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Inside

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An Overview of the Credit Score Disclosure Requirements for Risk-Based Pricing Notices

By Laura Gleason, Senior Consumer Regulations Analyst, Federal Reserve Bank of Philadelphia

On January 15, 2010, the Board of Governors of the Federal Reserve System (Board) and the Federal Trade Commission (FTC) jointly issued final rules implementing the risk-based pricing requirements under the Fair Credit Reporting Act (FCRA) (January 2010 Final Rules). These rules generally require a creditor to provide a consumer applying for credit with a notice when, based on the consumer's credit report, the creditor provides credit to the consumer on less favorable terms than it provides to other consumers.[1] The final rule was effective January 1, 2011. *Outlook* reviewed these requirements in detail in *An Overview of the Risk-Based Pricing Implementing Regulations*, published in the fourth quarter 2010 issue,[2] and in a webinar titled *Risk-Based Pricing Notices* on February 16, 2011.[3]

On July 21, 2010, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). Section 1100F of the Dodd-Frank Act amended the FCRA to require disclosure of credit scores and information relating to credit scores for both risk-based pricing and FCRA adverse action notices. On July 15, 2011, the Board and the FTC jointly issued final rules to implement section 1100F for risk-based pricing notices (July 2011 Final Rules). This article reviews the credit score disclosure requirements for risk-based pricing notices that were added under the Dodd-Frank Act.[4]

CREDIT SCORE DISCLOSURE REQUIREMENTS FOR RISK-BASED PRICING NOTICES

When Must a Credit Score and Information Relating to a Credit Score Be Disclosed on a Risk-Based Pricing Notice?

A creditor must disclose a consumer's credit score and information relating to

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[1] http://www.federalreserve.gov/newsevents/press/bcreg/20091222b.htm

[2] http://bit.ly/rb-article

[3] http://tinyurl.com/rb-webinar

[4] The Board also published adverse action model notices to reflect the new credit score disclosure requirements for FCRA adverse action notices. These model notices were published under Regulation B and may be used to fulfill both the Equal Credit Opportunity Act and FCRA adverse action notice requirements. See 76 Fed. Reg. 41,590, 41,598 (July 15, 2011). The Board's announcement and the *Federal Register* notices are available at: http://1.usa.gov/score-rule.

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The Federal Reserve Board's Interim Final Rule on Valuation Independence

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In response to the financial crisis, the Board of Governors of the Federal Reserve System (Board) exercised its rulemaking authority under the Home Ownership and Equity Protection Act in 2008 to amend Regulation Z to provide several new protections for consumer mortgages.[1] The final rule, which became effective October 1, 2009, included appraiser independence requirements in §226.36(b) designed to ensure the integrity of real estate appraisals used in closed-end mortgages. Subsequently, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act),[2] which largely codified the protections of §226.36(b) into new section 129E of the Truth in Lending Act (TILA), 15 U.S.C. §1639e, while also adding new protections. For example, while §226.36(b) was limited to closed-end consumer credit transactions secured by a principal dwelling, section 129E applies to *all* consumer credit transactions secured by a principal dwelling, including home equity lines of credit.

In October 2010, the Board published an interim final rule to implement section 129E's requirements, which became effective on April 1, 2011.[3] The Board's rule, which creates new §226.42 of Regulation Z and replaces the Board's prior rule under §226.36(b),[4] imposes the following requirements:

- Prohibits coercion and other similar actions designed to cause persons who perform property valuations to base the appraised value of properties on factors other than their independent judgment;
- Prohibits persons who perform property valuations and valuation management companies hired by lenders from having financial or other interests in the properties or the credit transactions;
- Prohibits creditors from extending credit based on a valuation if the creditor knows beforehand of violations involving coercion or conflicts of interest, unless the creditor determines that the value of the property is not materially misstated or misrepresented;
- Requires that creditors or settlement service providers that have information about appraiser misconduct file reports with the appropriate

[1] 73 Fed. Reg. 44,522 (July 30, 2008)

[2] Public Law 111–203, 124 Stat. 1376 (July 21, 2010)

[3] The Board's announcement and the *Federal Register* notice are available at: http://1.usa.gov/value-rules. Section 129E(g) directed the Board to publish an interim final rule within 90 days of the Dodd-Frank Act's enactment and provides discretionary authority for further rulemaking, guidance, and policy statements to be implemented jointly by the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the National Credit Union Administration Board, the Federal Housing Finance Agency, and the Consumer Financial Protection Bureau. See TILA 129E(g)(1); 15 U.S.C. §1639e(g)(1).

[4] Although the interim final rule replaces §226.36(b), the protections of §226.36(b) have been incorporated into the new rule.

state licensing authorities; and

- Requires the payment of reasonable and customary compensation to appraisers who are not employees of the creditors or of the appraisal management companies hired by the creditors.

This article reviews these requirements and also briefly discusses the long-standing prudential appraisal regulations and guidelines of the federal banking agencies, including the recently revised *Interagency Appraisal and Evaluation Guidelines* issued by the agencies in December 2010.

COVERED PERSONS AND TRANSACTIONS

The interim final rule applies to a covered person, defined as a creditor with respect to a covered transaction or a person providing settlement services, as defined in the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. §2601 *et seq*. See 12 U.S.C. §2602(3). This latter definition includes, for example, appraisers, mortgage brokers, title insurers, and realtors. A "covered transaction" is defined as an extension of consumer credit that is or will be secured by the consumer's principal dwelling, including home equity lines of credit.

In several key provisions, the rule uses the phrase "valuation" instead of "appraisal" because in some jurisdictions appraisers are licensed or certified, and the rule is not limited to these appraisers but applies more broadly to any person valuing real estate in a covered transaction. For example, some real estate agents make valuations and are subject to the rule if they make a valuation for a covered transaction.[5] "Valuation" is defined in §226.42(b)(3) as an "estimate of the value of the consumer's principal dwelling in written or electronic form, other than one produced solely by an automated model or system." This definition specifically excludes valuations based on an automated valuation system.

REQUIREMENTS OF THE INTERIM FINAL RULE

§226.42(c): Coercing and Misrepresenting Value of Consumer's Dwelling Prohibited

Under the rule, a covered person is prohibited in a covered transaction from directly or indirectly coercing, extorting, inducing, bribing, intimidating, compensating, or colluding with a person preparing real estate valuations, or performing valuation management functions, to cause the valuation assigned to a consumer's principal dwelling to be based on any factor other than the independent judgment of the person who prepares the valuation. The meaning of these terms is based on their definition under applicable state law or contract.

A violation of §226.42(c) occurs if a person engages in one of these actions for the purpose of causing the value assigned to the dwelling to be based on a factor other than the independent judgment of the person preparing the valuation. For example, asking the person preparing the valuation to consider additional, appropriate property information does not violate §226.42(c) "because such request does not supplant the independent judgment of the person that prepares a valuation."[6] The rule covers both direct and indirect conduct. For example, if a creditor attempts to pressure an appraiser into making a valuation not based on the appraiser's independent judgment by threatening to withhold future business, the threat violates the rule.[7]

To facilitate compliance, the final rule provides examples of coercion violations:

- Seeking to influence a person who prepares a valuation to report a minimum or maximum value for the consumer's principal dwelling;
- Withholding or threatening to withhold timely payment to a person who prepares a valuation or performs valuation management functions because the person does not value the consumer's principal dwelling at or above a certain amount;
- Implying to a person who prepares valuations that current or future retention of the person depends on the amount at which the person estimates the value of the consumer's principal dwelling;
- Excluding a person who prepares a valuation from consideration for future engagement because the person reports a value for the consumer's princi-

[5] See comment 226.42(c)(1)-3 of the Regulation Z Official Staff Commentary (Commentary).

[6] See comment 226.42(c)(1)-2.

