



BANKING ON A SOLID FOUNDATION

# COMPLIANCE PIPELINE

## Homeowner Flood Insurance Affordability Act of 2014

April 30, 2014

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On March 24, 2014 legislation entitled the Homeowner Flood Insurance Affordability Act of 2014 (HFIAA) was passed to delay the implementation of certain provisions of the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters). One primary purpose of the HFIAA is to reinstate lower insurance rates for grandfathered properties that were repealed under Biggert-Waters mandates. Under Biggert-Waters, flood insurance rates were significantly increased to offset the financial instability of the NFIP and to more accurately represent the risk. This change is intended to provide consumer relief and to provide more time for Congress, FEMA, and the insurance industry to determine a better long term solution to bring solvency back to the NFIP.

In addition, the HFIAA extends the effective date for new escrow rules required under Biggert-Waters from July 6, 2014, to January 1, 2016 and provided additional clarifications on the applicability of such rules. In the proposed joint agency regulations, the escrow requirement would also have applied to “outstanding loans” after the effective date. However, language in the bill clarifies that escrow requirements would apply only to loans originated, refinanced, increased, extended, or renewed on or after January 1, 2016. Creditors and/or servicers of “outstanding loans” on or after January 1, 2016 will be required, however, to offer and make available the borrower’s option to have escrow for required flood insurance.

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## Foreign Sanctions Evaders List Update

The U.S. Department of the Treasury has recently released an update to the Foreign Sanctions Evaders (FSE) list. The FSE list is published by the Office of Foreign Assets of Control (OFAC) and includes a list of foreign individuals and entities determined to have violated, conspired to violate, or caused a violation of U.S. sanctions on Syria or Iran. Transactions by U.S. persons or within the United States involving persons sanctioned under this authority are prohibited, effectively cutting the listed persons off from the U.S. marketplace and financial system. The FSE list is not part of the Specially Designated Nationals (SDN) list; however, individuals and companies on the FSE list may also appear on the SDN List.

Financial institutions are required to have policies and procedures in place to ensure that they do not conduct business with anyone listed on the FSE list. If a financial institution currently holds an account for a listed person, the account should not be blocked. A U.S. person may not provide or procure goods or services, including financial services, or technology to or from a listed person without authorization from OFAC, unless the transaction is otherwise exempt from regulation.

For a copy of the list and further questions visit: [http://www.treasury.gov/resource-center/sanctions/SDN-List/Pages/fse\\_list.aspx](http://www.treasury.gov/resource-center/sanctions/SDN-List/Pages/fse_list.aspx)

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## FinCEN Advisory FIN-2013-A008

On October 18, 2013, the Financial Action Task Force (FATF) updated its list of jurisdictions with strategic anti-money laundering or combating the financing of terrorism (AML/CFT) deficiencies. These changes may affect U.S. financial institutions' obligations and risk-based approaches with respect to relevant jurisdictions. As stated within the advisory, financial institutions are expected to develop and implement additional due diligence procedures with respect to the jurisdictions listed within the advisory to further protect the international financial system from AML/CFT risks.

Financial institutions should ensure that their enhanced due diligence programs include, at a minimum, steps to:

- Conduct enhanced scrutiny of correspondent accounts to guard against money laundering and to identify and report any suspicious transactions, in accordance with applicable law and regulation

- Determine whether the foreign bank for which the correspondent account is established or maintained in turn maintains correspondent accounts for other foreign banks that use the foreign correspondent account established or maintained by the covered financial institution and, if so, take reasonable steps to obtain information relevant to assess and mitigate money laundering risks associated with the foreign bank's correspondent accounts for other foreign banks, including, as appropriate, the identity of those foreign banks
- Determine, for any correspondent account established or maintained for a foreign bank whose shares are not publicly traded, the identity of each owner of the foreign bank and the nature and extent of each owner's ownership interest.

For more information visit: [http://www.fincen.gov/statutes\\_regs/guidance/html/FIN-2013-A008.html](http://www.fincen.gov/statutes_regs/guidance/html/FIN-2013-A008.html)

## Homeowner Flood Insurance Affordability Act of 2014 (Continued from Page 1)

Under the HFIAA, escrows will be optional on:

- Second liens (if proper coverage is in place in connection with the first lien)
- Condo and co-op loans where there is a residential condominium building association policy with adequate flood insurance
- HELOCs
- Commercial purpose loans secured by a residence
- Nonperforming loans
- Loans with a term of 12 months or less

An overview of the proposed regulations to implement Biggert-Waters was included in the October 31, 2013 edition of the Compliance Pipeline. There will be significant changes to the NFIP Program and to the flood regulations before they are finalized to implement the changes made by the HFIAA.

