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CFPB EXPANDS SMALL CREDITOR AND RURAL AREA EXCEPTIONS

On September 21, 2015, the CFPB issued a final rule amending the definitions of “small creditor” and “rural and underserved areas” which should be beneficial to many community banks and other small mortgage lenders. Small creditors operating predominately in rural and underserved areas are exempt from compliance with certain provisions of the 2013 mortgage rules. For example, the current rules extend Qualified Mortgage status to loans that small creditors hold in their portfolio even if the consumer’s debt to income ratio exceeds 43%, and small creditors can originate Qualified Mortgages with a balloon payment under a temporary exception. Small creditors that serve predominantly rural and underserved areas can originate Qualified Mortgages with a balloon payment, can originate high-cost mortgages with a balloon payment, and are not required to establish escrow accounts for higher-priced mortgages. The CFPB’s stated goal for changing the definitions is to “increase the number of financial institutions able to offer certain types of mortgages in rural and underserved areas, and give small creditors time to adjust their business practice to comply with the rule.”

The final rule will increase the origination limit from 500 first-lien mortgage loans to 2000. This amount will not include loans held in portfolio by the creditor and its affiliates. The CFPB made this change because of the importance of small creditors making portfolio loans that larger creditors may not be willing to make or for which a secondary market may not be available.

The current \$2 billion asset limit for small-creditor status will remain, but the final rule requires that assets of mortgage originating affiliates now be included in this calculation. This is based on the creditor’s total assets as of the end of the preceding calendar year, and the threshold will continue to be adjusted annually for inflation. The CFPB also expanded the definition of “rural area” to include census blocks that are not in an urban area, as opposed to the current list including counties only. Two new safe harbors are also added for making the determination of rural areas. First, a creditor may rely on two new automated tools that will be on the CFPB’s website. Creditors may also continue to rely on the county lists on the CFPB’s website. The determination of whether a creditor operates predominately in rural or underserved areas has been changed from any of the three preceding years to the immediately preceding year.

The final rule establishes a grace period for creditors that either exceed the origination limit, asset limit or fail to operate predominately in rural and underserved areas. If the determination is made as of December 31 of a

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certain year that the creditor no longer meets one or more of the requirements for treatment as a small creditor, then the creditor may continue to treat applications received before April 1 of the following year as though the small creditor status remains in place. In other words, the creditor will have until April 1 to comply with all requirements in place for lenders without small creditor status.

The temporary exemption for small creditors to make balloon-payment Qualified Mortgages currently is set to expire on January 10, 2016; however, the new, final rule extends the exemption to applications received before April 1, 2016.

These changes go into effect as of January 1, 2016.

(Memrie Fortenberry)

RECENT CFPB DEVELOPMENTS

MARKETING SERVICES AGREEMENTS.

On October 8, 2015, the CFPB issued Compliance Bulletin 2015-05 which deals with RESPA compliance issues and the use of Marketing Services Agreements. A Compliance Bulletin is basically an expression of the CFPB's opinion regarding a certain subject. It is not a rule making and does not require any comment period. Nevertheless, it expresses the thinking of the CFPB and, in the case of Marketing Services Agreements ("MSA's"), their thoughts are highly critical.

The law involved is the Real Estate Settlement Procedures Act ("RESPA") which has been in effect since 1974 and, among other things, prohibits kickbacks or referral fees in connection with the provision of real estate settlement services. RESPA provides for both civil and criminal penalties.

"Settlement Services" under RESPA includes title searches, title insurance, the services of an attorney, document preparation, surveys, credit reports, appraisals, inspections, broker services, real estate agent services, loan origination activities, loan processing, and loan underwriting activities. So pretty much all real estate lending activities are covered.

The basic prohibition is contained in Section 8(a) of RESPA which prohibits any "fee, kickback or thing of value" to be given in return for the referral of a settlement service. It becomes complicated when RESPA goes on to say, "nothing in this section shall be construed as prohibiting ... the payment to any person of a bona fide salary or compensation or other payment for goods or facilities or for services actually performed."

So what does this mean?

The CFPB in its Compliance Bulletin lists a number of examples of Marketing Services Agreements or similar arrangements that have resulted in enforcement actions against a variety of settlement service providers. It points out that every case is potentially different and will involve a fact-intensive inquiry. It does not prohibit Marketing Services Agreements in every instance. And yet the Compliance Bulletin does not give even one example of a Marketing Services Agreement that would pass muster. In a telling assessment, the CFPB states, "nevertheless, any agreement that entails exchanging a thing of value for referrals of settlement services business involving a federally-related mortgage loan likely violates RESPA, whether or not an MSA or some related arrangement is part of the transaction." That language would seem to foretell the outcome of any regulatory agency inquiry into a joint marketing services arrangement.