[7] See comment 226.42(c)(1)-4.

pal dwelling that does not meet or exceed a predetermined threshold; and
- Conditioning the compensation paid to a person who prepares a valuation on consummation of the covered transaction.[8]

The rule also prohibits persons preparing valuations from mischaracterizing the value of the property by either falsifying or materially misrepresenting or altering a valuation. A misrepresentation or alteration is material if it would have a significant effect on the value assigned to the property.[9]

To facilitate compliance, §226.42(c)(3) identifies six examples of permissible conduct that would not violate the prohibition on coercion and on mischaracterizing, misstating, or falsifying a valuation:

- Asking a person who prepares a valuation to consider additional, appropriate property information, such as information about comparable properties, to make or support a valuation;
- Asking a person who has prepared a valuation to provide further detail, substantiation, or explanation for the value assigned;
- Asking a person who prepared a valuation to correct errors in the valuation;
- Obtaining multiple valuations for the consumer's principal dwelling to select the most reliable valuation;
- Withholding compensation because a person conducting a valuation breached contractual duties in providing the valuation or provided substandard services; and
- Taking action permitted or required by applicable federal or state statute, regulation, or agency guidance.

§226.42(d): Prohibited Conflicts of Interest in Preparing a Valuation

The final rule also prohibits conflicts of interest for appraisers to ensure that the integrity of a valuation is not compromised. To address this concern, the rule prohibits a person from preparing a valuation for a covered transaction in which he has a direct or indirect interest, financial or otherwise, in the property or transaction.[10]

Because some creditors employ staff members to perform valuations, the rule specifically addresses the circumstances in which employees of creditors and affiliates of creditors, as well as providers of multiple settlement services, can perform valuations without violating the conflict of interest prohibition. The conflict rules are designed to establish a firewall between the loan production department ordering the valuation and the valuation department. Because it is often not feasible to separate these functions in small financial institutions, the regulation creates two sets of firewall requirements: one for institutions with assets of $250 million or less, and one for institutions with assets greater than $250 million.

Conflict Rules for Institutions with Assets of $250 Million or Less. To qualify for the safe harbor for small institutions, a creditor must have assets of $250 million or less as of December 31 in both of the past two calendar years. An employee or affiliate of a creditor can perform a valuation provided the following conditions are satisfied:

- The compensation of the person preparing the valuation is not based on the value arrived at for the valuation; and
- The employee, officer, or director who orders, performs, or reviews the valuation must abstain from any decision to approve, deny, or set the terms of the transaction.

Conflict Rules for Institutions with Assets Greater Than $250 Million. The safe harbor rules are slightly different for institutions with assets greater than $250 million for either of the past two calendar years. For these institutions, an employee or affiliate can perform a valuation provided the following conditions are met:

- The compensation of the person performing the valuation is not based on the value arrived at in a valuation;
- The person performing the valuation or performing valuation management functions is not part of the creditor's loan production function and does not report to a person whose compensation is based on the closing of the transaction for which the valuation is prepared; and

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[8] See 12 C.F.R. §226.42(c)(1)(i).

[9] See 12 C.F.R. §226.42(c)(2).

[10] See 12 C.F.R. §226.42(d)(1).

- An employee, officer, or director in the creditor's loan function is not involved, directly or indirectly, in selecting, influencing, retaining, or recommending the person performing the valuation.

Conflict Rules for Providers of Multiple Settlement Services. The interim final rule also has a safe harbor for settlement service providers that prepare valuations or perform valuation management functions in addition to performing another settlement service for the transaction.[11] For these providers, the conflict rules described above for employees or affiliates of creditors apply as follows: (1) if the creditor has assets of $250 million or less, the employee/affiliate conflict rules for creditors with assets equal to or less than $250 million apply; (2) otherwise, the employee/affiliate conflict rules for creditors with assets greater than $250 million apply.

Management Valuation Functions. It is important to note that the rule's prohibitions on coercion and conflicts of interest discussed above apply not only to valuations but also to "management valuation functions." Section 226.42(b)(4)(iv) defines this term to include recruiting or employing a person to prepare a valuation, managing the process of preparing a valuation, and reviewing the work of a person who prepares valuations. For example, some financial institutions employ staff to review valuations to ensure they accurately reflect the value of the property.

§226.42(e): Credit Extension Prohibited

The interim final rule also prohibits creditors from extending credit when they know that one of the valuation requirements in §226.42(c) or (d) has been violated. However, the rule contains an exception if the creditor acts with due diligence to determine that the violation does not materially misrepresent or misstate the value of the consumer's principal dwelling. A valuation materially misrepresents or misstates the value of the dwelling if the misstatement or misrepresentation affects the credit decision or the terms on which the credit is extended.

§226.42(f): Customary and Reasonable Compensation

Another requirement of the interim final rule is that the compensation that creditors and their agents provide to a fee appraiser must be "customary and reasonable." "Fee appraiser" is defined as either (1) a state-licensed or certified natural person performing appraisal services for a fee but is not an employee of the person engaging the appraiser; or (2) an organization that in the ordinary course of business employs state-licensed or certified appraisers and receives a fee for performing appraisals.[12]

To facilitate compliance, the rule includes two presumptions of compliance for the customary and reasonable compensation requirement. First, a creditor and its agent are presumed to comply with the rule if the fee paid to the appraiser is reasonably related to the recent rates paid for appraisal services in the relevant geographic market, and the creditor or agent has adjusted the recent rate after taking into account specified factors, such as the type of property, the scope of work, and the appraiser's qualifications and experience. To qualify for this presumption, the creditor must not have engaged in any anti-competitive actions in violation of state or federal law that affect the appraisal fee, such as price fixing or restricting others from entering the market. See comments 226.42(f)(2)(i)-1, -2, -3 and 226.42(f)(2)(ii)-1, -2.

Second, a creditor and its agent are also presumed to comply with the interim final rule if they determine the fee by relying on third-party information, such as a government agency fee schedule, an academic study, or an independent private-sector survey. Consistent with the Dodd-Frank Act's requirements, third-party surveys and similar studies must not include fees paid to appraisers by appraisal management companies. See comments 226.42(f)(3)-1, -2, -3.

Volume discounts are permitted, as long as the compensation is customary and reasonable. Comment 226.42(f)(1)-5 provides this example of permissible

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[11] For this discussion, "settlement service" has the same meaning as that used in RESPA, namely, services provided "in connection with a real estate settlement including, but not limited to, the following: title searches, title examinations, the provision of title certificates, title insurance, services rendered by an attorney, the preparation of documents, property surveys, the rendering of credit reports or appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, the 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 loans), and the handling of the processing, and closing or settlement" 12 U.S.C. §2602(3).

[12] The organization must also not be subject to the appraisal management company registration requirements under the Financial Reform, Recovery, and Enforcement Act of 1989 (12 U.S.C. §331 *et seq.*), as amended by section 1473(f)(2) of the Dodd-Frank Act.

The New Dollar Threshold for Regulation Z Coverage

By Laura Gleason, Senior Consumer Regulations Analyst, Federal Reserve Bank of Philadelphia

Congress enacted the Truth in Lending Act (TILA) in 1968 "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices."[1] In 1969, a non-dwelling-secured consumer credit transaction[2] was subject to TILA and Regulation Z, TILA's implementing regulation, if the transaction: a) had an amount financed in the amount of $25,000 or less, in the case of closed-end credit; or b) had a written credit limit of $25,000 or less, in the case of open-end credit. When the $25,000 threshold was set, a new Corvette sold for under $5,000. But today, 43 years later, the average selling price of a new car exceeds the threshold by nearly $5,000.[3]

Although consumer credit transactions in any amount that are secured by the consumer's dwelling have been subject to Regulation Z since 1969 and, more recently, private education loans (PELs) have been covered regardless of loan amount,[4] Congress recognized that it was time to update TILA's threshold for the remaining categories of consumer credit. Under §1100E of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act),[5] the dollar threshold value for TILA coverage was increased from $25,000 to $50,000, effective July 21, 2011. On April 4, 2011, the Board of Governors of the Federal Reserve System (Board) issued a final rule amending Regulation Z to implement §1100E.[6] This article reviews the requirements of the final rule.

