January 2018

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

Department of Defense Amends Military Lending Act Interpretive Rule.

In mid-December, with little warning or fanfare, the Department of Defense (DoD) issued clarifications to its interpretive rules regarding the Military Lending Act (MLA). The clarifications will impact creditors. What follows is a brief overview of some recent developments regarding the MLA, and the interpretive rules and clarifications.

In July 2015, the DoD issued a final rule (2015 Final Rule or Rule) amending its regulation implementing the MLA primarily for the purpose of extending the protections of the MLA to a broader range of closed-end and open-end credit products, rather than the limited credit products that were covered prior to the amendments.

In addition, the 2015 Final Rule amended other provisions such as those relating to the optional mechanism a creditor may use when assessing whether a consumer is a ‘‘covered borrower,’’ and the disclosures that a creditor must provide to a covered borrower. It also implemented the enforcement provisions of the MLA.

Following issuance of the 2015 Final Rule, the DoD received requests from the financial services industry to provide interpretations of certain points raised by the Rule. The DoD addressed some of these points by issuing an interpretive rule in the form of 19 questions and answers. The DoD issued this first set of interpretations on August 26, 2016 (2016 Interpretive Rule). However, in the industry's view, the 2016 Interpretive Rule did not adequately address some of the points previously raised. In response, the DoD issued another interpretive rule (2017 Interpretive Rule) to provide clarification to several of the existing questions and answers (#2, #17, #18, and #19). The 2017 Interpretive Rule also added a new question and answer (#20).

As with the 2016 Interpretive Rule, the DoD took the position that the 2017 Interpretive Rule did not change the regulation implementing the MLA, but merely stated the DoD's preexisting interpretations of an existing regulation. Thus, under provisions in the Administrative Procedure Act, the DoD asserted that the 2017 Interpretive Rule was exempt from notice and comment requirements, and, was effective immediately upon publication in the *Federal Register*. The 2017 Interpretive Rule was published in the *Federal Register* on December 14, 2017.

Creditors should review their MLA procedures in light of the 2017 Interpretive Rule, and make adjustments, as applicable. This may require a review of all three documents noted above. The 2015 Final Rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2015-07-22/pdf/2015-17480.pdf; the 2016 Interpretive Rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2016-08-26/pdf/2016-20486.pdf; and the 2017 Interpretive Rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2017-12-14/pdf/2017-26974.pdf.

For your convenience, the questions and answers portion of the 2017 Interpretive Rule is reprinted below.

2. *Does credit that a creditor extends for the purpose of purchasing a motor vehicle or personal property, which secures the credit, fall within the exception to "consumer credit" under 32 CFR 232.3(f)(2)(ii) or (iii) where the creditor simultaneously extends credit in an amount greater than the purchase price of the motor vehicle or personal property?*

Answer: The answer will depend on what the credit beyond the purchase price of the motor vehicle or personal property is used to finance. Generally, financing costs related to the object securing the credit will not disqualify the transaction from the exceptions, but financing credit-related costs will disqualify the transaction from the exceptions. Section 232.3(f)(1) defines ‘‘consumer credit’’ as credit offered or extended to a covered borrower primarily for personal, family, or household purposes that is subject to a finance charge or payable by written agreement in more than four installments. Section 232.3(f)(2) provides a list of exceptions to paragraph (f)(1), including an exception for any credit transaction that is expressly intended to finance the purchase of a motor vehicle when the credit is secured by the vehicle being purchased and an exception for any credit transaction that is expressly intended to finance the purchase of personal property when the credit is secured by the property being purchased.

A credit transaction that finances the object itself, as well as any costs expressly related to that object, is covered by the exceptions in § 232.3(f)(2)(ii) and (iii), provided it does not also finance any credit-related product or service. For example, a credit transaction that finances the purchase of a motor vehicle (and is secured by that vehicle), and also finances optional

leather seats within that vehicle and an extended warranty for service of that vehicle is eligible for the exception under § 232.3(f)(2)(ii). Moreover, if a covered borrower trades in a motor vehicle with negative equity as part of the purchase of another motor vehicle, and the credit transaction to purchase the second vehicle includes financing to repay the credit on the trade-in vehicle, the entire credit transaction is eligible for the exception under § 232.3(f)(2)(ii) because the trade-in of the first motor vehicle is expressly related to the purchase of the second motor vehicle. Similarly, a credit transaction that finances the purchase of an appliance (and is secured by that appliance), and also finances the delivery and installation of that appliance, is eligible for the exception under § 232.3(f)(2)(iii).

In contrast, a credit transaction that also finances a credit-related product or service rather than a product or service expressly related to the motor vehicle or personal property is not eligible for the exceptions under § 232.3(f)(2)(ii) and (iii). For example, a credit transaction that includes financing for Guaranteed Auto Protection insurance or a credit insurance premium would not qualify for the exception under § 232.3(f)(2)(ii) or (iii). Similarly, a hybrid purchase money and cash advance credit transaction is not expressly intended to finance the purchase of a motor vehicle or personal property because the credit transaction provides additional financing that is unrelated to the purchase. Therefore, any credit transaction that provides purchase money secured financing of a motor vehicle or personal property along with additional "cashout" financing is not eligible for the exceptions under § 232.3(f)(2)(ii) and (iii) and must comply with the provisions set forth in the MLA regulation.

17. *Does the limitation in § 232.8(e) on a creditor using a check or other method of access to a deposit, savings, or other financial account maintained by the covered borrower prohibit the borrower from granting a security interest to a creditor in the covered borrower's checking, savings or other financial account?*

Answer: No. The prohibition in § 232.8(e) does not prohibit covered borrowers from granting a security interest to a creditor in the covered borrower's checking, savings, or other financial account, provided that it is not otherwise prohibited by other applicable law and the creditor complies with all other provisions of the MLA regulation, including the limitation on the MAPR to 36 percent. As discussed in Question and Answer #16 of these Interpretations, § 232.8(e) prohibits a creditor from using the borrower's account information to create a remotely created check or remotely created payment order in order to collect payments on consumer credit from a covered borrower or using a postdated check provided at or around the time credit is extended.

Section 232.8(e)(3) further clarifies that covered borrowers may convey security interests in checking, savings, or other financial accounts by describing a permissible security interest granted by covered borrowers. Borrowers may convey security interests for all types of consumer credit covered by the MLA regulation.

Creditors should also note, however, that 32 CFR 232.7(a) provides that the MLA does not preempt any State or Federal law, rule or regulation to the extent that such law, rule or regulation provides greater protection to covered borrowers than the protections provided by the MLA. For example, although the MLA regulation does not prohibit borrowers from conveying security interests in all types of consumer credit covered by the regulation, including credit card accounts, such accounts may also be subject to other laws, rules and regulations governing offsets and security interests. See, e.g., 12 CFR 1026.12(d).

18. *Does the limitation in § 232.8(e) on a creditor using a check or other method of access to a deposit, savings, or other financial account maintained by the covered borrower prohibit a creditor from exercising a statutory right, or a right arising out of a security interest a borrower grants to a creditor, to take a security interest in funds deposited within a covered borrower's account at any time?*

Answer: No. In addition to the security interests granted by borrowers to creditors, as discussed in Question and Answer #17 of these Interpretations, above, under certain circumstances Federal or State statutes may grant creditors statutory liens on funds deposited within covered borrowers' asset accounts. Section 232.8(e) does not prohibit a creditor from exercising rights to take a security interest in funds deposited into a covered borrower's account at any time, including enforcing statutory liens, provided that it is not otherwise prohibited by other applicable law and the creditor complies with all other provisions of the MLA regulation, including the limitation on the MAPR to 36 percent. For example, under 12 U.S.C. 1757(11) Federal credit unions may "enforce a lien upon the shares and dividends of any

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member, to the extent of any loan made to him and any dues or charges payable by him.''

As discussed in Question and Answer #16 of these Interpretations, § 232.8(e) serves to prohibit a creditor from using the borrower's account information to create a remotely created check or remotely created payment order in order to collect payments on consumer credit from a covered borrower or using a postdated check provided at or around the time credit is extended. Section 232.8(e)(3) describes a permissible activity under § 232.8(e). However, the fact that § 232.8(e)(3) specifies a particular time when a creditor may take a security interest in funds deposited in an account does not change the general effect of the prohibition in § 232.8(e). Therefore, § 232.8(e) does not impede a creditor from—for example—exercising a statutory right to take a security interest in funds deposited in an account at any time, provided that the security interest is not otherwise prohibited by other applicable law and the creditor complies with all other provisions of the MLA regulation, including the limitation on the MAPR to 36 percent.

Creditors may exercise the right to take a security interest in funds deposited into a covered borrower's account in connection with all types of consumer credit covered by the MLA regulation, including credit card accounts, provided the creditor's actions are not prohibited by other State or Federal law, rule or regulation that provides greater protection to covered borrowers than the protections provided in the MLA. For example, although the MLA regulation does not prohibit borrowers from conveying security interests in all types of consumer credit covered by the regulation, including credit card accounts, such accounts may also be subject to other laws, rules and regulations governing offsets and security interests. See, e.g., 12 CFR 1026.12(d).

20. *To qualify for the optional safe harbor under 32 CFR 232.5(b)(3), must the creditor determine the consumer's covered borrower status simultaneously with the consumer's submission of an application for consumer credit or exactly 30 days prior?*

Answer: No. Section 232.5(b)(3)(i) and (ii) permit the creditor to qualify for the safe harbor when it makes a timely determination regarding the status of a consumer at the time the consumer either initiates the transaction or submits an application to establish an account, or anytime during a 30-day period of time prior to such action. Therefore, a creditor qualifies for the safe harbor under § 232.5(b) when the qualified covered borrower check that the creditor relies on is conducted at the time a consumer initiates a credit transaction or applies to establish an account, or up to 30 days prior to the action taken by the consumer. Similarly, the timing provisions in § 232.5(b)(3)(i) and (ii) permit a creditor to qualify for the safe harbor when it conducts a qualified covered borrower check simultaneously with the initiation of the transaction or submission of an application by the consumer or during the course of the creditor's processing of that application for consumer credit. ■

Recently Enacted Legislation Expands Who May Receive Property Through Transfer by Affidavit

On December 1, 2017, 2017 Wisconsin Act 90 amended Wisconsin Statute Section 867.03 relating to the transfer by affidavit option for small estates. The Act added a category of affiants who may receive property left by a decedent.

Generally speaking, Wisconsin Statute Section 867.03 provides for classifications of persons (known as affiants) who may receive property less than or equal to $50,000 in value left by a decedent. Prior to Act 90 those affiants were limited to: any heir of the decedent, trustee of a revocable trust created by the decedent, or person who was guardian of the decedent at the time of the decedent's death.

As of December 1, 2017, a person named in the will to act as personal representative may also receive property of a decedent subject to certain requirements.

Act 90 also created 867.03(1j) requiring that a person who receives an affidavit from a person named in the will to act as personal representative may not transfer any money due the decedent until 30 days after receiving the affidavit. If, during the 30-day period, the person who received the affidavit receives an affidavit for the same decedent from another person, the person who received the affidavits may not transfer any money due the decedent unless ordered to do so by a court.

Meaning, that if a financial institution receives a transfer by affidavit from a person named in a will to act as personal representative, the institution should have procedures in place to wait 30 days before transferring property. If, during that 30-day period, the financial institution receives another valid transfer by affidavit, no property should be transferred to any party until instructed by court order.

2017 Wisconsin Act 90 may be viewed at: http://docs.legis.wisconsin.gov/2017/related/acts/90 ■

member, to the extent of any loan made to him and any dues or charges payable by him.''

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Meaning, that if a financial institution receives a transfer by affidavit from a person named in a will to act as personal representative, the institution should have procedures in place to wait 30 days before transferring property. If, during that 30-day period, the financial institution receives another valid transfer by affidavit, no property should be transferred to any party until instructed by court order.

2017 Wisconsin Act 90 may be viewed at: http://docs.legis.wisconsin.gov/2017/related/acts/90 ■

Tax Reform Impact on Home Equity Loans

There continues to be much confusion around the impact of the new tax law on home equity lines of credit and home equity loans. While bankers should not be providing tax advice as taxpayers should be consulting with their own professional advisor, WBA realizes it is helpful for bankers to have a general understanding of the impact their loan products have on borrowers to not only answer general questions but also to guide bank product development and marketing strategies. This article will attempt to explain the tax law changes as it relates to home equity loans.

The general rule for taxpayers itemizing deductions is that effective for tax years beginning after December 31, 2017, and before January 1, 2026, the Tax Cuts and Jobs Act (TCJA) no longer allows a deduction for interest on home equity debt regardless of when the home equity debt was originally incurred, and regardless of the lien position of the home equity debt. In other words, there is no grandfathering treatment for existing home equity loans and the rules apply whether the loan is a first, first-lien equivalent, or true second mortgage on a principal residence and/or second home. For taxpayers who will not benefit from itemizing deductions under the new law, this analysis is inapplicable.

The only important exception to this general rule for home equity debt is if the ***purpose*** of the debt qualifies under the tax code as "acquisition indebtedness." Under the tax code, acquisition indebtedness of a principal residence and/or second home is debt that is incurred in acquiring, constructing, or substantially improving a qualified residence. "Qualified residence" is also a defined term under the tax code but generally includes the taxpayer's principal residence and one and one other residence of the taxpayer. Acquisition indebtedness also includes indebtedness from the refinancing of other acquisition indebtedness, but only to the extent of the amount of the refinanced indebtedness. It is the responsibility of the taxpayer, not the bank, to keep track of debt that is acquisition indebtedness compared to debt that is for other purposes.

Under the new law, the aggregate amount a taxpayer may treat as acquisition indebtedness can't exceed $750,000 ($375,000 for married persons filing separately). Any acquisition debt (whether a traditional closed-end mortgage or home equity debt qualifying as acquisition indebtedness) incurred on or before December 15, 2017 is instead subject to the $1,000,000 ($500,000 for married persons filing separately) acquisition debt limit. Note that in applying the $750,000/$375,000 acquisition debt limit to any indebtedness incurred after December 15, 2017, the $750,000/$375,000 limit must be reduced (but not below zero) by the amount of any indebtedness incurred on or before December 15, 2017 that is treated as acquisition indebtedness for purposes of the qualified residence interest (QRI) deduction for the tax year.

As an example, assume a taxpayer had a first mortgage of $150,000 of which $100,000 was from refinancing the original acquisition mortgage and $50,000 was cash taken out for college costs. The $100,000 would be acquisition debt and the $50,000 would be home equity debt. Assume that same taxpayer also took out a $25,000 home equity line of credit for the sole purpose of remodeling the kitchen. That debt would qualify as acquisition debt because it is for the purpose of improving a qualified residence. In this example, the total acquisition debt would be $125,000 – the portion of the mortgage loan used for acquisition and the home equity line of credit. The interest on the portion of the mortgage loan ($50,000) that was used for college costs would be nondeductible. Tracing rules apply that consider the least advantageous debt to be paid off first, so principal on the first mortgage would be applied to the home equity portion first.

Again, it is important to not give your customers tax advice as often bankers do not know how debt proceeds, particularly home equity debt proceeds, are spent by borrowers. It is expected that the IRS will issue guidance on this and other aspects of the TCJA. WBA will inform the membership as such guidance is published. ■

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Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

Customer Due Diligence Rule

In May of 2016 the Financial Crimes Enforcement Network (FinCEN) issued final rules under the Bank Secrecy Act implementing customer due diligence (CDD) requirements. The CDD requirements require financial institutions to identify and verify the identity of beneficial owners of legal entity customers. The final rule makes certain additional amendments to certain anti-money laundering program (AML) requirements.

The final rule was effective July 11, 2016. The final rule is applicable on May 11, 2018. This article highlights certain provisions of the final rule, seeks to present its various requirements generally, and prepare financial institutions for the upcoming applicability date. As this article's scope is general rather than comprehensive, WBA recommends that financial institutions consult the final rule in its entirety when reviewing its CDD and AML program. The final rule may be found at: https://www.gpo.gov/fdsys/pkg/FR-2016-05-11/pdf/2016-10567.pdf.

