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Inside

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Interagency Flood Insurance Regulation Update Webinar: Questions and Answers

On October 22, 2015, the Federal Reserve System hosted an interagency Outlook Live webinar titled "Interagency Flood Insurance Regulation Update."[1] Speakers from the Board of Governors of the Federal Reserve System, the Farm Credit Administration, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency (collectively, the agencies) discussed the amendments to their flood insurance regulations, which were published in July 2015 (80 Fed. Reg. 43216, July 21, 2015). Participants submitted a significant number of questions before and during the session. Because of time constraints, only a portion of those questions were answered during the webcast. This article addresses some of the most common questions received. Staff from each of the presenting agencies assisted in providing responses to these participant questions.

ESCROW

1. Does the requirement to escrow flood insurance premiums and fees apply when a loan does not experience a triggering event, such as when the loan is modified without being increased, extended, or renewed; the loan is assumed by another borrower; or the building securing the loan is remapped into a Special Flood Hazard Area (SFHA)?

No, the requirement is subject to certain exceptions. The agencies' regulations provide that a lender or its servicer is required to escrow flood insurance premiums and fees when a designated loan is made, increased, extended, or renewed (a triggering event), unless either the lender or the loan is excepted from the escrow requirement. Until the loan experiences a triggering event the lender is not required to escrow flood insurance premiums and fees unless (i) a borrower requests the escrow in connection with the agencies' regulatory requirement that the lender provide an option to escrow for outstanding loans or (ii) the lender determines that a loan exception to the escrow requirement no longer applies. A designated loan is a loan secured by a building or mobile home that is located or is to be located in an SFHA, in which flood insurance is available under the National Flood Insurance Act (the act).

2. If the borrower has already been granted an exception from the lender to escrow for taxes, homeowner's insurance, and flood insurance, does the lender or its servicer still need to send a notice to offer the ability to escrow for the flood insurance?

Yes. The agencies' regulations do not exclude loans for which borrowers have previously waived escrow from the requirement to offer and make the option

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[1] An archived version of the webinar is available online at https://consumercomplianceoutlook.org/outlook-live/2015/interagency-flood-insurance-regulation-update.

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Credit and Debit Card Issuers' Obligations When Consumers Dispute Transactions with Merchants

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Debit and credit card transactions increased significantly between 2000 and 2012, the most recent period evaluated in the Federal Reserve's triennial payment card study. During this period, the number of credit card transactions increased from 15.6 billion to 26.2 billion, while the number of debit card transactions grew from 8.3 billion to 47 billion.[1]

Given the high volume of transactions, it is not surprising that disputes can occur when consumers use a credit or debit card to pay a merchant for a good or service. For example, if a card is used to purchase an item online that is delivered damaged and the merchant refuses to take it back, the consumer might contact the card issuer to dispute the transaction. The question then arises: What are the card issuer's compliance obligations under federal law for merchant disputes?

The answer depends on whether the consumer paid the merchant with a debit or credit card because the consumer protections for these payment cards derive from different federal laws — the Truth in Lending Act (TILA) for credit cards and the Electronic Fund Transfer Act (EFTA) for debit cards. Under Regulation Z, TILA's implementing regulation, credit card issuers have two separate legal obligations that could apply to merchant disputes. By contrast, under Regulation E, EFTA's implementing regulation, debit card issuers only have obligations if a consumer alleges an error with the fund transfer underlying the purchase.

To facilitate compliance, this article reviews a card issuer's obligations under Regulations Z and E when a cardholder disputes a transaction with a merchant for goods or services purchased with a credit or debit card. This discussion is based solely on federal consumer protection laws. The card issuer may have other obligations under state law or under the rules of the payment processing network through which the card was issued, such as Visa or MasterCard.

TRUTH IN LENDING ACT (REGULATION Z)

Congress passed 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] to avoid the uninformed use of credit."[2] In 1974, Congress amended TILA through the passage of the Fair Credit Billing Act (FCBA) "to protect the consumer against inaccurate and unfair credit billing and credit card practices."[3]

Under the FCBA, as implemented in Regulation Z, credit card issuers have two separate obligations that may apply to merchant disputes. First, under 12 C.F.R. §1026.13(a), issuers must investigate and resolve certain billing errors, including

[1] Federal Reserve Bank Services, "The 2013 Federal Reserve Payments Study: Recent and Long-Term Trends in the United States: 2000–2012," July 2014, www.frbservices.org/files/communications/pdf/general/2013_fed_res_paymt_study_detailed__rpt.pdf.
[2] 15 U.S.C. §1601(a)
[3] Section 302 of the FCBA, Pub. Law 93–495 (October 28, 1974). Codified at 15 U.S.C. §1601(a).

a transaction reflected on a periodic statement involving goods or services that the consumer (or representative) did not accept or was not delivered or was not delivered as agreed. Comment 13(a)(3)-1 of the official staff commentary (commentary) for Regulation Z provides these examples for this type of billing error:

- the appearance on a periodic statement of a purchase when the consumer refused to take delivery of the goods because the goods did not comply with the contract;
- delivery of property or services different from that agreed upon;
- delivery of the wrong quantity;
- late delivery; or
- delivery to the wrong location.

The commentary further clarifies that the error does not apply to a dispute relating to the quality of goods or services that the consumer accepts (whether acceptance occurred is determined by state or other applicable law).

A credit card issuer's compliance obligation under §1026.13(a) is triggered when the consumer sends a written notice to the issuer within 60 days after the issuer provides the periodic statement that reflects the alleged billing error.[4] The consumer is not required to notify the merchant and attempt to resolve the dispute, assuming the consumer did not accept the goods.[5] The card issuer must provide a written acknowledgment to the consumer within 30 days of receiving the billing error notice and investigate and resolve the alleged error within two complete billing cycles (but in no event later than 90 days) of receiving the billing error notice. Until a billing error is resolved, the consumer is entitled to withhold payment to the card issuer for the amount owed the merchant and any associated finance charges, and the issuer is prohibited from reporting negative information about the consumer's credit standing (for example, to a consumer reporting agency) because the consumer failed to pay this amount. If the creditor determines that a billing error has occurred as asserted, it must credit the consumer's account with the full disputed amount, including any associated finance charges.[6]

The second consumer protection in a merchant dispute is found under §1026.12(c), which permits a consumer to assert against the card issuer any defenses and claims (except tort claims) arising out of a transaction paid with a credit card.[7] This right applies only if the cardholder attempted in good faith to resolve the dispute with the merchant and the transaction exceeds $50 and occurred in the same state as the cardholder's designated address or within 100 miles of that address.[8] The amount of the claim is limited by the amount of credit outstanding for the disputed transaction at the time the cardholder first notifies the card issuer of the claim or defense.