THE NEW THRESHOLD RULE

A key distinction between the old threshold rule and the new one is that the old threshold for closed-end credit was based on the value of the amount financed, while the new rule is based on the amount of credit extended. To illustrate this difference, assume under the original threshold of $25,000 that the consumer obtains a car loan in the amount of $25,050. Assume further that the consumer must separately pay a $75 credit report fee. The amount financed under those conditions would be $24,975, and the loan would be subject to Regulation Z because the amount financed does not exceed $25,000. Now, assume under the new $50,000 threshold that a consumer obtains a car loan in the amount of $50,050 and pays the same $75 credit report fee. Although the amount financed is $49,975, the loan would not be subject to Regulation Z because the amount of credit extended exceeds $50,000.

Second, the rule requires the threshold to be adjusted for inflation on January 1 of each year. The threshold amount will increase (rounded to the nearest $100 increment) by any annual percentage increase in the consumer price index for urban wage earners and clerical workers (CPI-W), as published by the Bureau of Labor Statistics for June 1 of the prior year. The threshold will not decrease if the index value decreases. The applicable threshold will be $50,000 until December 31, 2011. The Board recently announced the first CPI-W adjustment to $51,800 effective January 1 through December 31, 2012.[7]

The remainder of this article discusses the threshold changes in more detail.

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[1] Section 102(a) of TILA, 15 U.S.C. §1601(a)

[2] "Consumer transaction" in this article means credit extended by a creditor to a consumer for a consumer purpose, as these terms are defined in §226.2(a).

[3] The National Association of Automobile Dealers reports that the average selling price of a new car in 2010 was $29,793. See http://bit.ly/car-price, p. 3.

[4] The Board amended Regulation Z effective February 14, 2010 to add new requirements for PELs, as defined in §226.46(b)(5). PELs are subject to Regulation Z regardless of the loan amount. See §226.3(b)(1)(i)(B).

[5] Public Law 111-203, 124 Stat. 1376, 2111 (July 21, 2010)

[6] 76 Fed. Reg. 18,354 (April 4, 2011). The Board's announcement and the *Federal Register* notice are available at: http://1.usa.gov/Threshold-change.

OPEN-END CREDIT

For open-end credit extensions, the final rule offers two methods for determining if an account is exempt under the revised threshold. The first method determines exemption based on the credit limit at the time the account is opened. The second method determines exemption based on the amount of the initial advance. If the account qualifies under either method, it is exempt, although an account can lose its exempt status in certain circumstances based on subsequent events.

Credit Limit

The Official Staff Commentary (Commentary) for Regulation Z states that an open-end account is exempt from Regulation Z if "the creditor makes a firm written commitment at account opening to extend a total amount of credit in excess of the threshold amount in effect at the time the account is opened with no requirement of additional credit information for any advances on the account (except as permitted from time to time with respect to open-end accounts pursuant to §226.2(a)(20))."[8]

The account balance under such a credit limit does not have to exceed the applicable threshold amount to remain exempt from Regulation Z. As long as the credit limit at account opening exceeds the threshold and is not secured by real or personal property used or expected to be used as the consumer's principal dwelling, the account is exempt from Regulation Z, even if the threshold is later increased because of changes in the CPI-W. For example, if a credit card was issued on January 2, 2012 with a $55,000 credit limit, and the consumer's balance on the first periodic statement was $10,000, the account is exempt. If the threshold was later increased to $60,000, the account would remain exempt because the credit limit at account opening exceeded the threshold then in effect. However, if the creditor later reduces the credit limit below the threshold then in effect (for example, in response to negative information obtained from a consumer reporting agency during an account review), the exemption no longer applies unless the account is exempt based on the amount of the initial credit extension, as discussed below.

Conversely, if the credit limit at account opening does not exceed the applicable threshold amount, the account is subject to Regulation Z, even if the account balance exceeds the applicable threshold at a later date unless the initial extension of credit exceeds the applicable threshold. For example, on January 1, the applicable threshold is $50,000, and an account is opened on March 1 with a credit limit of $45,000. The initial extension of credit on April 1 is $10,000, and the balance on July 1 is $52,000 because the creditor permitted the debtor to make additional transactions in excess of the credit limit. The account is not exempt.

Initial Credit Extension

The second method for qualifying for the exemption is based on the initial extension of credit. Even if the credit limit at account opening does not exceed the applicable threshold, an account can still be exempt from Regulation Z if the initial credit extension exceeds the applicable threshold. Comment 226.3(b)-2.i.A.1 of the Commentary provides this example: "Assume that the threshold amount in effect on January 1 is $50,000. On February 1, an account is opened but the creditor does not make an initial extension of credit at that time. On July 1, the creditor makes an initial extension of credit of $60,000. In this circumstance, no requirements of this Part apply to the account."

But if the creditor makes an initial extension of credit that does not exceed the threshold amount in effect, the account is not exempt, and the creditor must have satisfied the requirements of Regulation Z from the date the account was opened. Comment 226.3(b)-2.i.A.2 provides this example: "Assume that the threshold amount in effect on January 1 is $50,000. On February 1, an account is opened but the creditor does not make an initial extension of credit at that time. On July 1, the creditor makes an initial extension of credit of $50,000 or less. In this circumstance, the account is not exempt and the creditor must have satisfied all of the applicable requirements of this Part from the date the account was opened (or earlier, if applicable)."

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[7] The Board's announcement and the *Federal Register* notice are available at: http://1.usa.gov/2012-threshold.

[8] Comment 226.3(b)-2.i.B

News from Washington: Regulatory Updates

The Consumer Financial Protection Bureau (CFPB) publishes a final list of rules it will be enforcing. On July 21, 2011, the CFPB issued a final list of rules it will enforce against the institutions under its supervision. The CFPB's enforcement authority is defined by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and other applicable laws. Accordingly, the published list has no substantive effect and merely provides a convenient reference source. The list of rules includes the Equal Credit Opportunity Act (Regulation B), the Home Mortgage Disclosure Act (Regulation C), the Electronic Fund Transfer Act (Regulation E), Registration of Residential Mortgage Loan Originators (Regulation H, Subpart I), the Consumer Leasing Act (Regulation M), Privacy of Consumer Financial Information (Regulation P), the Fair Credit Reporting Act (Regulation V) (subject to certain exceptions), the Truth in Lending Act (TILA) (Regulation Z), and the Truth in Savings Act (Regulation DD). The *Federal Register* notice is available at: http://www.gpo.gov/fdsys/pkg/FR-2011-07-21/pdf/2011-18426.pdf.

The Board of Governors of the Federal Reserve System (Board) releases report on college credit card agreements. On July 8, 2011, the Board issued its second annual report on College Credit Card Agreements pursuant to the Credit Card Accountability Responsibility and Disclosure Act. The report covers all 1,004 credit card agreements in effect in 2010 between issuers and institutions of higher education and related entities, such as alumni groups. It includes such data as yearly payments by the issuers to the institutions and changes in the number of accounts compared to the first annual report in 2009. The Board's announcement and the report are available at: http://www.federalreserve.gov/newsevents/press/bcreg/20110707a.htm.