Definitions

Covered Financial Institution

Covered financial institution bears the same meaning set forth in 31 CFR § 1010.605(e)(1). Generally speaking, this means federally regulated banks and federally insured credit unions, mutual funds, brokers or dealers in securities, futures commission merchants, and introducing brokers in commodities.

Account

Account bears the same meaning set forth in 31 CFR § 1020.100(a):

Account means a formal banking relationship established to provide or engage in services, dealings, or other financial transactions including a deposit account, a transaction or asset account, a credit account, or other extension of credit. Account also includes a relationship established to provide a safety deposit box or other safekeeping services, or cash management, custodian, and trust services.

Account does not include:

1. A product or service where a formal banking relationship is not established with a person, such as check-cashing, wire transfer, or sale of a check or money order;

2. An account that the bank acquires through an acquisition, merger, purchase of assets, or assumption of liabilities; or

3. An account opened for the purpose of participating in an employee benefit plan established under the Employee Retirement Income Security Act of 1974.

Beneficial owner

The final rule defines beneficial owner as each of the following:

1. Each individual, if any, who, directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, owns 25 percent or more of the equity interests of a legal entity customer; and

2. A single individual with significant responsibility to control, manage, or direct a legal entity customer, including:

   - An executive officer or senior manager (e.g., a Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, or Treasurer); or

   - Any other individual who regularly performs similar functions.

Legal Entity Customer

A legal entity customer is defined by the final rule as a corporation, limited liability company, or other entity created by the filing of a public document with a Secretary of State or similar office, a general partnership, and any similar entity formed under the laws of a foreign jurisdiction that opens an account. This includes limited partnerships, business trusts that are created by a filing with a state office, and any other entity created in this manner. A legal entity customer does not include sole proprietorships, unincorporated associations, or natural persons opening accounts on their own behalf.

The final rule excludes from the definition of legal entity customer certain entities that are subject to Federal or State regulation and for which information about their beneficial ownership and management is available from the Federal or State agencies. Within § 1010.230(e)(2) of the final rule is a list of various examples of customers specifically exempt from the definition of legal entity customer.

It is worth nothing that trusts are generally not included in the definition of legal

entity customer. The definition of legal entity customers only includes statutory trusts created by a filing with the Secretary of State or similar office. Otherwise, trusts are exempt. The rationale being that a trust is a contractual arrangement between the person who provides the funds or other assets and specifies the terms (grantor) and the person with control over the assets (trustee), for the benefit of those named in the trust deed (beneficiaries). Considering the general definition of legal entity customer to mean entity created by filing, and the fact that formation of a trust does not generally require any action by the state, it is understandable that trusts are generally not covered.

Financial institutions are however reminded to consider the Customer Identification Program (CIP) notion that, while financial institutions are not required to look through a trust to its beneficiaries, they "may need to take additional steps to verify the identity of a customer that is not an individual, such as obtaining information about persons with control over the account." Also consider banks own CIP policies. It is WBA's understanding that many financial institutions identify and verify the identity of trustees, because trustees will necessarily be signors on trust accounts.

Beneficial ownership requirements

As of **May 11, 2018**, covered financial institutions must establish and maintain written procedures that are reasonably designed to identify, verify, and record the identities of beneficial owners of legal entity customers and to include such procedures in their AML compliance program. Identification must occur at the time a new account is opened, unless the customer is otherwise excluded. This may be accomplished by obtaining certain information required by the rule, being certified by the individual as to its accuracy. The final rule provides a model certification form that can be used for this purpose.

Similar to CIP requirements for individual customers, the final rule requires covered financial institutions to collect from the legal entity customer the name, date of birth, address, and social security number or other government identification number (passport number or other similar information in the case of foreign persons) for beneficial owners at the time a new account is opened.

It is not enough to collect a certification of this information. A financial institution must also verify the identity of each beneficial owner identified. At a minimum, the final rule requires that a financial institution's procedures include the same elements to verify beneficial owners as those under its CIP rule. Those procedures must also be incorporated into the financial institution's anti-money laundering procedures. Note that the information collected on beneficial owners must be collected in addition to those the institution is required to collect on the customer (customer in this situation meaning the legal entity) under CIP requirements.

Finally, a covered financial institution must establish procedures for making and maintaining a record of all information obtained under its procedures designed to implement the above requirements. At a minimum the record must include:

1. For identification, any identifying information obtained by the covered financial institution pursuant to its identification requirements, including without limitation the certification (if obtained); and

2. For verification, a description of any document relied on (noting the type, any identification number, place of issuance and, if any, date of issuance and expiration), of any nondocumentary methods and the results of any measures undertaken, and of the resolution of each substantive discrepancy.

A covered financial institution must retain the records made for identification for five years after the date the account is closed, and the records made for verification for five years after the record is made.

The final rule also amends the AML program requirements for each covered financial institution to explicitly require covered institutions to implement and maintain appropriate risk-based procedures for conducting ongoing customer due diligence.

A covered financial institution's AML program must include, at a minimum:

1. A system of internal controls;

2. Independent testing;

3. Designation of a compliance officer or individual(s) responsible for day-to-day compliance;

4. Training for appropriate personnel; and

5. Appropriate risk-based procedures for conducting ongoing CDD to understand

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the nature and purpose of customer relationships and to conduct ongoing monitoring to identify and report suspicious transactions, and, on a risk basis, to maintain and update customer information.

Conclusion

WBA recommends that financial institutions review the final rule in its entirety. As the final rule requires financial institutions to establish their own written procedures, all personnel involved with legal entity customers should familiarize themselves with their financial institution's specific policies and procedures. For example, what means of certification does bank's written policies require? What level of verification is required? These are questions unique to each financial institution's own CDD program. ■

Agencies Issue Semiannual Regulatory Agendas.

- The Bureau of Consumer Financial Protection (CFPB) published its agenda as part of the Fall 2017 Unified Agenda of Federal Regulatory and Deregulatory Actions. CFPB reasonably anticipates having the regulatory matters identified in the agenda under consideration during the period from **11/01/2017** to **10/31/2018**. The next agenda will be published in spring 2018, and will update the agenda through fall 2018. The agenda may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-01-12/pdf/2017-28241.pdf. *Federal Register*, Vol. 83, No. 9, 01/12/2018, 1968-1972.

- The Board of Governors of the Federal Reserve System (FRB) published its agenda as part of the Fall 2017 Unified Agenda of Federal Regulatory and Deregulatory Actions. FRB reasonably anticipates having the regulatory matters identified in the agenda under consideration during the period from **11/01/2017** to **10/31/2018**. The next agenda will be published in spring 2018, and will update the agenda through fall 2018. The agenda may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-01-12/pdf/2017-28245.pdf. *Federal Register*, Vol. 83, No. 9, 01/12/2018, 2014-2015.

- The Department of Housing and Urban Development (HUD) published its agenda as part of the Fall 2017 Unified Agenda of Federal Regulatory and Deregulatory Actions. HUD reasonably anticipates having the regulatory matters identified in the agenda under consideration during the period from **11/01/2017** to **10/31/2018**. The next agenda will be published in spring 2018, and will update the agenda through fall 2018. The agenda may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-01-12/pdf/2017-28214.pdf. *Federal Register*, Vol. 83, No. 9, 01/12/2018, 1882-1883.

- The Department of the Treasury (Treasury) published its agenda as part of the Fall 2017 Unified Agenda of Federal Regulatory and Deregulatory Actions. Treasury reasonably anticipates having the regulatory matters identified in the agenda under consideration during the period from **11/01/2017** to **10/31/2018**. The next agenda will be published in spring 2018, and will update the agenda through fall 2018. The agenda may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-01-12/pdf/2017-

March 2018

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Special Focus

Mortgage Servicing Rules on Successors in Interest

Beginning April 19, 2018, banks who service residential mortgage loans, including "small servicers" ("**banks**"), must be prepared to properly communicate with potential and confirmed successors in interest in accordance with the Consumer Financial Protection Bureau's (CFPB) Final 2016 Mortgage Servicing Rule ("**Rule**"). In August 2016, CFPB issued the Rule, which amended certain mortgage servicing provisions under Regulation X and Regulation Z (altogether, these are referred to as the "**Mortgage Servicing Rules**"). Among those amendments were provisions related to communicating with potential and confirmed successors in interest. These amendments require a bank to implement policies and procedures to obtain proper documentation to confirm a person's identity and ownership interest in the transferred property and communicate with such individuals. In addition to these policy/process changes, a bank's personnel and technology will be affected, as well.

Who is a Successor in Interest?

Successors in interest under the Mortgage Servicing Rules are persons who have received an ownership interest in the mortgaged property, provided that ownership interest is transferred from a borrower via one of five types of transfers:

1. Transfer by devise, descent, or operation of law on the death of a joint tenant or tenant by the entirety;

2. Transfer to a relative resulting from the death of a borrower;

3. Transfer where the spouse or children of the borrower become an owner of the property;

4. Transfer resulting from the decree of a dissolution of marriage, legal separation agreement, or from an incidental property settlement agreement by which the spouse of the borrower becomes an owner of the property; or

5. A transfer into an inter vivos trust in which the borrower is and remains a beneficiary and which does not relate to a transfer of rights of occupancy in the property.

For example, let's assume Bob has a mortgage on his principal residence that is serviced by your Bank. When Bob dies, he leaves his home to his only child, Clara. Clara is a successor in interest.

It's important to note that a successor in interest includes anyone who has received an ownership interest in the mortgaged property via one of the described transfer mechanisms and is not limited to individuals who have assumed the loan obligation. While some successors in interest may assume the loan obligation, some may not.

Furthermore, once a successor in interest is confirmed, the successor in interest is considered and must be treated as a borrower for purposes of the Mortgage Servicing Rules. In other words, the successor in interest "stands in the shoes" of the borrower and must now receive all required servicing-related notices and communications that would have otherwise been delivered to the transferor borrower, as required. For example, Clara must now receive payoff statements, if requested, on the property transferred by Bob and is entitled to submit a loss mitigation application that the bank must review and evaluate in accordance with the Mortgage Servicing Rules.

During the rulemaking process, some commenters expressed concerns that sensitive information about the mortgage loan obligation will now be shared with successors in interest who have an ownership interest but do not assume the mortgage loan obligation. In response to this concern, banks are permitted, but not required, to withhold sensitive information about the borrower(s), such as location and contact information and specific personal financial information, in certain circumstances. If your bank is interested in withholding sensitive information, where available, be sure to familiarize yourself with the specificities in the Rule.

How will the Bank become aware of a potential Successor in Interest?

There are several ways in which a bank may become aware of a potential successor in interest. One example is that the bank becomes aware of the death of its customer. If the bank becomes aware of the death of a customer, the bank has no responsibility to search for a potential successor in interest. The Rule makes it clear that it is not incumbent on a bank to search for a potential successor in interest if it has not been made aware of the existence of that potential successor in interest. Alternatively, a bank may be notified by a potential successor in interest themselves. For example, a successor

in interest may call the bank to alert the bank of a transfer of ownership interest or, a person other than the borrower could submit a loss mitigation application. In both these instances, the bank should treat these individuals as potential successors in interest (even if the individual does not use the term "successor in interest") and should adhere to its policy regarding communicating with such individuals, as discussed below. Additionally, and importantly, the bank should train its staff to (a) properly identify such communications as communications from potential successors in interest and (b) direct such individuals to key mortgage servicing staff.

What is required of the Bank once there is a *potential* Successor in Interest?

Put simply, the bank must have policies and procedures in place to communicate with potential successors in interest. These policies and procedures must address the following:

- How to promptly respond to potential successors in interest;
- What information is required to identify a potential successor in interest's identity and ownership interest and how such a request for documentation is made to potential successors in interest; and
- Upon receipt of such information, promptly make a determination and notify the person that the bank has:
  a) Confirmed the person's status as a successor in interest;
  b) Determined that additional documents are required (and what those documents are) in order to determine if the individual is a successor in interest; OR
  c) Determined that the person is not a successor in interest

Banks should be aware that "prompt"/"promptly" is not defined in the Rule, as the CFPB recognized that a "prompt" communication would depend on the facts and circumstances at issue. A Bank should consider addressing how to "promptly" communicate by establishing reasonable timeframes in its policy, while retaining some flexibility for exceptional circumstances.

Furthermore, banks should carefully consider what information it will require to identify a potential successor in interest's ownership interest in the mortgaged property and list such information in its policy. It is advised that a bank seek legal counsel to determine what documentation will properly identify a transfer of ownership (for all five types of transfers) in the jurisdictions in which the bank services mortgage loans. For example, in Wisconsin, where the mortgaged property is transferred at the borrower's death to an individual who has survivorship rights in the property (e.g. the property automatically transferred to them through a Trust), a bank should request a death certificate and a copy of the recorded "Termination of Decedent's Interest" form. This documentation will likely vary outside the state of Wisconsin.

What responsibilities does the Bank have once a Successor In Interest is confirmed?

Once a successor in interest is verified, a bank has the option of sending a Written Disclosure and Acknowledgment Form ("**Acknowledgment**") (see 1024.32(c) for form requirements). This Acknowledgment indicates, among other things, that the individual has been confirmed as a successor in interest and requires that the successor in interest return a signed Acknowledgment before receiving certain notices and communications about the mortgage loan. This puts the onus on the confirmed successor in interest to notify the bank that he/she would like to receive notices and communications about the mortgage loan; the bank will not be required to provide the successor in interest with any notices and communications about the mortgage loan until a signed Acknowledgment is received. It's important to note that this optional Acknowledgment will only apply to successors in interest who have not assumed the mortgage loan. If a successor in interest has assumed the mortgage loan obligation, those individuals must automatically receive notices and communications about the mortgage loan; in other words, the bank cannot require a successor in interest who is obligated on the loan to sign an Acknowledgment before receiving notices and communications about the mortgage loan. If a bank does not require an Acknowledgment, the bank should begin sending notices and communications, as appropriate, to the confirmed

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successor in interest as soon as successor in interest status is confirmed.

A bank should consider whether or not requiring an Acknowledgment is practical. For example, are systems set up to differentiate confirmed successors in interest – those who have signed an Acknowledgment, those who have not signed an Acknowledgment, and those who don't receive an Acknowledgment because they are obligated on the mortgage loan? Either way, whether or not a bank requires an Acknowledgment should be in the policy.

Finally, once a successor in interest is confirmed and the bank has received a signed Acknowledgment, if required, the successor in interest must be treated as a borrower and receive all notices and communications, as required, that would have been provided to the transferor borrower under the Mortgage Servicing Rules. Of course, some sensitive personal information related to the loan may be omitted, as described above.

Are there any Small Servicers Exemptions from the Successor in Interest Requirements?

Generally speaking, there is no exemption for small servicers as it relates to the successor in interest provisions. Small servicers should be prepared to comply with the successor in interest requirements, as described above. Small servicers should note, however, that they retain the same exemptions with respect to confirmed successors in interest as they had when servicing the transferor borrower/customer. This is because confirmed successors in interest "stand in the shoes" of the borrower/customer. For example, small servicers are exempt from providing periodic statements to borrowers for covered mortgage loans. A small servicer retains this exemption from providing a successor in interest with a periodic statement. In contrast, small servicers must comply with requirements to provide a payoff statement when requested by a successor in interest, as there is no existing exemption for small servicers.

For additional information regarding these and other requirements under the Mortgage Servicing Rules, visit the CFPB's Mortgage Servicing Implementation Page at https://www.consumerfinance.gov/policy-compliance/guidance/implementation-guidance/mortserv/

WBA wishes to thank Atty. Lauren C. Capitini, Boardman & Clark, llp for providing this article. ■

The Horizon Bank v. Musikantow Case: Unexpected Contract Interpretation Means Banks Need to Revisit Their Guaranty and Stipulation Language

On March 6, 2018, the Wisconsin Supreme Court issued its decision in the case of *Horizon Bank, NA v. Marshalls Point Retreat LLC*. The facts in the case, as well as the legal arguments raised, are somewhat complex, and the Court's decision raises some troubling issues for lenders in the state.

