Consumer Compliance
Hot Topics

2015 Regulatory Update Seminar
Federal Reserve Bank of Kansas City
Agenda

• Regulatory Timeline:
  ➢ Issued in 2014
  ➢ On the Horizon for 2015

• Areas of Supervisory Focus:
  ➢ Fair Lending
  ➢ Unfair or Deceptive Acts or Practices (UDAP)
  ➢ Flood
  ➢ Vendor Management

• Outreach and Resources
Regulatory Timeline

• Issued in 2014:
  - Electronic Fund Transfers (Regulation E) Amendment
  - Privacy of Consumer Financial Information (Regulation P) Amendment

• On the Horizon for 2015:
  - Home Mortgage Disclosure Act (HMDA) Data Collection and Reporting Changes
  - Truth in Lending Act (TILA) – Real Estate Settlement Procedures Act (RESPA) Disclosure Integration
  - Pre-Paid Cards
  - Consumer Financial Protection Bureau (CFPB) Proposal to Expand “Small Creditor” and “Rural” Definitions
Areas of Supervisory Focus
Areas of Supervisory Focus

Fair Lending

42% of bank examinations where supervisory follow-up was required in 2014 had weaknesses identified in their fair lending programs

- Pricing and Underwriting Discretion
- Overlooking Market Demographics
- Lack of Data Analysis
Areas of Supervisory Focus
Unfair or Deceptive Acts or Practices

Increasing Trend in Consumer Complaint Activity

Failing to Consider Customer Impact

Complex or Non-Traditional Offerings

Thinking UDAP Does Not Apply to Your Bank’s Products
Areas of Supervisory Focus

Flood

Approximately half of our examinations in 2014 cited violations of the flood requirements. These violations can result in civil money penalty assessments.

- Lack of Technical Knowledge
- Weak Processes and Procedures
- Inadequate Monitoring
More of our state member banks are using vendors in a way that increases their consumer compliance risk.

- Reliance on Vendor for Compliance
- Direct Contact with Bank Customers
- Insufficient Ongoing Monitoring
Areas of Supervisory Focus
Areas of Supervisory Focus
Fair Lending

Risk Factors

Marketing
Overt
Pricing
Redlining
Steering
Underwriting
Areas of Supervisory Focus
Fair Lending (Cont’d)

2014 Fair Lending Focal Point Review Break-Down

- Pricing: 64%
- Redlining: 22%
- Underwriting: 14%
### Areas of Supervisory Focus

**Fair Lending (Cont’d)**

#### Mitigating PRICING and UNDERWRITING Risks

<table>
<thead>
<tr>
<th>Policies and Procedures</th>
<th>Active Monitoring</th>
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<tr>
<td>• Establish and provide clear pricing and underwriting guidelines for loan officers for all products, using objective criteria such as credit score, DTI ratio, age of collateral, etc.</td>
<td>• Review all loans to ensure they are underwritten and priced in accordance with your guidelines and to ensure that exceptions are properly documented in files</td>
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<td>• Include only objective criteria in any risk-based pricing methods</td>
<td>• Track exceptions for all loans and denials and monitor these exceptions for trends (who is getting them, who is granting them?)</td>
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<td>• Ensure pay structures do not incentivize loan officers for charging higher interest rates or fees</td>
<td>• Review all pricing and underwriting guidelines when revisions are made and when new loan products are introduced</td>
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<td>• Limit the numbers of exceptions allowed and set minimum documentation standards for when exceptions are made</td>
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## Areas of Supervisory Focus

**Fair Lending (Cont’d)**

### Mitigating REDLINING Risks

#### Policies and Procedures

- Include consideration of area demographics both inside and immediately outside your assessment area in:
  - Strategic planning initiatives
  - Risk assessment activities
  - Marketing and outreach activities

#### Active Monitoring

- Monitor the bank’s lending patterns for consistency with market demographics
- Monitor product and service offerings for consistency in offerings from location to location
- Verify that marketing efforts include your entire market/trade area
- Review loan approvals and denials:
  - Are they representative of overall area demographics?
  - Are all geographic areas of your market being penetrated?
Areas of Supervisory Focus
Fair Lending (Cont’d)