For example, a consumer uses a credit card to purchase a product for $200 from a merchant in the same state as the consumer (based on the cardholder's address), and the product is delivered damaged to the consumer. If the merchant refuses to take it back, the cardholder could dispute the transaction with the card issuer based on the defense that the merchant sent a damaged item. The cardholder could also withhold payment on the amount of the transaction and associated finance charges until the matter is resolved. The commentary clarifies that §1026.12(c) "merely preserves the consumer's right to assert against the card issuer any claims or defenses that can be asserted against the merchant. *It does not determine what claims or defenses are valid as to the merchant; this determination must be made under state or other applicable law*"(emphasis added).[9]

One potentially confusing issue is the interplay between the protections of §1026.12(c) and §1026.13(a). For example, if both sections apply to a particular dispute, can the consumer invoke them both? The commentary discusses the overlap and differences between these sections and clarifies that each section operates independently of the other:

> The §1026.12(c) credit card "holder in due course" provision deals with the consumer's right to assert against the card issuer a claim or defense concerning property or services purchased with a credit card, if the merchant has been unwilling to resolve the dispute. *Even though certain merchandise disputes, such as non-delivery of goods, may also constitute "billing errors" under §1026.13, that section operates independently of §1026.12(c)*. The cardholder whose asserted billing error involves undelivered goods may institute the error resolution procedures of §1026.13; but whether or not the cardholder has done so, the cardholder may assert claims or defenses under §1026.12(c). Conversely, the consumer may pay a disputed balance and thus have no further right to assert claims and defenses, but still may assert a billing error if notice of that billing error is given in the proper time and manner. An assertion that a particular transaction resulted from unauthorized use of the card could also be both a "defense" and a billing error.[10]

[4] 12 C.F.R. §1026.13(b)(1). The notice must be sent to the address the issuer specified for billing errors.
[5] Comment 13(a)(3)-3
[6] 12 C.F.R. §1026.13(d)
[7] 12 C.F.R. §1026.12(c)
[8] 12 C.F.R. §1026.12(c)(3)(i)(B). State law determines where a transaction occurred. Comment 12(c)(3)(i)(B)-1.
[9] Comment 12(c)-2.
[10] 12 C.F.R. §1005.11(a)(1)(i)-(vii)

In summary, credit card issuers have certain obligations when a cardholder disputes a transaction with a merchant and contacts the issuer. Whether §§1026.12, 1026.13, or both apply depends on where the product was purchased, the type of merchant dispute, whether there is an outstanding balance on the transaction, whether the good or service was accepted, whether the consumer has attempted to resolve the dispute with the merchant, and how and when the consumer contacts the card issuer. Each section is independent of the other, so even though one section may apply to a dispute, it would not preclude the consumer from obtaining protection under the other section if applicable.

A CARD ISSUER'S OBLIGATIONS FOR MERCHANT DISPUTES DEPEND ON WHETHER A CREDIT OR DEBIT CARD WAS USED AND CERTAIN OTHER FACTORS.

ELECTRONIC FUND TRANSFER ACT (REGULATION E)

The EFTA was enacted in 1978 to provide consumer protections for electronic fund transfers (EFTs), including debit card transactions, and is implemented through Regulation E.[11] Among other provisions, the EFTA provides consumers with the right to dispute "errors" related to their debit cards. The regulation defines an error as:

- an unauthorized EFT;
- an incorrect EFT to or from the consumer's account;
- the omission of an EFT from a periodic statement;
- a computational or bookkeeping error made by the financial institution relating to an EFT;
- the consumer's receipt of an incorrect amount of money from an electronic terminal;
- an EFT not identified on an electronic terminal receipt, a periodic statement, or in connection with a preauthorized transfer to the consumer's account as required by regulation; or
- the consumer's request for documentation required by the regulation or for additional information or clarification concerning an EFT.[12]

Unlike Regulation Z, Regulation E does not define an error to include the right to dispute a transaction with a merchant because of a problem with goods or services. While a consumer may assert an error with respect to the EFT underlying the purchase of goods or services, a merchant dispute about an issue with the goods or services would generally not qualify. For example, an unauthorized EFT is narrowly defined as "an electronic fund transfer from a consumer's account initiated by a person other than the consumer without actual authority to initiate the transfer and from which the consumer receives no benefit."[13]

However, Regulation E does apply to an error in the amount a merchant charged the consumer's card. For example, if a consumer disputed a transaction because the merchant inadvertently charged the consumer's card twice, the card issuer would have to investigate the alleged additional charge because the regulation protects against "an incorrect electronic fund transfer to or from the consumer's account."[14]

Thus, in contrast to Regulation Z's protections for credit cards, Regulation E provides more limited protection for disputes with a merchant arising from a debit card transaction. When the EFTA was enacted in 1978, debit cards were not available for point-of-sale transactions,[15] so it is not surprising that the EFTA does not cover certain merchant disputes. By contrast, when the FCBA was enacted in 1974, credit cards were used for point-of-sale transactions, and Congress specifically provided protections for certain merchant disputes.[16]

CONCLUSION

Card issuers will likely see an increase in the number of cardholder disputes as the percentage of consumer transactions paid with debit and credit cards continues to increase. A card issuer's obligations for merchant disputes depend on whether a credit or debit card was used and certain other factors. Thus, it is important for debit and credit card issuers and their staffs to understand their obligations under Regulations Z and E when a consumer files a dispute. Specific issues and questions should be raised with your primary regulator. ■

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[11] 12 C.F.R. §1005.2(m)
[12] 12 C.F.R. §1005.11(a)(1)(ii)
[13] Pub. Law No. 95-630 (November 10, 1978). Codified at 15 U.S.C. §1693 et seq.
[14] 12 C.F.R. §1005.11(a)(1)(ii)
[15] Stan Sienkiewicz, "The Evolution of EFT Networks from ATMs to New On-Line Debit Payment Products," Payment Cards Center, Federal Reserve Bank of Philadelphia, 2002, pp. 5–7.
[16] Section 170 of the FCBA (15 U.S.C. §1666i)

continued from Page 1

available to escrow flood insurance premiums and fees. Consequently, lenders or their servicers still must send a notice of the option to escrow flood insurance premiums and fees to borrowers who have previously waived escrow or for whom lenders previously offered an option to escrow. Although a borrower may have previously decided to waive escrow or had already been offered an option to escrow, it is possible that the borrower's circumstances have changed, and if offered another chance to escrow, the borrower may desire to do so.

