the secondary market to another investor. The fact that a custodian retains possession of the loan on behalf of the LLC does not, in my opinion, overcome the language in the introductory sentence of Ark. Code Ann. § 23-39-102(5)(A) wherein reference is made to any person who "directly or indirectly" engages in the activities listed. By acting through a custodian, it seems to me that the LLC is acting "indirectly" to sell the loan.

3. "Repo" Financing.

I also must disagree with your conclusion regarding the necessity for registration under the "repo" financing scenario. Although perhaps elevating form over substance, a "repo" undeniably involves the purchase and subsequent resale back of the subject matter involved, in this instance a mortgage loan. There appears to be no exception from Ark. Code Ann. § 23-39-102(5)(A)(iii) merely because the purchase and sale are dependent on one another.

4. Holders of Participation Certificates

The language of Ark. Code Ann. §23-39-102(5)(A) again leads to the conclusion that one cannot avoid the registration requirement by doing indirectly through another what one could not do directly. In this instance, provided that the "investors" do not qualify for the de minimus exception set forth in §23-39-102(5)(B), registration appears necessary due to the language of §23-39-102(5)(A)(iii).

5. Special Purpose Entities in "Pass Through" Structures.
6. Delaware Business Trusts in Bond Deals

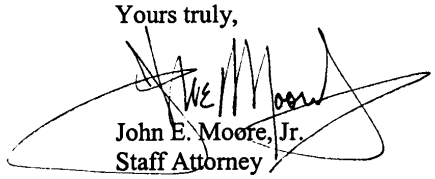
Both of these scenarios present situations that appear to be extremely fact sensitive, and hence, I am unable to give you a blanket response regarding either of them. I will note however, that the fact situation as set forth in the SPE scenario specifically makes reference to the "transfer" of the property by the SPE. It is difficult to imagine in what fashion the transfer could take place if the SPE did not have an ownership interest in the mortgage loan, regardless of the fact that the SPE may not appear in the chain of title. It also seems difficult to understand how the SPE insulates the ultimate certificate holder from the bankruptcy of the originator or issuer if the SPE is not in the chain of title.

As to the Delaware Business Trust scenario, I do not believe that the mere fact that legal title is not recorded in the name of the trust prevents the trust from having to register if it otherwise would be required to register. Although you have stated that one should assume that Ark. Code Ann. §23-39-306(a) is inapplicable for purposes of this discussion, I note that subparagraph (a)(1) thereof may be effective to raise an exemption because of the fact that the acting party is a trust.

As to both of these scenarios, I would lean toward believing registration to be applicable, but would certainly entertain an argument, supported by appropriate facts, to the contrary.

I hope the discussion set forth above is helpful to you. As I mentioned at the outset, it is entirely possible that given specific facts, a different conclusion might be reached. Should you have any questions or desire to discuss this matter, please feel free to contact me.

Yours truly,



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September 9, 1999

BY FACSIMILE AND REGULAR MAIL

Mr. Rick Weaver
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Arkansas Securities Department
Heritage West Building, Suite 300
201 East Markham Street
Little Rock, AR 72201

Re: Licensing Requirements under Various Financing Scenarios

Dear Mr. Weaver:

I am writing to inquire whether certain financing arrangements that are commonly used in the mortgage industry would trigger the registration, bond and net worth requirements of the Arkansas Mortgage Loan Company and Loan Broker Act, Ark. Code Ann. § 23-39-101, *et seq.* (the "Act"). For the purpose of this inquiry, please assume that the exemptions from the registration, bond and net worth requirements of the Act, set forth in Ark. Code Ann. § 23-39-306(a) (e.g., being a depository institution or HUD approved lender), are *not* applicable. Further, for the purpose of this inquiry, please also assume that the entity involved in the various financing arrangements described below is a Delaware limited liability company with its principal place of business in New York (hereinafter referred to as "LLC"). LLC does not employ personnel in Arkansas or maintain a place of business in the state.

1. Purchase and Sale of Mortgage Loans on a Secondary Market Basis

In the first scenario, LLC purchases and sells residential (including multifamily) and commercial first and subordinate lien mortgage loans on a "secondary market basis." In other words, the originating lender uses its own funds to originate the loans in its own name and subsequently sells the loans to LLC at market value. This scenario does *not* involve "table-funding" whereby LLC would advance funds to the settlement lender at closing and the settlement lender would contemporaneously assign the loan to LLC.

Under our interpretation of the Act, absent an exemption, the purchase and sale of mortgage loans (regardless of type or lien) triggers the registration, bond and net worth requirements of the statute.

2. **"Warehouse" Lending**

Under the second scenario, LLC would provide a "warehouse" line of credit to the originating lender. A warehouse lender provides a source of funds to the originating lender so that the loans can be made and takes a pledge of the loans as collateral for the advance of money. In the event of a default by the originating lender under the warehouse line, the warehouse lender would become the holder of the loans. Unlike a table-funding arrangement, however, the borrowers never have contact with the warehouse lender, unless the originating lender defaults under the warehouse line and the warehouse lender takes possession of the loans and begins to service the obligations.

It should be noted that in some warehouse funding arrangements, such as the ones entered into by LLC, in the event of a default by the originating lender under the warehouse line, the warehouse lender does not take actual possession of the loans (and does not record legal title in its own name), and does not service the obligations. Rather, a custodian retains possession of the loans and a third party servicer services the obligations until the loans are sold in the secondary market to another investor.