The Case

This case involved a typical lending situation. The bank made a loan to a borrower, secured by an upscale house in Sister Bay, Wisconsin. The owner of the borrower provided an unlimited guaranty of the debt. After multiple unsuccessful attempts to sell the property, the borrower defaulted. The bank brought one action under which it sought *both* to foreclose upon the property and to obtain a judgment on the guaranty. Importantly, before the sheriff's sale of the property, the parties (including the guarantor) entered into a negotiated stipulation in which they agreed in writing to resolve all issues in one proceeding and agreed to the terms of an "order of judgment."

The order for judgment stated that the borrower owed the bank approximately $4 million, and granted the bank a money judgment in the same amount against the guarantor. The key language of the stipulation is the following:

> "[t]he amount paid to [the bank] from the proceeds of [the] sale of the Premises, remaining after

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Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

FinCEN's April 3, 2018 FAQs on Customer Due Diligence Requirements for Financial Institutions

Introduction

As the May 11, 2018 applicability date rapidly approaches for the Financial Crimes Enforcement Network's (FinCEN's) Customer Due Diligence (CDD) final rule, FinCEN issued a second set of Frequently Asked Questions to assist covered financial institutions in understanding the scope that rule. FinCEN's first set of FAQs on the CDD rule was published on July 19, 2016. FinCEN has indicated it may issue additional FAQs, guidance, or grant exceptive relief as appropriate. For your convenience, we are providing below the April 3, 2018 FAQs in their entirety with minor formatting changes to accommodate the format of *WBA Compliance Journal*.

Frequently Asked Questions (FAQs)

Question 1: Beneficial ownership threshold

Can a covered financial institution adopt and implement more stringent written internal policies and procedures for the collection of beneficial ownership information than the obligations prescribed by the Beneficial Ownership Requirements for Legal Entity Customers (31 CFR 1010.230)?

A. Yes. Covered financial institutions may choose to implement stricter written internal policies and procedures for the collection and verification of beneficial ownership information than the requirements prescribed by the Rule.

Transparency in beneficial ownership provides highly valuable information that supports law enforcement, tax, regulatory or counterterrorism investigations.

The Rule sets forth the standard for collecting such valuable information at 25 percent of beneficial ownership. Therefore, covered financial institutions will meet their beneficial ownership obligations by collecting information on individuals, if any, who hold directly or indirectly, 25 percent or more of the equity interests in and one individual who has managerial control of a legal entity customer. A covered financial institution may choose, however, to collect such information on natural persons who own a lower percentage of the equity interests of a legal entity customer as well as information on more than one individual with managerial control.

Question 2: Interaction of the beneficial ownership threshold with other AML program obligations

Are there circumstances where covered financial institutions should consider collecting beneficial ownership information at a lower equity interest threshold under the anti-money laundering (AML) program rules with regard to certain customers?

A. There may be circumstances where a financial institution may determine that collection and verification of beneficial ownership information at a lower threshold may be warranted, based on the financial institution's own assessment of its risk relating to its customer.

Transparency in beneficial ownership, however, is only one aspect of a covered financial institution's customer due diligence obligations. A financial institution may reasonably conclude that collecting beneficial ownership information at a lower equity interest than 25 percent would not help mitigate the specific risk posed by the customer or provide information useful to the financial institution in analyzing the risk. Rather, any additional heightened risk could be mitigated by other reasonable means, such as enhanced monitoring or collecting other information, including expected account activity, in connection with the particular legal entity customer.

In all cases, however, it is important that covered financial institutions establish and maintain written procedures that are reasonably designed to identify and verify the identity of beneficial owners of legal entity customers and to include such procedures in their AML compliance program.[1]

Question 3: Collection of beneficial ownership information for direct and indirect owners: Legal entity customers with complex ownership structures

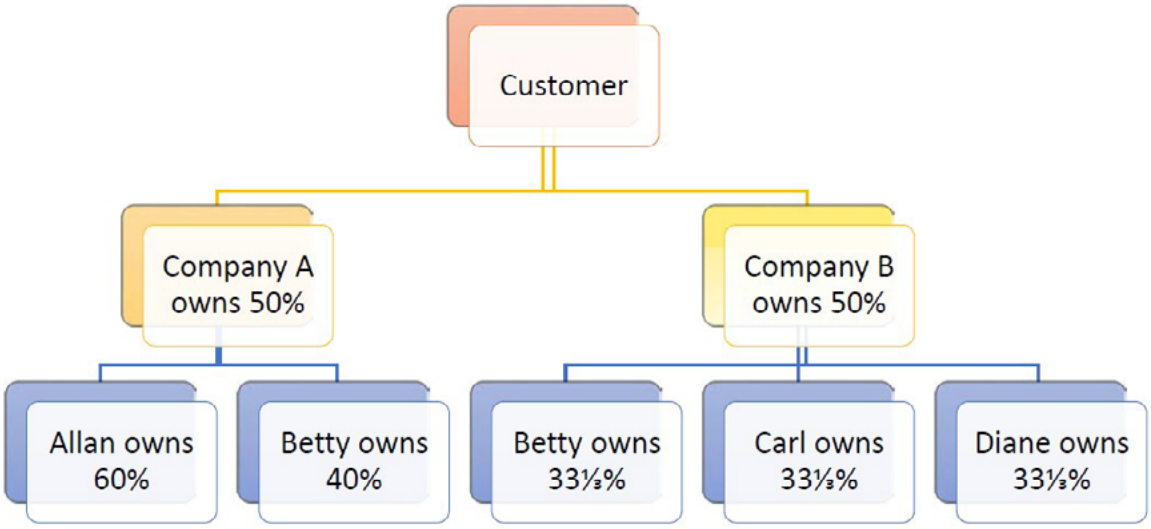
When a legal entity is identified as owning 25 percent or more of a legal

entity customer that is opening an account, is it necessary for a covered financial institution to request beneficial ownership information on the legal entity identified as an owner?

A. Under the Rule's beneficial ownership identification requirement, a covered institution must collect, from its legal entity customers, information about any individual(s) that are the beneficial owner(s) (unless the entity is excluded or the account is exempted). Therefore, covered financial institutions must obtain from their legal entity customers the identities of individuals who satisfy the definition, either directly or indirectly through multiple corporate structures, as illustrated in the following example.

For purposes of the Rule, Allan is a beneficial owner of Customer because he owns indirectly 30 percent of its equity interests through his direct ownership of Company A. Betty is also a beneficial owner of Customer because she owns indirectly 20 percent of its equity interests through her direct ownership of Company A plus 16⅔ percent through Company B for a total of indirect ownership interest of 36⅔ percent. Neither Carl nor Diane is a beneficial owner because each owns indirectly only 16⅔ percent of Customer's equity interests through their direct ownership of Company B.

A covered financial need not independently investigate the legal entity customer's ownership structure and may accept and reasonably rely on the information regarding the status of beneficial owners presented to the financial institution by the legal entity customer's representative, provided that the institution has no knowledge of facts that would reasonably call into question the reliability of the information.



Question 4: Identification and Verification: Methods of verifying beneficial ownership information

What means of identity verification are sufficient to reliably confirm beneficial ownership under the CDD Rule?

A. Covered financial institutions must verify the identity of each beneficial owner according to risk-based procedures that contain, at a minimum, the same elements financial institutions are required to use to verify the identity of individual customers under applicable Customer Identification Program ("CIP") requirements. This includes the requirement to address situations in which the financial institution cannot form a reasonable belief that it knows the true identity of the legal entity customer's beneficial owners.[2] Although the CDD Rule's beneficial ownership verification procedures must contain the same elements as existing CIP procedures, they are not required to be identical to them.[3] For example, a covered financial institution's policies and procedures may state that the institution will accept photocopies of a driver's license from the legal entity customer to verify the beneficial owner(s)' identity if the beneficial owner is not present, which is not permissible in the CIP rules. (See Question 6.)

A financial institution's CIP must contain procedures for verifying customer identification, including describing when the institution will use documentary, non-documentary, or a combination

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of both methods for identity verification.[4] Covered financial institutions may use the same methods to verify the identity of the beneficial owner of a legal entity customer. In addition, in contrast to the CIP rule, the CDD Rule expressly authorizes covered financial institutions to use photocopies or other reproduction documents for documentary verification.[5]

Documentary verification may include unexpired government-issued identification evidencing nationality or residence and bearing a photograph or similar safeguard, such as a driver's license or passport.[6] Non-documentary methods of verification may include contacting a beneficial owner; independently verifying the beneficial owner's identity through the comparison of information provided by the legal entity customer (or the beneficial owner, as appropriate) with information obtained from other sources; checking references with other financial institutions; and obtaining a financial statement.[7]

Financial institutions should conduct their own risk-based analysis to determine the appropriate method(s) of verification and the appropriate documents or types of photocopies or reproductions to accept in order to comply with the beneficial owner verification requirement.

Question 5: Collection of beneficial ownership information: Required addresses

What address should be obtained for a legal entity customer's beneficial owner(s) to comply with the certification requirement – residential or business?

A. The address requirements for certification under the CDD Rule are the same as those outlined in the CIP rule. For an individual beneficial owner, covered financial institutions must obtain either a residential or a business street address. If neither is available, acceptable substitutes may include an Army Post Office (APO) or Fleet Post Office (FPO) box number, or the residential or business street address of next of kin or of another contact individual.[8]

Question 6: Identification and verification: Legal entity customer representative

What process should a covered financial institution use to identify and verify the identity of a beneficial owner of a legal entity customer when the beneficial owner is unavailable to appear in person during the opening of a new account and chooses to provide to the legal entity's representative a copy of a driver's license?

A. A covered financial institution may identify the beneficial owner(s) of a legal entity customer either by obtaining a completed Certification Form or equivalent information from the legal entity customer's representative and may rely on such information, provided that it has no knowledge of facts that would reasonably call into question the reliability of such information.[9] Furthermore, covered financial institutions may verify the identity of a beneficial owner who does not appear in person, through a photocopy or other reproduction of a valid identity document, or by non-documentary means described in response to Question 4 above.

Question 7: Identification and verification: Existing customers as beneficial owners of new legal entity customer accounts

If an individual named as a beneficial owner of a new legal entity account is an existing customer of the covered financial institution subject to the financial institution's CIP, is a covered financial institution still required to identify and verify the identity of this individual, or may it rely on the CIP identification and verification of the individual that it previously performed?

A. In general, covered financial institutions must identify and verify the identity of the beneficial owner(s) of legal entity customers at the time each new account is opened. However, if the individual identified as the beneficial owner is an existing customer of the financial institution and is subject to the financial institution's CIP, a financial institution may rely on information in its possession to fulfill the identification and verification requirements, provided the existing information is up-to-date, accurate, and the legal entity customer's representative certifies or confirms (verbally or in writing) the accuracy of the pre-existing CIP information.

For example, a representative of X Corp opens a new account for the company at a covered financial institution and identifies John Doe, who has a personal account at the institution, as a 25 percent equity owner of X Corp. As required under the CIP rule, the institution identified and verified John Doe's identity at the time the personal account was established. In this situation, a covered financial institution may rely on the pre-existing CIP identification and verification information it maintains for John Doe, provided that X Corp's representative certifies or confirms (verbally or in writing) the accuracy of the pre-existing information on John Doe in order to comply with the Rule. The covered financial institution's records of beneficial ownership for the new account could cross-reference the relevant CIP records and the verification of information would not need to be repeated.

Question 8: Location of Certification Form or Appendix A to the final rule

Are covered financial institutions required to use the beneficial ownership Certification Form (Appendix A to the Rule) and if so, how can they obtain a copy of the Form?

A. There is no requirement that covered financial institutions use the Certification Form. Rather, the form is optional and provided for the convenience of covered financial institutions as one possible method to obtain the required beneficial ownership information. Financial institutions may choose to comply with the requirements of the Rule by using

another method, such as through the institutions' own forms, or any other means that comply with the substantive requirements of this obligation. Covered financial institutions should retain the form and not file it with FinCEN.

Covered financial institutions may obtain a fillable and non-fillable copy of the optional Certification Form in Appendix A of the CDD Rule at https://www.fincen.gov/resources/filing-information.

Question 9: Retention of beneficial ownership information: Multiple sets of beneficial ownership certification documents

If a covered financial institution has updated the beneficial ownership information on the account(s) of a legal entity customer, and subsequently a new account is opened on behalf of the same legal entity customer, is the institution required to retain all sets of beneficial ownership documentation, thereby retaining up to three sets of information: the original set collected at account opening, the updated set, and a third, a duplicate of the second (updated) set for the new account?

A. Yes. Covered financial institutions are required to retain all beneficial ownership information collected about a legal entity customer. Identifying information, including the Certification Form or its equivalent, must be maintained for a period of five years after the legal entity's account is closed.[10] However, all verification records must be retained for a period of five years after the record is made.[11] Therefore, whether a financial institution must retain a set of identification or verification records is dependent upon the date an account is opened and closed, or the date a record is made. For example, if a covered financial institution relies on pre-existing beneficial ownership information in its possession as true and accurate identification information when opening a new account for a legal entity customer, the financial institution should maintain the original records, and any updated information, including a record of **any verbal or written confirmation** of pre-existing information (for example, as described in Questions 7 and 10), until five years after the closing of the new account in order to comply with the recordkeeping requirements in the regulation. Covered financial institutions must also retain a description of every document relied on for verification, any non-documentary methods and results of measures undertaken for verification, as well as the resolution of any substantive discrepancies discovered in identifying and verifying the identification information for five years after the record is made.

Question 10: Identification and verification: Certification when a single legal entity customer opens multiple accounts

If a legal entity customer opens multiple accounts at a covered financial institution (whether or not simultaneously), must the financial institution identify and verify the customer's beneficial ownership for each account?

A. Generally, covered financial institutions must identify and verify the legal entity customer's beneficial ownership information for each new account opening, regardless of the number of accounts opened or over a specific period of time. However, an institution that has already obtained a Certification Form (or its equivalent) for the beneficial owner(s) of the legal entity customer may rely on that information to fulfill the beneficial ownership requirement for subsequent accounts, provided the customer certifies or confirms (verbally or in writing) that such information is up-to-date and accurate at the time each subsequent account is opened and the financial institution has no knowledge of facts that would reasonably call into question the reliability of such information. The institution would also need to maintain a record of such certification or confirmation, including for both verbal and written confirmations by the customer.

Question 11: Identification and verification: Accounts for internal recordkeeping or operational purposes

FinCEN understands that after a covered financial institution (particularly in the securities and futures industries) opens a new account for a legal entity customer and identifies its beneficial ownership, the financial institution may subsequently open one or more additional accounts or subaccounts for that customer – for the institution's own recordkeeping or operational purposes and not at the customer's specific request – so that the customer may, for example invest in particular products or implement particular trading strategies. Would such accounts fall within the definition of "new accounts" for purposes of the beneficial ownership requirement?

A. The beneficial ownership requirement applies to a "new account," which is defined to mean "each account o*pened ... by a legal entity customer*"[12] [emphasis added]. An account (or subaccount) relating to a legal entity customer will not be considered a "new account" or an "account" for purposes of the Rule when a financial institution creates such an account (or subaccount) for its own administrative or operational purposes and not at the customer's request—such as to accommodate a specific trading strategy—and the financial institution has already collected beneficial ownership information on such legal entity customer. The distinction between such accounts opened by customers and those opened solely by the financial institution is consistent with the Rule's purpose to mitigate the risks related to the obfuscation of beneficial ownership when a legal entity tries to access the financial system through the opening of a new account.[13]

This interpretation is limited to accounts (or subaccounts) created solely to accommodate the business of an existing legal entity customer that has previously identified its beneficial ownership. Thus, the following accounts (or subaccounts) would not fall within this interpretation:

- accounts (or subaccounts) created to accommodate a trading strategy being carried out by a separate legal entity, including a subsidiary of the existing legal entity customer; and,

- accounts (or subaccounts) through which the customer of a financial institution's existing legal entity customer carries out trading activity directly through the financial institution without intermediation from the existing legal entity customer.