The Compliance Bulletin provides a sample of instances that have led to enforcement actions in the past. The list is merely representative:

- Steering of business in return for kickbacks and referral fees;
- Failing to disclose an affiliate relationship with an appraisal management company;
- Failing to tell consumers that they have the option of shopping for services before directing them to an affiliate;
- Taking payments from settlement service providers without performing any contractually-obligated services;
- A settlement service provider defraying marketing expenses of a mortgage lender; and
- Marketing to settlement service providers in an effort to create more Marketing Services Agreements.

The CFPB concluded its guidance by stating that Marketing Services Agreements necessarily involve substantial legal and regulatory risk that is less capable of being controlled by careful monitoring than previously thought.

The result is a strong warning that Marketing Service Agreements, especially lucrative ones, are very likely to draw regulatory criticism and perhaps the civil and criminal penalties provided by RESPA.

ARBITRATION. In a separate move, the CFPB announced that it was considering proposing rules that would ban financial services providers from using arbitration agreements that block consumers from pursuing class action claims.

Nationwide, many credit card, loan and deposit account agreements contain arbitration agreements that allow either the consumer or the financial service provider to require that any dispute be resolved by arbitration instead of

litigation. Class actions on behalf of numerous customers that are similarly situated are prohibited. The prohibition against the practice of joining numerous small claims into one massive lawsuit was what largely propelled the use of arbitration agreements. That was certainly the case in Mississippi a number of years ago.

The Dodd-Frank Act required the CFPB to perform a study of the use of arbitration agreements and gave the CFPB the power to issue regulations to address that practice. Although there are a few more steps that must be taken, it seems clear that the CFPB will require significant changes to the arbitration agreement process which may severely limit the benefits of arbitration.

It is possible that arbitration agreements may continue to exist, but will be required to specifically provide that they do not prevent or limit the filing of a class action lawsuit. While the arbitration of an individual claim that does not rise to class action status will continue to have many benefits, you have to wonder about the process of informing consumers, and their attorneys, that they can avoid the arbitration process by simply filing suit as a class action. Of course there are procedural protections that prevent frivolous class action claims, and in some cases a class action can actually serve to eliminate much of the risk of a multitude of small, individual claims being asserted. However, the very thought of “class action” in most cases proves frightening and in the past has been used as a tactic to try to force large and early settlement offers.

The CFPB is not all wrong when it says that many small claims just can’t be pursued on an individual basis and that class actions are the only way for consumers to get relief. Nevertheless, it also seems clear that lawyers for class action plaintiffs are likely to be the biggest beneficiaries, and it may not lead to significant benefits to consumers if arbitration

disappears from the consumer financial services sector.

We will keep you posted on the CFPB's final action.

HMDA FINAL RULE. Finally, the CFPB finalized its proposed Rule amending Regulation C which implements the Home Mortgage Disclosure Act. This change was also mandated by the Dodd-Frank Act and seeks to require disclosure of significantly more information about a covered bank's closed-end mortgage loan and open-end lines of credit secured by a dwelling.

This action continues a trend in recent years of increasing the number of data points required to reported, which can in turn be correlated to such discriminatory lending issues as race, national origin, age, and gender of a bank's customer base.

Among the new data points added are the applicant's or borrower's age, credit score, automated underwriting system information, unique loan identifier, property value, application channel, points and fees, borrower-paid origination charges, discount points, lender credits, loan term, prepayment penalty, non-amortizing loan features, interest rate, MLO identifier, and others. Changes are also made to the manner in which the borrower's ethnicity, race and gender data are collected and recorded.

This latest rule will have a significant impact on your compliance function since much more data must be collected, recorded, verified and reported. But the most important impact could come as a result of the expanded regression analysis that the regulators will be able to conduct when scoping your Fair Lending exams. That review will be complicated further when the regulators compare your data to that of a group of your "peer" banks. This will add to the real need for banks to know their numbers

in advance and be able to explain them to the regulators or defend them if need be.

(Ed Wilmesherr)

DOD EXPANDS MILITARY LENDING ACT RULES

In July 2015, the U.S. Department of Defense issued a final rule expanding the scope of its Military Lending Act (MLA) regulations. The MLA imposes an interest rate limit on extensions of consumer credit made to covered borrowers. The MLA also places conditions and disclosure requirements on lenders who extend consumer credit to covered borrowers. The final rule makes changes to the definition of consumer credit and to lender disclosure requirements and puts in place two new safe harbors available to lenders when making the determination of whether a borrower is a covered borrower for purposes of the MLA.