3. Is the option to escrow notice required for all outstanding loans that are not exempt and secured by residential real estate or just those that are in a flood zone?

Under the agencies' regulations, lenders or their servicers are required to offer and make the option available to escrow flood insurance premiums and fees for all outstanding designated loans secured by residential improved real estate or mobile homes as of January 1, 2016, or July 1 of the first calendar year in which the lender no longer qualifies for the small lender exception to the escrow requirement. The requirement to provide the option to escrow notice does not apply to loans or lenders that are excepted by the agencies' regulations from the general escrow requirement. The option to escrow notice requirement also does not apply to loans that are not subject to the mandatory purchase requirement.

4. If a lender does not qualify for the small lender exception and purchases a portfolio of loans secured by residential improved real estate or mobile homes from a small lender eligible for the exception, must the purchasing lender require an escrow account on the designated loans in the portfolio or provide notice of the option to escrow to the borrowers?

It depends. Under the agencies' regulations, the requirement to notify borrowers of the option to escrow applies to a lender's loans outstanding as of January 1, 2016. Therefore, if a lender purchased a portfolio of loans secured by residential improved real property or mobile homes prior to January 1, 2016, and the loans remained outstanding in the lender's portfolio as of that date, the lender would be required to provide the notice of the option to escrow to borrowers on designated loans. On the other hand, if the portfolio purchase occurred after January 1, 2016, a lender that does not qualify for the small lender exception would not be required by the agencies' regulations to send the notice of the option to escrow. Nor would an escrow have to be established on the designated loans in the portfolio because the purchase of a portfolio of loans is not a triggering event. However, if a triggering event occurs in connection with any designated loan in the portfolio after the purchase, the lender or its servicer would need to require an escrow for flood insurance premiums and fees.

5. Is it true that lenders qualifying for the small lender exception are not required to provide borrowers the escrow notice or the option to escrow notice?

Yes. Lenders that qualify for the small lender exception are not required to provide borrowers either the escrow notice or the option to escrow notice unless the lender ceases to qualify for the small lender exception.

6. If a lender does not escrow for taxes or homeowner's insurance, is it still required to escrow for flood insurance under the new rule? If yes, is the lender obligated to escrow for taxes and other insurance because it escrows for flood insurance pursuant to the rule?

If a lender or its servicer is required to escrow for flood insurance under the new rule, it must do so even if it does not escrow for taxes or other insurance. A lender or servicer is not, however, obligated to escrow for taxes and other insurance because it escrows for flood insurance pursuant to the agencies' flood rule, although other regulations may apply that require the escrow. Furthermore, a lender may always choose to require an escrow even when it is not mandated.

Lenders that qualify for the small lender exception are not required to provide borrowers either the escrow notice or the option to escrow notice unless the lender ceases to qualify for the small lender exception.

7. For which types of loans must a lender or its servicer provide the option to escrow notice? If a loan is subject to an exception (e.g., a business purpose loan), does a lender that does not qualify for the small lender exception still have to provide an option to escrow notice in connection with that loan?

Lenders or their servicers that do not qualify for the small lender exception must provide the option to escrow notice to borrowers for designated loans secured by residential improved real estate or mobile homes outstanding as of January 1, 2016. However, if a loan is subject to another exception (e.g., business, commercial, or agricultural purpose), the lender or its servicer is not required to provide an option to escrow in connection with that loan.

8. If a creditor originates a second mortgage loan for a property located in an SFHA and it is determined that the first lienholder does not have sufficient flood insurance coverage for both liens and is not currently escrowing for flood insurance, does the second lienholder have to escrow for the additional amount of flood insurance coverage?

Under the agencies' regulations, junior lienholders are not required to escrow for flood insurance if the borrower has obtained flood insurance for a closed-end second mortgage loan that meets the mandatory purchase requirement. Thus, the lender or its servicer must ensure that adequate flood insurance is in place. Question No. 36 of the July 2009 Interagency Questions and Answers Regarding Flood Insurance explains the requirements for junior lienholders. If adequate flood insurance is not obtained, the lender or servicer would need to escrow. However, the escrow requirements do not apply to a junior lien that is a home equity line of credit (HELOC).

9. Does a lender or its servicer have to escrow for loans when the property is not located in an SFHA but the borrower chooses to buy flood insurance?

Under the agencies' regulations, a lender and its servicers are only required to escrow for loans that are secured by residential improved real estate or mobile homes located or to be located in SFHAs where flood insurance is available under the National Flood Insurance Program and that experience a triggering event (i.e., made, increased, extended, or renewed) on or after January 1, 2016, unless either the lender or the loan qualifies for an exception. If the property securing the loan is not located in an SFHA, the lender or its servicer is not required to escrow, although the lender or its servicer may choose to do so.

10. Is there an exception to the escrow requirement for loans secured by multifamily buildings? Is there an exception for commercial loans?

The agencies' regulations specify that the escrow requirements do not apply to a loan that is an extension of credit primarily for business, commercial, or agricultural purposes, even if secured by residential real estate. In addition, the escrow requirements would not apply to a loan secured by a particular unit in a multifamily residential building if a condominium association, cooperative, homeowners association, or other applicable group provides an adequate policy and pays for the insurance as a common expense. Otherwise, the escrow requirements would generally apply to loans for units in multifamily residential buildings.

FORCE-PLACED INSURANCE

11. Following a flood map change, is a regulated lending institution required to force place flood insurance during the 45 days following the notice to the borrower, or can the institution wait 45 days after notifying the borrower?

