

Common Violations & Hot Topics

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Agenda

- Regulation C – Home Mortgage Disclosure Act
 - Common violations & risk mitigation strategies
- Regulation B—Equal Credit Opportunity Act
 - Spousal signature violations & risk mitigation strategies
- Regulation H – Flood Insurance
 - Common violations, consequences of noncompliance, & the 2015 final rule
- FTC Act, Section 5 – Unfair or Deceptive Acts or Practices
 - Overview of risks & risk mitigation strategies



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HMDA Reporting

How is HMDA data used?

Determine whether financial institutions are serving community housing needs

Assist public officials in distributing public sector investments to attract private investment areas in need

Identify possible discriminatory lending patterns

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HMDA Reporting Errors

Rate Spread	Action Taken & Date	Property Location	Applicant(s) Data
<ul style="list-style-type: none"> Avoid reporting data for loans not subject to the requirement Limit calculation & data entry errors 	<ul style="list-style-type: none"> Select the appropriate action taken code Develop a standard for date selection 	<ul style="list-style-type: none"> Avoid data entry & address selection errors Employ a reliable system for addresses not easily coded 	<ul style="list-style-type: none"> Report original application information Follow Appx. B to collect information when not provided with in-person applications Report gross annual income relied upon for credit decision

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HMDA Compliance Management

Data reviews & audits

- Use the source of the information rather than boarding documents or worksheets
- Identify and address the root cause of errors
- For systemic errors, review & correct all appropriate lines
- Verify all transactions are reported

Training & staff support

- Ensure regular training for staff involved in reporting of HMDA
- Develop a reliable system for investigation of questions & atypical situations
- Develop internal Q&As & job aids that are readily accessible

Internal routines & controls

- Standardize practices whenever possible, i.e. the note date is the action taken date for originated loans
- Synchronize processes, i.e. adverse action notice date is action taken date
- Automate where possible

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HMDA Looking Ahead

August 2015

Final HMDA rule (based on CFPB's Spring 2015 [Regulatory Agenda](#))

January 2017

Earliest possible data collection under final rule (based on expected issue date & *minimum* 9-month implementation period)

March 2018

Earliest possible data submission under final rule

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HMDA Resources

- 2010 Outlook Live [Tips for Reporting Accurate HMDA and CRA Data](#) and follow-up [Q&A Article](#)
- Consumer Compliance Outlook Articles:
 - [Improving and Using HMDA Data in Your Compliance Program](#) (2009)
 - [HMDA Data Collection and Reporting](#) (2012)
 - [View from the Field: Commonly Cited Compliance Violations in 2011 \(rate-spread loans, loan purpose, and action taken\)](#) (2012)
 - [Government Monitoring Information Requirements Under the HMDA and the ECOA](#) (2013)
- Outlook Live [2014 Consumer Compliance Hot Topics](#)
- [A Guide to HMDA Reporting, Getting it Right!](#) (2013)
- [Proposed HMDA Rule](#)

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Regulation B—Equal Credit Opportunity Act Spousal Signature Violations & Risk Mitigation Strategies

- The Federal Reserve supervises state member banks of \$10B or less for compliance with the Equal Credit Opportunity Act ("ECOA"), which is implemented by Regulation B
- The ECOA and Regulation B prohibit discrimination on the basis of marital status
- Regulation B contains special requirements for spousal signatures on notes or guarantees
- Marital status discrimination is one of the most often cited violations of Regulation B and the source of many fair lending referrals to the U.S. Department of Justice

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Spousal Signatures – General Rule

- The general rule is that a creditor shall not require the signature of an individual applicant’s spouse (other than a joint applicant) on any credit instrument if the individual applicant qualifies under the creditor’s standards of creditworthiness

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Spousal Signatures – Joint Intent

- If spouses intend to jointly apply for credit, the creditor should:
 - Obtain evidence of such intent at the time of application. For example, signatures later obtained on the note may not be used to show intent to jointly apply for credit
 - Use a method that is distinct from the means used to affirm the accuracy of information. For example, signatures on a joint financial statement affirming the veracity of information are not sufficient
 - Consider using the model forms in Appendix B to Regulation B, but ensure the forms are properly completed. For example, failing to have the applicants check the box for joint intent may not provide sufficient evidence

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Spousal Signatures – Exceptions

Secured Credit

- If an individual applicant qualifies for secured credit, the creditor still may require a spousal signature on any instrument reasonably believed to be necessary under applicable state law to ensure access to the property in the event of default
 - For example, if the individual applicant qualifies for a mortgage loan, the creditor may require the spouse’s signature on the mortgage (or other security instrument), but **may not** require the spouse to sign the note

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Spousal Signatures – Exceptions

(continued)

Unsecured Credit

- If an individual applicant relies on property jointly held with a spouse to qualify for unsecured credit, the creditor may require a spousal signature on any instrument reasonably believed to be necessary under applicable state law to ensure access to the property in the event of the death or default of the applicant
 - Note on Valuation: A creditor **may not** request that a non-applicant joint owner spouse sign any instrument **unless** the valuation of the applicant’s interest in the jointly-held property does not support the credit requested