Question 12: Collection of beneficial ownership information: Product or service renewals

Are financial institutions required to have their legal entity customers certify the beneficial owners for existing customers during the course of a financial product renewal (*e.g.*, a loan renewal or certificate of deposit)?

A. Yes. Consistent with the definition of "account" in the CIP rules and subsequent interagency guidance,[14] each time a loan is renewed or a certificate of deposit is rolled over, the bank establishes another formal banking relationship and a new account is established. Covered financial institutions are required to obtain information on the beneficial owners of a legal entity that opens a new account, meaning (in the case of a bank) for each new formal banking relationship established, even if the legal entity is an existing customer. For financial services or products established before May 11, 2018, covered financial institutions must obtain certified beneficial ownership information of the legal entity customers of such products and services at the time of the first renewal following that date. At the time of each subsequent renewal, to the extent that the legal entity customer and the financial service or product (*e.g.*, loan or CD) remains the same, the customer certifies or confirms that the beneficial ownership information previously obtained is accurate and up-to-date, and the institution has no knowledge of facts that would reasonably call into question the reliability of the information, the financial institution would not be required to collect the beneficial ownership information again. In the case of a loan renewal or CD rollover, because we understand that these products are not generally treated as new accounts by the industry and the risk of money laundering is very low, if at the time the customer certifies its beneficial ownership information, it also agrees to notify the financial institution of any change in such information, such agreement can be considered the certification or confirmation from the customer and should be documented and maintained as such, so long as the loan or CD is outstanding.

Question 13: Collection of beneficial ownership information: Existing accounts

Are covered financial institutions required to collect or update beneficial ownership information on customers with accounts opened prior to May 11, 2018, the Rule's applicability date?

A. Financial institutions are not required to conduct retroactive reviews to obtain beneficial ownership information from customers with accounts opened prior to May 11, 2018. The obligation to obtain or update beneficial ownership information on legal entity customers with accounts established before May 11, 2018, is triggered when a financial institution becomes aware of information about the customer during the course of normal monitoring relevant to assessing or reassessing the risk posed by the customer, and such information indicates a possible change of beneficial ownership.[15]

Question 14: Obligation to solicit or update beneficial ownership information absent specific risk-based concerns

Are covered financial institutions required to obtain or update beneficial ownership information during routine periodic reviews of existing accounts, absent risk- based concerns; that is, are such reviews a trigger for the application of the Rule's beneficial ownership requirements?

A. No. Covered financial institutions do not have an obligation to solicit or update beneficial ownership information as a matter of course during regular or periodic reviews, absent specific risk-based concerns. Financial institutions are required to develop and implement risk-based procedures for conducting ongoing customer due diligence, including regular monitoring to identify and report suspicious activity and, on a risk basis, to maintain and update customer information. Thus, periodic reviews are not by themselves a trigger to obtain or update beneficial ownership information. As stated in response to Questions 13 and 16, the obligation to obtain or update information is triggered when, in the course of normal monitoring, a financial institution becomes aware of information about a customer or an account, including a possible change of beneficial ownership information, relevant to assessing or reassessing the customer's overall risk profile. Absent such a risk-related trigger or event, collecting or updating of beneficial ownership information is at the discretion of the covered financial institution. Financial institutions may exercise this discretion to collect or update beneficial ownership information on customers as often as they deem appropriate.

Question 15: Processes for monitoring and updating customer information

Are covered financial institutions required to implement different processes than currently established to comply with the Rule's ongoing monitoring and updating requirement?

A. To the extent that a covered financial institution has monitoring processes in place that allow the institution to meet the Rule's requirements, such institution may use its existing monitoring processes to comply with customer due diligence monitoring and updating obligations. As the preamble to the Rule states, "current industry practice to comply with existing expectations for SAR reporting should already satisfy this proposed requirement."[16]

Question 16: Updating beneficial ownership information

If an update to beneficial ownership information is required, can the change(s) be made in a covered financial institution's databases without physically obtaining and re-certifying the information?

A. It depends. A covered financial institution must develop written internal policies, procedures, and internal controls with respect to collecting, maintaining, and updating a legal entity's beneficial ownership information. The Rule requires that covered financial institutions monitor and, on a risk- basis, update the customer information, including the beneficial ownership information, and does not require re-certification when the information is up-to-date and accurate.[17] Covered financial institutions may therefore update their records to reflect a change of information for an existing beneficial owner using the same or similar processes the institution implemented to record account information it obtains from customers in connection with the institution's account opening processes. For example, if the update were only to a change of address for an existing beneficial owner whose identity information has already been collected and verified, then full re-certification would likely not be required. In this circumstance, it may be reasonable for the covered financial institution to communicate verbally with the legal entity customer to confirm the accuracy of the change of address and reflect such information in its databases. If, however, the updated information were a change of beneficial ownership, then the new beneficial owner's identity would need to be collected, certified, and verified.

Question 17: Beneficial ownership information: Identifying and verifying at account opening compared to updating after a risk- related trigger

Does FinCEN distinguish between the requirements for identifying and verifying beneficial owner information at the time of a new account opening and at the time of a triggering event?

A. No. Whether a covered financial institution identifies and verifies the identity of the beneficial owner at the time a legal entity initially opens a new account or at the time of a triggering event, the fundamental elements of identification and verification are the same. That is, covered financial institutions must identify each beneficial owner by obtaining their name, date of birth, address, and identifying number (such as a social security number or other identifying number permissible under the CIP rule), and verify their identities. However, financial institutions' written policies, procedures, and processes, as well as the sum of information, may differ with respect to the collection of information at the time a legal entity customer initially opens a new account or at the time an existing account is updated after a triggering event.

On or after May 11, 2018, when a legal entity customer initially opens a new account or an existing account is updated to incorporate beneficial ownership information for the first time in response to a triggering event, covered financial institutions must identify and verify the identity of beneficial owners as set forth in section 1010.230(b).

In contrast, the breadth of information collected as the result of a triggering event during the normal course of monitoring to identify and report suspicious activity and to maintain and update customer information should be determined by what information has changed. That is, only the information that has changed must be updated (*e.g.*, changing the address of the beneficial owner). To the extent that the triggering event results in a determination that the beneficial ownership of the legal entity may have changed entirely, the identity of any new beneficial owner(s) must be collected, certified, and verified, consistent with section 1010.230(b).

Question 18: Collection of beneficial ownership information: Pooled Investment Vehicles whose operators or advisers are not excluded from the definition of legal entity customer

Are covered financial institutions required to identify and verify the identity of the beneficial owners that own 25 percent or more of the ownership interests of a pooled investment vehicle whose operators or advisers are not excluded from the definition of legal entity customer?

A. No. Although the Rule requires covered financial institutions to collect and verify the identity of beneficial owners who own 25 percent or more of the equity interests of a legal entity customer, in general, institutions are not required to look through a pooled investment vehicle to identify and verify the identity of any individuals who own 25 percent or more of its equity interests. Because of the way in which ownership of a pooled investment vehicle fluctuates, it would be impractical for covered financial institutions to collect and verify ownership identity for this type of entity. Therefore, there is no requirement that the financial institution should request the customer to look through the pooled investment vehicle to determine and report any individual's equity interest. However, covered financial institutions must collect beneficial ownership information for the pooled investment vehicle under the control prong to comply with the Rule (i.e., an individual with significant responsibility to control, manage, or direct the vehicle; such individuals could be, *e.g.*, a portfolio manager, commodity pool operator, commodity trading advisor, or general partner of the vehicle).[18]

Question 19: Collection of beneficial ownership information: Trusts with multiple trustees

When 25 percent or more of the equity interests of a legal entity customer are owned by a trust that is overseen by co-trustees (multiple trustees), are covered financial institutions required to identify and verify the identity of all co-trustees?

A. No. If a trust owns directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, 25 percent or more of the equity interests of a legal entity customer, the beneficial owner under the ownership/equity prong is the trustee. Where there are multiple trustees or co-trustees, financial institutions are expected to collect and verify the identity of, at a minimum, one co-trustee of a multi-trustee trust who owns 25 percent or more of the equity interests of a legal entity customer that is not subject to an exclusion. A covered financial institution may choose to identify additional co-trustees as part of its customer due diligence, based on its risk assessment and the customer risk profile and in accordance with the institution's account opening procedures.

Question 20: Collection of beneficial ownership information: Trustee entity as a beneficial owner

If a legal entity is the trustee (*e.g.*, law firm, bank trust department, etc.) of a trust that owns 25 percent or more of the equity interests of a legal entity customer, can that entity be identified as a beneficial owner under the ownership/equity prong or does a natural person need to be so identified?

A. If a trust owns directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise, 25 percent or more of the equity interests of a legal entity customer, the beneficial owner for purposes of the *ownership/equity prong* is the trustee, regardless of whether the trustee is a natural person or a legal entity.[19] In circumstances where a natural person does not exist for purposes of the ownership/equity prong, a natural person would not be identified. However, a covered institution should collect identification information on the legal entity trustee as part of its CIP, consistent with the covered institution's risk assessment and the customer risk profile. In addition to the o*wnership/equity prong*, covered financial institutions are also required to identify and verify a natural person as the beneficial owner of the legal entity customer under the control prong to comply with the Rule.[20] The ownership/equity and control prongs, although related, are independent requirements. Thus, satisfaction of, or exclusion from, regulatory obligations under one prong does not mean a covered financial institution's obligations under the other prong are also satisfied or excluded.

Question 21: Verification of claims of exclusion from the definition of "legal entity customer"

What methods should covered financial institutions use to verify eligibility for exclusion from the definition of a "legal entity customer"?

A. Several types of legal entity customers are excluded from the collection and verification requirements of the Rule, under section 1010.230(e)(2), because, for example, their regulators require the reporting of beneficial ownership information or such information is publicly available. A financial institution may rely on information provided by the legal entity customer to determine whether the legal entity is excluded from the definition of a legal entity customer, provided that it has no knowledge of facts that would reasonably call into question the reliability of such information. Whether a financial institution has such knowledge would depend on the facts and circumstances at the time an account is opened. Covered financial institutions must establish and maintain written risk-based procedures reasonably designed to identify and verify the identity of the beneficial owners of all legal entity customers at the time a new account is opened, unless the customer is otherwise excluded from the definition of legal entity customer. Covered financial institutions are expected to address and specify, in their risk-based written policies and procedures, the type of information they will obtain and reasonably rely upon to determine eligibility for exclusions.

Question 22: Definition of legal entity customer: Sole proprietorship and unincorporated associations

Are sole proprietorships formed by spouses or other unincorporated associations considered legal entity customers under the Rule?

A. No. Sole proprietorships—individual or spousal—and unincorporated associations are not legal entity customers as defined by the Rule, even though such businesses may file with the Secretary of State in order to register a trade name or establish a tax account. This is because neither a sole proprietorship nor an unincorporated association is a separate legal entity from the associated individual(s), and therefore beneficial ownership is not inherently obscured.[21]

Question 23: Definition of charities, non-profits or similar entities

Are covered financial institutions limited to the Internal Revenue Code (IRC) definitions of charities, non-profits, or similar entities when assessing their eligibility for exclusion from the definition of legal entity customer?

A. No. The exclusion from the definition of legal entity customer for charities and non-profit entities is not limited to those entities that meet the definition or description of charitable, nonprofit, or similar entities under the IRC. The Rule does not rely on the tax-exempt status of an entity as described in the IRC. All nonprofit entities—whether or not tax-exempt—that are established as a nonprofit, or nonstock corporation, or similar entity that has been validly organized with the proper State authority are excluded from the *ownership/equity prong* of the requirement because nonprofit entities generally do not have ownership interests.[22] Financial institutions, however, are required to collect beneficial ownership information under the *control prong* from any such entity.[23]

Question 24: Definition of legal entity customer: Publicly traded companies and entities listed on foreign exchanges.

Are companies publicly traded in the United States and entities listed on foreign exchanges excluded from the definition of legal entity customer and, therefore, excluded by the Rule?

A. Companies traded publicly in the United States are excluded from the definition of legal entity customer. Specifically, the Rule excludes from the definition of legal entity customer certain entities that are considered "exempt persons" under 31 CFR 1020.315(b). This includes any company (other than a bank) whose common stock or analogous equity interests are listed on the New York Stock Exchange, the American Stock Exchange (currently known as NYSE American), or NASDAQ stock exchange.[24] The Rule also excludes a U.S. entity when at least 51 percent of its common stock or analogous equity interest is held by a listed entity.[25] These U.S. companies are excluded from the Rule because they are subject to public disclosure and reporting requirements that provide information similar to what would otherwise be collected under the Rule.

Companies listed on foreign exchanges are not excluded from the definition of legal entity customer. Such companies may not be subject to the same or similar public disclosure and reporting requirements as companies publicly traded in the United States and, therefore, collecting beneficial ownership information for them is required.

Question 25: Collection of beneficial ownership information: Legal entities listed on foreign exchanges

May covered financial institutions take a risk-based approach for collecting beneficial ownership information from legal entity customers listed on foreign exchanges?

A. No. Financial institutions may not take a "risk-based approach" to collecting the required beneficial ownership information from legal entity customers that are listed on foreign exchanges, because such institutions are not excluded from the definition of legal entity customer. However, as they may with regard to other legal entity customers, whether listed or not, covered institutions may rely on the public disclosures of such entities, absent any reason to believe such information is inaccurate or not up-to-date.

Question 26: Foreign financial institutions

Does the exclusion for foreign financial institutions from the Rule's definition of "legal entity customer" depend on whether the beneficial ownership requirements applied by such institution's foreign regulator match U.S. requirements?

A. No. For purposes of beneficial ownership identification, the Rule excludes from the definition of "legal entity customer" a foreign financial institution created in a non-U.S. jurisdiction when the foreign regulator for that financial institution collects and maintains information on the beneficial owner(s) of the regulated institution.[26] The rule does not require covered financial institutions to research the specific transparency requirements imposed on a foreign financial institution by its regulator and compare them with those imposed on U.S. financial institutions by U.S. Federal functional regulators. However, if the foreign regulator does not collect and maintain beneficial ownership information on the foreign financial institution it regulates, then U.S. financial institutions will have to collect and maintain beneficial ownership information on accounts opened by foreign financial institutions in compliance with the Rule. As with any exclusion, covered financial institutions may rely on the representations of its legal entity customer as to whether an exclusion applies, provided that they have no knowledge of facts that would reasonably call into question the reliability of such representation. (See Question 21.)

For purposes of existing customer due diligence requirements, covered financial institutions that maintain correspondent accounts for foreign financial institutions are already required to establish and maintain specific risk-based due diligence procedures and controls for such accounts that include consideration of all relevant factors,[27] and are required to identify beneficial ownership for certain high-risk foreign banks.[28] These correspondent accounts will continue to be subject to these existing requirements rather than the requirements set forth in the AML Program requirements contained in the Rule.

Question 27: Exclusion from the definition of legal entity customer: U.S. Government list of foreign regulators that maintain beneficial ownership information

Will the U.S. Government maintain a list of non-U.S. jurisdictions where the regulator of financial institutions within that jurisdiction maintains beneficial ownership information regarding the financial institutions they regulate or supervise?

A. No. Covered financial institutions should contact the relevant foreign regulator or use other reliable means to ascertain whether the foreign regulator maintains beneficial ownership information for the financial institutions that it regulates or supervises.