The agencies' regulations permit a lender or its servicer to force place flood insurance beginning on the date the borrower's policy lapsed or did not provide sufficient coverage to ensure continuous flood coverage for both the institution and the borrower, and any time after that date. However, if a borrower fails to obtain flood insurance within 45 days of the lender's notification to the borrower of the need to obtain flood insurance, the lender must force place flood insurance at that time.

12. If the need for flood insurance on a property was mistakenly not required because of a vendor error and is later discovered, is the process to cure the same as if the property newly became covered under the act? If not, what procedural steps must be taken?

The same procedures must be followed when a lender or its servicer discovers that improved collateral real property is not covered by flood insurance because of vendor error that is used when flood insurance coverage for such property becomes necessary as the result of a mapping change. Under the agencies' regulations, if a lender, or a servicer acting on its behalf, determines at any time during the term of a designated loan that the building or mobile home and any personal property securing the designated loan is not covered by flood insurance or that the coverage is inadequate, the lender or its servicer must notify the borrower of the need to obtain adequate flood insurance at the borrower's expense. If the borrower fails to obtain adequate flood insurance within 45 days after notification, the lender must purchase flood insurance on behalf of the borrower.

13. If a lender cannot get a full refund from the insurance company because the borrower did not provide proof of coverage in a timely manner, is the lender required to refund the full premium to the customer?

The agencies' regulations specifically require the refund of force-placed insurance premiums for any overlap period and do not provide any exceptions to that requirement. Moreover, the agencies clarified in the supplementary information accompanying the July 2015 Final Rule that a lender's refund obligation is not subject to the insurer's refund of the premium.

14. If a lender or its servicer is required to force place flood insurance because the property was remapped into an SFHA, may the lender or its servicer charge the borrower as of the date the lender receives notice of the remapping?

The agencies' regulations provide that a lender or its servicer may charge the borrower for the cost of premiums and fees incurred for coverage beginning on the date on which flood insurance coverage lapsed or did not provide sufficient coverage. When a lender or its servicer receives notice of a property being remapped into an SFHA, the effective date of the remapping change is the date the property has insufficient coverage. Therefore, along with sending the appropriate notice to the borrower to purchase adequate flood insurance, the lender or its servicer can force place flood insurance beginning on the effective date provided in the date of notice of remapping and, also as of that day, charge the borrower for the force-placed insurance provided force-placed insurance is in place. However, if the borrower purchases an adequate flood insurance policy, the lender or its servicer would need to reimburse the borrower for premiums and fees charged for the force-placed coverage during any period of overlapping coverage.

DETACHED STRUCTURES

15. Has the Consumer Financial Protection Bureau (CFPB) revised the Special Information Booklet required by Section 13 of the Homeowner Flood Insurance Affordability Act (HFIAA) to require that language related to detached structures be included in the required Special Information Booklet?

Yes. The CFPB has revised the Special Information Booklet as required by Section 13 of the HFIAA, which also amends Section 5(b) of RESPA (12 U.S.C. 2604(b)), to require language related to detached structures. The booklet, titled "Your Home Loan Toolkit: A Step-by-Step Guide," states: "Although you may not be required to maintain flood insurance on all structures, you may still wish to do so, and your mortgage lender may still require you to do so to protect the collateral securing the mortgage. If you choose to not maintain flood insurance on a structure, and it floods, you are responsible for all flood losses relating to that structure."

16. If a borrower currently has a flood insurance policy on a detached structure that does not serve as a residence, can the lender or its servicer cancel its requirement to carry that flood insurance?

If a borrower has a flood insurance policy on a detached structure, which is part of residential property that does not serve as a residence, the borrower is no longer required by statute to have flood insurance on that building. The lender may allow the borrower to cancel the policy. As the agencies noted in the supplementary information accompanying the July 2015 Final Rule, for detached structures that are of relatively high value, if warranted as a matter of safety and soundness, the lender may continue to require flood insurance coverage on the detached structure in that such coverage may be in the borrower's best interest.

If a borrower has a flood insurance policy on a detached structure, which is part of residential property that does not serve as a residence, the borrower is no longer required by statute to have flood insurance on that building.

17. If a property is remapped into a flood zone, does that trigger a review of the intended use of each detached structure?

A lender must examine the status of a detached structure upon a qualifying triggering event (i.e., making, increasing, extending, or renewing a loan). However, consistent with existing obligations under the agencies' regulations, if a lender determines at any time that a property has become subject to the mandatory flood insurance purchase requirement and, as a result, the collateral is uninsured or underinsured, the lender has a duty to inform the borrower of the obligation to obtain or increase insurance coverage. The agencies agree that lenders do not have a duty to monitor the status of a detached structure following the lender's initial determination because of the minimal postclosing communications with borrowers or lack of systematic inspections of the property. However, as discussed in Question No. 7 of the agencies' July 2009 Interagency Questions and Answers Regarding Flood Insurance, regardless of the lack of such requirement in the agencies' regulations, sound risk management practices may lead a lender to conduct scheduled periodic reviews that track the need for flood insurance on a loan portfolio.

18. Can a lender review current loans in its portfolio as flood insurance policies renew and determine that it would no longer require flood insurance on a detached structure in a flood zone if the structure does not provide contributory value?

A lender or its servicer could initiate such a review; however, the agencies' regulations do not permit the exemption of structures from the mandatory flood insurance purchase requirement based solely on their contributory value. Flood insurance is not required, in the case of any residential property, on any structure that is a part of such property but is detached from the primary residential structure and does not serve as a residence. In addition, other exemptions could apply, such as the exemption for state-owned property covered under a policy of self-insurance satisfactory to the administrator of the Federal Emergency Management Agency, the exemption for property securing any loan with an original principal balance of $5,000 or less, or the exemption for a loan with a repayment term of one year or less.

Specific issues and questions should be raised with your primary regulator. ■

Compliance Alert

On April 7, 2016, the Board of Governors of the Federal Reserve System issued Consumer Affairs (CA) Letter 16-1 to address the new examination procedures for the Flood Disaster Protection Act.

The Task Force on Consumer Compliance of the Federal Financial Institutions Examination Council recently developed interagency examination procedures for the Flood Disaster Protection Act (FDPA). The revised procedures supersede the prior procedures transmitted in CA 97-1.

