

STATE OF OHIO
DEPARTMENT OF COMMERCE
Division of Financial Institutions
Consumer Finance

In the matter of:) <u>Notice of Intent to Deny</u>
) <u>Mortgage Broker Certificates of Registration</u>
) <u>and Notice of Opportunity for a Hearing</u>
AMERICAN MORTGAGE COMPANY 2, LLC) Case Numbers: 05-0001-MBD
75 East Wilson Bridge Road)
Worthington, OH 43085)
-and-)
AMERICAN MORTGAGE COMPANY 3, LLC) 05-0002MBD
415 Glensprings Drive, Suite 203)
Cincinnati, OH 45246)
-and-)
AMERICAN MORTGAGE COMPANY 5, LLC) 05-0003-MBD
106 West Ash Street)
Piqua, OH 45436)
-and-)
AMERICAN MORTGAGE COMPANY 6, LLC) 05-0004-MBD
75 East Wilson Bridge Road)
Worthington, OH 43085)
-and-)
AMERICAN MORTGAGE COMPANY 8, LLC) 05-0005-MBD
75 East Wilson Bridge Road)
Worthington, OH 43085)
)

JURISDICTION

The Ohio Department of Commerce, by and through the Superintendent of the Division of Financial Institutions ("DFI"), is charged with the responsibility of administering and enforcing the Ohio Mortgage Broker Act, codified in Ohio Revised Code ("R.C.") Chapter 1322.

RESPONDENTS

AMERICAN MORTGAGE COMPANY 2, LLC is a limited liability company that has applied to the DFI for a mortgage broker certificate of registration.

AMERICAN MORTGAGE COMPANY 3, LLC is a limited liability company that has applied to the DFI for a mortgage broker certificate of registration.

AMERICAN MORTGAGE COMPANY 5, LLC is a limited liability company that has applied to the DFI for a mortgage broker certificate of registration.

AMERICAN MORTGAGE COMPANY 6, LLC is a limited liability company that has applied to the DFI for a mortgage broker certificate of registration.

AMERICAN MORTGAGE COMPANY 8, LLC is a limited liability company that has applied to the DFI for a mortgage broker certificate of registration.

STATEMENT OF FACTS

American Mortgage Service Company (“AMSCo”), an S corporation held by Edward Wolterman and Elvera Bergdolt, is a mortgage banking company that originates approximately \$400 million annually in mortgage volume. AMSCo is registered with the Division as a mortgage broker. AMSCo processes, underwrites and closes its own loans in its own name and with its own credit line. In addition to its main office, AMSCo has five registered branch offices located in Ohio that are staffed to handle on-site underwriting and processing to support local originations.¹

In order to capture a larger market share, AMSCo has created five limited liability companies: American Mortgage Company 2, LLC (“AMC 2”), located in AMSCo’s Worthington branch office; American Mortgage Company 3, LLC (“AMC 3”), located in AMSCo’s main office in Cincinnati; American Mortgage Company 5, LLC (“AMC 5”), located in AMSCo’s Piqua branch office; American Mortgage Company 6, LLC (“AMC 6”), located in AMSCo’s Worthington branch office; and American Mortgage Company 8, LLC (“AMC 8”), also located in AMSCo’s Worthington office. (Hereinafter AMC 2, AMC 3, AMC 5, AMC 6, and AMC 8 will collectively be referred to as “LLC.”) The principal office for each LLC is AMSCo’s main office.

AMSCo will retain 51% ownership in each LLC², and will solicit high volume producing real estate agents to purchase the remaining minority interest. The 49% interest will be sold in non-fractional blocks of 3.5% for a total cost of \$300, to a minimum of 10 and a maximum of 14 real estate agents. Each real estate agent will have the right to purchase only one block totaling 3.5% ownership. In the event fewer than 14 real estate agents purchase interest in the LLC, AMSCo will purchase the remainder. The real estate agents will have the opportunity to refer business to the LLC, and will receive profits generated by the LLC to which they refer business based on their ownership share, not on the amount of business referred.

Initially each LLC will hire one employee who qualifies as an operations manager. Each LLC will rent office space³ and equipment from AMSCo. The real estate agents who purchase an interest in an LLC will provide customers they refer to the LLC a disclosure statement informing the customer that

¹ AMSCo’s main office is located at 415 Glensprings Drive, Suite 203, in Cincinnati, Ohio. AMSCo has five registered branch offices located at: 75 East Wilson Bridge Road in Worthington, Ohio; 1180 Stone Drive in Harrison, Ohio; 106 West Ash Street in Piqua, Ohio; 2621 Dryden Road, Suite 203, in Dayton, Ohio; and 48 Main Street in Enon, Ohio. AMSCo also does business in the state of Kentucky as Kentucky Mortgage. Additionally, AMSCo owns 50% of Ball Mortgage, located in Lexington, KY and 49% of Housing Financial Group, an Ohio mortgage company.