Credit score disclosure requirements for risk-based pricing and adverse action notices. On July 7, 2011, the Board and the Federal Trade Commission (FTC) announced the implementing regulations for the credit score disclosure requirements mandated by §1100F of the Dodd-Frank Act. Under the final rule, when lenders issue risk-based pricing or adverse action notices under the Fair Credit Reporting Act, they must disclose the consumer's credit score if the score was used in making the determination that led to the issuance of the notice. *Outlook* reviews the requirements in detail in "An Overview of the Credit Score Disclosure Requirements for Risk-Based Pricing Notices" on page one of this issue. The Board and the FTC's joint announcement and the *Federal Register* notice are available on the Board's website at: http://www.federalreserve.gov/newsevents/press/bcreg/20110706a.htm.

Banking agencies publish host state loan-to-deposit ratios. On June 30, 2011, the Board, the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) (agencies) made public the updated host state loan-to-deposit ratios that the agencies use for verifying compliance with §109 of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 during a bank's Community Reinvestment Act (CRA) examination. The agencies' announcement is available at: http://www.federalreserve.gov/newsevents/press/bcreg/20110630a.htm.

The Board announces debit card interchange fee standards. On June 29, 2011, the Board announced a final rule establishing standards for debit card interchange fees, as required by §1075 of the Dodd-Frank Act. These provisions are effective October 1, 2011. Debit card interchange fees are received by the card-issuing bank whenever a debit card it issues is used in a transaction. Under the final rule, the maximum permissible interchange fee that an issuer may receive for an electronic debit transaction will be the sum of 21 cents per transaction and 5 basis points multiplied by the value of the transaction. The Board also approved an interim final rule that allows for an upward adjustment of no more than 1 cent to an issuer's debit card interchange fee if the issuer develops and implements policies and procedures reasonably designed to achieve the fraud-prevention standards set out in the interim final rule. When the adjustment is combined with the maximum permissible interchange fee under the interchange fee standards, a covered issuer eligible for the fraud-prevention adjustment could receive an interchange fee of up to approximately 24 cents for the average debit card transaction, which is valued at $38. Card issuers that, with their affiliates, have assets under $10 billion are exempt from the fee standards. The final rule also prohibits issuers and networks from limiting the number of networks that can process their debit transactions to less than two unaffiliated networks. Issuers and networks are also prohibited from inhibiting merchants' ability to choose among those different debit processing networks. The Board's announcement and the *Federal Register* notices for the final rule and the interim final rule are available at: http://www.federalreserve.gov/newsevents/press/bcreg/20110629a.htm.

The CFPB solicits comments on the size and scope of covered nonbank institutions. The Dodd-Frank Act requires the CFPB to implement a risk-based supervision program for nondepository financial services firms in the residential mortgage, private education lending, and payday lending markets. The CFPB must also implement a supervision program for nondepositories that are a "larger participant" in a market for other consumer financial products or services as defined by the rule. On June 29, 2011, the CFPB published a request for comments on which other nonbank markets the CFPB should regulate and how larger participants should be defined. The CFPB is required to issue a rule defining larger participants by July 21, 2012. The request for comment included six markets in the initial rule: debt collection, consumer reporting, consumer credit and related activities, money transmitting and related activities, prepaid cards, and debt relief services. Comments were due by August 15, 2011. The CFPB's announcement and the *Federal Register* notice are available at: http://1.usa.gov/larger-participant.

The CFPB seeks comments on draft Good Faith Estimate (GFE) and TILA combined disclosure form. Section 1032(f) of the Dodd-Frank Act requires the CFPB to combine the GFE and TILA early disclosures into one form. Currently, consumers receive a two-page TILA form and a three-page GFE. On May 18, 2011, the CFPB published two draft combined forms for comment. The forms received over 13,000 comments, and on June 27, 2011, the CFPB issued two proposed revised forms and solicited further comment, particularly as to the disclosure of closing costs. The CFPB's announcement is available at: http://www.consumerfinance.gov/know-before-you-owe-were-back/.

The Board adjusts HOEPA fee-based trigger for high-cost loans to $611. On June 13, 2011, the Board announced its annual adjustment to the dollar amount of fees that trigger additional disclosure requirements and restrictions under Regulation Z and the Home Ownership and Equity Protection Act for certain "high-cost" home mortgage loans. The dollar amount of the fee-based trigger has been adjusted to $611, effective January 1, 2012. The Board's announcement and *Federal Register* notice are available at: http://www.federalreserve.gov/newsevents/press/bcreg/20110613c.htm.

Regulators issue list of nonmetropolitan distressed or underserved middle-income geographies. On June 1, 2011, the Board, the FDIC, the OCC, and the Office of Thrift Supervision issued their annual list of nonmetropolitan distressed or underserved areas. These areas will qualify for community development designation under the CRA. The 2011 list (and lists from previous years) can be found on the Federal Financial Institutions Examination Council's website at: http://www.ffiec.gov/cra/examinations.htm.

The Board issues proposed rule on remittance transfer protections. On May 23, 2011, the Board issued a proposal to implement protections for consumers who send remittance transfers to recipients in a foreign country, as required by §1073 of the Dodd-Frank Act. The proposed rules would require a written pre-transfer disclosure stating the fees and taxes and the amount to be received by the recipient and the sender's error resolution rights. A provider of remittance services would also have to disclose the exchange rate except under certain circumstances, such as when the government in the recipient country sets the exchange rate or the rate is required to be set only after the funds are retrieved in the recipient country. Final rules, which are required by January 21, 2012, will be issued by the CFPB. The Board's announcement and the *Federal Register* notice are available at: http://www.federalreserve.gov/newsevents/press/bcreg/20110512a.htm.

On the Docket: Recent Federal Court Opinions*

REGULATION X - REAL ESTATE SETTLEMENT PROCEDURES ACT (RESPA)

The U.S. Supreme Court will decide RESPA standing issue for statutory damages. *First American Financial Corp. v. Edwards*, 131 S.Ct. 3022 (2011). The U.S. Supreme Court agreed to review a Ninth Circuit decision, *Edwards v. First American Corp*, 610 F.3d 514 (9th Cir. 2010), to determine whether a homeowner alleging a violation of the Real Estate Settlement Procedures Act's (RESPA) anti-kickback provision has standing to sue if the consumer was not overcharged. The plaintiff used Tower City Title Agency (Tower) as her settlement agent, which referred her to First American Title Insurance for title insurance. The plaintiff alleged that First American violated §8 of RESPA by entering into an exclusivity agreement with Tower, under which Tower would refer all title business to First American in exchange for a kickback. The defendants moved to dismiss the case for a lack of standing because the plaintiff sought only statutory damages for the title company's violation but did not allege she was overcharged, as Ohio law requires all title insurers to charge the same price. The Ninth Circuit held that the standing requirement was satisfied because Congress provided a right of action for violations of the referral provisions, including statutory damages, even if the plaintiff was not overcharged. The court cited recent decisions from the Third and Sixth Circuits that reached the same conclusion. See *Carter v. Welles-Bowen Realty, Inc.,* 553 F.3d 979, 989 (6th Cir. 2009) and *Alston v. Countrywide Financial Corp.,* 585 F.3d 753, 755 (3d Cir. 2009). The Supreme Court's opinion in this matter could have wide-ranging implications because many consumer protection laws provide statutory damages for violations, including RESPA, the Truth in Lending Act, the Fair Credit Reporting Act, and the Electronic Fund Transfer Act. The case is scheduled to be decided in the court's 2011 term, which ends in June 2012.

Affiliated business arrangements violate RESPA unless they meet three conditions. *Minter v. Wells Fargo Bank,* N.A., 274 F.R.D. 525 (D. Md. 2011). Consumers filed suit alleging that Wells Fargo Bank and Long & Foster Real Estate, Inc., along with their joint venture mortgage lender Prosperity Mortgage Company, violated §8 of RESPA, which prohibits the receipt of unearned fees and referral fees. However, §8(c)(4) expressly states that RESPA does not prohibit affiliated business arrangements when the affiliation and related charges are disclosed, the borrower is not required to use the affiliate's services, and there are no prohibited payments between the affiliates. The defendants argued that even if the joint venture did not meet these conditions, it did not necessarily violate the §8 prohibition on unearned fees and referral fees. The court disagreed, holding that to comply with §8 of RESPA, affiliated business arrangements must (1) involve a "bona fide provider of settlement services" and (2) conform to the three conditions in §8(c)(4).