The procedures were updated to reflect a July 2015 interagency rulemaking addressing force placement of flood insurance, escrow of flood insurance premiums and fees, and exemption to the mandatory purchase of flood insurance requirement for certain detached structures. This rulemaking was the subject of the article "Agencies Issue Final Rule for New Flood Insurance Requirements" in the Third/Fourth Quarter 2015 issue of *Consumer Compliance Outlook*. The agencies also conducted a webinar on the new requirements in October 2015. A follow-up Q&A article from the webinar begins on page 1 in this issue of *Outlook*.

With the implemented changes in the July 2015 rulemaking, the procedures require examiners to verify that the institution provides a refund to the borrower of all force-placed insurance premiums and any fees that the borrower paid during any period of overlap between the borrower's policy and the force-placed policy. The examination objectives in the new procedures include a requirement to determine whether the institution's flood insurance premiums need to be escrowed if mandated by law. In addition, the procedures include a requirement that, if a detached structure is not covered by flood insurance, the examiner must review the institution's documentation for this conclusion and verify that the structure meets the exemption. ■

Proposed Changes to the Uniform Interagency Consumer Compliance Rating System

On May 3, 2016, the Federal Financial Institutions Examination Council (FFIEC) published in the *Federal Register* proposed changes to the Uniform Interagency Consumer Compliance Rating System, more commonly known as the CC Rating System. 81 Fed. Reg. 26553 (May 3, 2016).

BACKGROUND

The current CC Rating System, adopted in 1980, is a supervisory policy for evaluating financial institutions' adherence to consumer compliance requirements. The CC Rating System is based on a scale of 1 through 5, in increasing order of supervisory concern. Thus, 1 represents the highest rating and consequently the lowest level of supervisory concern, and 5 represents the lowest rating and consequently the most critically deficient level of performance and the highest degree of supervisory concern. When using the CC Rating System to assess an institution, the banking agencies do not consider an institution's record of lending performance under the Community Reinvestment Act (CRA) because institutions are evaluated separately for the CRA.

PURPOSE OF THE REVISIONS

The agencies are proposing to revise the current CC Rating System to better reflect current consumer compliance supervisory approaches. The revisions are designed to more fully align the rating system with the agencies' current risk-based, tailored examination approaches. The proposed revisions to the CC Rating System were not developed to set new or higher supervisory expectations for financial institutions, and their adoption will represent no additional regulatory burden.

When the current CC Rating System was adopted in 1980, examinations focused more on transaction testing for regulatory compliance than on evaluating the sufficiency of an institution's compliance management system (CMS) to ensure compliance with regulatory requirements and to prevent consumer harm. In the intervening years, each of the FFIEC agencies has adopted a risk-based consumer compliance examination approach to promote strong compliance risk management practices and consumer protection within supervised financial institutions. Risk-based consumer compliance supervision evaluates whether an institution's CMS effectively manages the compliance risk in the products and services offered to its customers. Under risk-based supervision, examiners tailor supervisory activities to the size, complexity, and risk profile of each institution and adjust these activities over time. Although compliance management programs vary based on the size, complexity, and risk profile of supervised institutions, all institutions should maintain an effective CMS. The sophistication and formality of the CMS typically increase commensurate with the size, complexity, and risk profile of the entity.

As the agencies drafted the proposed rating system definitions, one objective was to develop a rating system appropriate for evaluating institutions of all sizes. Therefore, the first principle discussed within the CC Rating System conveys that the system is risk-based to recognize and communicate clearly that compliance management programs vary based on the size, complexity, and risk profile of supervised institutions. This principle is reinforced in the Consumer Compliance Rating Definitions by conveying to examiners that assessment factors associated with an institution's CMS should be evaluated commensurate with the institution's size, complexity, and risk profile.

In developing the revised CC Rating System, the agencies believe it is also important for the new rating system to establish incentives for institutions to promote consumer protection by preventing, self-identifying, and addressing compliance issues in a proactive manner. The proposed rating system would also create a framework for the agencies to recognize institutions that consistently adopt these compliance strategies.

Another benefit of the proposed CC Rating System is to promote coordination, communication, and consistency among the agencies, consistent with the agencies' respective supervisory authorities. Pursuant to the proposal, each of the agencies would use the same CC Rating System to assign a consumer compliance rating to all supervised institutions, including banks and nonbanks. Furthermore, revising the rating system definitions responds to requests from industry representatives who have asked that the CC Rating System be updated.

The full text of the proposal is available at www.gpo.gov/fdsys/pkg/FR-2016-05-03/pdf/2016-10289.pdf. The comment period closes on July 5, 2016. ■

News from Washington: Regulatory Updates*

The Board of Governors of the Federal Reserve (Board) repeals Regulation AA. The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) repealed the Board's rulemaking authority to write rules that address unfair or deceptive acts or practices, which were contained in the Board's Regulation AA. The Dodd-Frank Act provides the Consumer Financial Protection Bureau (CFPB) separate authority to promulgate rules to identify and prohibit unfair, deceptive, or abusive acts or practices. The legislative repeal of the Board's rulemaking authority nullified the provisions in Regulation AA, including the Board's "credit practices rule." Regulation AA prohibited banks from using certain practices to enforce consumer credit obligations and from including these practices in their consumer credit contracts. In 2014, the Board joined the CFPB, the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) in issuing interagency guidance, stating that, depending on the facts and circumstances, a depository institution might violate the prohibition against unfair or deceptive practices in the Federal Trade Commission (FTC) Act and the Dodd-Frank Act if it engages in the practices prohibited by the former credit practices rule.

The Board proposes to repeal Regulation C. The Dodd-Frank Act transferred rulemaking authority for several federal consumer protection statutes, including the Home Mortgage Disclosure Act (HMDA), from the Board to the CFPB. The Board implemented the HMDA through Regulation C, 12 C.F.R. Part 203. Following the enactment of the Dodd-Frank Act, the CFPB issued an interim final rule creating its own Regulation C; see 12 C.F.R. Part 1003. Because the Board no longer has legal authority to issue implementing regulations for the HMDA, it is proposing to repeal its Regulation C, 12 C.F.R. Part 203. The comment period closed April 22, 2016.

