

# **Dodd-Frank: Where Are We Now**

**As of June 1, 2011**

**A BAI Learning & Development White Paper**

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### BAI LEARNING & DEVELOPMENT WHITEPAPER

There have been a multitude of activities in connection with the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), especially lately. Many have taken place relative to swaps and other investment activities pursuant to Title VII of the Act and have come from the Securities and Exchange Commission (SEC) and the Commodities Future Trading Commission (CFTC). This white paper will not concentrate on those activities, nor will it focus on high-level activities such as the “living will” requirement, the “Volcker Rule,” orderly liquidation proceedings, systemically important institutions, or incentive compensation rules. Rather, it will focus on activities directly affecting retail banking.

#### **July 21, 2011 Approaching**

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We are rapidly approaching the “magic date” when it comes to the Dodd-Frank Act: July 21, 2011. As this date is exactly one year after the bill was signed into law by the President, it is the “transfer date” for several critical Dodd-Frank Act activities. On this date the Office of Thrift Supervision (OTS) operations transfer to the Office of the Comptroller of the Currency (OCC). In addition, the Consumer Financial Protection Bureau (CFPB or Bureau) officially commences operations, assuming authority over all consumer protection regulations and responsibility for supervision of banks with assets over \$10 billion.

July 21, 2011, is also the effective date for many provisions of the Act that do not have alternative effective dates listed or plans for such dates set forth.

The Dodd-Frank Wall Street Reform and Consumer Protection Act; Public Law 111-203; 124 Stat. 1376 (H.R. 4173):

[http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111\\_cong\\_bills&docid=f:h4173enr.txt.pdf](http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h4173enr.txt.pdf)

#### **Elimination of the OTS; Transfer to the OCC**

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To address the OTS-into-OCC combination (from Dodd-Frank Section 312), the OCC issued a **proposed rule** on May 25, 2011. The rule also addresses Dodd-Frank mandated changes to federal preemption for national banks and federal savings associations, including their operating subsidiaries and affiliates (Section 1044 and 1046), and visitorial authority (Section 1047), which is the right of the agency to visit, or examine, covered institutions.

The proposal’s **OTS-to-OCC provisions** include:

- OCC agency function and operation rules will be altered to include supervisory jurisdiction over federal savings associations upon the transfer (these rules relate to availability and release of information, post-employment restrictions for senior examiners, and similar issues); and
- The OCC assessment fee rule will now include the same assessment schedule for national banks and federal savings associations. For thrifts now regulated by the OCC, their assessments normally due on July 31, 2011, would be deferred until September 30, 2011 (using June 30 data).

The OCC will also soon issue an interim final rule with a request for comments (to be effective on July 21, 2011) to **republish OTS regulations** the OCC will enforce. They will be renumbered and issued as OCC rules. More comprehensive and substantive amendments to those regulations will be made at some point after July 21, 2011.

**Preemption and visitorial powers amendments** include:

- Preemption and visitorial power standards applicable to national banks and subsidiaries will be made applicable to federal thrifts and their subsidiaries;
- Preemption for national bank and federal thrift operating subsidiaries and affiliates will be eliminated;
- Language from OCC rules providing that state laws that "obstruct, impair or condition" a national bank's powers are preempted will be removed; and
- The OCC's visitorial powers rule will be changed to recognize the ability of state attorney generals to bring enforcement actions in court to enforce non-preempted state laws against national banks and federal thrifts.

The rule also revises federal branch and agency rules to line up with the permanent increase in deposit insurance coverage (Section 335).

OCC NR 2011-62: <http://www.occ.treas.gov/news-issuances/news-releases/2011/nr-occ-2011-62.html>

OCC Bulletin 2011-20: <http://www.occ.gov/news-issuances/bulletins/2011/bulletin-2011-20.html>

OTS CEO Letter 387: <http://www.ots.treas.gov/files/25387.pdf>

Proposed rule (5/26/11; 76 FR 30557):

<http://www.gpo.gov/fdsys/pkg/FR-2011-05-26/pdf/2011-12859.pdf>

## **Consumer Financial Protection Bureau Operational Developments**

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There has been a fair amount of political discourse surrounding the powers and authority of the new Bureau. One interesting fact is that the CFPB's headquarters will be the Washington D.C. location presently occupied by the OTS, which will officially cease to exist the same date the Bureau commences operations.

As of June 1, 2011, there has been no Director candidate yet nominated by the President.

### *Congressional Concerns about the CFPB's Upcoming Operations*

Some critical questions regarding the Bureau's operations have been asked by members of Congress. On January 18, 2011, the House Financial Services Subcommittee on Oversight and Investigations sent a letter to Elizabeth Warren, Assistant to the President and Special Adviser to the Secretary of the Treasury, addressing how the Bureau will be established.

Among the issues on which the Subcommittee requested information:

- A description of departments and positions within in the Bureau's organization chart;
- An update on the Bureau's hiring process;
- When a permanent Director of the CFPB would be named;
- An explanation of Elizabeth Warren's responsibilities and authority;
- An update on the Bureau's budget projections and whether it is anticipated that additional appropriations would be requested for Financial Year 2011 or 2012;
- What Warren's suggestions would be to bring more accountability and oversight to the Bureau;
- Descriptions of Warren's meetings with "top financial industry executives" and other governmental agencies on rulemaking;
- Information on the CFPB's authority to reexamine rulemakings from other federal agencies; and
- How the Bureau plans to evaluate its efforts to avoid over-regulation that might harm financial innovation and lower-income Americans.

