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American Bankers Association

Washington Update

September 1, 2015

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Banking 2015

Recommendations for Congress

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Banking 2015

- Banks offer services ranging from a child's first savings account to a retiree's annuity
- Congress needs to remove impediments that affect banks' ability to create jobs and promote growth
  - 58% of banks have cancelled or deferred new products due to regulatory costs and risks
  - 44% of banks have reduced existing consumer financial products or services due to regulatory burden
- Bankers can reach Congress since banks have branches and offices in every congressional district in every state

Banking 2015

- Recommendations for Congress
  - Reduce Unnecessary Paperwork
    - Streamline Currency Transaction Report requirements
    - Require greater accountability from law enforcement on the use of Bank Secrecy Act data
    - Reduce redundant privacy notices
    - Address challenges of mortgage lending disclosures
  - Create a More Balanced, Transparent Approach to Exams
    - Provide an independent appeals process
    - Require clear and verifiable cost-benefit analysis with new rules

Banking 2015

- Recommendations for Congress
  - Limit burdensome “trickle-down” regulations
    - Eliminate unnecessary stress tests for mid-size banks
    - Require targeted rulemaking by regulators
    - Remove arbitrary thresholds that do not correspond to a bank’s risk and business model
    - Exempt small banks from CFTC clearing requirements
    - Ensure capital rules for systemically important financial institutions (SIFIs) and applied only to SIFIs

Banking 2015

- Recommendations for Congress
  - Eliminate unreasonable legal risks
    - Reduce the threats of patent trolls
    - Remove uncertainties in the application of fair lending requirements
  - Protect the Payment System
    - Ensure that all financial institutions – bank and non-bank – are subject to the same rules and oversight
    - Avoid technology mandates
- EGRPRA – The Economic Growth & Regulatory Paperwork Reduction Act of 1996

Diversity & Fair Lending

The State of Affairs

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Diversity Standards

- June 10, 2015 – Six federal agencies issued a final policy statement setting out standards under section 342 of the Dodd-Frank Act
- The final standards are a general statement of policy
  - They do not create new legal obligations
  - They are completely voluntary
  - They are designed to let individual institutions tailor the standards to suit their own needs and to reflect the company's size, business model, strategic plan, customers base and markets served

Diversity Standards

- The Standards cover five elements the agencies will use when assessing a company's approach to diversity and inclusion:
    1. Organizational commitment to diversity & inclusion
    2. Workforce profile and employment practices
    3. Procurement and business practices
    4. Practices to promote transparency about a company's diversity & inclusion
    5. Self-assessment

Disparate Impact

- On June 25, 2015, the United States Supreme Court held that the Fair Housing Act (FHA) recognizes disparate impact theory as a means to identify discrimination
- Although the industry had argued to the contrary, the decision affirms lower court findings that disparate impact theory is recognized by the FHA and which has been applied by banking regulators for more than 20 years
- The case did not address whether the Equal Credit Opportunity Act (ECOA) recognizes a disparate impact theory of discrimination

Disparate Impact

- The Court raised concerns about potential abuse of the theory, possibly leading to unconstitutional application of the theory
- As a result, the Court outlined important steps when disparate impact theory is applied
    1. Statistical analysis alone is insufficient
    2. A specific policy or procedure must be identified and shown to be the cause of the statistical disparity
    3. A legitimate business reason for adopting that policy or procedure can overcome the presumption of discrimination
    4. To show discrimination, the claimant must clearly demonstrate an alternative policy or procedure that was no more burdensome that would not have a discriminatory effect

Disparate Impact

- On August 5, ABA wrote to the Attorney General, HUD, the federal banking agencies and CFPB
  - We pointed out that the Supreme Court set forth the proper interpretation for the use of disparate impact theory
  - We recommended that agencies focus their efforts to identifying and eliminating instances of disparate treatment
  - We urged the agencies to use disparate impact theory "only when there is demonstrable evidence that the lender is applying an artificial, arbitrary, and unnecessary barrier in its credit granting process"
  - We recommended all the agencies review and update their guidance, examination procedures and, where appropriate, regulations to be consistent with the law as set forth by the Court

Small Business Lending

- Section 1071 of the Dodd-Frank Act amended the Equal Credit Opportunity Act (ECOA) to add a new data collection point for business loans
- Information will be collected for applications for loans to women-owned businesses, minority-owned businesses and small business loans
- In April 2011, the CFPB issued guidance stating that the CFPB would not enforce Section 1071 until it had issued implementing regulations
- The CFPB has not yet proposed a rule