Question 28: Exclusion from the definition of legal entity customer: Non-U.S. governmental department, agency, or political subdivision engaged only in governmental activities

What types of entities would be considered a "non-U.S. governmental department, agency or political subdivision that engages only in governmental rather than commercial activities"[29] such that they would qualify for exclusion from the definition of a legal entity customer?

A. Examples of legal entity customers that would be considered non-U.S. governmental entities engaged in only governmental and not commercial activities include entities that are owned and operated by a non-U.S. government

agency or political subdivision, such as embassies or consulates, as well as entities that are instrumentalities of a foreign government, such as government-owned enterprises engaging in activities that are exclusively governmental in nature, that is, activities involving the direct exercise of legislative, executive, or judicial authority and which do not involve taking profits from the endeavor. Those State-owned enterprises engaged in profit-seeking activities, including, among others, sovereign wealth funds, airlines, or oil companies, would not qualify for the legal entity customer exclusion. Generally, many State-owned enterprises may not have an individual that owns at least a 25 percent equity interest because a governmental department, agency, or political subdivision holds such interest.

In these circumstances, a covered financial institution would only be required to identify an individual under the control prong. Similarly, with respect to a State-owned enterprise that is a pooled investment vehicle not subject to another exclusion, financial institutions would be required to obtain beneficial ownership information under the control prong but not under the ownership/equity prong of the definition of beneficial owner.

Furthermore, similar to other instances of identification and verification within the Rule's context, a covered financial institution may reasonably rely upon the representations of the legal entity customer, absent knowledge of facts that would call into question the reliability of the beneficial ownership information provided to the financial institution.

Question 29: Private label retail credit accounts established at the point of sale

Does the point of sale exception only apply to accounts opened at the cash register or does it refer to all applications for credit accounts that are for use at the private label retailer only?
A. The Rule provides an exemption from the requirements for a covered financial institution that "opens an account for a legal entity customer that is: [a]t the point- of-sale to provide credit products, including commercial private label credit cards, solely for the purchase of retail goods and/or services at these retailers, up to a limit of $50,000." The point of sale exemption is provided for retail credit accounts opened to facilitate purchases made at the retailer because of the very low risk posed by opening such accounts at the brick and mortar store.

Question 30: Equipment Finance and Lease Exemption: Definition of equipment

What kind of businesses and equipment are covered under the equipment finance exemption?

A. The Rule reflects FinCEN's understanding that businesses require financing to obtain equipment to conduct ongoing business operations. Many such businesses, including both large and small businesses, open accounts solely for the purpose of financing the purchase or lease of that equipment. Subject to certain limitations, the Rule provides an exemption from the requirement to identify and verify the identity of a legal entity customer's beneficial owners for equipment finance and lease accounts established at a covered financial institution because of the low risk for money laundering posed by these accounts.[30] The exemption is intended to cover business equipment such as farm equipment, construction machinery, aircraft, computers, printers, photocopiers, and automobiles that a business purchases or leases. The Rule does not limit the exemption to small businesses. Regardless of the application of the exemption, a covered financial must comply with all other applicable BSA/AML obligations, which may include the obligation to file SARs where there is a suspicion that the equipment may be used to facilitate criminal activity.

Question 31: Equipment Finance and Leasing Exemption: Accounts opened to finance the purchase or leasing of equipment

Does the equipment lease and purchase exemption apply when the customer leases directly from the covered institution?

A. Yes, consider the following. Aviation LLC, which operates several flight training schools, visits Aircraft Vendor to acquire five aircraft for its flight training schools. Aviation LLC selects the aircraft and contacts the Lessor Covered Financial Institution to obtain the necessary equipment finance to acquire the aircraft. After a review of the aircraft and Aviation LLC's business, the Lessor Covered Financial Institution agrees to purchase the aircraft from Aircraft Vendor and then lease them to Aviation LLC for a specified rent amount and duration. The Lessor Covered Financial Institution purchases the aircraft, pays the purchase price directly to Aircraft Vendor, and obtains title to the aircraft as collateral. The Lessor Covered Financial Institution then enters into a lease agreement with Aviation LLC, which opens an account at the financial institution solely for the purpose of obtaining the aircraft and making periodic rent payments. There is no possibility of a cash refund to Aviation LLC under the lease terms.

The equipment lease and purchase exemption would apply because the account established at the covered financial institution meets all of the requirements of the exemption, which are that (1) the account's purpose is to finance the purchase or leasing of equipment, (2) payments are remitted directly by the financial institution to the vendor or lessor, and (3) there is no possibility of a cash refund on the account activity. First, Covered Financial Institution remit full payment directly to the vendor and obtained title to the equipment in order to lease the equipment to the legal entity customer. Second, Aviation LLC opened the account solely for the purpose of financing an equipment lease to acquire aircraft for its training schools. Finally, there is no possibility of a cash refund to Aviation LLC. As noted in the final rule, accounts created to provide financing for equipment lease or purchase, subject

to certain conditions, are exempt from the beneficial ownership requirement because they present a low risk for money laundering and terrorist financing.[31]

Question 32: Currency Transaction Report (CTR) and aggregation of transactions

Under what circumstances should the transactions of a legal entity customer and those of the beneficial owner(s) be aggregated for purposes of filing a CTR? Are financial institutions required to proactively cross-check beneficial ownership information to comply with the CTR aggregation requirement?

A. As a general matter, financial institutions are required to aggregate multiple currency transactions "if the financial institution has knowledge that [the multiple transactions] are by or on behalf of any person and result in either cash in or cash out totaling more than $10,000 during any one business day."[32] With respect to legal entity customers that may share a common owner, unless there is an affirmative reason to believe otherwise, covered financial institutions should presume that different businesses that share a common owner are operating separately and independently from each other and from the common owner. Thus, absent indications that the businesses are not operating independently (*e.g.*, the businesses are staffed by the same employees and are located at the same address, the accounts of one business are repeatedly used to pay the expenses of another business or of the common owner), financial institutions should not aggregate transactions involving those businesses with those of each other or with those of the common owner for CTR filing.[33]

Question 33: Listing beneficiaries on CTRs

When completing a CTR for a business (i.e., corporations, limited liability companies, and general partnerships) will beneficial owners now need to be listed as beneficiaries in such CTRs? If yes, would this also include trust and estate accounts?

A. No. The Rule does not change the existing currency transaction reporting requirements or any guidance FinCEN published pursuant to this reporting requirement. Thus, a covered financial institution is not required to list the beneficial owners of a business, or trust or estate account, when completing a CTR as a matter of course. A financial institution must list a beneficial owner in Part 1 of the CTR only if the financial institution has knowledge that the transaction(s) requiring the filing is made on behalf of the beneficial owner and results in either cash in or cash out totaling more than $10,000 during any one business day.

Question 34: Impact of the Rule on the AML program Board of Directors or senior management review process

Are covered financial institutions now required to follow specific procedures to approve changes to AML programs or require Boards of Directors or senior management to approve such changes? Can Federal functional regulators direct financial institutions within their jurisdiction to follow a specific approval process?

A. Covered financial institutions may continue to follow their existing internal procedures for approving AML program changes, including changes that incorporate the Rule's new program requirements. However, these procedures should be consistent with the requirements and expectations of the institution's Federal functional regulator.

Question 35: Documenting nature and purpose of customer relationship on a risk-basis

The Rule requires financial institutions to understand "the nature and purpose of customer relationships to develop a customer risk profile." What type of information should financial institutions collect to satisfy this requirement and may the documentation of the nature and purpose of a customer relationship be made on a risk-basis?

A. Understanding the nature and purpose of a customer relationship in order to develop a customer risk profile is an important part of ongoing customer due diligence, and is required for all customers and accounts. An understanding based on category of customer means that for certain lower-risk customers, a financial institution's understanding of the nature and purpose of a customer relationship can be developed by inherent or self-evident information, such as the type of customer or type of account, service, or product or other basic information about the customer including information obtained at account opening.

The profile may, but need not, include a system of risk ratings or categories of customers. Accordingly, the documentation that is required to demonstrate an understanding of the nature and purpose of a customer relationship would vary with the type of customer, account, service, or product.

Question 36: Use of information on customer risk profile

Once the nature and purpose of a customer relationship has been established, what are FinCEN's expectations concerning the use of this information?

A. Understanding the nature and purpose of a customer relationship—the information gathered about a customer at account opening—is essential to developing a customer risk profile. This information should be used to develop a baseline against which customer activity, such as the customer's expected use of wires or typical number of deposits in a month, can be assessed for possible suspicious activity reporting. If account activity changes, particularly with regard to what should be anticipated based on the original nature and purpose of the account, risk-based monitoring may identify a need to update customer information, including, as appropriate, beneficial ownership.

Question 37: The nature and purpose of customer relationship

In understanding the nature and purpose of customer relationships, are financial institutions required to develop and document customer risk profiles for self- evident products or customer type (*e.g.*, a safe deposit box)?

A. Financial institutions must implement risk-based procedures as part of their AML program to demonstrate an understanding of the nature and purpose of customer relationships to develop customer risk profiles. Customer risk profiles refer "to the information gathered about a customer at account opening used to develop a baseline against which customer activity can be assessed for suspicious activity reporting. This may include self-evident information such as the type of customer, or type of account, service or product."[34] It is reasonable that in the case of certain products, such as safety deposit boxes, the nature and purpose are self-evident and therefore no additional documentation would be needed to demonstrate an understanding of their nature and purpose, beyond the documentation to establish the particular type of account.

For Further Information

Additional questions or comments regarding the contents of this Guidance should be addressed to the FinCEN Resource Center at FRC@fincen.gov, (800) 767-2825, or (703) 905-3591. Financial institutions wanting to report suspicious transactions that may relate to terrorist activity should call the Financial Institutions Toll-Free Hotline at (866) 556-3974 (7 days a week, 24 hours a day). The purpose of the hotline is to expedite the delivery of this information to law enforcement. Financial institutions should immediately report any imminent threat to local-area law enforcement officials.

Conclusion

WBA encourages financial institutions to carefully review all of the FAQs and the final rule soon, as there is very little time before the applicability date. If you would like to view the official April 3, 2018 CDD FAQs document, it is available at: https://www.fincen.gov/sites/default/files/2018-04/FinCEN_Guidance_CDD_FAQ_FINAL_508_2.pdf. The July 19, 2017 CDD FAQs document is available at: https://www.fincen.gov/resources/statutes-regulations/guidance/frequently-asked-questions-regarding-customer-due-diligence. The CDD final rule document is available at: https://www.fincen.gov/resources/statutes-regulations/federal-register-notices/customer-due-diligence-requirements. A summary of the rule is available in the February 2018 edition of *WBA Compliance Journal*. Financial institutions should also check with their forms vendor to determine the availability of certification forms to assist compliance with the rule. FIPCO® offers the following forms in the Compliance Concierge software, and in both hard copy and electronic formats: WBA 140A General Instructions and Certification of Beneficial Owner(s); and WBA 140B Certification of No Change in Prior Certification.

ENDNOTES

1. *See* 31 U.S.C. § 5318(h); 31 CFR 1010.230(a).

2. Under the CIP rules, a financial institution's CIP must include procedures for responding to circumstances in which the financial institution cannot form a reasonable belief that it knows the true identity of a customer. These procedures should describe: (1) when the institution should not open an account; (2) the terms under which a customer may use an account while the institution attempts to verify the customer's identity; (3) when it should close an account, after attempts to verify a customer's identity have failed; and (4) when it should file a Suspicious Activity Report in accordance with applicable laws and regulations. *See*, *e.g.*, 31 CFR 1020.220(a)(2)(iii).

3. *See* 31 CFR 1020.220(a)(2); 31 CFR 1023.220(a)(2); 31 CFR 1024.220(a)(2); or 31 CFR 1026.220(a)(2).

4. *See* 31 CFR 1020.220 (a)(2)(ii).

5. *See* 31 CFR 1010.230(b)(2).

6. *See* 31 CFR 1020.220 (a)(2)(ii)(A).

7. *See* 31 CFR 1020.220 (a)(2)(ii)(B).

8. *See* 31 CFR 1020.220(a)(2)(i)(3); 31 CFR 1023.220(a)(2)(i)(3); 31 CFR 1024.220(a)(2(i)(3)); 31 CFR 1026.220(a)(2)(i)(3).

9. *See* 31 CFR 1010.230(b)(1).

10. *See* 31 CFR 1010.230(i)(2).

11. Id.

12. *See* 31 CFR 1010.230(g). In addition, the term "account" is defined by reference to the definition in the CIP rules. 31 CFR 1010.230(c).

13. *See* 68 FR at 25093 (The preamble to the CIP rules provides that "Treasury and the Agencies note that the [USA PATRIOT] Act provides that the regulations shall require reasonable procedures for 'verifying the identity of any person seeking to open an account.' Because these transfers are not initiated by customers, these accounts do not fall within the scope of section 326.")

14. *See* "Interagency Interpretive Guidance on Customer Identification Program Requirements under Section 326 of the USA PATRIOT Act, FAQs: Final CIP Rule," p. 8 (April 28, 2005).

15. *See* 81 FR at 29421.

16. 81 FR 29420.

17. *See e.g.*, 31 CFR 1020.210(b)(5)(ii) (for banks); 1023.210(b)(5)(ii) (for brokers or dealers in securities), 1024.210(b)(5)(ii) (for mutual funds), 1026.210(b)(5)(ii) (for futures commission merchants and introducing brokers in commodities).

18. In cases where such manager, operator or advisor is itself an entity, then it would be necessary to identify an individual with

responsibility to control, manage or direct the manager, operator, advisor or general partner. *See* 31 CFR 1010.230(e)(3)(i), 81 FR at 29415.

19. *See* 31 CFR 1010.230(d)(3).

20. *See* 31 CFR 1010.230(d)(2).

21. *See* 81 FR, 29398, 29412 (May 11, 2016).

22. *See* 81 FR at 29412.

23. Id.

24. *See* 31 CFR 1020.315 (b)(4).

25. *See* 31 CFR 1020.315 (b)(5).

26. *See* 31 CFR 1010.230(e)(1)(xiv).

27. *See* 31 CFR 1010.610(a)(2)(iv).

28. *See* 31 CFR 1010.610(b)(3).

29. 31 CFR 1010.230(e)(2)(xv).

30. *See* 31 CFR 1010.230(h)(1)(iv).

31. Id.

32. 31 CFR 1010.313.

33. *See* FinCEN Ruling 2001–2, "Currency Transaction Reporting: Aggregation," (Aug. 23, 2001) and FinCEN Guidance 2012-G001, "Currency Transaction Report Aggregation for Businesses with Common Ownership," (March 16, 2012), respectively. See also 81 FR at 29409.

34. 81 FR 29398, 29398 (May 11, 2016).■

Regulatory Spotlight

Agencies Finalize Appraisal Threshold Increase to CRE Transactions.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) issued a final rule to amend the agencies' regulations requiring appraisals of real estate for certain transactions. The final rule increases the threshold level at or below which appraisals are not required for commercial real estate transactions from $250,000 to $500,000. The final rule defines "commercial real estate transaction" as a real estate-related financial transaction that is not secured by a single l-to-4 family residential property. It excludes all transactions secured by a single 1-to-4 family residential property, and thus construction loans secured by a single l-to-4 family residential property are excluded. For commercial real estate transactions exempted from the appraisal requirement as a result of the revised threshold, regulated institutions must obtain an evaluation of the real property collateral that is consistent with safe and sound banking practices. The final rule is effective **04/09/2018**. The rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-04-09/pdf/2018-06960.pdf. *Federal Register*, Vol. 83, No. 68, 04/09/2018, 15019-15036.

Agencies Issue Correction to Community Reinvestment Act Regulations.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) issued a correction to the final rule on the Community Reinvestment Act (CRA) regulation published in the *Federal Register* on **11/24/2018**. The correction addresses two additional comments that were timely submitted but inadvertently not included in the rulemaking record of the CRA final rule. The sections of the correction document are effective as if they had been included in the "Supplementary Information" section of the CRA final rule, effective **01/01/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-04-10/pdf/2018-06963.pdf. *Federal Register*, Vol. 83, No. 69, 04/10/2018, 15298-15301.