Spousal Signatures – Exceptions

(continued)

“Reasonable Belief”

- Note that the creditor’s “reasonable belief” as to what instrument (security instrument or note) the non-applicant spouse must sign according to state law should be supported by a thorough review of relevant law or an opinion of the state attorney general
- Creditors should obtain the legal analysis *prior* to implementing a policy requiring spousal signatures on the security instrument or note

Spousal Signatures – Exceptions

(continued)

Business Credit

- In the case of a loan to a business, the creditor may require the personal guarantee of the partners, directors, or officers of a business, and the shareholders of a closely held corporation, even if the business is creditworthy
- However, the requirement for a guarantee must be based on the guarantor’s relationship to the business, and not on a prohibited basis
 - For example, the creditor may not require guarantees only of the married officers of the business

Spousal Signatures – Additional Parties

- If an individual applicant does *not* qualify for credit, the bank may require an additional party, such as a co-signer or guarantor, but the creditor **may not** require that the additional party be the applicant’s spouse
 - Note on Renewals: If the borrower’s creditworthiness is reevaluated when the credit is renewed, a creditor **must** determine whether the additional party is still warranted, and, if not, release the additional party

Spousal Signature Requirements

Scenario 1

- Sally Jones applies for a term loan for her small business and provides joint financial statements as part of the application process. The bank adds Sally’s husband to the application, and requires both spouses to sign the note.

Question

- Is this permissible under Regulation B?

Spousal Signature Requirements (continued)

Scenario 1

- Sally Jones applies for a term loan for her small business and provides joint financial statements as part of the application process. The bank adds Sally’s husband to the application, and requires both spouses to sign the note.

Answer

- No, the bank’s practice is not permissible. The creditor may not presume that the submission of joint financial information constitutes an application for joint credit.

Spousal Signature Requirements (continued)

Scenario 2

- The bank provides a loan to ABC Marketing, which is owned by Mark Phillips. The bank's loan officer requires Mark's wife, Sue Phillips, to provide a personal guarantee although she has no relationship to the business. During the bank's exam, the loan officer tells examiners that he "always likes to get the wife's guarantee."

Question

- Is this permissible under Regulation B?

Spousal Signature Requirements (continued)

Scenario 2

- The bank provides a loan to ABC Marketing, which is owned by Mark Phillips. The bank's loan officer requires Mark's wife, Sue Phillips, to provide a personal guarantee although she has no relationship to the business. During the bank's exam, the loan officer tells examiners that he "always likes to get the wife's guarantee."

Answer

- No, the bank's practice is not permissible. If the business is creditworthy, the bank may not require the personal guarantee of a spouse who is not a partner, director, or officer of the business.

Spousal Signature – Risk Mitigation Strategies

- To mitigate the risk of a spousal signature violation and discrimination on the basis of marital status, a bank should:
 - Ensure that there are clear Regulation B policies and procedures for all credit products, including for commercial and agricultural loans. These loans are a frequent source of violations
 - Ensure adequate training for loan officers
 - Obtain adequate written evidence at the time of application of the spouse's intent to jointly apply for credit
 - Obtain appropriate legal analysis prior to implementing spousal signature requirements
 - Conduct periodic reviews or audits for compliance with Regulation B

Signature Requirement Resources

- Consumer Compliance Outlook Articles
 - [Regulation B and Marital Status Discrimination: Are You in Compliance?](#) (2008)
 - [View from the Field: Commonly Cited Compliance Violations in 2011 \(spousal signature & adverse action\)](#) (2012)

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Flood Disaster Protection Act

- 12 CFR § 208.25(c)(1) – Requirement to purchase flood insurance when the loan is secured by a property in an SFHA
- 12 CFR § 208.25(g) – Force placement required by bank any time during the loan term if property not sufficiently covered by flood insurance

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Pattern or Practice Considerations

1. A common cause or source within the financial institution's control (including third party vendors);
2. Grounded in a written or unwritten policy or established practice;
3. Noncompliance occurred over an extended period of time;
4. The relationship of the instances of noncompliance to one another (for example, whether the instances of noncompliance occurred in the same area of a financial institution's operations);

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Pattern or Practice Considerations

(continued)

- 5. The number of instances of noncompliance is significant relative to the total number of applicable transactions;
- 6. A financial institution was cited for violations of the NFIA and Regulation H during prior examinations;
- 7. Financial institution's internal and/or external audit process had not identified and addressed deficiencies in its flood insurance compliance; and
- 8. The financial institution lacks generally effective flood insurance compliance policies and procedures and/or a training program for its employees.