² Each LLC is identical, with the exception of office location, and will be discussed as one.

³ AMSCo has subleased a 205 sq. ft. space of its Worthington office to AMC 2; AMSCo has subleased a 205 sq. ft. space of its Cincinnati office to AMC 3; AMSCo has subleased a 205 sq. ft. space of its Piqua branch office to AMC 5; AMSCo has subleased a 205 sq. ft. space of its Worthington office location to AMC 6; and AMSCo has subleased an additional 205 sq. ft. space of its Worthington branch office to AMC 8.

the agent has a financial interest in the LLC and that the customer is not required to utilize the services of the LLC.

After a lengthy investigation, the DFI has concluded that the LLC applications should be denied. In making this determination, the DFI took an in-depth look at how the LLCs were established and how they will operate in consideration of the Ohio Mortgage Broker Act's anti-kickback provision, which makes it illegal for any mortgage broker or loan officer to:

Pay or receive, directly or indirectly, a referral fee or kickback of any kind to or from a bona fide third party or other party with a related interest in the transaction, such as a home improvement builder, real estate developer, or real estate broker or agent, for the referral of business.

R.C. § 1322.071(B)(3). Violation of this anti-kickback provision not only carries administrative penalties, but also constitutes a fourth degree felony. (See R.C. § 1322.99(B).) Paying or receiving, directly or indirectly, kickbacks of any kind to a party with a related interest for the referral of business constitutes improper, fraudulent, and or dishonest dealings in dereliction of R.C. § 1322.07(C).

Initially, the form and structure of the LLCs did not concern Division officials. In fact, AMSCo had submitted an application for a mortgage broker certificate of registration on September 12, 2003, for a company AMSCo named American Mortgage Company 1, LLC ("AMC 1"). AMSCo represented that the limited liability company was an innovative joint venture between itself and real estate agents. AMSCo touted the company as a bona fide joint venture under federal mortgage and lending laws because the LLC would employ a person to perform the loan originations, the real estate agents would provide customers disclosures concerning their interest in the LLC, and the agents would only receive payment in the form of profits in proportion to their ownership interest.

While the application for AMC 1 was pending, AMSCo submitted the application for AMC 2 on October 28, 2003. The DFI issued AMC 1 a mortgage broker certificate of registration on November 21, 2003. Noticing that AMC 1 and AMC 2 each only employed one employee and operated from the same office, which was also a branch office of AMSCo, and that each restricted ownership to AMSCo and to "10 to 14 high volume real estate agents," the DFI decided to examine AMC 2 more closely. During the course of the investigation, AMSCo submitted the application for: AMC 6 on May 24, 2004; AMC 3 on June 22, 2004; AMC 8 on July 26, 2004; and AMC 5 on July 28, 2004.

Evidence before the DFI shows that the LLCs are not bona fide joint venture mortgage brokerage companies, but are sham arrangements created to disguise kickbacks to real estate agents for the referral of business, in violation of R.C. § 1322.071(B)(3)⁴. Each LLC was created solely by AMSCo, who has or will solicit 14 high volume real estate agents to each purchase 3.5% ownership in a LLC for a price of

⁴ All analyses and conclusions have been based solely on Ohio law.

\$300. The real estate agents may refer business to the LLC, and in turn will be paid profits from the LLC.

The real estate agents have no right or authority to act for or to bind the LLC. The full extent of business risk involved for the real estate agents/owners is the loss of his or her capital contribution (\$300), or being bought out by AMSCo at any time for any reason for the amount of the agent's capital contribution. AMSCo need not provide any reason for purchasing a real estate agent's share, but has expressly stated that it may do so if the agent fails to maintain his or her livelihood as a real estate agent in Ohio, or the agent fails to act as the listing and or selling agent for the sale of at least ten (10) housing units⁵ per year, which housing units must be subject to actual closing and sale.

The only responsibilities the real estate agents have is to refer business to the LLC in order to generate profits, to attend a minimum of two quarterly meetings each calendar year, and not to disclose confidential information about the LLC, such as terms, conditions and discussions regarding his/her ownership interest. Agents agree not to divert any customer or business account of the LLC to any competitor, but waive such restriction and any potential conflict of, for, or concerning AMSCo.

In return for their \$300 investment, at the end of each year each real estate agent is to receive a distribution, in relation to his or her ownership interest, of the LLC's net cash flow⁶ for the year. Agents need not be concerned with federal income taxes because distributions will be made to each agent/owner prior to April 15th, in the amount necessary to pay the tax due by such real estate agent as the result of the allocation of the LLC's taxable income or gain to such agent for such fiscal year.

