March 11, 2015

CFPB Report Outlines Legal Violations Uncovered by Supervision

By Anna DeSimone

The CFPB has published Supervisory Highlights which summaries compliance violations uncovered by the bureau's supervision. Please click on the link to view the full 20-page report.

http://www.consumerfinance.gov/reports/supervisory-highlights-winter-2015/

Within the detailed section concerning mortgage origination, a key violation pertained to "an effective compliance management system." A recommended component includes a compliance audit program. Bankers Advisory, a CliftonLarsonAllen, LLP Division has 30 years direct experience in performing comprehensive compliance and fair lending assessments.

Please contact me at anna@bankersadvisory.com to discuss how our 30 years of experience can help your organization meet its important compliance objectives. For more information, see Compliance Services and Fair Lending.

http://cdn.s3.webcontentor.com/OFFICE/BANKER01/files/misc_files/140410082233_QUALITY CONTROL.pdf

http://cdn.s3.webcontentor.com/OFFICE/BANKER01/files/misc_files/140410082258_FAIR LENDING.pdf

March 11, 2015, the Consumer Financial Protection Bureau (CFPB) released its latest supervision report highlighting legal violations uncovered by the Bureau's examiners. The Bureau found deceptive student loan debt collection practices, unfair and deceptive overdraft practices, mortgage origination violations, fair lending violations, and mishandled disputes by consumer reporting agencies. The report also shows that CFPB supervisory resolutions resulted in remediation of $19.4 million to more than 92,000 consumers.

The March 2015, which is the seventh edition of supervisory highlights, generally covers supervisory activities between July 2014 and December 2014. Among the findings were:

- **Deceptive student loan debt collection practices**
- **Unfair and deceptive overdraft practices**
- **Mortgage origination violations**

- **Fair lending violations**
- **Mishandling of disputes by consumer reporting agencies**

In all cases where CFPB examiners find violations of law, they alert the institutions to their concerns and outline necessary remedial measures. When appropriate, the CFPB opens investigations for potential enforcement actions. The CFPB expects all entities under its supervision to respond to customer complaints and identify major issues and trends that may pose broader risks to their customers.

Additional detail is provided for each area concerning origination and fair lending

<u>Mortgage Origination Violations</u>

Bureau examiners found that some loan originators illegally received compensation based on the terms of the loan. Examiners also found that at some loan originators the amounts disclosed on the HUD-1 form improperly exceeded those disclosed on the Good Faith Estimate. Some loan originators advertised the length of payment, amount of payments, numbers of payments, and finance charges without providing the required disclosures. And, the Bureau found weaknesses in compliance management systems that played a significant role in the identified violations.

Loan originators cannot receive compensation based on a term of a transaction

Examiners found that branch managers were loan originators and owners of related marketing services entities. Supervision found instances of improperly allocated expenses on branch income statements which resulted in marketing services entities receiving income based on the profitability of retail loans originated by branch managers. Consequently, branch managers, as owners of the marketing services entities, received compensation based on the terms of transactions originated by the branch managers themselves. Supervision directed that compensation to loan originators based on a term of a transaction, including branch managers, cease.

Improper use of lender credit absent changed circumstances

Examiners identified practices that caused the amounts disclosed on the HUD-1 to exceed those disclosed on the GFE. Due to inadequate training and compliance policies and procedures, a lender credit in one or more examinations was reduced on the HUD-1 to prevent the borrower, on a no-cost refinance, from receiving excess cash-back at closing. This reduction, however, in the absence of changed circumstances, impermissibly increased the final adjusted origination charge, a violation of Regulation X. The difference in the amounts disclosed was refunded to consumers.

Failing to provide the Good Faith Estimate in a timely manner

Examiners identified policies and procedures that did not define sufficiently when an application was received. As a result, the lender did not measure the three-business-day period accurately, and this caused the good faith estimates to be delayed beyond the three-business-day requirement, a violation of Regulations X and Z. Examiners directed appropriate corrective action.