Coverage. Currently, consumer credit covered by the existing rule is limited to short term, low dollar, closed-end payday type loans; vehicle title loans with terms of 181 days or less; and tax refund anticipation loans. Under the new rules, the definition of "consumer credit" is expanded to include all types of credit covered by Regulation Z/Truth-in-Lending with a couple of exceptions. The final rule covers any extension of credit for personal, family or household purposes to an active-duty service member or dependent that is subject to a finance charge or payable by written agreement in more than four installments. Residential mortgages and purchase money transactions secured by automobiles and other personal property are still excluded. The new rule now covers most types of consumer credit including student loans and overdraft lines of credit. Open-end credit, such as a credit card account, was previously exempt under the MLA. Credit card accounts are no longer exempt, but the rule does not apply to credit card accounts until October 3, 2017, with

the possibility of an additional one year extension to be considered later.

Covered Borrower. The final rule only applies to extensions of credit to a “covered borrower” which is a member of the armed forces on active duty or on active Guard and Reserve duty, and their dependents. Dependents can include the spouse and child, and in some cases, a parent or parent-in-law or an unmarried person in the legal custody of the servicemember. The existing rule provides a safe harbor for a lender in making the determination of whether a borrower is a covered borrower by obtaining the borrower’s self-certification in a Covered Borrower Identification Statement. That safe harbor will expire on October 3, 2016, but the final rule makes two new safe harbors available. Lenders may conduct a covered-borrower check by using information obtained either from the MLA database or from information in a consumer report from a nationwide consumer reporting agency to determine whether the borrower is a covered borrower. If one of these sources is used and the lender complies with the appropriate time and recordkeeping requirements in the final rule, then a safe harbor will be granted.

MAPR. Consumer credit to a covered borrower is limited to a 36% Military Annual Percentage Rate (MAPR), which is an all-inclusive rate and includes many charges that are excluded from the finance charge and APR under Reg. Z. The final rule provides some guidance in calculating the MAPR and eliminates some prior finance charge exceptions. For closed-end credit, the MAPR is calculated in the same way as the APR under Reg. Z except that it must also include any charges for credit insurance, debt cancellation or suspension products, application fees, participation fees, and fees for any ancillary products sold in connection with the credit extension.

The MAPR for open-end credit is calculated in the same way as the effective APR for a billing

cycle under Reg. Z and includes all of the fees included for closed-end credit. As a result, a fee may not be charged in a billing cycle where there is no balance except for a participation fee not in excess of \$100 per year. And, the final rule carves out of the MAPR certain credit card fees -other than a periodic rate- such as application fees, participation fees, or transaction-based fees if the fee is bona fide and reasonable. Reasonableness is determined by comparing the fee with fees typically imposed by other creditors for a similar product. A safe harbor is provided for a fee that is not more than the average amount charged by 5 or more creditors who have U.S. credit cards with outstanding balances totaling at least \$3 billion at any time during the 3-year period preceding the time the average is computed. This exclusion does not apply to credit insurance premiums, debt cancellation or debt suspension fees, or any ancillary product fees. And, if a creditor charges any fee that is not bona fide or reasonable in addition to a finance charge included in the MAPR, then the total amount of all fees must be included in the MAPR even if some of the fees might have otherwise been excluded.

Disclosures. The disclosure requirements were amended in several ways. First, the requirement for clear and conspicuous disclosures was removed. Second, the final rule simplifies the information a creditor must provide. In addition to disclosures required by Reg. Z, a creditor must provide a statement of the MAPR that describes the charges the creditor may impose, but the creditor will no longer be required to provide the computed MAPR or the total dollar amount of the charges. Instead, the final rule provides a model statement describing the MAPR, and a creditor may use the model statement or a substantially similar statement. Also, the requirement for creditors to provide a specific statement regarding protections available under federal law was removed.

The creditor must also provide a clear description of the payment obligation, which can be satisfied by using the payment schedule or account-opening disclosures under Reg. Z. In addition to the written disclosures required, the creditor must provide orally the statement of the MAPR and the description of the payment obligation. However, a creditor may now provide the oral disclosures either in person or by providing a toll-free number the borrower may use to obtain the disclosures. If the creditor elects to provide a toll-free number, it must include that number on the application form or with the statement of the MAPR.

Limitations and Prohibitions. Creditors are prohibited from requiring covered borrowers to submit to arbitration and any arbitration provision is unenforceable. A creditor other than a bank, savings association or credit union is prohibited from accepting a vehicle title as security for a loan and from rolling over or renewing covered consumer credit with new covered consumer credit by the same lender. Creditors are prohibited from: using a check or other means of accessing a deposit account, except for a security interest in funds deposited after the extension of credit; requiring use of an allotment to repay the obligation; imposing any prepayment penalty on covered credit; or requiring covered borrowers to waive any right to legal recourse under any state or federal law, including the SCRA.

Penalties. If a creditor fails to comply with the MLA, then the contract with the borrower is deemed void from inception. Also, creditors may be exposed to civil liability for violations including actual damages of not less than \$500 per violation, punitive damages and declaratory relief as allowed by a court, and reasonable attorneys' fees and expenses. Criminal penalties are provided for knowing violations.