Letter to Elizabeth Warren: <http://randy.house.gov/uploads/Letter%20to%20Elizabeth%20Warren.pdf>

In response to whether the Bureau may or may not have the statutory ability to make or enforce regulations after July 21, 2011, if a permanent Director has not yet been named or confirmed by the Senate, the Treasury ventured the opinion that the Dodd-Frank Act gives the Treasury Secretary (Timothy Geithner) the ability to act in the stead of the CFPB Director if one had yet been named. Based on this, it appears the Bureau will go forward with any and all planned activities on July 21, 2011, even if a Director has not yet taken charge.

Other members of Congress have raised significant concerns around the structure of the Bureau's leadership. In fact, three bills have been introduced that would alter the structure of the Bureau:

- One (H.R. 1121) would alter the leadership structure of the agency from that of a single director to a five-member commission;
- Another (H.R. 1667) would require the CFPB to have a director confirmed by the Senate before it could exercise its authorities; and
- The third (H.R. 1315) would allow a majority of banking regulators and others on the Financial Services Oversight Council (FSOC) to veto CFPB regulations they deem inconsistent with safety and soundness principles.

Given the lack of bipartisan agreement on these issues, however, there is **little chance of any significant statutory change in the Bureau's structure before July 21, 2011.**

Members of Congress are not the only ones raising concerns regarding CFPB issues. Acting Comptroller John Walsh, in testimony offered before Congress, discussed concerns about how supervision of large banks would be handled with the Bureau. Fair lending issues, in particular, were discussed, as the Act transfers authority over Regulation B (Equal Credit Opportunity Act, ECOA) to the CFPB, while the Fair Housing Act (FHA) remains with the existing regulatory agencies.

The OCC indicated concern about possible duplication of fair lending supervision and enforcement. Walsh also stated concern over who would handle consumer complaints for large banks.

Testimony from the hearing:

[http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Hearing&Hearing\\_ID=c43953db-0fd7-43c3-b6b8-97e2d0da3ef7](http://banking.senate.gov/public/index.cfm?FuseAction=Hearings.Hearing&Hearing_ID=c43953db-0fd7-43c3-b6b8-97e2d0da3ef7)

#### *The Bureau's Priorities*

Warren has also indicated in separate remarks that more than **half of the Bureau's budget will be dedicated to supervision and enforcement**, described as the Bureau's top priority. Another quarter of the budget will be dedicated to consumer education and outreach, along with management of consumer complaints. The remainder will be dedicated to efforts such as rulemaking and research.

#### *Coordinated Supervision with the States*

The Conference of State Bank Supervisors (CSBS), in early January, 2011, signed a memorandum of understanding (MOU) with the CFPB (through the Treasury Department) to establish **coordination and cooperation between the Bureau and state regulatory authorities** in connection with offerings of consumer financial products and services.

State regulators and the CFPB agreed to:

- Promote consistent examination procedures and effective enforcement of state/federal consumer laws;
- Attempt to minimize regulatory burden and efficiently deploy supervisory resources; and
- Consult each other regarding the standards, procedures, and practices used to conduct compliance examinations of consumer financial products and service providers.

Treasury Press Release tg-1016: <http://www.treasury.gov/press-center/press-releases/Pages/tg1016.aspx>

CSBS Media Release 1/4/11: <http://www.csbs.org/news/press-releases/pr2011/Pages/pr-010411.aspx>

In addition, on April 11, 2011, the Bureau announced (through the Treasury) an agreement on a Joint Statement of Principles with the National Association of Attorneys General (NAAG) to govern their interactions regarding enforcement. In it, the parties agree to **work with each other to identify enforcement priorities, share complaints, and support the other's enforcement efforts**. This could also include joint or coordinated investigations and enforcement actions.

The amount of cooperation and sharing of analyses, information, and complaints between the states and CFPB shows that future rulemaking and priorities of the Bureau will be heavily influenced by information and developments within the states. In the end, the influence of state regulators will likely increase dramatically.

Treasury Press Release tg-1134 (4/11/11):

<http://www.treasury.gov/press-center/press-releases/Pages/tg1134.aspx>

#### *SCRA Warning*

An example already of the Bureau's opinion over what it perceives to be an infringement of consumer protections is the so-called "**Petraeus Letter**." Holly Petraeus, newly-appointed head of the CFPB's Office of Servicemember Affairs (established by Section 1013(e)), sent a letter in February to the top 25 U.S. banks reminding them of their **duties under the Servicemembers Civil Relief Act (SCRA)**.

The letter urged SCRA training and file reviews to ensure SCRA compliance (neither of which is required under the SCRA statute). Petraeus also recommended banks reach out to consumers when they have reason to believe that a borrower may be an active duty member of the military. This letter provides a sign of where the Bureau may feel entitled to recommend practices beyond the normal scope of existing laws and regulations. It will have to be seen whether this becomes Bureau standard practice.