PREEMPTION

Federal Arbitration Act preempts state law restrictions on certain arbitration clauses. *AT&T Mobility LLC v. Concepcion,* 131 S.Ct. 1740 (2011). In a significant ruling, the Supreme Court held that the Federal Arbitration Act (FAA) prevents a state court from invalidating contract clauses that waive a consumer's right to participate in classwide arbitration proceedings. The plaintiffs sued AT&T for advertising its phones as free with the purchase of telephone service, even though it charged $30.22 in sales tax on the phone. The parties' contract mandated that any disputes would be resolved by individual arbitration, precluding both court litigation and classwide arbitration. The Ninth Circuit found the contract's arbitration provision unconscionable and invalid under California law as formulated in *Discover Bank v. Superior Court*, 36 Cal. 4th 148, 113 P. 3d 1100 (2005). The Supreme Court reversed the Ninth Circuit's ruling, holding that California law as interpreted by the court in *Discover Bank* is preempted by the FAA, which supports the enforceability of arbitration clauses. The Supreme Court determined that "[r]equiring the availability of classwide arbitration interferes with fundamental attributes of arbitration and thus creates a scheme inconsistent with the FAA."

The *Concepcion* case is likely not the final word on the use of mandatory arbitration clauses in the consumer financial services industry. Under §1028 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), the Consumer Financial Protection Bureau (CFPB) is required to conduct a study of the effect of mandatory arbitration clauses on consumers and provide a report to Congress. If supported by the results of the study, the CFPB may prohibit or restrict mandatory arbitration clauses to protect consumers. In addition, §1414(e)(1) of the Dodd-Frank Act prohibits the use of mandatory arbitration clauses in open- and closed-end consumer credit transactions secured by a consumer's principal dwelling.

State statute banning check-cashing fee is preempted by National Bank Act (NBA). *Baptista v. JPMorgan Chase Bank, N.A.,* 640 F.3d 1194 (11th Cir. 2011). The plaintiff's class-action lawsuit alleged that JPMorgan Chase violated a Florida state statute by charging a check-cashing fee. Chase argued that the plaintiff's claims were preempted by the NBA. The Dodd-Frank Act amended the NBA to state that "State consumer financial laws are preempted, only if …the State consumer financial law prevents or significantly interferes with the exercise by the national bank of its powers." The Eleventh Circuit interpreted this language to mean that a state law is preempted only when it presents a significant conflict with federal law. Applying this standard, the court concluded that a Florida ban on check-cashing fees significantly conflicts with a regulation of the Office of the Comptroller of the Currency (OCC), 12 C.F.R. §7.4002(a), which provides that a national bank may "charge its customers non-interest charges and fees, including deposit account service charges," and defines a customer to include "any person who presents a check for payment." Because Congress intended the OCC to have the power to regulate banking and the OCC regulation specifically authorizes a practice banned by the state statute, the court held that the state statute is preempted.

FAIR HOUSING ACT

Disparate impact claim examined. *Greater New Orleans Fair Housing Action Center v. U.S. Department of Housing & Urban Development*, 639 F.3d 1078 (D.C. Cir. 2011). The Court of Appeals for the District of Columbia Circuit reversed a trial court decision granting injunctive relief to plaintiffs on their disparate impact claim. African-American homeowners and two fair housing organizations filed a lawsuit alleging that Louisiana's Office of Community Development (OCD), a state agency, violated the Fair Housing Act because its formula for awarding grants provided by Congress to rebuild homes damaged or destroyed by Hurricanes Katrina and Rita had a disparate impact on African-American homeowners. HUD was also sued because it approved the grants and the formula used in awarding them. The amount of the state agency's grant was based on the lesser of the home's pre-hurricane value and the cost to rebuild or repair the home. The plaintiffs argued this formula had a disparate impact because African-American homeowners are likely to live in neighborhoods with lower property values than in predominantly white neighborhoods. To prove disparate impact, a plaintiff must show "proof of disproportionate impact, measured in some plausible way," which usually requires a plaintiff to "demonstrate with statistical evidence that the practice or policy has an adverse effect on the protected group." The plaintiffs' claim relied on a study showing a "resource gap" between white and African-American grant recipients, based on the difference between total resources available to homeowners for rebuilding and the cost of rebuilding. The court found that the "resource gap" was an inappropriate benchmark for measuring the effect of the grant formula and that a more appropriate benchmark, such as the total value of OCD grants, showed African-American homeowners received more funding than white homeowners. The court reversed the trial court's injunction and remanded the case for further proceedings.

REGULATION Z - TRUTH IN LENDING ACT (TILA)

Effect of technical violations on right of rescission. *In re: Fuller,* 642 F.3d 240 (1st Cir. 2011). After Deutsche Bank initiated foreclosure proceedings on the plaintiffs' residence, plaintiffs sued to rescind their mortgage transaction under a Massachusetts state law similar to TILA. The plaintiffs argued that the lender incorrectly identified the loan closing date in the rescission notice and failed to identify the date by which they would be allowed to rescind the mortgage. The First Circuit, relying on its prior cases, reiterated that "technical deficiencies do not matter if the borrower receives a notice that effectively gives him notice as to the final date for rescission and has the three full days to act." The court noted that the plaintiffs signed the right to cancel forms and dated them August 12, 2003, and thus knew the correct closing date. Further, the rescission notice disclosed their right to cancel within three business days of the date of the transaction. The court therefore determined that the plaintiffs received adequate notice of their right to cancel. This case reflects a continued split between the First and Seventh Circuits about the effect of technical violations on the right of rescission. In the Seventh Circuit, technical violations of the rescission requirements can trigger the three-year rescission period.

* Links to the court opinions are available in the online version of *Outlook* at: http://www.consumercomplianceoutlook.org.

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An Overview of the Credit Score Disclosure Requirements for Risk-Based Pricing Notices

a credit score on a risk-based pricing notice when the score of the consumer to whom the creditor extends credit or whose extension of credit is under review is used in setting the material terms of credit.[5] The use of the credit score does not have to be the sole or primary factor in setting the terms of credit to be subject to the disclosure requirement — it need only be a factor. If the creditor did not use a credit score at all in setting the material credit terms, the creditor is not required to disclose the consumer's credit score or information relating to a credit score.[6]

What Information Must Be Disclosed?

In addition to the information required by the January 2010 Final Rules, the following information generally must be disclosed on risk-based pricing notices if a credit score is used in setting the material terms of credit:

- A statement that a credit score is a number that takes into account information in a consumer report, that the consumer's credit score was used to set the terms of credit offered, and that a credit score can change over time to reflect changes in the consumer's credit history;
- The credit score used by the creditor in making the credit decision;
- The range of possible credit scores under the model used to generate the credit score;
- The key factors that adversely affected the credit score (discussed below);
- The date on which the credit score was created; and
- The name of the consumer reporting agency or other person that provided the credit score.[7]

Creditors generally must disclose no more than four key factors. However, if one key factor is the number of inquiries made with respect to the consumer report, this factor must be disclosed and may constitute a fifth factor. If a creditor is using a credit score purchased from a consumer reporting agency, the consumer reporting agency is in the best position to identify the key factors that affected the score. Thus, the creditor could rely on the information from the consumer reporting agency in its disclosure to consumers.

How Many Credit Scores Must Be Disclosed?