To prepare for these changes, it is recommended that a Bank monitor for additional changes in flood insurance law, regulations, and guidance as well as begin assessing the impact to loan origination, servicing, and customer service.

FEMA has dedicated a webpage on its site to keeping interested parties informed about developments in flood insurance laws and regulations.

<http://www.fema.gov/flood-insurance-reform>

We will provide a detailed analysis of these new requirements in a later edition once the joint agency regulations are finalized to implement the changes mandated by the HFIAA.



## Small Entity Compliance Guides

The Consumer Financial Protection Bureau (CFPB) published several small entity compliance guides to help with the implementation of the Dodd - Frank Mortgage Rules covering ATR/QM, escrow rules, ECOA evaluations, TILA & RESPA servicing, and several more areas. The CFPB continued to update these small entity compliance guides as the final rules became effective. If you are utilizing these guides make sure you have the most updated copies as most have an effective date of January 2014. To review the most updated small entity compliance guides click the link below.

<http://www.consumerfinance.gov/regulatory-implementation/title-xiv/>



## Updated Handbooks

The CFPB announced the availability of three revised consumer publications, including a consumer information brochure and two booklets required under the Real Estate Settlement Procedures Act (RESPA), Regulation X, and the Truth in Lending Act (TILA), Regulation Z. These publications are titled: What You Should Know About Home Equity Lines of Credit, the Consumer Handbook on Adjustable-Rate Mortgages, and the Shopping for Your Home Loan: Settlement Cost Booklet.

Those who provide these publications may, at their option, immediately begin using the revised HEL-OC Brochure, CHARM Booklet, or Settlement Cost Booklet, or suitable substitutes to comply with the requirements in Regulations X and Z. The Bureau understands, however, that some may wish to use their existing stock of publications. Therefore, those who provide these publications may use earlier versions of these publications until existing supplies are exhausted.

## ATR Concerns Relative to Construction Lending

Ability to Repay (ATR) requirements under Regulation Z, Truth in Lending Act may be the most significant hardship of the Dodd – Frank act for community banks and their customers in relation to outstanding balloon notes. The ATR requirements do not apply to a temporary or "bridge" loan with a term of 12 months or less, such as a loan to finance the purchase of a new dwelling where the consumer plans to sell a current dwelling within 12 months or a loan to finance the initial construction of a dwelling. Caution must be used when employing this exception for temporary or "bridge" loans as they generally result in a balloon due at maturity.

Community banks should take special care to ensure that the origination of a temporary loan is nevertheless evaluated for repayment ability. Significant issues can arise when the initial construction of a dwelling is completed and the borrower is unable to obtain financing under the ATR rules. It is recommended that community banks use caution

when originating construction loans as they may be ultimately faced with a situation where the bank cannot prove repayment ability on paper using verifiable information once the balloon matures. The same holds true for temporary loans where a borrower is trying to sell a former dwelling. As a fail-safe, proper underwriting under the Bank's internal ATR rules should be considered even with construction loans and temporary loans.



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## Reg E Opt In and UDAAP?

In most instances, account opening is where the customer is given the opportunity to decide if he or she wants to participate in the overdraft privilege program and opt-in for Regulation E purposes. As a precaution to giving new customers immediate access to the overdraft protection program, many institutions have instituted a 30-45 day time frame to monitor the customer's account activity and determine if overdraft protection is appropriate for that customer. This is a safe and sound banking practice that is looked favorably upon by examiners. However, it is important that banks review customers' opt-in decisions when determining that overdraft protection is **not** appropriate.

When the customer does not meet initial eligibility of the overdraft program or if an existing customer is suspended from the program, the customer should be opted out for Regulation E. Even though a customer has previously opted-in for one time debit card and ATM overdrafts, the bank has decided not to extend overdraft protection to that customer. Continuing to allow customers to overdraw

their account and charging a fee for one time point of sale or ATM transactions after removing the overdraft program service is a possible UDAAP violation and could lead to reimbursement of funds. The primary deceptive or abusive practice noted would be the fact that the bank doesn't permit the customer to have access to overdraft services but still retains the ability to charge for one-time debit card / ATM overdrafts in force pay situations that would have otherwise been declined. The customer's Regulation E opt-in should move in concert with the availability of an overdraft program (e.g. if the customer does not have the overdraft service at a particular time they should not be opted-in for Regulation E). It is strongly encouraged that all banks review their Regulation E opt-in procedures when customers do not maintain good standing or are suspended from overdraft programs to avoid potential UDAAP violations. Please remember many varieties of overdraft services exist and if you have any questions please contact Steve H. Powell & Company.