Effective Date. The final rule is effective as of October 1, 2015 but only applies to consumer credit transactions with a covered borrower

entered into on or after October 3, 2016. In addition, credit card accounts are not included in the definition of "consumer credit" until October 3, 2017. The civil liability provisions apply to consumer credit extended on or after January 2, 2013.

(Memrie Fortenberry)

MSRCG MEETING TO BE HELD ON NOVEMBER 17, 2015

The MSRCG will hold its November Annual Meeting on November 17, 2015, at The Racquet Club of Memphis in the Large Ballroom located at 5111 Sanderlin Avenue, Memphis, Tennessee. Registration will begin at 9:00 a.m. with the meeting to begin at 9:30 a.m.

During the November meeting, we feature an outstanding panel of speakers from the Federal Reserve, the FDIC and the OCC. Christine Anderson (FDIC) and Anita Albright-Gaymon will cover a variety of BSA topics such as transaction testing and monitoring for suspicious activity. (Note: The BSA section will be from 2:00-3:00.) Meredith Anderson (Fed. Res.), Polly Radford and Basil Carroll (FDIC) will cover a variety of topics including revisions to flood insurance requirements and UDAAP issues, vendor risk management and error resolution procedures. Our speakers will also share observations about recent compliance exams for issues like the Ability-to-Repay and QM rules.

We are also excited that Kevin Henry (FED), Julie Banfield and Chris Finnegan (FDIC), and Joe Meade (FDIC – BSA) will be coming to the meeting.

As always, the dress code for this occasion is casual, and lunch will be provided. We ask that you fax or e-mail your registration to Liz

Crabtree no later than Thursday, November 12, 2015, so that arrangements for lunch can be finalized. We look forward to seeing you there.

(Ed Wilmesherr)

**MRCG MEETING
TO BE HELD ON NOVEMBER 19, 2015**

The MRCG will hold its November Annual Meeting on November 19, 2015, at the Mississippi Sports Hall of Fame & Museum Conference Center, 1152 Lakeland Drive, Jackson, Mississippi. Registration will begin at 9:00 a.m. with the meeting to begin at 9:30 a.m..

During the November meeting, we will feature an outstanding panel of speakers from the Federal Reserve, the FDIC and the OCC. Christine Anderson (FDIC) will cover a variety of BSA topics such as transaction testing and monitoring for suspicious activity. (Note: The BSA section will be from 2:00-3:00.) Meredith Anderson (Fed. Res.), Michael Edwards (OCC), and Basil Carroll (FDIC) will cover a variety of topics including revisions to flood insurance requirements and UDAAP issues, vendor risk management and error resolution procedures. Our speakers will also share observations about recent compliance exams for issues like the Ability-to-Repay and QM rules.

We are also excited that Kevin Henry (FED) and Chris Finnegan (FDIC) will be coming to the meeting.

As always, the dress code for this occasion is casual, and lunch will be provided. We ask that you fax or e-mail your registration to Liz Crabtree no later than Friday, November 13, 2015, so that arrangements for lunch can be finalized. We look forward to seeing you there.

(Ed Wilmesherr)

MRCG-MSRCG COMPLIANCE CALENDAR

10/03/2015 – TRID regulations effective	05/19/2016 – MRCG Quarterly Meeting
11/17/2015 – MSRCG Annual Meeting	05/24/2016 – MSRCG Quarterly Meeting
11/19/2015 – MRCG Annual Meeting	07/21/2016 – MRCG/MSRCG Joint Steering Committee Meeting
01/01/2016 – Flood insurance escrow rules effective	08/18/2016 – MRCG Quarterly Meeting
01/01/2016 – Reg. Z changes to small creditor serving rural/underserved areas effective	08/23/2016 – MSRCG Quarterly Meeting
01/21/2016 – MRCG/MSRCG Joint Steering Committee meeting	09/15/2016 – MRCG/MSRCG Joint Steering Committee Meeting
04/01/2016 – Small creditor temporary balloon QM exception expires	11/15/2016 – MSRCG Annual Meeting
06/30/2016 – Deadline for notices re: option to escrow flood premiums for existing loans	11/17/2016 – MRCG Annual Meeting
10/03/2016 – DoD MLA consumer credit rules effective	01/01/2017 – HMDA exception for low volume depository institutions effective
02/18/2016 – MRCG Quarterly Meeting	10/03/2017 – MLA coverage expands to include credit cards
02/23/2016 – MSRCG Quarterly Meeting	01/01/2018 – Revised HMDA data collection begins
04/21/2016 - MRCG/MSRCG Joint Steering Committee meeting	01/01/2019 – Revised HMDA data reporting begins