When a creditor uses multiple credit scores in setting the terms of credit, the creditor must disclose any one of those scores. Alternatively, the creditor, at its option, may disclose multiple scores used in setting the material terms of credit. If a creditor obtained multiple credit scores but used only one score, only that score must be disclosed. For example, if the creditor regularly requests scores from several consumer reporting agencies and uses only the lowest score, then the lowest score must be disclosed.

What Types of Credit Scores Must Be Disclosed?

A creditor must disclose "the credit score used by the person in making the credit decision" on a risk-based pricing notice.[8] "Credit score" has the same meaning used in §609(f)(2)(a) of the FCRA.

Most credit scores that meet the FCRA definition are scores that creditors obtain from consumer reporting agencies. The FCRA credit score definition specifically excludes some — but not all — proprietary scores. The definition of credit score does not include any mortgage score or rating of an automated underwriting system that considers one or more factors in addition to credit information, including the loan-to-value ratio, the amount of down payment, or the financial assets of a consumer. Thus, if a creditor uses a proprietary score that is based on one or more of these fac-

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[5] 12 C.F.R. §222.73(a)(1)(ix) (risk-based pricing); 12 C.F.R. §222.73(a)(2)(ix) (account review)

[6] 76 Fed. Reg. at 41,606

[7] 12 C.F.R. §222.73(a)(1)(ix) (risk-based pricing notice); 12 C.F.R. §222.73(a)(2)(ix) (account review notice)

[8] 12 C.F.R. §222.73(a)(1)(ix)(B) (risk-based pricing notice); 12 C.F.R. §222.73(a)(2)(ix)(B) (account review notice)

tors in addition to information obtained from a consumer reporting agency, this proprietary score is not a credit score and thus does not need to be disclosed to the consumer. In contrast, if a creditor uses a proprietary score that only includes information acquired from a consumer reporting agency in setting the material terms of credit or reviewing the account, the proprietary score would be a credit score for purposes of the FCRA and would be required to be disclosed to the consumer.

If a creditor uses both a proprietary score that does not meet the definition of a credit score and a credit score from a consumer reporting agency in setting the material terms of credit or reviewing the account, the creditor would disclose the credit score from the consumer reporting agency. Similarly, if a creditor uses a credit score from a consumer reporting agency as an input to a proprietary score, but that proprietary score itself is not a credit score, the creditor would disclose the credit score from the consumer reporting agency.[9]

No Credit Score. In some cases, a creditor that provides risk-based pricing notices to consumers may try to obtain a credit score for an applicant, but the applicant may have insufficient credit history for the consumer reporting agency to generate a credit score. In these instances, the creditor cannot and is not required to disclose credit score information if an applicant has no credit score.[10]

Multiple Consumers. In some cases, a creditor may use the credit score of a guarantor or co-signer, but not the credit score of the consumer to whom it extends credit or whose extension of credit is under review. A creditor may be required to provide a risk-based pricing notice to the consumer to whom it extends credit or whose application is under review but is not required to provide a risk-based pricing notice to the guarantor or co-signer. When a creditor uses the credit score only of a guarantor or co-signer to set the terms of credit for the consumer to whom it extends credit or whose extension of credit is under review, a person shall not include a credit score in the general risk-based pricing notice or account review notice provided to the consumer.[11]

In a transaction involving two or more borrowers, a creditor must provide a general risk-based pricing notice or an account review notice to all of the co-borrowers and not only to the borrower whose credit score was used in setting the material terms of credit.[12] Whether the consumers have the same address or not, a creditor must provide a separate notice to each consumer if a notice includes a credit score(s). Each separate notice that includes a credit score(s) must contain only the credit score(s) of the consumer to whom the notice is provided and not the credit score(s) of the other consumer. If the consumers have the same address and the notice does not include a credit score(s), a creditor may provide a single notice addressed to both consumers.[13]

WHEN A CREDITOR USES MULTIPLE CREDIT SCORES IN SETTING THE TERMS OF CREDIT, THE CREDITOR MUST DISCLOSE ANY ONE OF THOSE SCORES. ALTERNATIVELY, THE CREDITOR, AT ITS OPTION, MAY DISCLOSE MULTIPLE SCORES USED IN SETTING THE MATERIAL TERMS OF CREDIT.

Risk-Based Pricing Model Forms

The Board and the FTC's joint rulemaking under the FCRA includes model forms for risk-based pricing notices that require credit score disclosures.[14] Model Form H-6 of the Board's rules and Model Form B-6 of the FTC's rules may be used when a creditor used a credit score in deciding upon an initial extension of credit. Model Form H-7 of the Board's rules and Model Form B-7 of the FTC's rules may be used when a creditor used a credit score during an account review.

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[9] 76 Fed. Reg. at 41,605

[10] 76 Fed. Reg. at 41,610

[11] 76 Fed. Reg. at 41,607

[12] 76 Fed. Reg. at 41,609

[13] 12 C.F.R. §222.75(c)(1)

[14] The risk-based pricing notice forms with credit score disclosures are available at: http://bit.ly/credit-score-forms.

Credit Score Disclosure Exception to Risk-Based Pricing Notice

The January 2010 Final Rules included a compliance option in which a creditor may choose to send a credit score exception notice to all credit applicants instead of providing a risk-based pricing notice to certain consumers. The agencies clarified in the July 2011 Final Rules that creditors may continue to provide credit score exception notices to all credit applicants in lieu of providing risk-based pricing notices to some consumers.[15]

Effective Date

The requirements for disclosing credit scores and related information under section 1100F of the Dodd-Frank Act became effective on July 21, 2011. The effective date for the regulations issued by the Board and the FTC was August 15, 2011.[16]

CONCLUSION

Creditors should ensure that their risk-based pricing notices comply with these new requirements. Specific issues and questions about consumer compliance matters should be raised with your primary regulator.

[15] 76 Fed. Reg. at 41,607-08

[16] 76 Fed. Reg. at 41,611

CONTINUED FROM PAGE 5...

The Federal Reserve Board's Interim Final Rule on Valuation Independence

compensation: "[A]ssume that a fee appraiser typically receives $300 for appraisals from creditors with whom it does business; the fee appraiser, however, agrees to reduce the fee to $280 for a particular creditor, in exchange for a minimum number of assignments from the creditor."

§226.42(g): Mandatory Reporting of Appraiser Misconduct

The final requirement of the rule is that if a covered person discovers that the Uniform Standards of Professional Appraisal Practice[13] or ethical or professional requirements for appraisers under applicable state or federal statutes or regulations have been violated, the person must refer the matter within a reasonable period of time to the appropriate state agency if the failure to comply is material. A violation is material if it is likely to significantly affect the value assigned to the consumer's principal dwelling.

Penalties

Section 129E(k) provides that violations of the valuation independence requirements are subject to both the regular civil remedies available to consumers in §130 for TILA violations, 15 U.S.C. §1640, as well as civil penalties. The civil penalties are $10,000 a day for each day a violation occurs for the first violation and $20,000 a day for subsequent violations. The federal agencies identified in §108 of TILA, 15 U.S.C. §1607, are charged with assessing the penalties.

PRUDENTIAL APPRAISAL REGULATIONS AND GUIDELINES

While the Board's new interim final rule applies to covered persons in covered transactions, the Federal Reserve and the other federal agencies that regulate financial institutions adopted prudential appraisal regulations for federally regulated institutions' real estate-related financial transactions in 1990.[14] Further-

[13] The USPAP are available at: http://www.uspap.org/toc.htm.

[14] OCC: 12 C.F.R. part 34, subpart C; FRB: 12 C.F.R. part 208, subpart E, and 12 C.F.R. part 225, subpart G; FDIC: 12 C.F.R. part 323; OTS: 12 C.F.R. part 564; and NCUA: 12 C.F.R. part 722

more, the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision issued *Interagency Appraisal and Evaluation Guidelines* in October 1994 to provide guidance on the agencies' expectations for a regulated institution's collateral valuation practices. More recently, in December 2010, the federal banking agencies and the National Credit Union Administration issued revised guidelines.[15] The revised guidelines describe the agencies' risk management expectations for an effective collateral valuation function, including appraisals, that an institution should have to support its credit underwriting process, for both consumer and commercial real estate lending activity. These revised guidelines also emphasize the importance of ensuring that the appraisal process operates independently from an institution's loan production function.