• Fair Lending Compliance Resources:
  - Consumer Compliance Outlook Webinars and Q and As (2011-2014)
    https://consumercomplianceoutlook.org/outlook-live
  - Hispanic/Gender Database and Excel V Look-up instructions (refer to presentation materials for “Indirect Auto Lending-Fair Lending Considerations”)
  - CFPB’s – “Explore the Data” web page
    http://www.consumerfinance.gov/hmda/explore
  - CA Letter 09-6: Revised FFIEC Fair Lending Examination Procedures and Use of Specialized Examination Techniques
  - CFPB’s Equal Credit Opportunity Act Examination Procedures
Areas of Supervisory Focus
Unfair or Deceptive Acts or Practices

Technical compliance with existing consumer protection rules is not sufficient to manage UDAP risks
Areas of Supervisory Focus
Unfair or Deceptive Acts or Practices (Cont’d)

<table>
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<tr>
<th>Unfair</th>
<th>Deceptive</th>
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<tr>
<td>• Causes or is likely to cause substantial injury to consumers;</td>
<td>• A representation, omission, or practice that is misleading or is likely to mislead the consumer;</td>
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<td>• Cannot be reasonably avoided by consumers; and</td>
<td>• The consumer’s interpretation of the representation, omission, or practice is considered reasonable under the circumstances; and</td>
</tr>
<tr>
<td>• Is not outweighed by countervailing benefits to consumers or to</td>
<td>• The misleading representation, omission, or practice is material.</td>
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<td>competition.</td>
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<td>• Public policy may be considered.</td>
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Areas of Supervisory Focus
Unfair or Deceptive Acts or Practices (Cont’d)

Mitigating UDAP Risks

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<td>• Integrate the consideration of UDAP into your business decision framework</td>
<td>• Review complaint activity; look beyond individual complaints for trends</td>
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<tr>
<td>• Consider impact to the customer at all stages, including design, marketing, application, underwriting, pricing, disclosure, delivery channel, servicing, etc.</td>
<td>• Include all complaints, those received in person, on the phone, in the mail, through social media, etc.</td>
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<td>• Take vendor management seriously; make sure you understand how the product or service really works</td>
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Areas of Supervisory Focus
Flood

We continue to see banks with inadequate controls in this area
### Areas of Supervisory Focus

**Flood (Cont’d)**

#### Mitigating Flood Risks

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<tr>
<td>• Provide technical training to employees with flood insurance responsibilities</td>
<td>• Know which loans on your books require flood insurance</td>
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<td>• Establish strong policies and procedures to support compliance with initial and ongoing requirements</td>
<td>• Review files to ensure:</td>
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<tr>
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<td>➢ Determination of flood zone is completed</td>
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<td>➢ Flood insurance requirement notice is provided to the borrower in a reasonable amount of time prior to closing</td>
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<td>➢ Insurance is in place prior to closing (an application is not sufficient)</td>
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<td>➢ Required insurance coverage is calculated correctly</td>
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<td>➢ Adequate insurance is maintained throughout the life of the loan</td>
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<td>➢ Force placement procedures are followed correctly</td>
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Increasingly, our banks are using vendors to meet strategic initiatives.
### Areas of Supervisory Focus

**Vendor Management (Cont’d)**

#### Mitigating Vendor Management Risks

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<tr>
<td>• Apply the same due diligence you would for any in-house product or service</td>
<td>• Conduct initial and ongoing reviews of the vendor’s performance, consider their status in the industry, qualifications, operations and risk controls for compliance, and future viability</td>
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<tr>
<td>• Establish and use a vendor risk management policy and associated procedures</td>
<td>• Conduct initial and ongoing contract review for clear expectations concerning consumer compliance</td>
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<tr>
<td>• Reference SR Letter 13-19/CA Letter 13-21</td>
<td>• Review complaint activity; look beyond individual complaints for trends</td>
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<td>• Ensure the bank’s board provides proper oversight</td>
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Resources

• UDAP Resources:
  - CA Letter 13-22: Social Media: Consumer Compliance Risk Management Guidance:
    http://www.federalreserve.gov/bankinforeg/caletters/caltr1322.htm
  - 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:

• Vendor Management Resources:
  - CA Letter 13-21: Guidance on Managing Outsourcing Risk:
    http://www.federalreserve.gov/bankinforeg/srletters/sr1319.htm
Outreach and Resources

• Community Banking Connections Newsletter:
  http://www.communitybankingconnections.org/subscribe.cfm

• Consumer Compliance Outlook Publication:
  http://www.philadelphiafed.org/bank-resources/publications/consumer-compliance-outlook/

• Outlook Live Audio Conference Series:

• Fed Connections:
  https://www.kansascityfed.org/fedconnections

• Your Bank’s Consumer Affairs Contact
Questions