The "Petraeus Letter": [http://www.buckleysandler.com/SCRA\\_Petraeus\\_Letter.pdf](http://www.buckleysandler.com/SCRA_Petraeus_Letter.pdf)

#### *Consumer Complaint Database*

Section 1013(b)(3)(a) directs the Bureau to establish a "single, toll-free telephone number, a website, and a database or utilizing an existing database to facilitate the centralized collection of, monitoring of, and response to **consumer complaints regarding consumer financial products or services**." In the March 9, 2011, Federal Register, the Bureau (through the Treasury) published a request for comments regarding the methodology of how the intake of consumer complaints should be handled.

Public comments were sought on the following issues:

- Whether collection of complaints, questions, and similar information relating to consumer financial products and services is necessary for Bureau's performance, and whether it will have practical uses;
- Methods for enhancing the quality, usefulness, and clarity of the information;
- Methods for minimizing reporting and recordkeeping burdens on respondents, including possible use of automated collection techniques;
- Startup costs to operate, maintain, and purchase services to provide information; and
- What types of information would be useful for the Bureau to collect through its intake forms.

Request for Comment (3/9/11; 76 FR 13018): <http://edocket.access.gpo.gov/2011/pdf/2011-5349.pdf>

### *CFPB's List of Regulations*

In the May 31, 2011, Federal Register, the CFPB published a list (as required by Section 1063 of Dodd-Frank) of the 47 regulations over which it will have authority and will enforce beginning July 21, 2011.

This list includes:

- Equal Credit Opportunity Act/ECOA (currently administered by the Fed: Reg. B, 12 CFR 202);
- Home Mortgage Disclosure Act/HMDA (Fed: Reg. C, 12 CFR 203);
- Electronic Fund Transfers (Fed: Reg. E, 12 CFR 205);
- SAFE Act, Registration of Residential Mortgage Loan Originators (OCC: 12 CFR 34.101–.105 & Appendix A to Subpart F; Fed: Reg. H, Subpart I, 12 CFR 208.101–105 & Appendix A to Subpart I; FDIC: 12 CFR 365.101–.105 & Appendix A to Subpart B; OTS: 12 CFR 563.101–.105 & Appendix A to Subpart D; NCUA: 12 CFR 761);
- Consumer Leasing (Fed: Reg. M, 12 CFR 213);
- Privacy of Consumer Financial Information (OCC: 12 CFR 40; Fed: Reg. P, 12 CFR 216; FDIC: 12 CFR 332; OTS: 12 CFR 573; NCUA: 12 CFR 716; FTC: 16 CFR 313);
- Fair Credit Reporting Act/FCRA (OCC: 12 CFR 41; Fed: Reg. V, 12 CFR 222; FDIC: 12 CFR 334; OTS: 12 CFR 571; NCUA: 12 CFR 717; FTC: 16 CFR 603), except provisions affecting:
  - Effective dates, disposal of consumer information, duties regarding the detection, prevention, and mitigation of identity theft, duties of card issuers regarding changes of address, and Appendix J (Interagency Guidelines on Identity Theft Detection, Prevention, and Mitigation);
- Truth in Lending Act/TILA (Fed: Reg. Z, 12 CFR 226);
- Truth in Savings Act/TISA (Fed: Reg. DD, 12 CFR 230; NCUA: 12 CFR 707);
- Adjustable-Rate Mortgages regulation (only as applied to non-federally chartered housing creditors under the Alternative Mortgage Transaction Parity Act/AMTPA (OCC: 12 CFR 34.20–.25);
- Adjustments to home loans regulation (only as applied to non-federally chartered housing creditors under AMTPA) (OTS: 12 CFR 560.35);
- Alternative Mortgage Transactions regulation (only as it relates to AMTPA) (OTS: 12 CFR 560.210-220);
- Loans to members and lines of credit to members under AMTPA (NCUA: 12 CFR 701.21);
- Requirements for Insurance, only with respect to Truth in Savings, Privacy of consumer financial information, and Registration of residential mortgage loan originators (NCUA: 12 CFR 741);
- Disclosure Requirements for Depository Institutions Lacking Federal Depository Insurance (FTC: 16 CFR 320);
- Mortgage Assistance Relief Services (FTC: 16 CFR 322);
- Use of Pre-notification Negative Option Plans (FTC: 16 CFR 425);
- Rule Concerning Cooling-Off Period for Sales Made at Homes or at Certain Other Locations (FTC: 16 CFR 429);
- Preservation of Consumers' Claims and Defenses (FTC: 16 CFR 433);
- Credit Practices (FTC: 16 CFR 444);
- Mail or Telephone Order Merchandise (FTC: 16 CFR 435);
- Disclosure Requirements and Prohibitions Concerning Franchising (FTC: 16 CFR 436);
- Disclosure Requirements and Prohibitions Concerning Business Opportunities (FTC: 16 CFR 437);
- Procedures for State Application for Exemption from the Provisions of the [Fair Debt Collection Practices] Act (FTC: 16 CFR 901);
- Hearing Procedures Pursuant to the Administrative Procedure Act (HUD: 24 CFR 26.28-.56)
- Civil Money Penalties: Certain Prohibited Conduct (only as applied to RESPA and the Interstate Land Sales Full Disclosure Act/ILSA) (HUD: 24 CFR 30);
- Land Registration (HUD: 24 CFR 1710);
- Purchasers' Revocation Rights, Sales Practices, and Standards (HUD: 24 CFR 1715);
- Formal Procedures and Rules of Practice (HUD: 24 CFR 1720);
- Real Estate Settlement Procedures Act/RESPA (HUD: 24 CFR 3500); and
- Investigations in Consumer Regulatory Programs (only as applied to RESPA and ILSA) (HUD: 24 CFR 3800).