HMDA

- The Dodd-Frank Act, section 1094, expanded the data points required for compliance with the Home Mortgage Disclosure Act (HMDA)
- Last July, the Consumer Financial Protection Bureau (CFPB) proposed regulatory changes to implement the statutory requirements and collect additional data to assess fair lending and how financial institutions are meeting housing needs
- The changes would greatly expand the data collected and reported

HMDA

- As proposed:
  - Large institutions would report quarterly
  - The threshold for all filers would change to require reporting by those that make 25 or more covered loans annually
  - The reporting would apply to all home-secured loans, including commercial loans, home equity loans and reverse mortgages
- A final rule has not been issued
  - The Bureau's semi-annual agenda issued May 22, 2015 suggested a final rule would be issued in August 2015
- Data collection would not begin before January 1, 2017

The Military Lending Act

An Overview of the New Requirements

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Military Lending Act

- On July 22, the Department of Defense (DOD) published final amendments to the Military Lending Act (MLA) regulation
- The MLA rule, originally adopted in 2007, imposes special disclosure requirements and places restrictions on the terms of certain consumer loans made to military personnel, their spouses and dependents
- The original rule was narrowly restricted to vehicle title loans, refund anticipation loans and payday loans. The revised rule significantly expands coverage to include all consumer credit except for residential mortgages and purchase money loans
- Responsibility for determining whether an applicant is covered rests with the creditor

Military Lending Act

- The Final Rule:
  - Covers consumer loans as defined in Regulation Z
    - Residential mortgages & purchase money loans such as car purchase loans are excluded
  - Limits what banks may charge in fees and interest on certain consumer loans by imposing a 36% "military" APR cap
    - The 36% cap is ***not*** a 36% interest rate cap nor a 36% APR cap, but an MAPR cap that is an "all-in" APR that includes other fees such as application fees and annual fees that are not finance charges under Regulation Z
  - Requires special disclosures for military personnel, their spouses & dependents
  - Prohibits enforcement of arbitration agreements
  - Prohibits certain terms, provisions, including:
    - Waivers of the right to legal recourse under any state or federal law;
    - Imposition of "onerous legal notice provisions";
    - Demands of "unreasonable notice from the covered borrower as a condition for legal action"; and
    - Use of a check or other method of access to a bank account which may prohibit "liquid" secured credit.

Military Lending Act

- Banks are now responsible for determining an applicant's military status
  - As a practical matter, banks must inquire "directly or indirectly" with the DOD database or a nationwide consumer reporting agency that provides the information – *if one exists*
- *Effective Date:* October 3, 2015
- *Mandatory Compliance Date*: October 3, 2016
  - Credit cards have a compliance date of October 3, 2017 and the Secretary of Defense may extend that one year to October 2018.

Military Lending Act

- ***The regulation prohibits providing a consumer loan with an MAPR that exceeds 36%. How is the MAPR different from the APR under Regulation Z?***
  - The MAPR calculation also includes:
    - Fees not considered "finance charges" under Regulation Z, such as application and "participation" fees, such as annual fees
    - Fees and premiums for credit insurance, debt cancellation, and debt suspension, fees for a credit-related ancillary product sold in connection with the credit transaction for closed-end and credit or an account for open-end credit.
    - Fees for any ancillary product sold with an extension of credit to a covered borrower *if* the ancillary product is associated with an extension of credit – which could arise at any time in an ongoing open account for consumer credit.
  - Certain "bona fide" fees may be excluded for credit cards
    - Identifying bona fide fees is extremely complex
    - If fees include both bona fide and non-bona fide fees, a credit card issuer may not exclude the bona fide fee from the MAPR calculation. Instead, the presence of any non-bona fide fee requires all fees to be included in the calculation

Military Lending Act

- For open-end credit, the DOD re-introduced the “effective” or “historic” APR concept
  - This requires a retroactive calculation of the APR, based on the customer’s actual balance and actual fees imposed during a billing period.
  - The Federal Reserve Board’s abandoned this calculation because it was confusing for consumers
  - It could cause even small, modest fees to exceed the 36% MAPR significantly depending on the outstanding balance during a billing cycle
  - IF there is no outstanding balance, a creditor may not impose any fee or charge during that billing period except for a participation fee or annual fee that is $100 or less