CFPB Finalizes Amendments to Regulation Z.

The Bureau of Consumer Financial Protection (CFPB) issued a final rule amending certain Regulation Z mortgage servicing rules issued in 2016 relating to the timing for servicers to transition to providing modified or unmodified periodic statements and coupon books in connection with a consumer's bankruptcy case. The rule is effective **04/19/2018**. The final rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-03-12/pdf/2018-04823.pdf. *Federal Register*, Vol. 83, No. 48, 03/12/2018, 10553-10559.

CFPB Issues Solicitations for Applications for Membership of Consumer Advisory Board and Councils.

CFPB invites the public to apply for membership for appointment to its Consumer Advisory Board, Community Bank Advisory Council, and Credit Union Advisory Council. Membership of the Board and Councils includes representatives of consumers, communities, the financial services industry and academics. Appointments to the Board are typically for three years and appointments to the Councils are typically for two years. However, the Director of CFPB may amend the respective Board and Council charters from time to time during the charter terms, as the Director deems necessary to accomplish the purpose of the Board and Councils. CFPB

May 2018

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

Black Hole Rule Summary

On April 26, 2018, the Bureau of Consumer Financial Protection (CFPB) issued the **"Black Hole" Final Rule** (Black Hole Rule). The Rule is effective and mandatory on June 1, 2018. The CFPB issued the Black Hole Rule to rectify issues lenders face with respect to resetting tolerance, also known as the "Black Hole issue." The Black Hole issue arises when a lender is permitted under 1026.19(e)(3)(iv) to issue a revised disclosure and reset tolerance but, due to the timing rules for the provision of TRID disclosures, neither a Loan Estimate nor Closing Disclosure can be issued to reset tolerance; thus, there is a "black hole." The Black Hole Rule rectifies this issue.

Specifically, effective June 1, 2018, lenders may use a Closing Disclosure or Corrected Closing Disclosure to reset tolerance without regard to how many days remain before consummation. For example, assuming a lender has issued both a Loan Estimate and Closing Disclosure and there is a permissible circumstance under 1026.19(e)(3)(iv) for revising a fee/charge that arises ten days before closing, the creditor may provide a Corrected Closing Disclosure to a customer and successfully reset that charge for tolerance purposes. Under the existing TRID Rules, Lenders would not have been permitted to issue a Corrected Closing Disclosure to reset tolerance in those circumstances.

What this means for lenders is that a Loan Estimate, Revised Loan Estimate, Closing Disclosure, or Corrected Closing Disclosure may be used to reset a tolerance for a fee/charge under permissible circumstances. Timing rules related to the provision of TRID disclosures still apply. For example, a lender cannot issue a Loan Estimate if a Closing Disclosure has been provided to the customer. And, an initial Closing Disclosure must still be provided to the consumer at least three business days before consummation.

WBA wishes to thank Atty. Lauren C. Capitini, Boardman & Clark, llp for providing this article. ■

Summary of 2017-2018 Legislative Session

The following article is the second in a series of articles covering Wisconsin legislative activity relevant to the banking industry during the 2017-2018 session. The first article appeared in the November 2017 Compliance Journal. This article provides a summary of several new laws, including those signed through April 17, 2018. For more comprehensive information on these items, please review the applicable Act.

Prize Linked Savings Programs

Wisconsin law prohibits conducting an illegal lottery. 2017 Wisconsin Act 72 creates an exemption from the definition of lottery for certain savings promotion programs. A federal-chartered or state-chartered financial institution may conduct or participate in savings promotion programs that meet all the requirements.

A savings promotion program is defined as a contest to encourage savings deposits. Meaning, a financial institution may hold a contest or promotion to encourage savings deposits in which depositors may win prizes. There are certain requirements for qualifying accounts (being those accounts eligible to win prizes) such as comparable fees, chance of winning, and participation.

Date of enactment: November 27, 2017

For the full requirements see 2017 Wisconsin Act 72 here: https://docs.legis.wisconsin.gov/2017/related/acts/72

Transfer by Affidavit Option

The transfer by affidavit is an option for certain individuals to close out small estates. Previously, three individuals could utilize the transfer by affidavit option: the heir of the decedent, a trustee of a revocable trust created by the decedent, and person who was guardian of the decedent at the time of the decedent's death. 2017 Wisconsin Act 90 permits, in addition to those individuals, a person named in the will to act as a personal representative, to use the transfer by affidavit option.

If a person receives an affidavit from a person named in the will to act as personal representative, they may not transfer any money due to the decedent until 30 days after receiving the affidavit. If, during the

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Specifically, effective June 1, 2018, lenders may use a Closing Disclosure or Corrected Closing Disclosure to reset tolerance without regard to how many days remain before consummation. For example, assuming a lender has issued both a Loan Estimate and Closing Disclosure and there is a permissible circumstance under 1026.19(e)(3)(iv) for revising a fee/charge that arises ten days before closing, the creditor may provide a Corrected Closing Disclosure to a customer and successfully reset that charge for tolerance purposes. Under the existing TRID Rules, Lenders would not have been permitted to issue a Corrected Closing Disclosure to reset tolerance in those circumstances.

What this means for lenders is that a Loan Estimate, Revised Loan Estimate, Closing Disclosure, or Corrected Closing Disclosure may be used to reset a tolerance for a fee/charge under permissible circumstances. Timing rules related to the provision of TRID disclosures still apply. For example, a lender cannot issue a Loan Estimate if a Closing Disclosure has been provided to the customer. And, an initial Closing Disclosure must still be provided to the consumer at least three business days before consummation.

WBA wishes to thank Atty. Lauren C. Capitini, Boardman & Clark, llp for providing this article. ■

Summary of 2017-2018 Legislative Session

The following article is the second in a series of articles covering Wisconsin legislative activity relevant to the banking industry during the 2017-2018 session. The first article appeared in the November 2017 Compliance Journal. This article provides a summary of several new laws, including those signed through April 17, 2018. For more comprehensive information on these items, please review the applicable Act.

Prize Linked Savings Programs

Wisconsin law prohibits conducting an illegal lottery. 2017 Wisconsin Act 72 creates an exemption from the definition of lottery for certain savings promotion programs. A federal-chartered or state-chartered financial institution may conduct or participate in savings promotion programs that meet all the requirements.

A savings promotion program is defined as a contest to encourage savings deposits. Meaning, a financial institution may hold a contest or promotion to encourage savings deposits in which depositors may win prizes. There are certain requirements for qualifying accounts (being those accounts eligible to win prizes) such as comparable fees, chance of winning, and participation.

Date of enactment: November 27, 2017

For the full requirements see 2017 Wisconsin Act 72 here: https://docs.legis.wisconsin.gov/2017/related/acts/72

Transfer by Affidavit Option

The transfer by affidavit is an option for certain individuals to close out small estates. Previously, three individuals could utilize the transfer by affidavit option: the heir of the decedent, a trustee of a revocable trust created by the decedent, and person who was guardian of the decedent at the time of the decedent's death. 2017 Wisconsin Act 90 permits, in addition to those individuals, a person named in the will to act as a personal representative, to use the transfer by affidavit option.

If a person receives an affidavit from a person named in the will to act as personal representative, they may not transfer any money due to the decedent until 30 days after receiving the affidavit. If, during the

30-day period the person who received the affidavit receives an affidavit for the same decedent from another person, the person who received the affidavits may not transfer any money due the decedent unless ordered to do so by a court.

Date of enactment: November 30, 2017

See 2017 Wisconsin Act 90 here: https://docs.legis.wisconsin.gov/2017/related/acts/90

Procedures Related to a Sale of Foreclosed Property

Previously, certain foreclosure procedures applied to property located in a county with a population of 750,000 or more. This was typically referred to as the Milwaukee county confirmation procedure as the only county to which the requirements applied. 2017 Wisconsin Act 104 expands those procedures to apply to property located anywhere within the state of Wisconsin.

Generally speaking, following confirmation of sale and compliance with the terms of the sale, the Clerk of Courts must either provide the Register of Deeds with notice that a sheriff's deed is available, or transmit the deed to the Register of Deeds for recording. In the event of the latter, the Register of Deeds must retrieve the documents and fees from the Clerk of Courts within a reasonable period of time.

Date of enactment: November 30, 2017

See 2017 Wisconsin Act 104 here: https://docs.legis.wisconsin.gov/2017/related/acts/104

Guaranteed Asset Protection Waivers

A guaranteed asset protection (gap) waiver is a contractual obligation (typically provided for a fee) where a creditor agrees to cancel or waive all or part of amounts due on a borrower's finance agreement in the event of a total physical damage or loss or unrecovered theft of a motor vehicle. 2017 Wisconsin Act 161 permits sale of gap waivers in compliance with certain disclosure requirements under motor vehicle leases and sales.

Date of enactment: March 28, 2018

For the full requirements, see 2017 Wisconsin Act 161 here: https://docs.legis.wisconsin.gov/2017/related/acts/161

Uniform Adult Guardianship Jurisdiction

Wisconsin has generally incorporated the Uniform Adult Guardianship and Protective Proceedings Jurisdiction Act into Wisconsin law with some modifications. A Wisconsin court may utilize provisions under the Act to communicate with a court in another state concerning a guardianship. Financial institutions may begin to see guardianship orders issued by a court within another state that has been registered and recognized by a Wisconsin court in accordance with this Act.

Date of enactment: April 3, 2018

For the full details see 2017 Wisconsin Act 187 here: https://docs.legis.wisconsin.gov/2017/related/acts/187

Internet-Based Foreclosure Sale

This Act permits a county to enact an ordinance, following certain guidelines, permitting the sheriff or referee of a sale of foreclosed property to conduct such sale using an internet-based auction.

Date of enactment: April 3, 2018

See 2017 Wisconsin Act 208 here: https://docs.legis.wisconsin.gov/2017/related/acts/208

Floodplain Zoning Ordinances

This Act conforms certain Wisconsin zoning ordinances and floodplain determination requirements with a letter of map amendment issued by the Federal Emergency Management Agency (FEMA). FEMA issues flood insurance through the National Flood Insurance program (NFIP), but only if a community adopts and enforces floodplain management regulations that meet NFIP requirements. One such requirement is that a community's management regulations reflect FEMA flood maps.

Under this Act, a property owner who obtains a letter of map amendment from FEMA that amends the federal flood map, may present such amendment to a community, that must then adjust its zoning ordinance as necessary to conform to the amendment.

Date of enactment: April 3, 2018

See 2017 Wisconsin Act 242 here: https://docs.legis.wisconsin.gov/2017/related/acts/242

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Special Focus

Condominium Law and Rights

This Act affects rights with respect to first mortgage security interests in condominium units. Under the Act, a condominium may raise funds for the repair or replacement of common elements. Costs may be assessed against each unit owner, and the association may levy such assessments. Upon failure to pay, the association may foreclose. Upon acquiring title to the unit, the association may require the first mortgagee to either release the security interest in the unit or accept a quit claim deed from the association.

Additionally, the Act places joint and several liability upon the mortgagee who becomes the owner of a unit following foreclosure for any unpaid assessments due from the former owner during the 12 months prior to confirmation.

Date of enactment: April 16, 2018

The Act includes additional provisions, some of which may affect first mortgages, for example with respect to condominium declarations and voting at the association of unit owners. See 2017 Wisconsin Act 333 here: https://docs.legis.wisconsin.gov/2017/related/acts/333 ■

Regulatory Spotlight

Agencies Propose Amendments to Enhanced Supplementary Leverage Ratio Standards.

The Board of Governors of the Federal Reserve System (FRB), and the Office of the Comptroller of the Currency (OCC) proposed amendments that would modify the enhanced supplementary leverage ratio standards for U.S. top-tier bank holding companies identified as global systemically important bank holding companies (GSIBs) and certain of their insured depository institution subsidiaries. Specifically, the proposal would modify the current 2 percent leverage buffer, which applies to each GSIB, to equal 50 percent of the firm's GSIB risk-based capital surcharge. The proposal also would require a FRB- or OCC-regulated insured depository institution subsidiary of a GSIB to maintain a supplementary leverage ratio of at least 3 percent plus 50 percent of the GSIB risk-based surcharge applicable to its top-tier holding company in order to be deemed "well capitalized" under FRB's and OCC's prompt corrective action rules. Consistent with this approach to establishing enhanced supplementary leverage ratio standards for insured depository institutions, OCC is proposing to revise the methodology it uses to identify which national banks and Federal savings associations are subject to the enhanced supplementary leverage ratio standards to ensure that they apply only to those national banks and Federal savings associations that are subsidiaries of a Board-identified GSIB. FRB also is seeking comment on a proposal to make conforming modifications to the GSIB leverage buffer of FRB's total loss-absorbing capacity and long-term debt requirements and other minor amendments to the buffer levels, covered intermediate holding company conformance period, methodology for calculating the covered intermediate holding company long-term debt amount, and external total loss-absorbing capacity risk-weighted buffer. Comments are due **05/21/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-04-19/pdf/2018-08066.pdf. *Federal Register*, Vol. 83, No. 76, 04/19/2018, 17317-17327.

Agencies Request Comment on Information Collection.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) announced they seek comment on the information collection titled The Consolidated Reports of Condition and Income. The Agencies also gave notice that they sent the collection to OMB for review. Comments are due **05/11/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-04-11/pdf/2018-07443.pdf. *Federal Register*, Vol. 83, No. 70, 04/11/2018, 15678-15702.

CFPB Finalizes Amendments to Federal Mortgage Disclosure Requirements Under the Truth in Lending Act.

The Bureau of Consumer Financial Protection (CFPB) finalized amendments to Federal mortgage disclosure requirements under the Real Estate Settlement Procedures Act (RESPA) and the Truth in Lending Act (TILA) that are implemented in Regulation Z. The amendments relate to when a creditor may compare charges paid by or imposed on the consumer to amounts disclosed on a Closing Disclosure, instead of a Loan Estimate, to determine if an estimated closing cost was disclosed in good faith. The final rule is effective **06/01/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-05-02/pdf/2018-09243.pdf. *Federal Register*, Vol. 83, No. 85, 05/02/2018, 19159-19176.

CFPB Requests Comment on Consumer Complaint and Consumer Inquiry Handling Processes.

CFPB has requested comment on its consumer complaint and consumer inquiry processes to assist CFPB in assessing its handling of these processes and whether changes to its processes would be appropriate. Comments are due **07/16/2018**. The notice may be viewed at: https://www.gpo.

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

June 2018 WBA Legal Call Program Frequently Asked Questions

As a service provided exclusively to members, WBA offers legal information through its call program in response to compliance questions. The following questions and answers feature some recent frequently asked questions WBA has received through this program.

Q: Can a power of attorney act on an IRA account?

A: Yes, but only if the power of attorney (POA) agreement permits it.

The extent of an agent's authority to act under a POA agreement will always depend on the language within the agreement. It is very important that bank obtain a copy of any POA agreement presented and review the language within in order to determine the extent of the powers the agent has been granted. If a financial institution is unable to interpret the POA agreement WBA recommends working with an attorney to receive a legal opinion.

Wisconsin's Uniform Power of Attorney for Finances and Property Act under Chapter 244 governs POA agreements in Wisconsin. Chapter 244 provides for general authority with respect to banks and other financial institutions. One general power granted under statute permits an agent certain actions on an account. Account is a defined term under Wis. Stat. 705.01(1). That definition is broad enough to include an IRA.

Q: Can a power of attorney act on a trust account?

A: Yes, but only if the power of attorney (POA) agreement permits it.

Similar to the analysis above required to determine whether an agent can act on an IRA account, the ultimate authority of an agent depends on the language within the POA agreement. Meaning, an agent can act on an account owned by a trust if the agent has been granted authority to do so.