CFPB List (76 FR 31222; 5/31/11): <http://www.gpo.gov/fdsys/pkg/FR-2011-05-31/pdf/2011-13256.pdf>

### *New CFPB Website*

The Treasury Department launched the Bureau's website in February 2011. The site (<http://www.consumerfinance.gov>; <http://www.cfpb.gov>), although labeled a "beta" website, will be the site of the CFPB's activities. The stated goals of the site are to provide information about the Bureau through engagement with the public, with an emphasis on social media outlets (CFPB identities have been established on Facebook, Twitter, YouTube, and Flickr). The site also contains a listing of CFPB press releases.

Treasury Press Release tg-1150:

<http://www.treasury.gov/press-center/press-releases/Pages/tg1050.aspx>

### **The CFPB's Initiative to Combine Mortgage Loan Disclosures**

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One of the Bureau's first stated priorities is their effort to **combine the Reg. Z mortgage disclosure** (the Early Truth in Lending disclosure) **and the RESPA Good Faith Estimate (GFE)** into a single form, mandated by Section 1032. While each disclosure is required under separate federal laws (TILA and RESPA) in consumer-purpose mortgage transactions, the separate forms contain duplicative information and are overly complex. A combined form should make terms more clear and reduce compliance costs for lenders, as well.

The Bureau announced on May 18, 2011, their "**Know Before You Owe**" project, details of which are found on their website. **Two alternative prototype forms were published** as examples of a new disclosure to be provided to consumer applicants within three days of application for a covered mortgage loan (as required by both Reg Z and RESPA). Both consumers and industry representatives were asked to choose via an online interactive tool which prototype they felt was preferable. Testing will take place over several months and involve interviews with consumers, lenders, and brokers, after which the CFPB will embark on the formal rulemaking process to amend the rules.

As part of this same effort, the Bureau will also consider ways to refine disclosures provided at loan closing. This will likely extend into early 2012.

Treasury Press Release tg-1180:

<http://www.treasury.gov/press-center/press-releases/Pages/tg1180.aspx>

Know Before You Owe initiative and disclosure prototypes:

<http://www.consumerfinance.gov/knowbeforeyouowe/>

Proposed disclosure option A ("Pecan Bank"):

<http://www.consumerfinance.gov/wp-content/uploads/2011/05/disclosure2.pdf>

Proposed disclosure option B ("Ficus Bank"):

<http://www.consumerfinance.gov/wp-content/uploads/2011/05/disclosure1.pdf>

### **Amendments to Reg. Z (Truth in Lending)**

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The Dodd-Frank Act makes many changes to the Truth in Lending Act (TILA), some of which have already been implemented by the Federal Reserve in final form, while others have been proposed by the Fed and will be finalized by the Bureau as the CFPB gains authority over Reg. Z on July 21, 2011.

#### *Increase in Coverage Threshold*

One basic change made to TILA and therefore Reg. Z (and also to Reg. M, which covers Consumer Leasing) under Section 1100E is an **increase in the coverage threshold from \$25,000 to \$50,000**. Currently consumer loans that are not secured by real estate or a dwelling (or are not primarily for secondary education expenses) are exempt from Reg. Z requirements if the loan amount is over \$25,000.

The Fed has issued final rules (**effective July 21, 2011**) to increase these thresholds to the \$50,000 figure. In short, consumer credit transactions and consumer leases with transaction amounts up to \$50,000 will be covered by Regulations Z and/or Regulation M. The \$50,000 threshold is not static, either. Beginning the end of this year (December 31, 2011), the **threshold will be adjusted annually** based upon the Consumer Price Index (CPI) for Urban Wage Earners and Clerical Workers.

Fed Press Release 3/25/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110325a.htm>

Final Reg. M Rule (4/4/11; 76 FR 18349): <http://edocket.access.gpo.gov/2011/pdf/2011-7377.pdf>

Final Reg. Z Rule (4/4/11; 76 FR 18354): <http://edocket.access.gpo.gov/2011/pdf/2011-7376.pdf>

### *Appraisal Rules*

Section 1472 amends TILA by adding a subsection on “**appraisal independence requirements.**” The rules are intended to ensure appraisers use independent professional judgment when evaluating homes and are free from influence or pressure from parties having interests in the property or transaction. In addition, per Dodd-Frank requirements, the **Home Valuation Code of Conduct (HVCC) is no longer in effect.**

The Fed in October 2010, issued an **interim final rule (effective December 27, 2010, with compliance required April 1, 2011)** to implement the requirements to “protect the integrity of the appraisal process” when a consumer’s principal dwelling secures a Reg. Z-covered loan. This covers both closed-end loans as well as home equity lines of credit (HELOCs). Note also that the rule covers more than just appraisals and appraisers; evaluations performed by natural persons are also covered.