CONCLUSION

The Board's interim final rule on appraiser independence addresses many of the mortgage appraisal practices that may have contributed to the recent financial crisis. Implementing these rules will help maintain the integrity of dwelling-secured consumer credit transactions. Specific issues and questions about consumer compliance matters should be raised with your primary regulator.

[15] 75 Fed. Reg. 77,450 (Dec. 10, 2010). For Federal Reserve regulated institutions, refer to SR letter 10-16 for a copy of the guidelines.

Consumer Compliance Resources

Don't forget to visit the Consumer Compliance Resource page on our website: http://bit.ly/CCO_resource.

This page contains links to many helpful resources for compliance regulations and statutes.

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The New Dollar Threshold for Regulation Z Coverage

If an account exemption was based on an initial extension of credit that exceeded the applicable threshold at account opening, comment 226.3(b)-2.iii clarifies that the account will remain exempt from Regulation Z even under the following circumstances:

- The applicable threshold increases at a later date, even if the value of the subsequent threshold is greater than the amount of the initial extension of credit. For example, if the initial extension of credit at account opening was $52,000 and the applicable threshold at account opening was $50,000, the account is exempt from Regulation Z. If the applicable threshold increases the following year to $55,000, the account would still not be subject to Regulation Z.[9]
- There are no further extensions of credit.
- Subsequent extensions of credit are made but do not exceed the original threshold amount.
- The account balance is subsequently reduced below the original threshold amount.
- The account credit limit is subsequently reduced below the original applicable threshold limit.

Special Transition Rule for Accounts Exempt Before July 21, 2011

To facilitate the transition to the new threshold, the Board adopted a special transition rule for certain accounts that are currently exempt. If, on July 20, 2011, an open-end account is exempt from Regulation Z because of a firm commitment to extend more than $25,000 in credit,[10] the account will remain exempt until December 31, 2011. If that firm commitment is increased to at least $50,000 by December 31, the account will continue to be exempt. Otherwise, the exemption ends on January 1, 2012, and Regulation Z applies.

Subsequent Event: Addition of a Security Interest for Open-End Credit

An open-end account that is exempt from Regulation Z (for example, an account with a credit limit in excess of the threshold) would lose its exempt status if the creditor subsequently takes a security interest in real or personal property used or expected to be used as the consumer's principal dwelling. Furthermore, if the security interest is in the consumer's principal dwelling, the creditor must give the consumer the right to rescind the security interest consistent with §226.15.

If an exempt account becomes a covered account, the creditor must begin complying with all applicable provisions of Regulation Z within a reasonable period of time, including providing initial disclosures under §226.6 and periodic statements under §226.7.[11]

When Exempt Accounts Become Nonexempt

If an open-end account that initially qualified for the exemption no longer qualifies, the creditor must begin to comply with the applicable Regulation Z requirements "within a reasonable period of time."[12] The regulation's requirements apply to the existing balance on the account. However, the creditor need not comply with the regulation for the period of time when the account was exempt. For example, the Commentary specifies that the creditor must disclose new fees or charges but need not retroactively disclose fees or charges incurred while the account was exempt.

CLOSED-END CREDIT

The final rule states that a closed-end loan that is not 1) secured by real property, or 2) secured by personal property that serves as the consumer's principal dwelling, or 3) a private education loan under §226.46(b)(5)

continued

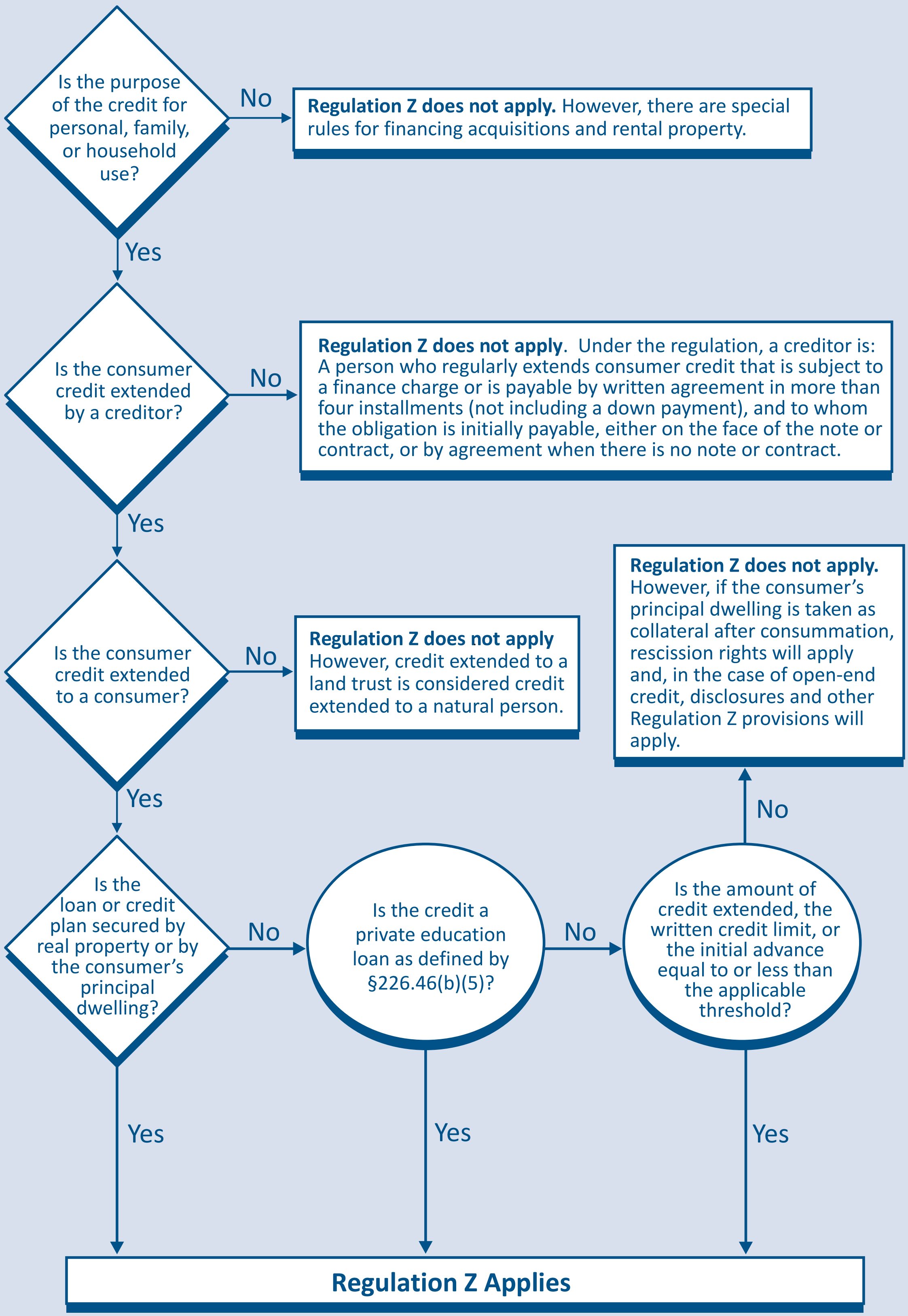
[9] Conversely, if the first advance *does not exceed* the applicable threshold in effect at the time of the extension (assume a $49,000 initial extension of credit and a $50,000 applicable threshold at account opening), the account is and remains subject to Regulation Z, even if the account balance later exceeds the original or any subsequent threshold amount. (This rule assumes that there is no firm commitment by the creditor to extend credit, other than the initial advance, in excess of the applicable threshold in effect at the time the account is opened.)