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Civil Money Penalties

- 12 CFR § 208.25(c) requirement to purchase flood insurance where available
- 12 CFR § 208.25(e) requirement involving escrowing of flood insurance premiums
- 12 CFR § 208.25(g) force placement of flood insurance
- 12 CFR § 208.25(i) notice of special flood hazards and the availability of federal disaster relief assistance
- 12 CFR § 208.25(j) notice of servicer and any change of servicer

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Civil Money Penalties *(continued)*

- The maximum CMP amount allowed under the Flood Disaster Protection Act, as amended by the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act), is \$2,000 per violation
- Violations that ended prior to the Biggert-Waters Act enactment date, July 6, 2012, are subject to a maximum CMP of \$385 per violation

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Flood Insurance Final Rule

Coverage Exemption: Detached, Nonresidential structures*

used primarily for personal, family, or household purposes

Residential property:

not joined by any structural connection to the residential structure

Detached:

generally does not include sleeping, bathroom, or kitchen facilities

Nonresidential:

*Eff. 3/21/14 Enactment of HFIAA



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Flood Insurance Final Rule (continued)

Force placement of flood insurance*

- Servicer *may* force place on the date coverage becomes inadequate
- Servicer *must terminate* force-placed coverage when borrower obtains coverage & *refund* premiums & fees charged during overlap

*Eff. 7/6/12 Enactment of Biggert-Waters Flood Insurance Reform Act



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Flood Insurance Final Rule (continued)

Mandatory Escrow of Flood Insurance Premiums
Effective for loans made, increased, extended, or renewed beginning January 1, 2016

Small Lender Exception:

Less than \$1 billion in assets

AND prior to 7/6/12, Not otherwise required by law to escrow for taxes & insurance

AND no policy of escrowing for taxes and insurance

Loan-related Exceptions:

Commercial or agricultural purpose

Subordinate liens with coverage in connection to first lien

Coverage provided through a governing association

HELOCs

Nonperforming loans (>90 days)

Terms of ≤ 12 months



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Flood Insurance Final Rule *(continued)*

Escrow Outstanding Loans at Borrower's Option By June 30, 2016

Servicer provides borrower option to escrow

Delivers or mails notice by 6/30/16
(Appendix B includes model clauses)

Receives borrower's request & begins escrow 'as soon as reasonably practicable'

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Flood Resources

- [Flood Insurance Rule](#)
- [CA 09-3](#): Interagency Q&A Regarding Flood Insurance
- [2011 Updates](#) to *Interagency Q&A Regarding Flood Insurance*
- [CA 13-2](#): Interagency Statement on the Impact of Biggert-Waters Act
- [CA 14-3](#): Interagency Statement on Increased Maximum Flood Insurance Coverage for Other Residential Buildings
- Outlook Live [2014 Consumer Compliance Hot Topics](#)
- [FDIC Banker Teleconference](#): Interagency Update on Mandatory Purchase Flood Insurance Purchase Requirements (December 2014)

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UDAP Examples

- Mortgage – Collecting PMI for uninsured loans
- Mortgage – Income fraud
- Mortgage – Unearned discount points
- Mortgage – Loan billing practices
- Credit Card – Debt collection, marketing
- Overdrafts – Automatic enrollment with limited disclosures/monitoring/controls
- Deposit – CD renewal rate lower than disclosed
- Deposit – Omission of material information on student accounts

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Product Lifecycle

Management Considerations	Incorporates the strategic thinking behind the establishment or development of a particular product, as well as any components tied to the product development (including controls, compensation, platforms, etc.) and the end benefit of the product to the institution
Product Design	Addresses the process of developing the actual product and specific considerations with regards to niche, profitability and fee structure
Marketing	Outlines the manner in which the product is targeted and marketed
Initial Interface	Incorporates the components of the initial interface, including the selling and/or application process



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Product Lifecycle *(continued)*

Origination or Consummation	Describes the process by which a customer is qualified for and/or obtains the product and enters into a contract
Usage	Incorporates any and all aspects of a product after the origination or consummation stage. Includes servicing, maintenance, dispute and resolution, changes in terms, default or misuse, additional fee infrastructure or other cost
Termination	Addresses the process of the consumer voluntarily ending the contract, or the institution's process of exiting the consumer from the product due to unfulfilled contractual provisions, or any other process whereby the relationship between the consumer and the product is severed



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Managing UDAP Risk in Third-Party Relationships

Select third parties carefully & actively oversee

Assess UDAP risk when selecting third parties	<ul style="list-style-type: none"> Consider the ability of the consumer to understand the product or service offered Consider the operations & internal controls of the third party
Assess UDAP risk when monitoring third parties	<ul style="list-style-type: none"> Consider consumer complaints & resolution Consider audit reports & other testing or evaluations



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UDAP Resources

- 2013 Outlook Live [UDAP— Analysis, Examinations, Case Studies, and Emerging Risks](#)
- [CA Letter 04-2](#): FRB and FDIC Joint Statement re Unfair or Deceptive Acts or Practices by State-Chartered Banks
- [CA Letter 05-2](#): Interagency Guidance on Overdraft Protection Programs
- [CA Letter 07-8](#): Consumer Compliance Examination Procedures for the Unfair or Deceptive Acts or Practices Provisions of Section 5 of the Federal Trade Commission Act
- [CA Letter 13-21](#): Guidance on Managing Outsourcing Risk
- [CA Letter 14-5](#): Interagency Guidance Regarding Unfair or Deceptive Credit Practices

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Questions?

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