Military Lending Act

- **"Bona fide" fees excluded from the MAPR calculation for credit cards**
  - Certain fees imposed on credit card accounts may be excluded from the calculation if they are "bona fide" and "reasonable for that type of fee."
  - Bona fide is not defined, though the regulation provides "standards" to assess whether a bona fide fee is "reasonable." The standard includes comparing fees "typically imposed by other creditors for the same or a substantially similar product or service" – "like-kind fees" – and offers the example of a cash advance fee. "Substantially similar product" is not defined.
  - Under the "safe harbor," a bona fide fee is "reasonable" if the fee is less than or equal to an average amount of a fee for the same or a "substantially similar" product or service charged by 5 or more creditors with at least $3 billion in an outstanding U.S. credit card balances during the last 3 years.9 A fee that is higher than an average amount calculated under this section may still be reasonable, "depending on other factors related to the credit card account." In addition, the fact that no other creditors charge a fee for the same or substantially similar product does not per se mean it is not reasonable.
  - The regulation recognizes that participation fees might vary depending on whether other fees are charged. Accordingly, it provides that a participation fee "may" be reasonable if the amount "reasonably corresponds to the credit limit in effect or credit made available when the fee is imposed, to the services offered under the credit card account or to other factors relating to the credit card account."

Military Lending Act - Disclosures

- **Required Disclosures:**
  - ***"Statement" of the MAPR***
    - Banks may comply with this provision by "describing the charges the creditor may impose related to the consumer credit to calculate the MAPR" and the rule provides a model
    - Lenders are not required to disclose the numerical MAPR.
  - ***Any disclosures required by Regulation Z***
  - ***A clear description of the payment obligation of the covered borrower.***
    - For closed-end credit, a payment schedule suffices.
    - For open-end credit, the account opening disclosures required under Regulation Z suffice.
- **Providing disclosures**
  - Disclosures must be provided in writing.
  - The statement of the MAPR and the payment obligation description must also be provided orally, although oral disclosures may be provided using a toll-free number.
    - The toll-free number must be provided on (1) the application form or (2) with the written disclosures described above.
  - Disclosures must be provided "before or at the time the borrower becomes obligated on the transaction or establishes an account for the consumer credit."

Military Lending Act - Status

- **Determining an applicant's military status**
  - The creditor is responsible for determining whether a borrower is covered
    - There is a safe harbor for using the DOD database or a national credit bureau
    - An applicant's declaration is not sufficient
    - Concerns remain about the reliability and availability of the DOD database
    - The final rule eliminated the provision on "actual knowledge" of status
  - Questions remain about verification and records
- **When is status determined**
  - A lender must determine status when an applicant initiates a transaction or 30 days prior
  - For pre-screened offers of credit , when a creditor processes a "firm offer of credit" no later than 60 days after the creditor provided the offer
- The rule prohibits lenders, including an assignee, from directly or indirectly obtaining information from any DOD database to ascertain whether a consumer "had been a covered borrower as of the date of that transaction or as of the date that account was established."

Military Lending Act

- **Penalties for violations**
  - ***Criminal penalties***: Creditors knowingly violating the regulation are subject to fines and imprisonment for up to one year
  - ***Voidance of the contract***: Any agreement is void from inception of the contract if any provision is violated
  - ***Private right of action and civil liability:*** A person who violates the regulation is liable to any actual damage, but not less than $500 for each violation, punitive damages, appropriate equitable or declaratory relief, and any other relief provided by law
- **Arbitration:** No agreement to arbitrate any dispute involving the extension of covered consumer credit to a covered borrower is enforceable against any covered borrower or any person who was a covered borrower when the agreement was made
- **Costs of the action:** Those found to violate the regulation are liable for the costs of the action and reasonable attorney fees
- **Regulation Z violation:** A violation of Regulation Z involving any product covered by the regulation is also a violation of the MLA

Other Issues on the Horizon

A Potpourri of What's on Deck

Major CFPB Initiatives

- TRID – Truth-in-Lending and RESPA Integrated Disclosures
  - Efforts continue to support efforts towards the integrated disclosure process that takes effect October 3, 2015
- Other Mortgage Rules
  - Finalization of amendments of rules for small creditors, especially those that operate in rural and underserved areas
  - Changes to mortgage servicing rules
- Prepaid Financial Products
  - Finalizing a December 2014 proposal that would create comprehensive consumer protections for prepaid products

Major CFPB Initiatives

- Continuing efforts on small dollar loans
- Ongoing analysis of overdraft services, conducting additional research into practices and consumer impact
- Developing proposed rules for debt collection practices, surveying consumers about their experience
- Conducting studies of arbitration and evaluating whether rules governing arbitration clauses may be warranted

QUESTIONS?

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