Under our interpretation of the Act, a warehouse lender would not be deemed a "mortgage loan company" within the meaning of the Act (*see* Ark. Code Ann. § 23-39-306(a)(A)) merely because it takes a pledge of the loans made by the originating lender as security for the granting of the warehouse line of credit. Consequently, we believe that the registration, bond and net worth requirements of the Act would not apply to a warehouse lender.

3. **"Repo" Financing**

In a variant of warehouse lending, LLC presently provides short-term financing to a number of institutions under a certain "repurchase" arrangement. Under this repurchase arrangement, the institution to whom LLC provides financing "sells" certain commercial and residential mortgage loans to LLC and then "repurchases" the mortgages a short time later at a premium repurchase price. Under the terms of the "repurchase" agreement, the mortgages that the institution has "sold" to LLC are transferred to a third party custodian during the term of the financing. LLC only takes possession of the mortgages if the institution defaults under its obligations set forth in the agreement or in the unlikely event that it does not "repurchase" the mortgages from LLC.

In some instances, however, like the warehouse lending scenario described above, the custodian retains possession of the mortgages and a third party servicer services the obligations until LLC sells the loans in the secondary market to another investor.

This arrangement is considered a "financing" for certain accounting purposes, and is analogous to taking a pledge of the loans under a warehouse lending agreement. In our view, the

providing of "repo" financing by LLC would not trigger the registration, bond and net worth requirements of the Act, especially if LLC does not take physical possession of the loans from the custodian in the event of a default under the "repo" agreement or if the loans are not repurchased by the "seller".

4. Holders of Participation Certificates

In another financing structure commonly used in the mortgage industry known as a participation arrangement, investors purchase undivided ownership interests in mortgage loans evidenced by a certificate. While legal title to the mortgage loans remains with the principal (e.g., the seller of the participation interests), the certificate holders (e.g., the purchasers of the participation interests) are the beneficial owners of the loans.

In a participation arrangement, the principal would become licensed as a "mortgage loan company" under the Act, but the investors purchasing the certificates would not become licensed under the Act. Under our interpretation of the statute, we believe that purchasers of participation certificates would not be deemed "mortgage loan companies," and hence, would not trigger the registration, bond and net worth requirements of the Act.

5. Special Purpose Entities in "Pass Through" Structures

When mortgage loans are securitized in the secondary market, a "pass-through" structure is frequently used. In a typical pass-through arrangement, the originator or acquirer (e.g., a secondary market purchaser) of the mortgages, as the case may be, transfers the mortgages to a special purpose entity ("SPE") which holds them for a very brief period of time (e.g., literally for only seconds). During the brief period of time that the SPE holds the loans, the promissory notes and assignments are not endorsed or assigned, as the case may be, in the SPE's name, and technically, the SPE does not appear in the chain of legal title. The SPE then transfers the mortgages to a trust, which ultimately issues certificates representing undivided ownership interests in the mortgages to investors. The trustee, who acts on behalf of the trust, is usually a depository institution, and hence, is exempt from most, if not all, state licensing requirements (such as those set forth in the Act).

These "pass-through" structures are used so that in the event that the originator or acquirer of the mortgage loans, as the case may be, becomes bankrupt, the loans that are ultimately securitized are not " put back" in the debtor's estate.

Because SPEs serving the function described above only hold the mortgages for a very brief period of time, and typically do not employ personnel or have an office, they rarely obtain state licenses. Arguably, SPEs are not "mortgage loan companies" within the meaning of the Act, and thus, would not trigger the registration, bond and net worth requirements of the Act. Again, in a "pass-through" securitization, the mortgage loans are transferred by the originator or acquirer, as the case may be, to the SPE who then transfers them to a trustee in exchange for certificates representing undivided interests in the loans. The certificates are then sold to investors by the originator or

acquirer, as the case may be, in exchange for cash. Until the originator or acquirer sells the certificates which represent the loans to investors, there is arguably no "purchase," "sale" or "exchange" within the meaning of the Act, and hence, the SPE would not appear to trigger the registration, bond and net worth requirements of the Act.

6. **Delaware Business Trusts in Bond Deals**

In debt transactions secured by mortgage loans, the mortgages are frequently transferred from the originator or secondary market purchaser of the loans, as the case may be, to an SPE, who then transfers them to a Delaware business trust. Although the Delaware business trust subsequently pledges the mortgages to a bond or indenture trust as security for the bonds, it ultimately issues notes to investors. While the Delaware business trust holds beneficial ownership of the mortgages on behalf of the note holders, legal title to these mortgages is always held by the bond trust. As in the "pass-through" structure described above, the trustee who acts on behalf of the bond trust, is customarily a depository institution, and hence, is exempt from most, if not all, state licensing requirements (such as those set forth in the Act). Because legal title is never recorded in the name of the Delaware business trust, we believe that the Delaware business trust would not trigger the registration, bond and net worth requirements of the Act in these circumstances.

Kindly confirm whether our interpretation of the registration, bond and net worth requirements of the Act is correct in the six financing arrangements described above.

Please do not hesitate to call me with any questions or if you would like me to clarify any of the above-mentioned items.

Very truly yours,

Stephen F.J. Ornstein

SFJO:db