Included in the rule are the following provisions:

- *Prohibitions against coercion:* This includes rules that **prohibit coercion, bribery, and undue influence** on the part of the lender to attempt to have the appraiser base the appraised value of properties on factors other than the appraiser’s independent judgment. Examples include implying that retention of the appraiser depends on the value returned, failing to compensate or retain the appraiser because the appraiser does not return the “right” value, and conditioning the appraiser’s compensation on whether or not the loan closes.
- *No mischaracterization:* **Values of property may not be “mischaracterized,”** meaning falsified or altered. In addition, persons may not attempt to induce others to misrepresent or falsify the value of a property;
- *Conflicts of interest:* Prohibitions against appraisers and appraisal management companies (AMCs) having financial or other interests in properties or transactions in which they participate;
- *Can’t close the loan:* A **prohibition** against the lender extending credit based on an appraised value if the **lender knew beforehand there was prohibited coercion or similar conduct** involved or the person has a conflict of interest in the property or transaction (unless “reasonable due diligence” demonstrates the value was not materially misstated);
- *Report appraiser misconduct:* A **lender must file a report with the appropriate state licensing authorities** (within a reasonable period of time) if it has information about appraiser misconduct relating to a violation of federal or state law, or USPAP requirements that has a “material” impact, meaning likely to affect the value assigned to the property; and
- *Reasonable and customary fees:* **Lenders may pay only “reasonable and customary” fees** to appraisers who are not employees. “Reasonable and customary” means reasonably related to recent rates paid for appraisal services in the appraiser’s geographic market. Lenders are presumed to comply if they rely on rates established by third party information, such as the appraisal fee schedule issued by the Veteran’s Administration (VA) or fee surveys performed by an independent third party (though no such other third parties were identified in the rule). Information relied upon must be objective, based on recent rates paid to a representative sample of providers, and must exclude fees paid to appraisers ordered by AMCs.

Fed Press Release 10/18/10: <http://www.federalreserve.gov/newsevents/press/bcreg/20101018a.htm>

Interim Final Rule (10/28/10; 75 FR 66554): <http://edocket.access.gpo.gov/2010/pdf/2010-26671.pdf>

### *Escrow Requirements (Final Rule and Proposed)*

Sections 1461 and 1462 make significant changes to TILA's required escrow provisions for covered loans. On February 23, 2011, the Fed issued both a final rule and request for public comment on a second rule under Reg. Z for certain home mortgage loans.

The **final rule (effective April 1, 2011)** increases the APR threshold for first-lien, jumbo mortgage loans and higher-priced mortgage loans (HPMLs) for determining whether the lender must establish an escrow account for property taxes and insurance for at least one year.

"Higher-priced" means the loan's APR exceeds the average prime offer rate (APOR, currently Freddie Mac's Primary Mortgage Market Survey, or PMMS, rate) for a comparable transaction, as of the date the rate is set, by 1.5 or more percentage points. "Jumbo" means the maximum principal amount for loans established by the Federal Housing Finance Agency (FHFA), the regulator of Fannie Mae and Freddie Mac. That amount is currently \$417,000 in non-high cost areas.

The threshold for required escrows for a first-lien, jumbo loan is now **2.5 percentage points above the APOR** as of the date the rate is set (it previously was 1.5 points).

This final rule does **not** change the required escrow APR threshold for non-jumbo loans. The rule does **not apply** to open-end credit plans (HELOCs), construction loans, temporary or bridge loans with terms of 12 months or less, or reverse mortgages.

The **proposed** rule would:

- Extend the minimum period an escrow account must be maintained for first-lien HPMLs (jumbo or otherwise) **from 1 to 5 years**. In certain circumstances, this period would be extended even longer (such as if the borrower was delinquent or otherwise in default);
- Provide an **exemption** from the mandatory escrow for certain loans secured by a condominium unit to planned unit developments and other similar properties;
- **Exempt** from the mandatory escrow requirement creditors that operate primarily in "rural or underserved" counties, annually originate 100 or fewer first-lien mortgage loans, and do not escrow for any mortgage loan serviced; and
- Require **new disclosure** explaining how the escrow account works or what the effects would be of not having an escrow account at all. These new disclosures would be required at least 3 business days before closing of the loan. An additional disclosure would be required at least 3 days before an escrow account is closed.

Fed Press Release 2/23/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110223b.htm>

Final Rule (3/2/11; 76 FR 11319): <http://edocket.access.gpo.gov/2011/pdf/2011-4384.pdf>

Proposed Rule (3/2/11; 76 FR 11598): <http://edocket.access.gpo.gov/2011/pdf/2011-4385.pdf>

### *Ability to Repay Proposal*

Section 1411 requires creditors, when making mortgage loans covered by TILA, to **determine a consumer's ability to repay before making a loan**, and also to establish minimum mortgage underwriting standards.

On April 19, 2011, the Fed issued a proposed rule under Reg. Z to implement these requirements. The rule would **apply to all consumer mortgage loans** covered by Reg. Z except HELOCs, timeshare plans, reverse mortgages, and temporary loans.

The proposal contains four alternative ways to comply with the requirement:

1. The lender would consider and verify eight (8) specified underwriting factors:
  - Income or assets relied upon in making the ability-to-repay determination;
  - Current employment status;
  - Monthly mortgage payment;
  - Monthly mortgage payment for any simultaneous mortgage loan;
  - Monthly payment for mortgage-related obligations;
  - Current debt obligations;
  - Monthly debt-to-income (DTI) ratio or residual income; and
  - Credit history.

If the loan is an adjustable rate mortgage (ARM) loan, the loan must be underwritten at the fully-indexed rate.