Improperly using advertisements with triggering terms without the required additional disclosures

Regulation Z requires advertisements to include disclosures when certain triggering terms are advertised. Examiners found in one or more institutions that social media advertising was not subject to monitoring or compliance audit, which are components of an effective compliance management system. Loan originators created their own advertisements and content. Loan originators advertised the length of payment, amount of payments, numbers of payments, and finance charges, without providing the required disclosures, a violation of Regulation Z. These institutions agreed to appropriate corrective actions.

Adverse action notice deficiencies and failure to provide the notice in a timely manner

CFPB examiners found one or more supervised entities failed to provide the requisite information in denial notices as set forth in Regulation B and failed to notify an applicant of action taken within 30 days after receiving the completed application. These errors were attributed to weaknesses in the compliance audit programs and the monitoring and corrective action component of the compliance programs. Supervision directed the supervised entities to conduct a review of all mortgage loan applications denied within the relevant time period and take appropriate corrective action, including providing corrected notices to applicants.

Deficiencies in compliance management systems

A sound and robust compliance management system is essential to ensuring compliance with Federal consumer financial law and preventing associated risks of harm to consumers. As noted in previous issues of Supervisory Highlights, an effective compliance management system includes board and management oversight, a compliance program, a consumer complaint management program, and a compliance audit program. The board of directors and senior management should, among other things, adopt clear policy statements concerning consumer compliance, establish a compliance function to set policies and procedures, and assign resources to the compliance function commensurate with the size and complexity of the supervised entity's practices and operations. A compliance program should include policies and procedures, training, and monitoring and corrective action processes. A compliance audit program should assist the board of directors or board committees in determining whether policies and standards adopted by the board are being implemented, and should also identify any significant gaps in board policies and standards.

At one or more institutions, examiners concluded that a weak compliance management system allowed numerous violations of Regulations B, X, and Z to occur. For example, in one or more instances, a supervised entity first adopted a compliance policy manual and hired a compliance officer shortly before the start of a Bureau examination, and as a result, lacked procedures to implement the manual and was unable to effectively communicate compliance responsibilities to employees. In one or more instances, an institution's board members did not receive any training, the training provided to employees was not comprehensive or accurate, and training content was neither kept current nor directed towards the appropriate employees.

At one or more institutions, Supervision found that compliance audits performed by third parties were limited in scope and failed to identify numerous regulatory violations found by examiners, and audit results were not reported to directors. Examiners directed the institutions to take appropriate action to address the weaknesses in order to implement effective compliance management systems.

Fair Lending Violations

Bureau examiners found that one or more institutions rejected mortgage applications from consumers because they relied on public assistance income, such as Social Security or retirement benefits, in order to repay the loan. Marketing materials contained written statements regarding the prohibition on non-employment sources of income, and discouraged applicants who received public assistance from applying for credit. This violates the Equal Credit Opportunity Act. CFPB examiners directed that remediation be made to harmed applicants.

Consideration of protected forms of income

Since the start of the Bureau's supervision program, examiners have conducted ECOA targeted mortgage origination reviews at institutions, both bank and nonbank, that receive about 40% of the applications and make about 40% of the originations reported pursuant to the Home Mortgage Disclosure Act (HMDA), and have found that many lenders operate in compliance with the ECOA and its implementing regulation, Regulation B. At some institutions, however, examiners have identified violations of the ECOA and Regulation B, including violations related to the failure to consider public assistance income or other sources of income protected by Regulation B.

During recent examinations, the Bureau's examination staff found one or more violations of the ECOA and Regulation B related to the treatment of protected forms of income. Applicants were automatically declined if they relied on income from a non-employment source, such as social security income or retirement benefits, in order to repay the loan. Marketing materials contained written statements regarding the prohibition and may have discouraged applicants who received public assistance or other protected sources of income from applying for credit.

The relevant supervised entities were directed by examination staff to identify applicants who were wrongly denied on the basis of their protected income source, as well as potential applicants who were discouraged by the marketing materials. Supervision also directed that remediation be made to harmed applicants and prospective applicants, including reimbursement of fees and interest; the opportunity to reapply; and additional remuneration for any consumers who were improperly denied and subsequently lost their homes.