The CFPB seeks comment on changing the threshold for requiring resubmission of mortgage data under the HMDA. On January 12, 2016, the CFPB published a notice in the *Federal Register* seeking public comment on whether to change its HMDA Resubmission Guidelines for data that will be submitted under the CFPB's recent amendments to Regulation C. Under current guidelines, institutions reporting fewer than 100,000 loans or applications on the HMDA loan application register (LAR) should be required to correct and resubmit HMDA data when errors are found in (1) 10 percent or more of the HMDA LAR sample entries or (2) 5 percent or more of the sample entries within an individual data field. Institutions reporting 100,000 or more entries on the HMDA LAR should be required to correct and resubmit HMDA data when errors are found in (1) 4 percent or more of the HMDA LAR sample entries or (2) between 2 percent and 4 percent of the sample entries within an individual data field. The request for comment lists 20 questions on which the CFPB is seeking comment, such as whether it should continue to use error percentage thresholds to determine the need for data resubmission or whether, if the thresholds are retained, they should be calculated differently than they are currently. The deadline for submitting comments was March 16, 2016.

Federal banking agencies release annual Community Reinvestment Act (CRA) asset-size threshold adjustments for small and intermediate small institutions. On December 22, 2015, the federal banking agencies announced the annual adjustment under the CRA to the asset-size thresholds used to define small bank, small savings association, intermediate small bank, and intermediate small savings association regulations. Financial institutions are evaluated under different CRA examination procedures based upon their asset-size classification. Institutions meeting the small and intermediate small institution asset-size thresholds are not subject to the reporting requirements that apply to large banks and savings associations. The annual adjustment to asset-size thresholds is based on the change in the average of the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W). Based on the .42 percent decline in the average of the CPI-W for 2015, the 2016 thresholds for small and intermediate small institutions are as follows:

- "Small bank" or "small savings association" refers to an institution that as of December 31 had assets of less than $1.216 billion in either 2014 or 2015.
- "Intermediate small bank" or "intermediate small savings association" refers to a small institution with assets of at least $304 million as of December 31 in both 2014 and 2015, and less than $1.216 billion as of December 31 in either 2014 or 2015.

The adjustments were effective January 1, 2016.

Federal banking agencies seek comment on interagency effort to reduce regulatory burden under the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA) of 1996. On December 23, 2015, the Board, the FDIC, and the OCC published their fourth and final notice in the *Federal Register* under the EGRPRA seeking comment on reducing regulatory burden through potential amendments

* Links to the announcements are available in the online version of *Outlook* at www.consumercomplianceoutlook.org.

to regulations pertaining to rules of procedure, safety and soundness, and securities. The regulations on which the agencies were seeking comment include interagency standards for appraisal management companies. They also invited the public to comment on any other agency final rule not included in a previous EGRPRA *Federal Register* notice. The comment period closed March 22, 2016. Additional information on the EGRPRA is available on the agencies' EGRPRA website at http://egrpra.ffiec.gov.

Agencies announce dollar thresholds in Regulations Z and M for exempt consumer credit and lease transactions. On November 25, 2015, the Board and the CFPB announced the dollar thresholds that will apply under Regulation Z (Truth in Lending Act (TILA)) and Regulation M (Consumer Leasing Act) for determining exempt consumer credit and lease transactions in 2016. The annual adjustment is based on the annual percentage increase in the CPI-W. If the CPI-W average has not increased, the Board and the CFPB maintain the exemption threshold from the prior year. Transactions at or below the thresholds are subject to the protections of the regulations. Because the CPI-W average declined, the agencies are maintaining the 2015 threshold of $54,600 effective January 1, 2016. Accordingly, the protections of the TILA and the Consumer Leasing Act generally will apply to consumer credit transactions and consumer leases of $54,600 or less in 2016. Note, however, that private education loans and loans secured by real property (such as mortgages) are subject to the TILA regardless of the loan amount.

Agencies announce the threshold for smaller loan exemption from appraisal requirements for higher priced mortgage loans. On November 25, 2015, the Board, the CFPB, and the OCC announced that the threshold exempting loans from special appraisal requirements for higher priced mortgage loans during 2016 will remain at $25,500. As with the Regulation Z and Regulation M thresholds mentioned in the previous item, adjustments are made annually to the threshold based on the change in the average of the CPI-W. Because the CPI-W average declined, the threshold will remain the same effective January 1, 2016. Special appraisal requirements for higher priced mortgage loans include a requirement that creditors obtain a written appraisal based on a physical visit to the home's interior before making a higher priced mortgage loan. The rules contain an exemption for loans of $25,000 or less, with that threshold also adjusted annually to reflect increases in the CPI-W average.

The Department of Defense (DoD) expands coverage of the Military Lending Act (MLA). On July 22, 2015, the DoD issued a final rule amending its regulation implementing the MLA. The DoD amended the regulation to extend the protections of the MLA to a wider range of closed-end and open-end credit products, including credit cards. The amended MLA regulation generally applies to all consumer credit, other than home-secured credit and loans, to finance the purchase of motor vehicles and other consumer goods that are secured by the purchased item. Extensions of credit covered by the rule would be subject to a 36 percent rate cap, based on the military annual percentage rate (MAPR). Among a range of other amendments, DoD's final rule modifies the following: The fees that must be included when calculating the MAPR, the optional safe harbor provisions for creditors to determine whether consumers are entitled to MLA protections, and MLA disclosure requirements. The compliance date for the amended rule is October 3, 2016, but for credit card accounts, the compliance date is October 3, 2017 (which may be extended by one year at the DoD's option). DoD's final rule was issued following required consultation with the Board, the CFPB, the FDIC, the FTC, the National Credit Union Administration, the OCC, and the Department of the Treasury. The *Federal Register* notice is available at www.gpo.gov/fdsys/pkg/FR-2015-07-22/pdf/2015-17480.pdf. ■

On the Docket: Recent Federal Court Opinions*

REGULATION Z — TRUTH IN LENDING ACT (TILA)

Ninth Circuit rules that a 2009 TILA amendment requiring notice to a borrower when a residential mortgage loan is transferred does not apply retroactively. *Talaie v. Wells Fargo Bank, N.A.*, 808 F.3d 410 (9th Cir. 2015). In 2009, Congress amended the TILA to require that, when a residential mortgage loan is sold, transferred, or assigned, the creditor that is the new owner or assignee must provide notice, in writing, to the borrower within 30 days. 15 U.S.C. §1641(g). The statute allows borrowers to sue for up to $4,000 in statutory damages in individual claims and up to $1 million in statutory damages in a class-action lawsuit along with actual damages, costs, and attorney's fees. In this class-action lawsuit, the plaintiffs alleged that U.S. Bank violated this provision by not providing notice for mortgage loans that Wells Fargo Bank transferred to U.S. Bank in 2006. The issue in the case was whether §1641(g) applied retroactively to loans transferred before the 2009 TILA amendment was enacted.