AMSCo's majority ownership interest in the LLCs can never be diluted. AMSCo's presence alone at a membership meeting constitutes quorum, and only AMSCo's vote is required for consent or approval of any action, decision, resolution, or other matter submitted for a vote or consent of the members. Each LLC will be managed by AMSCo, who will have the sole authority to, *inter alia*: control the LLC's business; to act for or to bind the LLC; to employ, engage, subcontract, and/or release from employment any person, agent, independent contractor, business, trust, or entity; to engage the services of attorneys, accountants, financial advisors, consultants, or other professionals or advisors of any kind; to avoid, cancel, re-negotiate, or terminate any contract or obligation; to obtain lender financing on ordinary and customary commercial terms, grant security interests to lenders in and to the property and interests of the LLC; to institute and/or defend the LLC against any lawsuits, arbitrations, mediations; to admit any person into membership. For its services as manager, AMSCo shall receive compensation as

⁵ The LLC's define a "housing unit" as any one to four family residential property located in the state of Ohio.

⁶ "Net cash flow" is the cash received by the LLC for the fiscal year after the payment of all operating expenses (which includes a payment of at least \$50,000 to AMSCo for managerial services) for such fiscal year and after the establishment of appropriate reserves, if any, for the LLC as determined by AMSCo.

determined by AMSCo, provided that the initial compensation shall be \$50,000.00/year unless the amount is increased by the written consent of a majority of the Membership units (AMSCo owns a majority share).

The role of the “operations manager” in each LLC is limited to originating loans and generating new business. Most of the operations managers were former AMSCo employees that just continue to perform the work they previously did for AMSCo.

The totality of the evidence before the DFI shows that the LLC arrangements afford compensation to real estate agents but impose on them no work or business risk beyond their initial \$300 investment. The substantial functions of the LLCs are actually provided by AMSCo, who otherwise could receive the referrals of business directly. In short, the LLCs are disguised referral fee arrangements and violate R.C. §§ 1322.071(B)(3) and 1322.07(C).

NOTICE OF PROPOSED ACTION

The Division intends to deny the application for a mortgage broker certificate of registration submitted by: American Mortgage Company 2, LLC; American Mortgage Company 3, LLC; American Mortgage Company 5, LLC; American Mortgage Company 6, LLC; and American Mortgage Company 8, LLC,⁷ because each company is merely a sham arrangement created to disguise kickbacks to real estate agents for the referral of business.

NOTICE OF OPPORTUNITY FOR A HEARING ON PROPOSED ACTION

Therefore, pursuant to R.C. Chapters 1322 and 119, AMC 2, AMC 3, AMC 5, AMC 6, and AMC 8 are hereby notified that thirty-one (31) days from the date of the mailing of this Notice, the Superintendent intends to issue an order denying their applications for mortgage broker certificates of registration.

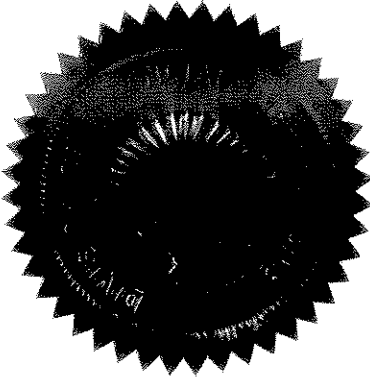
AMC 2, AMC 3, AMC 5, AMC 6, and AMC 8 are further notified, pursuant to R.C. Chapter 119, they are entitled to a hearing on this matter. If they desire to request a hearing, the request must be made in writing, and must be received in the offices of the Ohio Division of Financial Institutions within thirty (30) days of the time of the mailing of this Notice. Hearing requests should be addressed: Ohio Division of Financial Institutions, Attn: Amanda Axtell, Consumer Finance Counsel, 77 South High Street, 21st Floor, Columbus, Ohio 43215-6120.

At the hearing, AMC 2, AMC 3, AMC 5, AMC 6, and AMC 8 may appear in person, by their attorney, or by such other representative as is permitted to practice before the Agency, or the applicants


⁷ The Division is concurrently revoking the mortgage broker certificate of registration issued to AMC 1. See Consumer Finance Administrative Case No. 05-0001-MBR.

may present their positions, arguments, or contentions in writing, and, at the hearing, may present evidence and examine witnesses appearing for and against them.

If the Ohio Division of Financial Institutions does not receive a written request for a hearing in its offices within thirty (30) days of the time of the mailing of this Notice, the Superintendent will issue an order denying the applications for mortgage broker certificates of registration submitted by AMC 2, AMC 3, AMC 5, AMC 6, and AMC 8.



Signed and sealed this 18th day of February 2005.



ROBERT M. GRIESER
Deputy Superintendent for Consumer Finance
Division of Financial Institutions
Ohio Department of Commerce

AMC 2, LLC CERTIFIED MAIL: 7002 2030 0002 6804 0871