One additional consideration to make is that of granting authority. A trust is a separate legal entity from an individual, meaning it has its own interests and authorities distinct from that of an individual person. A power of attorney agreement creates authority between a principal (the person granting authority) and an agent (the person granted authority). A POA agreement giving authority to act on the finances of a natural person principal does not automatically mean the agent can act on accounts owned by a trust, even if the principal is a trustee of the trust. Because a trust account has its own authority and ownership interests, the principal must grant an agent authority to act through their powers as trustee. Authority to do so is derived from the trust agreement.

Thus, in order for an agent to act on a trust account, the POA must give them authority to do so, and that power must be permissible through the trust agreement.

Q: How is the section titled "to be completed by the financial institution (for an application taken in person):" of the Home Mortgage Disclosure Act's (HMDA) demographic information collection form completed when an application is not taken in person?

A: It is not completed unless the financial institution has a face-to-face meeting with the applicant before completion of the application process.

HMDA requires a financial institution to obtain certain demographic information from applicants. If the applicant does not provide that information, the financial institution must collect it based on visual observation. When this occurs, the financial institution must also complete the bottom section of the collection form indicating that the applicant's ethnicity, race, and sex was collected on the basis of visual observation or surname. For applications not taken in person, when the applicant does not provide this required information, and the financial institution does not have a later opportunity to collect it based on visual observation, this bottom portion of the form is not completed.

However, if the financial institution has a face-to-face meeting prior to conclusion of the application process, it must request the applicant's ethnicity, race, and sex. If the applicant does not provide the requested information during the in-person meeting, it must be collected on the basis of visual observation or surname. If such a meeting occurs after the application process is complete, for example, at closing or account opening, the financial institution is not required to obtain the applicant's

ethnicity, race, and sex, and thus, not required to complete the bottom portion of the demographic information form.

Q: What considerations apply to a non-resident alien loan applicant?

A: Bank's loan policy should discuss lending to non-resident aliens. Fair Lending and the Equal Credit Opportunity Act (ECOA) should also be considered.

The Fair Lending Act prohibits discrimination based on race, color, national origin, religion, sex, familial status, and disability. It does not include immigration status. ECOA, implemented by Regulation B, indicates in 1002.6(b)(7) that a creditor may consider the applicant's immigration status or status as a permanent resident of the United States, and any additional information that may be necessary to ascertain the creditor's rights and remedies regarding repayment.

So, a financial institution may consider immigration status when deciding whether to extend credit to a non-resident alien. However, lenders should be cautious that when making a credit decision, it is not based on any prohibited basis. For example, denying a loan to an immigrant based on their country of origin, rather than their status as an immigrant, would be a violation.

The commentary to Regulation B provides that the applicant's immigration status and ties to the community (such as employment and continued residence in the area) could have a bearing on a creditor's ability to obtain repayment. Accordingly, the creditor may consider immigration status and differentiate, for example, between a noncitizen who is a long-time resident with permanent resident status and a noncitizen who is temporarily in this country on a student visa.

The extent to which a creditor makes this consideration depends on a financial institution's loan policy. For example: does the financial institution have jurisdiction over the non-resident alien? If they are not a US-citizen, would bank be able to initiate proceedings against them? Are they a flight risk? What if their plans change and they return to their country of origin? Will bank be able and willing to pursue them if the loan goes into default?

These are questions that bank is permitted to ask, but their consideration depends on loan policy. Because of the complexities and fact-specific considerations involved, WBA also recommends working with bank's own counsel when considering lending to non-resident aliens.

Q: If a legal entity customer opens multiple accounts, is a certification as to beneficial ownership required for each new account?

A: Not if certain requirements are met. A financial institution that has already obtained certification from a legal entity customer may rely on that information to fulfill the beneficial ownership requirement for subsequent accounts, provided the customer certifies (in writing or orally) that such information is up-to-date and accurate at the time each subsequent account is opened and the financial institution has no knowledge of facts that would reasonably call into question the reliability of such information.

Q: Is a new certification as to beneficial ownership form required for a change in signors?

A: Not automatically. Only if the change in signors is the result of a change in the control person or a beneficial owner. A signer who is removed or added that is not the result of a change in control person or beneficial owner is not a new account or otherwise a triggering event.

Q: Is an extension, modification, or similar arrangement treated as a renewal per the April 3, 2018 FAQ?

A: Probably. The April 3, 2018 FAQ issued by FinCEN indicates that rollovers or renewals are considered new accounts for purposes of the rule. Due to the similarities in documentation and treatment of an extension, modification, or similar arrangement it is WBA's understanding that such continuations would be similar enough to a renewal to be considered a new account.

Q: Are loans or CDs opened prior to May 11, 2018 that automatically renew or roll over before August 9, 2018 exempt from the Customer Due Diligence (CDD) rule?

A: Yes.

The Financial Crimes Enforcement Network (FinCEN) issued new guidance on May 16, 2018 providing temporary relief from the requirements of its new CDD

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rule for certain types of accounts. Under the guidance, financial institutions who have accounts that were opened prior to May 11, 2018 but automatically roll over or renew in the next 90 days are not required to comply with the CDD rule until August 10, 2018.

FinCEN did not elaborate on the use of the word "automatically" but the guidance does discuss concern expressed by some financial institutions over their ability to comply with the rule because they had established automatic processes. WBA's understanding is that the temporary limited relief is in response to that concern regarding automatic processes. FinCEN will utilize those 90 days to review automatic renewals further.

Conclusion

If you have any questions related to these, or other compliance topics, please do not hesitate to call at 608-441-1200. ■

Regulatory Spotlight

Agencies Finalize Amendments to the Securities Transaction Settlement Cycle.

The Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) finalized a rule to shorten the standard settlement cycle for securities purchased or sold by national banks, federal savings associations, and FDIC-supervised institutions. The Agencies' final rule is consistent with an industry-wide transition to a two business-day settlement cycle, which is designed to reduce settlement exposure and align settlement practices across all market participants. The final rule is effective **10/01/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-06-07/pdf/2018-12267.pdf. *Federal Register*, Vol. 83, No. 110, 06/07/2018, 26347-26349.

Agencies Propose Amendments to Regulatory Capital Rules.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) issued a joint proposal to address changes to U.S. generally accepted accounting principles (U.S. GAAP) described in Accounting Standards Update No. 2016–13, Topic 326, Financial Instruments—Credit Losses (ASU 2016–13), including banking organizations' implementation of the current expected credit losses methodology. Specifically, the proposal would revise the agencies' regulatory capital rules to identify which credit loss allowances under the new accounting standard are eligible for inclusion in regulatory capital and to provide banking organizations the option to phase in the day-one adverse effects on regulatory capital that may result from the adoption of the new accounting standard. The proposal also would amend certain regulatory disclosure requirements to reflect applicable changes to U.S. GAAP covered under ASU 2016–13. In addition, the agencies are proposing to make amendments to their stress testing regulations so that covered banking organizations that have adopted ASU 2016–13 would not include the effect of ASU 2016–13 on their provisioning for purposes of stress testing until the 2020 stress test cycle. Finally, the agencies are proposing to make conforming amendments to their other regulations that reference credit loss allowances. Comments are due **07/13/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-05-14/pdf/2018-08999.pdf. *Federal Register*, Vol. 83, No. 93, 05/14/2018, 22312-22339.

Agencies Extend Comment Period from Proposed Amendments to Enhanced Supplementary Leverage Ratio Standards.

The Board of Governors of the Federal Reserve System (FRB) and the Office of the Comptroller of the Currency (OCC) published proposed amendments to the enhanced supplementary leverage ratio standards for U.S. top-tier bank holding companies identified as global systemically important bank holding companies, or GSIBs, and certain of their insured depository institution subsidiaries in the *Federal Register* on **04/19/2018**. The Agencies are now extending the comment period for the proposed amendments, comments are now due **06/25/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-05-25/pdf/2018-11336.pdf. *Federal Register*, Vol. 83, No. 102, 05/24/2018, 24233.

CFPB Requests Comment on Information Collection.

The Bureau of Consumer Financial Protection (CFPB) announced it seeks comment on the information collection titled Consumer Compliant Intake System Company Portal Boarding Form Information Collection System. CFPB also gave notice that it sent the collection to OMB for review. Comments are due **07/13/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-05-14/pdf/2018-10221.pdf. *Federal Register*, Vol. 83, No. 93, 05/14/2018, 22254-22255.

FFIEC Requests Comment on Information Collection.

The Federal Financial Institutions Examination Council (FFIEC) announced it seeks comment on the information collection titled Reporting information for the AMC Registry. FFIEC also gave notice that it sent the collection to OMB for review. Comments are due **06/14/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-05-15/pdf/2018-

July 2018

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

Key Provisions of the Economic Growth, Regulatory Relief and Consumer Protection Act

Congress passed the Economic Growth, Regulatory Relief and Consumer Protection Act (S. 2155) on May 22, 2018. The bill was signed by President Trump on May 24. While the Act is now law, many of its provisions require implementation from the Federal banking agencies in order to be effective. The Act provides some direct regulatory relief, but also serves as an acknowledgement of a need for change in the realm of deregulation. It passed by a bipartisan vote of 258-159 and represents a step in the right direction. What follows is not a comprehensive review of the Act, but a summary of key provisions related to the banking industry.

Title I. Improving Consumer Access to Mortgage Credit

Section 101

Creates a new category of qualified mortgage (QM) for purposes of meeting the Truth in Lending Act's (TILA) ability to repay requirements. This QM is available to financial institutions less than $10 billion in assets that originate and retain the loan in portfolio. To obtain QM status under this rule the loan must meet certain requirements:

- Restrictions on prepayment penalties;
- Total points and fees less than or equal to 3% of the loan amount;
- No negative amortization or interest only features; and,
- Fully amortized for fixed rate loan.

While this QM status is available as a matter of law, some clarification is still required by the Consumer Financial Protection Bureau (CFPB). For instance, CFPB must clarify the relationship between the new QM category and the existing small creditor QM.

Section 103

Provides an exception from appraisal requirements in rural areas. An appraisal for a federally-related mortgage loan is not required if the following criteria are met:

- Loan is under $400,000;
- Real property located in a rural area (under TILA);
- Within 3 days after providing the Closing Disclosure, contact at least 3 State certified appraisers;
    - These appraisers must not be available within 5 business days, and the financial institution must document this fact; and,
- Loan is held in portfolio.
    - May be sold or transferred under limited circumstances.

This relief is not available for high cost mortgage loans (under TILA) or, for loans where an appraisal would otherwise be required for safety and soundness reasons under other federal regulatory requirements.

Section 104

Exempts certain small-volume loan originators from the new HMDA reporting requirements. Financial institutions that originate fewer than 500 closed-end mortgage loans in each of the two preceding calendar years may revert to pre-January 2018 HMDA reporting requirements. Similarly, financial institutions that originate fewer than 500 open-end lines of credit in each of the two preceding calendar years may revert to pre-January 2018 reporting requirements. Thus, for HELOCs there is an:

- Exemption from HMDA reporting for HELOCs during 2018-2019 period; and,
- Limited HELOC reporting for post 2019 period.

None of the Section 104 exemptions apply to any bank that has received a "needs to improve" CRA rating during each of the last 2 most recent exams or a "substantial non-compliance" rating on its most recent exam. CFPB. The CFPB will need to implement, or rewrite, the existing HMDA rule to clarify Section 104's relation to current reporting requirements.

Section 108

Creates a new exemption from escrow requirements for residential mortgage

loans (under TILA) for financial institutions that:

- Have assets of $10 billion or less;
- Originated 1,000 or fewer first lien mortgages secured by a principal dwelling in the preceding year;
- Originated at least one covered transaction in a rural or underserved area (under TILA); and
- Do not maintain an escrow account for real estate secured loans other than when required for HPML or distressed customers. however, an HPML must continue to meet the covered transaction, extension, and asset threshold tests under 1026.35(b)(2)(iii).

This exemption is created in addition to the existing escrow exemption available under TILA. This exemption is not immediately effective. The CFPB must write implementing regulations in order for the exemption to become available. The Act does not give a timeline that CFPB must follow for implementation.

Section 109

Eliminates the 3-day waiting period required by the TILA/RESPA integrated disclosure rules when a consumer receives a second offer for credit by the same lender. Meaning, if the APR becomes inaccurate, by changing more than 1/8th of a 1% that results in a lower rate, a corrected Closing Disclosure is still required, but does not require a 3 day waiting period before closing.

Title II. Regulatory Relief and Protecting Consumer Access to Credit

Section 201

Simplifies the capital calculations for community banks that have less than $10 billion in assets by requiring the Federal banking agencies to establish a specified Community Bank Leverage Ratio between 8% and 10%. This specified ratio is designed to provide relief from Basel III capital standards for community banks. Financial institutions that maintain this ratio are presumed to be well capitalized an in compliance with risk based capital and leverage requirements.

Section 203

Exempts banks with less than $10 billion in assets from the Volcker Rule.

Section 205

Requires the federal banking agencies to implement regulations raising the eligibility for reduced Report of Condition and Income (short form call reports) from $1 billion to $5 billion in assets.

Section 210

Increases the asset threshold for the 18 month instead of 12 month examination cycle from $1 billion to $3 billion in assets.

Section 213

Permits the collection and use of certain information, such as a copy of a customer's driver's license, in connection with online banking.

Other Sections to Consider

As discussed above, this article does not provide a comprehensive analysis of S. 2155. It is designed to highlight certain portions of select sections within the Act. There are other sections in each title above, as well as titles not discussed above. Some of those titles not discussed that readers should be aware of are:

- Title III – Protections for Veterans, Consumers, and Homeowners;
- Title IV – Tailoring Regulations for Certain Bank Holding Companies;
- Title V – Encouraging Capital Formation; and,
- Title VI – Protections for Student Borrowers.

Conclusion

Readers are encouraged to consult S. 2155 to review the sections above in full, as well as those sections not discussed. The Act can be found here: https://www.congress.gov/bill/115th-congress/senate-bill/2155

In addition, if you missed the WBA webinar, Everything You Need to Know About S.2155 All Member Call, you can access its recording here: https://gsb.adobeconnect.com/pumj4imny6uh?proto=true ■

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Compliance Journal

Special Focus

Wisconsin's Industrial Hemp Pilot Research Program

Wisconsin has implemented an Industrial Hemp Pilot Research Program (Program) through 2017 Wisconsin Act 100 (Act). The Act allows Wisconsin farmers to obtain a permit to grow and sell industrial hemp. The Program is administered by Wisconsin Department of Agriculture, Trade and Consumer Protection (DATCP). Participants that obtain a license, and follow DATCP's requirements, are exempt from criminal prosecution, and products made from industrial hemp, including CBD, are lawful under Wisconsin law. While the Act provides protections under Wisconsin law, Federal law is another matter that will be discussed later in this article.

WBA expects that Wisconsin financial institutions will begin receiving requests from Program participants for deposit and loan products. While the Act does not place any specific requirements upon financial institutions, it is still prudent to ensure customers are operating within the law, and such accounts should be treated as a greater compliance risk. The following article presents the Act for financial institutions to better understand the requirements placed upon Program participants.

2017 Wisconsin Act 100

The Act was enacted November 30, 2017 and permits participants to plant, grow, cultivate, harvest, sample, test, process, transport, transfer, take possession of, sell, import, and export industrial hemp in this state to the greatest extent allowed under federal law. It directs DATCP to directs promulgate rules regulating such activities. Thus, industrial in hemp in Wisconsin will depend on DATCP regulation. However, it is still important to understand the provisions of The Act.

The Act defines industrial hemp as:

- The plant Cannabis sativa, or any part of the plant including the seeds, having a delta−9−tetrahydrocannabinol concentration of no more than 0.3 percent on a dry weight basis or the maximum concentration allowed under federal law up to 1 percent, whichever is greater. "Industrial hemp" includes a substance, material, or product only if it is designated as a controlled substance under the federal Controlled Substances Act under 21 USC 801 to 971 or the Uniform Controlled Substances Act under ch. 961 or both.

