COMPLIANCE PIPELINE

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Prepaid Cards and CIP

The CIP requirements for purchasers and holders of prepaid cards were never formally addressed by regulatory guidance which lead to a level of ambiguity in the industry. The standard practice was to maintain a gift card log, documenting the information required for the sale of monetary instruments. However, as the use of gift cards proliferates, regulators have become increasingly apprehensive about the potential for criminals to utilize them as a medium of exchange for illicit activities.

On March 21, 2016, a joint agency press release issued guidance for applying customer identification requirements on holders and purchasers of prepaid cards. The guidance requires banks to apply CIP requirements to purchasers and holders of reloadable prepaid cards or cards with access to credit or overdraft features. The requirements do not apply, however, to non-reloadable gift cards or cards without overdraft and credit features.

The guidance further addresses the CIP requirements for payroll and health benefit cards. For both payroll and health benefit cards, financial institutions need to apply the CIP rules to the employer and consider them a customer if they are the only party permitted to deposit funds onto the cards. If the employee possesses the ability to reload or deposit funds onto the account, CIP rules would apply to them also. To determine if the CIP rules apply to a specific customer or transaction, one must decide if the bank is establishing an "account" for the party involved. As noted above, an "account" would be established for the party involved if they have the ability to reload the card or access to overdraft or credit features.

The guidance also suggest that issuing banks should enter into well-constructed, enforceable contracts with third-party program managers that clearly define the expectations, duties, rights, and obligations of each party in a manner consistent with this guidance. Issuing institutions should review the guidance and ensure their current contracts meet regulatory expectations.

For further reading, visit *www.fdic.gov/news/news/financial/2016/fil16021a.pdf* .

Inside this issue:

FDIC Flood Insurance Video Update

The FDIC has recently updated its Directors' Resource Center online videos to reflect changes relative to the Biggert-Waters Flood Insurance Reform Act, the Homeowner Flood Insurance Affordability Act, and the agency's final rules on flood insurance in Part 339 of Title 12 of the Code of Federal Regulations. Compliance Officers, senior management and lenders may find this training tool useful. These and other videos can be found at *Directors' Resource Center Technical Assistance Video Program.*

CFPB Advisory on Elder Abuse

We have written in previous issues of the *Compliance Pipeline* about the importance of elder abuse and how banks can be prepared to address such situations when they arise. In March, the CFPB published an advisory on preventing and responding to elder financial exploitation which is a concise resource that can be a useful reference and learning tool. Institutions should review the advisory for best practices to consider regarding elder abuse.

The Panama Papers and U.S. BSA Implications

The Panama Papers release is inciting worldwide uproar concerning corporate anonymity and the United States is no exception. The largest leak of an offshore tax advisor in history, dubbed the Panama Papers, is putting pressure on governments to enhance identification requirements of persons and businesses associated with shell companies.

The leak, published by the International Consortium of Investigative Journalists (ICIJ), revealed multiple world leaders, politicians, and business executives utilizing shell companies to allegedly launder money and evade taxes via the Panamanian law firm Mossack Fonseca.

Although limited U.S. Persons were exposed in the leak, the process of creating anonymous businesses as used in Panama is legally permissible in the United States as well. Many pundits cite the lack of stringent identification laws as a key reason few U.S. individuals are named in the Panama Papers. Simply, it is easier to create a shell company at home.

Under current CIP rules in the U.S., Banks are required to identify the legal status of the corporation but are not required to identify individuals who set up accounts in the name of shell companies. However, the Panama Papers leaks have reignited lawmakers resolve to reform documentation of shell company beneficial ownership.

It is expected that the Treasury Department will expedite the long outstanding FinCEN proposed rule on beneficial ownership from mid-2014. As currently proposed, the rule will require financial institutions to identify individuals who own 25 percent or more of corporate entities as well as any individuals exercising control over those entities. Lawmakers have also introduced HR 3331, the Incorporation Transparency and Law Enforcement Assistance Act. This bill will direct the Treasury Department to issue regulations requiring corporations and limited liability companies formed in a state that does not already require basic disclosure to file information about their beneficial ownership with the Treasury as a backup. The bill also provided minimum identification requirements for states and implements potential civil money penalties.

Until the proposed rule is finalized, institutions should prepare for increased scrutiny in BSA exams focusing primarily on weaknesses in CIP policy and enhanced due diligence on any offshore or shell company activity.

Did You Miss the Special Compliance Alert?