2. The lender makes a "**qualified mortgage**," which provides the creditor with protection from liability so long as the loan does not have certain features. There are two proposed definitions of what could constitute a "qualified mortgage" under this rule:
  - Alternative 1:
    - The loan would not contain negative amortization, interest-only payments, a balloon payment, or a term over 30 years;
    - Total points and fees would not exceed 3% of the total loan amount;
    - Income or assets relied upon in making the ability-to-repay determination are considered and verified; and
    - Underwriting of the mortgage:
      - Would be based on the maximum interest rate that may apply in the first 5 years;
      - Uses a payment scheduled that fully amortizes the loan over the term; and
      - Takes into account any mortgage-related obligations.
  - Alternative 2: This contains all the criteria listed under Alternative 1, plus the creditor would also have to consider and verify the consumer's:
    - Employment status;
    - Monthly payment for any simultaneous mortgage;
    - Current debt obligations;
    - Monthly DTI or residual income; and
    - Credit history.
3. The lender could make a **balloon-payment "qualified mortgage"** with a loan term of five years or more if it operates in a rural or underserved area. When making these loans, the lender must comply with the requirements for a qualified mortgage and underwrite the loan based on the scheduled payments, except the balloon payment. What precisely would constitute a "rural or underserved area" has yet to be defined.
4. The lender would refinance a "**non-standard mortgage**" with risky features (such as negative amortization, interest-only payments, or a balloon payment) into a more stable "**standard mortgage**" that has a lower payment. The new loan must also have limits on fees and not contain risky features. The lender must underwrite the "standard mortgage" based on the maximum rate that could apply over the first 5 years, and must consider and verify the underwriting factors listed in the general ability-to-repay standard, except the consumer's income or assets.

The proposal would also limit prepayment penalties, extend the time lenders would be required to retain evidence of compliance with the ability-to-repay standard and prepayment penalty provisions. It would also prohibit structuring a closed-end loan as a HELOC to evade the rule's requirements.

Since by the time the proposal on escrow requirements and ability to repay will be finalized, the CFPB (not the Fed) will control Reg. Z, the Bureau will issue the final rule.

Fed Press Release 4/19/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110419a.htm>

Fed's "Highlights of Proposed Ability-to-Repay Rules":

<http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20110419a1.pdf>

Proposed Rule (5/11/11; 76 FR 27390):

<http://www.gpo.gov/fdsys/pkg/FR-2011-05-11/pdf/2011-9766.pdf>

### *Fed Abandons Earlier Reg. Z Proposals*

As the Dodd-Frank Act makes so many changes to TILA and the CFPB takes control of Reg. Z on July 21, 2011, the Fed announced on February 1, 2011, that it will **not** pursue final rulemaking on three previously-issued proposals it published in 2009 and 2010. Prior to Dodd-Frank, the Fed commenced a comprehensive review of the mortgage regulations in Reg. Z and had issued significant and extensive proposals affecting both Reg Z's closed- and open-end provisions.

The two proposals issued in August of 2009 contained revisions to disclosures for closed-end mortgage loans and HELOCs. The third, issued in September 2010, would have expanded the right to rescind to additional loan types and amended disclosures to explain the right to rescind, as well as clarified the lender's responsibilities if a loan were rescinded. In addition, it would have mandated disclosures for loan modifications and for loan servicers, and changed reverse mortgage disclosures and placed restrictions on certain advertising and sales practices for reverse mortgages.

Announcement of Fed not finalizing earlier proposals; Fed Press Release 2/1/11:

<http://www.federalreserve.gov/newsevents/press/bcreg/20110201a.htm>

Abandoned proposals:

Fed Press Release 7/23/09: <http://www.federalreserve.gov/newsevents/press/bcreg/20090723a.htm>

Open-end Proposal (8/26/09; 74 FR 43428): <http://edocket.access.gpo.gov/2009/pdf/E9-18121.pdf>

Closed-end Proposal (8/26/09; 74 FR 43232): <http://edocket.access.gpo.gov/2009/pdf/E9-18119.pdf>

Fed Press Release 8/16/10: <http://www.federalreserve.gov/newsevents/press/bcreg/20100816e.htm>

Disclosures/Rescission (9/24/10; 75 FR 58539): <http://edocket.access.gpo.gov/2010/pdf/2010-20667.pdf>

## **Credit Risk Retention Proposal**

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One of the most critical and controversial components of Dodd-Frank, Section 941, amends the Securities Exchange Act of 1934 to require sponsors of asset-backed securities (ABS) to **retain at least 5% of the credit risk** of the assets underlying the securities. It prohibits the securitizer from directly or indirectly hedging or otherwise transferring the risk the securitizer is required to retain.

The securitization "sponsor," meaning the party that takes the loan from the originator before it is packaged for the secondary market, is the one required to hold the required risk retention; however, the sponsor could **allocate a "proportional" share of the risk to the originator** of the loan. The eventual proportion allocated to the originator must be voluntary on the originator's part, and could be agreed to by contract between the parties.

On March 31, 2011, the OCC, Fed, FDIC, SEC, FHFA, and HUD issued a proposed rule to implement this provision. It would provide for a risk retention requirement of less than 5% for an ABS issuance collateralized by residential mortgages, commercial mortgages, commercial real estate loans, or automobile loans, if such loans meet underwriting standards established by the agencies. The proposal is a first shot across the bow, as there are many issues yet to be resolved before the rule can be finalized. In fact, more than 170 questions were posed in the proposal, including whether the definitions and restrictions are too narrow.