The court explained that the Supreme Court has ruled that retroactive application of statutes is "disfavored" and that this presumption can only be overcome where Congress has expressed a clear and unambiguous intent to apply a law retroactively. The court examined the text of the amendment and its legislative history and found no evidence that Congress intended for it to apply to loans whose ownership was transferred before it was enacted. The court also noted that it would have been impossible for creditors to comply with §1641(g) in connection with loans transferred more than a month before the statute was enacted, given that notice must be provided within 30 days of the transfer. Accordingly, noting that its holding was consistent with various other district court decisions interpreting §1641(g), the court affirmed the lower court's dismissal of the case.

Eleventh Circuit holds that a loan secured by a lien on a fixture was not subject to rescission because it did not create a security interest in the borrowers' principal dwelling. *Lankhorst v. Independent Savings Plan Company,* 787 F.3d 1100 (11th Cir. 2015). The plaintiffs financed the purchase of a water treatment system for their primary residence based, in part, on the defendant seller's representation of a low interest rate. After discovering that the rate was 17.99 percent, the plaintiffs filed suit, alleging that the creditor violated the TILA by not allowing for a three-business-day rescission period, required by §1635(a) of the TILA for certain principal dwelling-secured loans, and by not providing examples of minimum payments and the maximum repayment period, as required by §1637a(a)(9) of the TILA, for loans secured by a consumer's principal dwelling. The district court granted summary judgment for the defendant on the grounds that the applicable credit agreement did not convey a security interest in the plaintiffs' residence.

On appeal, the Eleventh Circuit affirmed, indicating that the right of rescission only applies to certain credit transactions secured by a consumer's principal dwelling. The credit agreement here solely created a purchase money security interest in any purchases that the plaintiffs made on the account; because the financing was only used to purchase the water system, it did not create a security interest in the plaintiffs' residence. The plaintiffs argued that the credit agreement indicated that a judgment obtained in the event of default would create a valid, enforceable lien against the plaintiffs' residence. However, the Eleventh Circuit found that, rather than establishing that the defendant had taken a security interest in the plaintiffs' residence, the credit agreement was clear that such a lien would be the product of a judgment after default via operation of state law and not the terms of the credit agreement: "it is not the Credit Agreement or UCC financing statement itself, but the judgment against the debtor, that gives rise to the potential lien against the home. The Florida statute converts a judgment to a lien against real property independent of this (or any) contract." Accordingly, the Eleventh Circuit affirmed the district court's ruling that the defendant did not take the necessary security interest in the plaintiffs' residence to allow them to obtain the TILA protections that they sought.

* Links to the announcements are available in the online version of *Outlook* at www.consumercomplianceoutlook.org.

SERVICEMEMBERS CIVIL RELIEF ACT (SCRA)

Court dismisses SCRA lawsuit for a loan obtained during active duty military service. *Hall v. Springleaf Financial Services, Inc.* --- F.Supp.3d ---- 2015 WL 7175789 (S.D. Miss. Nov. 13, 2015). The SCRA provides certain protections to servicemembers (and, in some cases, spouses, dependents, and other persons subject to the obligations of service members) on active duty military service, including a 6 percent cap on the interest rate for the duration of active duty military service that can be applied to debts incurred before that military service. 50 U.S.C. Appx. §527. The plaintiff, a captain in the Mississippi Army National Guard, entered active duty military service pursuant to a U.S. Army order beginning on October 10, 2012, and ending on October 9, 2013. On September 26, 2013, his active duty was extended to July 6, 2014, with the amended orders indicating an end date of September 30, 2013, for his original orders. On June 24, 2013, he obtained a loan from the defendant lender with an annual percentage rate of 34.37 percent. He subsequently requested that the lender reduce the rate to 6 percent pursuant to §527 of the SCRA. When the lender refused, he filed a lawsuit alleging a violation of §527. The court found that §527 solely applied to obligations or liabilities incurred *before* a servicemember enters active duty military service. Although the plaintiff's original tour of duty was extended after he secured the loan, this did not change the court's analysis because the statute indicates that a period of military service ends when a member is released from (or dies during) military duty, and the plaintiff was not released until July 6, 2014. The court found that he was not released from his active duty military service on September 30, 2013; rather, he was solely released from his original orders but remained on active duty. In other words, no ensuing new period of active duty began after the loan was extended. Accordingly, §527 did not apply. The court granted summary judgment on behalf of the lender.

FAIR CREDIT REPORTING ACT (FCRA)

Supreme Court to decide whether allegations of a willful FCRA violation in the absence of actual harm is sufficient to confer Article III standing. *Robins v. Spokeo, Inc.*, 742 F.3d 409 (9th Cir. 2014), *cert. granted*, 135 S. Ct. 1892 (2015). Under Article III of the Constitution, only persons suffering an actual or imminent concrete and particularized injury in fact that resulted from a defendant's conduct, and which can likely be redressed by a favorable decision, have standing to invoke the jurisdiction of the federal courts. There is a circuit split among federal appeals courts regarding whether a plaintiff who cannot prove actual or imminent harm from a federal law violation satisfies this standing requirement when a federal law provides for statutory damages (predetermined damages that must be paid if the plaintiff establishes a violation). Certain federal consumer protection laws allow for statutory damages in addition to actual damages that may be difficult for plaintiffs to demonstrate in some cases. The plaintiff alleged that Spokeo, an information-gathering website that offers various options for finding information about people, willfully violated the FCRA by including inaccurate personal information on its website that could potentially adversely affect his employment prospects as well as his ability to obtain credit and insurance. For willful violations, the FCRA allows statutory damages of up to $1,000 per violation, 15 U.S.C. §1681n(a); the plaintiff only sought such statutory damages. The district court dismissed the lawsuit for lack of standing on the grounds that the plaintiff did not allege an injury in fact and that any injuries that he did allege were not caused by the defendant's actions.