[10] Under current rules, an initial extension of credit in excess of $25,000 or an express written commitment to extend credit in excess of $25,000 would exempt the account from coverage.

[11] 76 Fed. Reg. at 18,364; comment 226.3(b)-4 (citing 3(b)-2.ii)

[12] Comment 226.3(b)-2.ii

Regulation Z - Coverage



is exempt from Regulation Z if either of the following conditions is met:

- The loan amount at consummation exceeds the applicable threshold at consummation.
- The creditor commits at consummation to extend a total amount of credit that will exceed the threshold in effect at consummation (e.g., in connection with a multiple advance construction loan).

The closed-end loan will remain exempt even if the loan balance drops below the applicable threshold or the total amount of credit extended under the commitment does not exceed the applicable threshold amount. The loan also remains exempt if the threshold amount increases at a later date.

Refinancings

A new loan that replaces an existing loan (e.g., a refinancing under §226.20(a)) must be evaluated on its own terms. Although the existing loan may be exempt, if the new loan does not itself meet exemption requirements, it is subject to Regulation Z.

For example, if the threshold at consummation of the existing loan was $50,000 and the existing loan amount was $52,000 at consummation, the existing loan is exempt from Regulation Z. Assume that in five years the loan balance is $40,000. The loan is still exempt from Regulation Z, even though the balance is below the original or any subsequent threshold. But if there is a refinancing with the existing loan balance of $40,000 paid in full and replaced by a new loan below the threshold (e.g., in the amount of $40,000), the new loan is subject to Regulation Z. Note that since applicable thresholds may increase but not decrease under the rule, the applicable threshold will never be less than $50,000.

Subsequent Event: Addition of a Security Interest for Closed-End Credit

In contrast to the requirements for open-end credit, an exempt closed-end loan does not lose its exempt status if the creditor subsequently takes a security interest in real or personal property used or expected to be used as the consumer's principal dwelling. However, since the addition of a security interest in the consumer's principal dwelling is considered a transaction for rescission purposes under §226.23, the creditor must provide the consumer with a notice of the right to rescind the security interest consistent with that section, just as it must with open-end credit under §226.15. But the right of rescission applies only to the added security interest, not the original obligation. Consequently, the creditor only has to provide the rescission notice under §226.23(b) and not new material disclosures. The rescission period starts to run from the delivery of the notice.[13] Also, if the addition of the security interest in the consumer's principal dwelling involved a refinancing, the closed-end loan itself would also be subject to Regulation Z, regardless of the value of the applicable threshold at the time of refinancing.

CONCLUSION

The Dodd-Frank Act updated the exemption threshold for TILA coverage from its 1960s level of $25,000 to $50,000 effective July 21, 2011 and included an annual inflation adjustment. As of January 1, 2012, the adjusted threshold will be $51,800. Creditors should ensure that their systems and their vendors' systems are in compliance, paying particular attention to the circumstances in which an account can lose its exempt status. Specific issues and questions about consumer compliance matters should be raised with your primary regulator.

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[13] Comment 226.23(a)-5

Regulatory Calendar*

EFFECTIVE DATE	STATUTE/ IMPLEMENTING REGULATION	REGULATORY CHANGE	*OUTLOOK* ARTICLE/ WEBINAR
1/1/2012	Reg. Z	Annual adjustment of fee-based trigger for HOEPA loans	
1/1/2012	Regs. Z/M	Annual adjustment of dollar threshold for exempt consumer credit and lease transactions	
10/1/2011	Reg. II	Final rule on debit card interchange fees and network exclusivity arrangements	
10/1/2011	Reg. Z	Final rule clarifying certain aspects of Credit CARD Act regulations	
8/15/2011	Reg. V	Final rule to implement Dodd-Frank Act credit score disclosure requirement for risk-based pricing notices	Q3 2011
8/15/2011	Reg. B	Amended model ECOA/FCRA adverse action notice that includes Dodd-Frank Act credit score disclosure requirements	
7/29/2011	SAFE Act	Deadline for mortgage loan originators employed by regulated institutions to register with SAFE Act registry	
7/22/2011	Reg. D	The CFPB interim final rule under AMTPA to authorize state-chartered or licensed creditors to continue making mortgage transactions under parity with federal law	
7/21/2011	Regs. Z/M	Final rule increasing transaction coverage for Regulations Z and M from $25,000 to $50,000	Q3 2011
7/21/2011	Reg. II	List of institutions subject to, and exempt from, debit card interchange fee standards	
7/21/2011	Reg. Q	Final rule repealing Regulation Q (prohibiting interest on demand deposits for member banks of the Federal Reserve System)	
*	Dodd-Frank Act	The CFPB seeks comment on rulemaking defining larger participants in certain consumer financial products and services markets	
*	Reg. RR	Proposal to implement Dodd-Frank Act provision defining "qualified residential mortgage" for purposes of securitization risk retention	
*	Reg. Z	Proposal to implement Dodd-Frank Act provision establishing ability-to-repay requirements for mortgages and limitations on prepayment penalties	W
*	Reg. E	Proposal to implement Dodd-Frank Act provision creating new consumer protections for remittance transfers	
*	Reg. CC	Proposal to amend Regulation CC regarding collection of checks and availability of funds	
*	Reg. B	Proposal to clarify data collection compliance requirements for motor vehicle dealers	
*	CRA	New list of distressed or underserved nonmetropolitan middle-income geographies	
5/1/2011	31 C.F.R. Part 212	Agencies issue interim final rule to garnishment restrictions of federal benefit payments paid by direct deposit	
4/1/2011	Reg. Z	Final rule establishing escrow requirements for jumbo HPMLs	
4/1/2011	Reg. Z	Final rule establishing restrictions on loan steering and loan originator compensation	W
4/1/2011	Reg. Z	Interim final rule for appraisal independence requirements	Q3 2011
*	Reg. Z	Proposal to lengthen HPML escrow period and exempt certain creditors	
*	Reg. Z	The Board does not expect to finalize three pending mortgage rulemakings	
1/30/2011	Reg. Z	Revised MDIA interim rule for mortgage loans with variable rates or payments	
1/19/2011	Reg. BB	CRA credit for certain Neighborhood Stabilization Program activities	W
1/1/2011	Reg. V	Risk-based pricing notices	Q4 2010 & W
1/1/2011	Reg. Z	Required notice to borrower when mortgage is sold or transferred	
1/1/2011	Reg. Z	HOEPA trigger amounts revised for 2011	
1/1/2011	Reg. BB	Annual CRA asset-size threshold adjustment	
1/1/2011	Reg. C	Annual HMDA asset-size exemption	
12/31/2010	Reg. P	New model privacy form and safe harbor	
11/3/2010	Reg. BB	CRA credit for institutions making low-cost education loans to low-income borrowers	
10/1/2010	Reg. Z	HPML escrow requirements for manufactured homes	
10/1/2010	SAFE Act	Registration requirement for mortgage loan originators	

*Rulemaking proposals generally do not have an effective date, except for some of the proposed Dodd-Frank Act implementing regulations because Congress specified the effective date in the legislation.

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Calendar of Events

October 15-21, 2011	ABA National Compliance School Emory Conference Center Hotel Atlanta, GA
October 16-21, 2011	ABA Graduate School of Compliance Risk Management Emory Conference Center Hotel Atlanta, GA
November 1-3, 2011	National Community Investment Fund Annual Development Banking Conference: Leveraging Capital for Change Federal Reserve Bank of Chicago Chicago, IL
November 6-9, 2011	CRA and Fair Lending Colloquium Baltimore Waterfront Marriott Baltimore, MD