### *Exemptions*

The proposed rules provided various **exemptions from the risk retention requirement**. Many of them have to do with ABS that are issued or collateralized by various obligations from federal or state authorities. Lenders, however, are mostly interested in exemptions for various loan types.

### *Qualified Residential Mortgage (QRM)*

The proposal exempts mortgage loans that meet stringent "**qualified residential mortgage**" standards. These standards include:

- A 20% downpayment requirement (meaning 80% or better LTV) for purchase loans, 75% LTV for refinancings, and 70% LTV for cash-out refinance. These ratios would be calculated **without** including mortgage insurance;
- Housing DTI of less than 28% (front-end ratio) and total DTI of less than 36% (back-end ratio);
- Specified credit history criteria (meaning no 60-day or worse delinquencies on any debt obligation within the past 24 months); and
- Various servicing requirements, such as a requirement that the originator incorporate loss mitigation actions and other procedures to deal with second liens when a first lien loan is modified.

Government-guaranteed securitizations of mortgages sold to Fannie Mae and Freddie Mac (the government-sponsored enterprises, or GSEs) **would also be exempt**, so long as the GSEs are in conservatorship or receivership with support from the federal government. This simply means **Fannie or Freddie loans would qualify for a 0% risk retention** requirement, again as long as the GSE remain under government conservatorship or receivership.

The rule also contains disclosure requirements to investors, to provide "material information" as to the securitizer's retained interests, and to monitor compliance.

As of June 1, the proposal had not yet been published in the Federal Register.

OCC NR 2011-39: <http://www.occ.gov/news-issuances/news-releases/2011/nr-ia-2011-39.html>

OCC Bulletin 2011-17: <http://www.occ.gov/news-issuances/bulletins/2011/bulletin-2011-17.html>

Fed Press Release 3/31/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110331a.htm>

FDIC PR-62-2011: <http://www.fdic.gov/news/news/press/2011/pr11062.html>

## **Credit Score Disclosures Proposal**

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Section 1100F amends the Fair Credit Reporting Act (FCRA) to require creditors to **disclose credit scores** and related information to consumers in both risk-based pricing notices and adverse action notices if a credit score was used in setting the terms of credit or taking adverse action

### *FCRA Risk-based Pricing Notices*

Both the Fed and Federal Trade Commission (FTC) on March 1, 2011, issued proposed rules to address this requirement. One proposal affects Reg. V to revise the content of risk-based pricing notices and to add model forms that include new credit score language. Both agencies noted, however, that the new requirement **does not change the alternative "exception notices"** used by lenders for mortgage loans and other types of credit, where the credit score and other disclosures are provided to all applicants early in the application process.

### *Reg. B and FCRA Adverse Action Notices*

A proposed amendment to Reg. B (ECOA) was also issued by the Fed to amend the **adverse action model forms** in that regulation. The Reg. B model adverse action form combine the notice requirements under both Reg. B and FCRA, so those forms will be changed to incorporate the requirement to include a credit score in a FCRA adverse action notice, if one was used, when taking adverse action.

Fed Press Release 3/1/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110301a.htm>

FTC Press Release 3/1/11: <http://www.ftc.gov/opa/2011/03/riskpricing.shtm>

Reg. B Proposal (3/15/11; 76 FR 13896): <http://edocket.access.gpo.gov/2011/pdf/2011-5417.pdf>

Reg. V Proposal (3/15/11; 76 FR 13902): <http://edocket.access.gpo.gov/2011/pdf/2011-5413.pdf>

## Commercial Data Collection Delay

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Section 1071 amends the Equal Credit Opportunity Act (ECOA) to impose a HMDA-like data collection and submission requirement on financial institutions for small business loan applications, and women- and minority-owned business loan applications. This provision of Dodd-Frank, however, listed no effective date or other information as to when regulations were to be written (by the CFPB, who assumes control over Reg. B); thus, the industry is left to wonder whether this requirement becomes effective on July 21, 2011. If so, what precisely should be collected, from whom, and when? The statutory language is not clear enough to provide concrete guidance.

On April 11, 2011, the General Counsel of the CFPB issued a letter announcing that although Section 1071 does indeed become effective on July 21, 2011, its **implementation will be delayed** until the Bureau's implementing regulations (yet to be written) are published and take effect. The letter states that the Bureau will "act expeditiously" to issue regulations and request input from all interested parties.

CFPB General Counsel Letter:

<http://www.consumerfinance.gov/wp-content/uploads/2011/04/GC-letter-re-1071.pdf>

## Funds Availability (Reg. CC) Changes

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Section 1086 amends the Expedited Funds Availability Act to provide that banks must make \$200 (rather than the \$100, as the existing rule requires) of the day's deposits available by the next business day after the day of deposit (unless a proper exception hold is taken). In addition, the amount will be raised every 5 years based on the rate of inflation. These provisions will be **effective July 21, 2011**, but were not issued by the CFPB. This portion of Reg. CC remains with the Federal Reserve.