On appeal, the Ninth Circuit reversed the district court's dismissal of the matter and remanded the case for further proceedings consistent with its decision. Specifically, the Ninth Circuit determined that it was not necessary for the plaintiff to prove any actual harm: "When, as here, the statutory cause of action does not require proof of actual damages, a plaintiff can suffer a violation of the statutory right without suffering actual damages." Moreover, the court found that the plaintiff's alleged violation of his statutory rights created by the FCRA satisfied Article III's injury in fact requirement and that the plaintiff adequately pleaded causation and redressability. The Supreme Court agreed to hear the defendant's appeal — and determine whether Congress may confer Article III standing upon a plaintiff who suffers no actual harm — during its current term.

Update: On May 16, 2016, as *Outlook* went to press, the Supreme Court issued a decision in this case, remanding it back to the Ninth Circuit for further consideration in light of the court's opinion. *Outlook* will discuss the opinion in the next issue. The decision is available at www.supremecourt.gov/opinions/15pdf/13-1339_f2q3.pdf. ■

TILA-RESPA Integrated Disclosure (TRID) Webinars

The Federal Reserve System regularly conducts Outlook Live webinars that focus specifically on consumer compliance topics. The compliance requirements for the new integrated mortgage disclosures required under the Truth in Lending Act and the Real Estate Settlement Procedures Act (also known as TRID) generated many questions from the industry to clarify compliance requirements. In response, the Federal Reserve System partnered with the Consumer Financial Protection Bureau to host seven TRID webinars. The table below provides links to the webinars, to the presentation slides, and to indexes of questions the presenters covered in the webinar.

Webinar	URL	Presentation Slides	Index of Questions Discussed
TILA-RESPA Integrated Disclosures, Part 1 — Overview of the Rule June 17, 2014. This webinar provided an overview of the final rule and the new disclosures and addressed a few basic compliance questions.	http://bit.ly/TRID-1	http://bit.ly/TRID1-slides	http://bit.ly/TRID1-question
FAQs on the TILA-RESPA Integrated Disclosures, Part 2 — Various Topics August 26, 2014. This webinar addressed specific questions, including application scope, record retention, timing for delivery, tolerance, and basic form contents.	http://bit.ly/TRID-2	http://bit.ly/TRID2-slides	http://bit.ly/TRID2-questions
FAQs on the TILA-RESPA Integrated Disclosures Rule, Part 3 — Completing the Loan Estimate October 1, 2014. This webinar discussed issues in completing the Loan Estimate.	http://bit.ly/TRID-3	http://bit.ly/TRID3-slides	http://bit.ly/TRID3-questions
TILA-RESPA Integrated Disclosures, Part 4 — Completing the Closing Disclosure November 18, 2014. This webinar discussed issues in completing the Closing Disclosure.	http://bit.ly/TRID-4	http://bit.ly/TRID4-slides	http://bit.ly/TRID4-questions
TILA-RESPA Integrated Disclosures, Part 5 — Implementation Challenges and Questions May 26, 2015. This webinar covered implementation challenges.	http://bit.ly/TRID-5	http://bit.ly/TRID5-slides	http://bit.ly/TRID5-questions
Know Before You Owe Mortgage Disclosure Rule — Construction Lending March 1, 2016. This webinar addressed TRID requirements for construction loans.	http://bit.ly/TRID-6	http://bit.ly/TRID6-slides	http://bit.ly/TRID6-questions
Know Before You Owe Mortgage Disclosure Rule: Post-Effective Date Questions & Guidance April 12, 2016. This webinar covered common questions that have been raised since the rule took effect on October 3, 2015.	http://bit.ly/TRID-7	http://bit.ly/TRID-7-slides	Not yet available

Regulatory Calendar*

Effective Date	Implementing Regulation	Regulatory Change	Outlook Live Webinar
1/1/18 (most provisions)	Reg. C	Final rule implementing Dodd-Frank Wall Street Reform and Consumer Protection Act changes to the Home Mortgage Disclosure Act (HMDA)	
N/A	Regs. Z and X	Proposed rule amendments to certain mortgage servicing provisions	
6/10/16	Regs. J and L	Final rulemaking adjustments to submission of filings under the Interstate Land Sales Full Disclosure Act	
3/31/16	Reg. Z	Interim final rule implementing Helping Expand Lending Practices in Rural Communities Act to broaden exemption for small creditors operating in rural and underserved areas	
3/3/16	Reg. Z	Final rule establishing application process for Designation of Rural Area under Federal Consumer Financial Law	
1/1/16	Reg. C	Final rule adjusting asset-size threshold for exemption from HMDA reporting	
1/1/16	Reg. Z	Final rule adjusting asset-size threshold to qualify for small creditor exemptions	
1/1/16	Reg. H	Final rule implementing provisions of the Homeowners Flood Insurance Affordability Act	10/22/15
1/1/16	Reg. Z	Final rule to expand definitions of small creditor and rural area for purposes of certain mortgage rules with reduced regulatory requirements for small creditors and small creditors operating primarily in rural areas	
12/24/15	Regs. Z and X	Technical correction to official staff commentary for Truth in Lending Act and Real Estate Settlement Procedures Act integrated disclosures (TRID) requirement	
12/4/15	Reg. P	Amendment to Gramm-Leach-Bliley privacy notice requirements in section 75001 of the Fixing America's Surface Transportation Act	
10/3/15	Regs. Z and X	Final rule extending integrated disclosure timing requirements for rate locks and requiring placement of the Nationwide Mortgage Licensing System and Registry (NMLSR) ID in TRID	4/12/16 3/1/16 5/26/15 11/18/14 10/1/14 8/26/14

* Links to the regulatory changes are available in the online version of *Outlook* at tinyurl.com/calendar-cco.
† Rulemaking proposals generally do not have an effective date.

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Calendar of Events 2016

June 12–15 — **ABA Regulatory Compliance Conference**
Manchester Grand Hyatt Hotel
San Diego, CA

June 15–17 — **EMERGE: Consumer Financial Health Forum**
American Banker and Center for Financial Services Innovation
The Roosevelt New Orleans
New Orleans, LA

September 21–23 — **Biennial Reinventing Our Communities Conference**
Federal Reserve Bank of Philadelphia
Hilton Philadelphia at Penn's Landing
Philadelphia, PA