## Regulation E Consumer Liability

Regulation E error disputes, as with any situation where a bank may debit funds from a consumer, always draws the scrutiny of regulators during exams. Debit card disputes are particularly frustrating because more often than not, the bank is left holding the bag. However, Regulation E does provide specific instances where the consumer may be held liable. From the commentary, "The extent of the consumer's liability is determined **solely** by the consumer's promptness in reporting the loss or theft of an access device. No agreement between the consumer and an institution may impose greater liability on the consumer for an unauthorized transfer than the limits provided in Regulation E."

Section 1005.6(b) describes the consumer's liability in detail for the loss or theft of an access device:

- **Timely notice given:** If the consumer notifies the financial institution within two business days after learning of the loss or theft of the access

device, the consumer's liability shall not exceed the lesser of \$50 or the amount of unauthorized transfers that occur before notice to the financial institution.

- **Timely notice not given:** If the consumer fails to notify the financial institution within two business days after learning of the loss or theft of the access device, the consumer's liability shall not exceed the lesser of \$500 or the sum of:
  - (i) \$50 or the amount of unauthorized transfers that occur within the two business days, whichever is less; and
  - (ii) The amount of unauthorized transfers that occur after the close of two business days and before notice to the institution, provided the institution establishes that these transfers would not have occurred had the consumer notified the institution within that two-day period.

### Regulation E Consumer Liability (Continued from previous page)

It is important to note the details of when timely notice is not given. Many bankers incorrectly assume that if the customer does not notify the bank within two days of the loss or theft of a device that the consumer's liability automatically increases to \$500. However, that is not the case. Regardless of when notice is given, the customer can only be held liable for \$50 or the amount of the unauthorized transactions, whichever is less, during the two business days. The \$500 liability only applies to **charges that occurred after** the two business day period when he or she first learned of the theft.

For example, if the customer notes two \$500 unauthorized transactions that occur on Monday, but does not report the loss of the card until Friday, the maximum amount of consumer liability is \$50 because no additional transactions occurred after the 2<sup>nd</sup> business day. In the same example, if a subsequent \$300 transaction had occurred on Thursday, the total consumer liability would be \$350 (\$50 during the two business days and \$300 for charges after the two business days where the bank could have prevented the loss had the bank been aware.)

It is important to remember that the \$50 and \$500 consumer liability limits only apply to lost or stolen access devices. If the bank uses VISA or MasterCard debit cards, it is recommended that the bank review the contract for situations where Zero Liability applies. If the consumer reports fraud, the bank cannot hold the customer liable for any amount unless it is not reported within 60 days of the statement date which contains the unauthorized electronic fund transfer. If the customer does not re-

port the fraud within 60 days, the consumer's liability shall not exceed the amount of the unauthorized transfers that occur after the close of the 60 days and before notice to the institution, and that the institution establishes would not have occurred had the consumer notified the institution within the 60-day period.

For instance, assume a consumer statement drops on January 1, 2014 with a \$100.00 fraudulent transaction on the preceding 28<sup>th</sup> of the month (12/28/13). If the cycle continues for the next four months resulting in \$500.00 of fraudulent transactions as of the May 1, 2014 statement, the bank is responsible for the first three fraudulent transactions 12/28/13, 1/28/14 & 2/28/14 as they happened within 60 days of the first statement containing the fraudulent activity. Subsequently, total consumer liability would be in place after the 2/28/14 transaction until the bank was notified of the activity by the consumer.

Again, error disputes are an increasingly frustrating topic for banks as more often than not the bank finds itself absorbing a loss. It is important to review the specifics on consumer liability so the bank doesn't find itself not only reimbursing a customer but explaining the situation to an examiner.

**Email us at [compliancnewsletter@shpco.net](mailto:compliancnewsletter@shpco.net) with any questions or comments.**

**Visit our website at [www.shpco.net](http://www.shpco.net) to register your email for the Compliance Pipeline!**

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