On March 3, 2011, the Fed issued a proposed rule amending Reg. CC to put this into place. The change was included with other (non-Dodd-Frank mandated) proposed amendments to Reg. CC, including:

- Entitling banks to expeditious returns of checks only if they agree to electronic receipt;
- Permitting paying banks to require checks be presented for same-day settlement electronically; and
- Shortening the exception hold period to 4 business days (from 7).

The proposal also removes all references in the regulation to "non-local" checks, so all checks would be subject to a 2-business-day hold period, eliminating the present rule that allows a 4-business-day hold for non-local checks. There are no longer any non-local checks, as all checks are processed through one Federal Reserve processing center (in Cleveland).

Proposed new model forms for making disclosures to consumers were also published.

Fed Press Release 3/3/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110303a.htm>

Proposed Rule (3/25/11; 76 FR 16862): <http://edocket.access.gpo.gov/2011/pdf/2011-5449.pdf>

## Repeal of Reg. Q

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Section 627 repeals the prohibition against paying interest on demand deposits, effectively doing away with the Fed's Regulation Q. On April 6, 2011, the Fed issued a proposal rule to repeal the regulation, which will become **effective July 21, 2011**.

On that date, financial institutions may offer interest-bearing checking accounts to any customer, whether consumer or commercial. Along with the repeal, the Fed sought comments on the effect of the repeal on balance sheets and income, impacts on short-term funding markets, expected demand for interest-bearing checking accounts, and the potential competitive burden on smaller institutions.

Fed Press Release 4/6/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110406a.htm>

Fed's Proposed Repeal (4/14/11; 76 FR 20892): <http://edocket.access.gpo.gov/2011/pdf/2011-9002.pdf>

On April 21, 2011, the FDIC issued a similar proposal to amend its regulations to conform to Section 627. The rule, which will apply to all insured, state-chartered, nonmember banks (meaning FDIC-regulated), will rescind 12 CFR Part 329, which implements the FDIC's prohibition against paying interest on demand deposits.

FDIC FIL-23-2011: <http://www.fdic.gov/news/news/financial/2011/fil11023.html>

FDIC's Proposed Repeal (4/15/11; 76 FR 21265): <http://edocket.access.gpo.gov/2011/pdf/2011-9210.pdf>

## Foreign Remittance Transfers under Reg. E

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Section 1073 amends the Electronic Fund Transfer Act, adding a new section to require providers of "**remittance transfers**" to provide disclosures about such transfers, including the exchange rate, applicable fees and taxes, and the amount to be received by the "**designated recipient**." Disclosures must be made both in English and the appropriate foreign language.

A "remittance transfer" is an electronic transfer of funds from a sender located in the U.S. to a "designated recipient" located in a foreign country.

On May 12, 2011, the Fed issued a proposal under Reg. E to require such providers to issue a written receipt when payment is made for a remittance transfer. This disclosure must include:

- Specified pre-payment disclosures;
- The date of availability of the funds;
- The recipient's contact information; and
- Information regarding the sender's error resolution and cancellation rights.

The proposal also includes two alternatives for implementing the liability standards for providers.

Fed Press Release 5/12/11: <http://www.federalreserve.gov/newsevents/press/bcreg/20110512a.htm>

Proposed rule (5/23/11; 76 FR 29902): <http://www.gpo.gov/fdsys/pkg/FR-2011-05-23/pdf/2011-12019.pdf>

## Permanent Deposit Insurance Increase

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Section 335 permanently increased the amount of federal (FDIC and NCUA) deposit insurance to **\$250,000 per category**, from \$100,000. This change was made pre-Dodd-Frank, in October 2008. The FDIC and NCUA also announced signage to reflect the new limit.

FDIC PR-2010-161: <http://www.fdic.gov/news/news/press/2010/pr10161.html>

FDIC FIL-40-2010: <http://www.fdic.gov/news/news/financial/2010/fil10040.html>

NCUA MR10-0722: [http://www.ncua.gov/news/press\\_releases/2010/MR10-0722\\$250KNCUAShareInsuranceProtectionNowPermanent.pdf##](http://www.ncua.gov/news/press_releases/2010/MR10-0722$250KNCUAShareInsuranceProtectionNowPermanent.pdf##)

*Unlimited Deposit Insurance on Noninterest-bearing Accounts*

Section 343 provides for **unlimited deposit insurance coverage on noninterest-bearing transaction accounts** from December 31, 2010, to December 31, 2012. This provision replaced unlimited coverage allowed under the Transaction Account Guarantee (TAG) Program. Coverage is limited to noninterest-bearing accounts and originally (per Dodd-Frank) did not cover interest-bearing NOW accounts or Interest on Lawyers Trust Accounts (IOLTAs).

However, an Act of Congress signed into law at the end of 2010 **continues unlimited deposit insurance protection for IOLTAs**. On January 18, the FDIC issued a final rule to include IOLTAs within the definition of "noninterest-bearing transaction accounts" for purposes of extending the temporary unlimited deposit coverage through December 31, 2012.

Act of Congress (Pub. L. 111-343): <http://www.govtrack.us/congress/billtext.xpd?bill=h111-6398>

FDIC PR-8-2011: <http://www.fdic.gov/news/news/press/2011/pr11008.html>

Final rule: 1/27/11 (76 FR 4813): <http://edocket.access.gpo.gov/2011/pdf/2011-1732.pdf>

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*To request an electronic copy of this whitepaper, contact [learn@bai.org](mailto:learn@bai.org).*

## About BAI

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