A Special Compliance Alert was emailed to *Compliance Pipeline* Subscribers on March 22, 2016. Just in case you missed it!

CFPB announces major changes to rural-or-underserved provisions

In the fall of 2015, the Consumer Financial Protection Bureau (CFPB) issued a final rule that revised the Regulation Z definitions of "small creditor" and "rural area" and made technical changes and clarifications to other sections of Regulation Z. These revisions affected which creditors were eligible to rely on certain special provisions, including special provisions allowing balloon-payment qualified mortgages and high-cost mortgages, and providing an exemption to the mandatory escrow requirements for higher priced mortgage loans (HPMLs) under Regulation Z. Prior to the January 1, 2016 effective date of the 2015 final rule, Congress enacted the Helping Expand Lending Practices in Rural Communities Act (HELP Act), which significantly broadened the class of small creditors which may be eligible under the Truth in Lending Act (TILA) for these special provisions.

On March 22, 2016, the CFBP issued an interim final rule effective March 31, 2016 to implement certain portions of the HELP Act. This interim final rule has a major impact on a financial institution's ability to make certain covered loans with balloon payments under ability to repay/ qualified mortgage and high cost lending requirements and eligibility for an exemption for mandatory escrow requirements for certain first lien HPMLs. The parts of the 2015 final rule not changed by the HELP Act and interim final rule will continue to remain in effect as of January 1, 2016.

Effective March 31, 2016, a small creditor is no longer required to extend more than 50 percent of its covered transactions secured by first liens on properties located in rural or underserved areas in order to be eligible for either of the two special balloon-payment provisions under Regulation Z. Under the interim final rule a small creditor will be eligible to rely on those special provisions if it originated at least one covered transaction secured by a first lien on a property located in a rural or underserved area in the preceding calendar year (or two preceding calendar years if the application is taken before April 1).

Note: the temporary provisions that permit any small creditor, regardless of where it operates, to originate balloon-payment qualified mortgages and balloon-payment high-cost mortgages only applies to applications received before April 1, 2016.

Effective March 31, 2016 a small creditor that operates in a rural or underserved area as noted above may also be exempt from establishing escrows for certain HPMLs, if certain conditions are met. Generally, a small creditor cannot rely on the exemption to the escrow requirement if it maintains an escrow account for any first lien real estate- or dwelling-secured consumer credit that it or an affiliate services, unless the escrow account was established for a first-lien HPML with an application received between April 1, 2010 and May 1, 2016 or if the escrow account was established as an accommodation to a distressed consumer.

Note: if a small creditor intends to close other escrow accounts maintained for non-HPML first lien real estate- or dwelling-secured consumer credit to take advantage of this new exemption, it must ensure the customer receives the Regulation Z 1026.20(e) escrow closing notice at least 30 days prior to closing the account.

The interim final rule also revises Regulation Z's definition of "rural area" to include a county or census block that the Bureau has designated as rural under the new application procedure set forth in the procedural rule which was effective March 3, 2016.

The CFPB will accept comments on the interim final rule for 30 days after its publication in the Federal Register. A copy of the final rule is available at:

http://files.consumerfinance.gov/f/201603_cfpb_operations-in-rural-areas-under-the-truth-in-lending-act-regulation-z-interim-final.pdf

Changes to MIRE Interpretations?

There has been increasing chatter among institutions about an interpretation change with examiners regarding to what constitutes a triggering term under Flood rules. The current triggers include making, increasing, renewing, or extending a loan also known as a MIRE event. This has become serious enough that the ABA has written a formal letter asking for clarification.

The possible change in interpretation by the regulators is regarding force-placing flood insurance being a MIRE event when adding force -placed flood insurance to the loan balance as examiners may treat this as "increasing" the loan. A MIRE event would require new flood determinations (unless the previous determination could be relied upon), a new signed notice of special flood hazard, and possibly having to add escrow to the loan unless an exemption or exception applied. As outlined in the letter from the ABA, there are a number of practical problems with this interpretation that don't appear to be in line with the spirit of the rules and could potentially cause consumer harm.

Hopefully the regulators will respond will clear guidance so institutions can ensure flood insurance force-placement procedures are in line with regulatory expectations. In the interim, institutions should contact their regulatory bodies for guidance on this topic and determine whether or not it would be appropriate to make changes to internal processes to comply with this new interpretation.

Email us at compliancenewsletter@shpco.net with any questions or comments.

Visit our website at www.shpco.net to register your email for the Compliance Pipeline!