LENDERS UPDATE™

ALT & ASSOCIATES NEWSLETTER

A COMPLIMENTARY SERVICE TO THE MORTGAGE LENDING INDUSTRY

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CFPB'S SUPERVISION REPORT

On October 31, the Consumer Financial Protection Bureau (CFPB) issued its first "Supervisory Highlights". This is the first in an ongoing periodic report on the CFPB's supervision of financial institutions and service providers to determine their compliance with applicable federal consumer financial laws. This report summarizes work completed by the CFPB between July 2011 and the end of September 2012. The Bureau communicates its findings to the entities it supervises, directing corrective action or, where consumers have experienced harm, order restitution. It may pursue other relief as appropriate.

The Bureau's goals or principles are 1) focus on consumers, 2) consistent standards and 3) supervision based on an analysis of available data. The current summary discusses deficient Compliance Management Systems (CMS), regulatory violations related to credit cards and credit reporting and to consumer finance law violations in mortgage lending. We will briefly summarize those related to mortgage lending.

In this first summary, substantial portions which we will not cover, are directed to violations by credit card issuers specifically Capital One Bank, Discover Bank and the American Express companies.

The entire report may be viewed on the CFPB's website under news reports for October 31.

The Bureau views a CMS as a critical component to ensure that the lender's policies and practices are in full compliance with requirements of federal consumer financial law and that these are being followed by the lender. The examiners consider whether the entity has addressed these specific issues:

- **internal controls and oversight,**
- **training,**
- **internal monitoring,**
- **complaint response,**
- **independent testing and audits,**
- **third-party service provider oversight,**
- **recordkeeping,**
- **product development,**
- **business acquisition, and**
- **marketing practices.**

The CFPB found financial institutions failed to adopt and/or follow internal policies and procedures. The report states that it is important for financial institutions to ensure that the policies and procedures that are adopted are clearly communicated to employees, fully implemented, and regularly followed. The examination evaluates both the understanding and application of the management program by its managers and employees. The examiner's work revealed situations in which many elements of a compliance policy were in place, but were not followed.

The summary also addresses the use of affiliate or third-party service providers by financial institutions. The supervision of these service providers is a key component of a CMS. The mere fact that an entity enters into a relationship with a service provider does not absolve the financial institution of responsibility for complying with the law.

Again, the examiners found instances of a failure to establish a comprehensive management program to manage and ensure the compliance of service providers. An example cited by the summary is of companies which fail to adequately coordinate their correspondence or disclosures to consumers with those of their service providers.

As some of you know from personal experience, fair lending is a significant issue. The CFPB requires that lenders establish fair lending policies, procedures and internal controls to ensure that it is operating in compliance with ECOA and

other applicable laws. The examiners have identified the following common characteristics to be associated with an adequate program:

- A fair lending policy statement,
- Regular training for employees, officers and board members,
- Monitoring for compliance with fair lending and other policies and procedures and for larger institutions, regular statistical analysis of data for potential disparities on a prohibited basis, and
- Assessment of marketing practices for loan products.

The examiners found instances in which institutions had no policies in place or failed to implement its policies across the entire range of product lines.

The CFPB also found numerous violations of federal consumer law made by mortgage originators, particularly involving RESPA and TILA. RESPA violations included failure to make proper disclosures of costs and other terms due to inadequate or improper Good Faith Estimates or HUD-1s. TILA violations included inaccurate interest rate disclosures and payment amounts and schedules, as well as disclosures regarding late payments, security interests and assumption policies.

Where violations have been found, institutions have been directed to implement proper policies, procedures, and monitoring to prevent re-occurrence and to ensure that third-party vendors, including mortgage brokers, are identified and included in the institution's oversight program and in relevant policies and procedures. New disclosures and, at times, reimbursement, have been ordered.

Another area of concern revealed by the Bureau's examinations is mortgage originator compliance with the Home Mortgage Disclosure Act (HMDA). Lenders are generally required to report specific information to regulators and the public. The CFPB expects financial institutions to have strong systems in place to ensure HMDA compliance. The examinations have identified significant error rates in data reported. The examiners have directed resubmission of data to correct errors and directed that financial institutions improve their data collection and reporting systems by modifying policies and procedures.

Perhaps a regular review of these supervisory reports should become mandatory reading as a part of any CMS.

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ALT & ASSOCIATES provides regulatory, compliance, operational advice and transactional assistance, as well as litigation representation, to the financial services industry. Over the past three decades, members of the firm have represented Institutional Lenders and Mortgage Bankers and Brokers in all aspects of their operations.

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