The definition, and scope of The Act, refers to the Federal Controlled Substances Act, which will be discussed later in this article.

To that extent, the scope of the Program is primarily one of research, but is broad in its applicability. Its purpose is to study the growth, cultivation, and marketing of industrial hemp. DATCP is to issue licenses and registrations to Program participants. Licensed participants, acting in accordance with the rules, receive safe harbor protections from prosecution when:

- Growing hemp within 0.7% THC of the 0.3% allowable amount.
- Buying and selling industrial hemp.
- Buying, selling, and processing hemp from certified seed.
- Processing hemp from certified seed.
- Sampling hemp.

Controlled Substances Act

While the possession, production, and sale of hemp and CBD oil is not illegal in Wisconsin when certain requirements are met, there is still a lack of clarity as to how industrial hemp is regulated on a Federal level. The concern is whether the activities permitted by The Act would conflict with the Federal Controlled Substances Act (CSA). The CSA regulates the manufacture, importation, possession, use, and distribution of certain substances. Certain substances are exempt, but the status of hemp is still unclear. Specifically excluded from the CSA are the:

- Mature stalks, fiber, oil or cake from seeds, any other compound, manufacture, salt, derivative, mixture, or preparation of mature stalks (except the resin extracted therefrom), fiber, oil, or cake, or the sterilized seed.

How this specifically applies to the industrial hemp industry in Wisconsin remains unclear. The Agricultural Act of 2014 (Farm Bill) was enacted in February of 2014 and authorizes certain agricultural programs for the period of 2014-2018. Contained within the Farm Bill are provisions relating to State Industrial Hemp Pilot Programs. In August of 2016, the Federal Government released a Statement of Principles on Industrial Hemp (Statement of Principles) in accordance with the Farm Bill.

Pursuant to the Farm Bill and the Statement of Principles the term "industrial hemp:"

- Includes the plant Cannabis sativa L. and any part or derivative of such plant, including seeds of such plant, whether growing or not, that is used exclusively for industrial purposes (fiber and seed) with a tetrahydrocannabinols concentration of not more than 0.3 percent on a dry weight basis. The term "tetrahydrocannabinols" includes all isomers, acids, salts, and salts of isomers of tetrahydrocannabinols.

The Statement of Principles discusses how the Farm Bill legalized the growing and cultivating of industrial hemp for research purposes in States where such growth and cultivation is legal under State law, notwithstanding existing Federal statutes that would otherwise criminalize such conduct. The statutorily sanctioned conduct, however, was limited to growth and cultivation by an institution of higher education or State department of agriculture for purposes of agricultural or other academic research or under the auspices of a State agricultural pilot program for the growth, cultivation, or marketing of industrial hemp.

Practical Considerations

While The Act authorizes the possession, production, and sale of hemp and CBD oil in Wisconsin, and the Farm Bill authorized State departments of agriculture to promulgate regulations to carry out these pilot programs, the status and treatment of industrial hemp under these programs is still in its infancy and financial institutions will want to stay abreast of developments as they occur. DATCP's current licensure includes limited activities. The Program creates a framework, enough to get growing and processing started, but does not cover everything that's possible under the Act. For example, while DATCP issues licenses to growers and processors, there is no "sale license" yet. So while The Act appears to authorize the sale of, for example, CBD oil, DATCP has yet to implement rulemaking regulating such activities.

Financial institutions working with customers participating the Wisconsin Program will want to fully understand the scope of those activities, and ensure the customer is in compliance with DATCP's requirements and remains in compliance. WBA expects that inevitably, growers and processors will seek loan products, which will carry additional considerations. In addition to all of the above considerations, financial institutions will need to make risk assessments based on the activity of the potential borrower. For example, as discussed above there are certified seed requirements, and THC level requirements. If DATCP finds a grower to be in violation of such requirements, it may require the entire crop to be destroyed.

Conclusion

Financial institutions in Wisconsin will want to consider their policies and procedures related to customers engaged in the growing, processing, and selling of industrial hemp and related products. While such activities are permissible in Wisconsin, financial institutions will want to work carefully with their legal counsel to develop appropriate policies and procedures, and likewise work carefully with their customers, and treat such accounts as a greater compliance risk. WBA will continue to monitor and report the developments in the hemp industry to its members.

For additional resources consider:

2017 Wisconsin Act 100: https://docs.legis.wisconsin.gov/2017/related/acts/100.pdf

The Wisconsin Department of Justice notice on industrial hemp: https://www.doj.state.wi.us/news-releases/ag-schimel-and-stakeholders-resolve-questions-surrounding-datcp-industrial-hemp

The Federal Statement of Principles: https://www.gpo.gov/fdsys/pkg/FR-2016-08-12/pdf/2016-19146.pdf ■

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ruling, a loan renewal must not be subject to a financial institutions underwriting review and approval. Similar to the considerations that must be made for CDs, WBA recommends financial institutions review their loan policies in the context of the relief ruling to determine whether renewals are made based upon underwriting review and approval.

Conclusion

The relief ruling eases some of the burden of the beneficial ownership rule by exempting certain renewals from identification and verification requirements that had previously been imposed upon them. However, it lacks clarity in its definitions as to what is covered. Because of the lack of clarity in the ruling, WBA recommends each financial institution fully review the relief ruling alongside potentially covered accounts.

The relief ruling can be found here: https://www.fincen.gov/sites/default/files/administrative_ruling/2018-09-07/Permanent%20Exceptive%20Relief%20Extension%20of%20Compliance%20Date%20CDs_final%20508.pdf

CFPB Issues Rule Implementing S.2155 HMDA Partial Exemption

On July 5, 2018, the Bureau of Consumer Financial Protection (CFPB) issued an interpretive and procedural rule (the rule) to implement and clarify portions of the Economic Growth, Regulatory Relief, and Consumer Protection Act (S.2155) related to the Home Mortgage Disclosure Act (HMDA). The President signed S.2155 into law on May 24, 2018. Section 104 of S.2155 amends HMDA by adding partial exemptions to certain reporting requirements. The rule implements and clarifies the Section 104 provisions of S.2155.

S.2155 Partial Exemption

Section 104 of S.2155 exempts certain small-volume loan originators from the new HMDA reporting requirements. Financial institutions that originate fewer than 500 closed-end mortgage loans and 500 open-end lines of credit in each of the two preceding calendar years may revert to pre-January 2018 HMDA reporting requirements. The threshold must be met separately for both closed-end and open-end. This means:

- Reporting closed-end loans following pre-2018 rules;
  - When originating fewer than 500 closed-end mortgage loans;
- Reporting open-end loans following pre-2018 rules;
  - When originating fewer than 500 open-end mortgage loans;
- Exemption from HMDA reporting for HELOCs during 2018-2019 period; and,
- Limited HELOC reporting for post 2019 period.

This exemption does not apply to any bank that has received a "needs to improve" CRA rating during each of the last 2 most recent exams or a "substantial non-compliance" rating on its most recent exam.

CFPB's Rule

The rule implements the partial exemption as discussed above. Whether a partial exemption applies to an institution's lending activity for a particular calendar year depends on an institution's origination activity in each of the preceding two years. For example, whether a partial exemption applies to closed-end loans for which final action is taken in 2019 depends on the number of closed-end loans originated by the insured depository institution in 2017 and 2018.

The rule's clarifications of the S.2155 partial exemption include:

- S.2155 does not define "closed-end mortgage loan" or "open-end line of credit." The rule clarifies that the CFPB believes S.2155 intended those terms to only include those loans that would otherwise be reportable under HMDA. For example, "agricultural purpose loans," as defined within Reg C, are not counted.
- If a financial institution qualifies for a partial exemption, S.2155 specifies that the requirements of HMDA section 304(b)(5) and (6) do not apply. The rule interprets those sections to include 26 specific data points. For a

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list of those data points, see the link to the rule at the end of this article.

- S.2155 does not require a universal loan identifier (ULI) for loans or applications that are partially exempt. However, loans and applications must be identifiable. The rule requires a non-universal loan identifier even for partially exempt loans that do not require a ULI. The non-universal loan identifier may be composed of up to 22 characters to identify the covered loan or application, which:
  1. May be letters, numerals, or a combination of letters and numerals;
  2. Must be unique within the insured depository institution; and
  3. Must not include any information that could be used to directly identify the applicant or borrower.

- As discussed above, an insured depository institution is not eligible for the S.2155 partial exemption if it has received a rating of "needs to improve record of meeting community credit needs" during each of its two most recent Community Reinvestment Act (CRA) examinations or a rating of "substantial noncompliance in meeting community credit needs" on its most recent CRA examination. The rule interprets this assessment to be made as of December 31 of the preceding calendar year.

Compliance Considerations

Covered financial institutions will want to consider their use of the S.2155 partial exemption based upon CFPB's clarifications within the rule. Operational considerations will also need to be made. For example, the rule permits optional reporting. Some covered financial institutions eligible for a partial exemption may decide to report, especially for data submission in 2019. As discussed above, whether a partial exemption applies is based on origination activity for the preceding two years. Some covered financial institutions may be unable to determine this just before data collection for the covered year. For example, as most institutions had already begun collection of 2018 data before S.2155 was signed, they may not have time to adjust their systems. As a result, some covered financial institutions may decide to optionally report in 2019, which the rule permits.

Conclusion

While S.2155 became law upon publication, CFPB's implementation of its HMDA provisions through the rule provides additional clarity to financial institutions eligible for the partial exemption. WBA recommends that financial institution's seeking to utilize the partial exemption review the rule in full. The rule is effective on September 7, 2018.

The rule may be found here: https://www.gpo.gov/fdsys/pkg/FR-2018-09-07/pdf/2018-19244.pdf ■

September 2018

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

FinCEN Provides Exceptive Relief from Beneficial Ownership Requirements

On September 7, 2018, the Financial Crimes Enforcement Network (FinCEN) issued a ruling (relief ruling) granting exceptive relief to covered financial institutions from the beneficial ownership requirements for legal entity customers (beneficial owner rule). Generally speaking, the beneficial owner rule requires financial institutions to identify and verify beneficial owners of legal entity customers upon opening a new account. FinCEN issued guidance to the beneficial owner rule in the form of an FAQ on April 3, 2018. The FAQ provides, in part, that for purposes of the rule, "new account" includes financial product renewals. The relief ruling overrides that portion of the FAQ. Pursuant to the relief ruling, a new certification of beneficial owner need not be obtained for certain rollovers, renewals, modifications, and extensions.

Accounts Eligible for Relief

The relief ruling exempts financial institutions from the rule's requirement to identify and verify the identity of beneficial owners when opening new accounts as a result of:

- A rollover of a certificate of deposit (CD);
- A renewal, modification, or extension of a loan (e.g., setting a later payoff date) that does not require underwriting review and approval;
- A renewal, modification, or extension of a commercial line of credit or credit card account (e.g., a later payoff date is set) that does not require underwriting review and approval; and
- A renewal of a safe deposit box rental.

For purposes of the relief ruling a CD is defined as a deposit account with a specified maturity date that cannot be withdrawn before that date without incurring a penalty. The term of the account may vary, but a customer cannot add additional funds during that term. The relief ruling further defines CDs as an account that will automatically renew absent affirmative action by the customer to close the account.

In addition to CDs as defined within the rule, the relief ruling applies to certain loans. The renewal, modification, or extension of a loan, commercial line of credit, and credit card is exempt from new certification as to beneficial owner requirements. However, as indicated above, this exemption hinges on whether the loan or line of credit requires the financial institution's underwriting review and approval. If the loan is not subject to such requirements, then the exception applies. If it is, then the beneficial ownership rule requirements do apply, even in the case of a renewal, modification, or extension.

Compliance Considerations

As of publication of this article FinCEN has not released additional guidance on the relief ruling. As such, there is no additional context to the exception other than what is contained within the relief ruling itself. Financial institutions will need to review the relief ruling and contact FinCEN and regulators to determine whether specific accounts or types of renewals meet the criteria for the exemption.

For example, if a financial institution offers a CD to which a customer may add funds, it is unclear whether such an account is covered by the relief ruling. As discussed above, FinCEN defines a CD as one to which the depositor cannot add additional funds to the CD during its term. Whether the ruling covers CDs not meeting that definition is a matter that each financial institution must decide based upon the terms of each of its products and its interpretation of the relief ruling.

Similarly, the relief ruling defines CDs as "automatically renewing absent affirmative action by the customer." FinCEN offers no additional guidance on this aspect of its definition of CD. Financial institutions will need to review their renewal procedures to determine whether affirmative action is taken by customers. For example, a financial institution may require a customer to sign at time of renewal. A question exists as to whether such signature is "affirmative action" and would prevent such a renewal from receiving the exceptive relief. Such questions must be answered based on each financial institution's renewal policy and its interpretation of the relief ruling.

The relief ruling provides no clarity to the concept of "underwriting review and approval." As discussed above, in order to receive the benefit of the relief

ruling, a loan renewal must not be subject to a financial institutions underwriting review and approval. Similar to the considerations that must be made for CDs, WBA recommends financial institutions review their loan policies in the context of the relief ruling to determine whether renewals are made based upon underwriting review and approval.

Conclusion

The relief ruling eases some of the burden of the beneficial ownership rule by exempting certain renewals from identification and verification requirements that had previously been imposed upon them. However, it lacks clarity in its definitions as to what is covered. Because of the lack of clarity in the ruling, WBA recommends each financial institution fully review the relief ruling alongside potentially covered accounts.

The relief ruling can be found here: https://www.fincen.gov/sites/default/files/administrative_ruling/2018-09-07/Permanent%20Exceptive%20Relief%20Extension%20of%20Compliance%20Date%20CDs_final%20508.pdf

CFPB Issues Rule Implementing S.2155 HMDA Partial Exemption

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S.2155 Partial Exemption

Section 104 of S.2155 exempts certain small-volume loan originators from the new HMDA reporting requirements. Financial institutions that originate fewer than 500 closed-end mortgage loans and 500 open-end lines of credit in each of the two preceding calendar years may revert to pre-January 2018 HMDA reporting requirements. The threshold must be met separately for both closed-end and open-end. This means:

- Reporting closed-end loans following pre-2018 rules;
  - When originating fewer than 500 closed-end mortgage loans;
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  - When originating fewer than 500 open-end mortgage loans;
- Exemption from HMDA reporting for HELOCs during 2018-2019 period; and,
- Limited HELOC reporting for post 2019 period.

This exemption does not apply to any bank that has received a "needs to improve" CRA rating during each of the last 2 most recent exams or a "substantial non-compliance" rating on its most recent exam.

CFPB's Rule

The rule implements the partial exemption as discussed above. Whether a partial exemption applies to an institution's lending activity for a particular calendar year depends on an institution's origination activity in each of the preceding two years. For example, whether a partial exemption applies to closed-end loans for which final action is taken in 2019 depends on the number of closed-end loans originated by the insured depository institution in 2017 and 2018.

The rule's clarifications of the S.2155 partial exemption include:

- S.2155 does not define "closed-end mortgage loan" or "open-end line of credit." The rule clarifies that the CFPB believes S.2155 intended those terms to only include those loans that would otherwise be reportable under HMDA. For example, "agricultural purpose loans," as defined within Reg C, are not counted.
- If a financial institution qualifies for a partial exemption, S.2155 specifies that the requirements of HMDA section 304(b)(5) and (6) do not apply. The rule interprets those sections to include 26 specific data points. For a

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Compliance Journal

Special Focus

CFPB Changes Summary of Rights Model Forms Required by FCRA

On May 24, 2018 President Trump signed the Economic Growth, Regulatory Relief, and Consumer Protection Act (Act) into law. Title III of the Act amends section 605A of the Fair Credit Reporting Act (FCRA) to require new notices to consumers. These new notices are required whenever a summary of rights must be provided pursuant to section 609 of the FCRA.

On September 18, 2018 the Bureau of Consumer Financial Protection (CFPB) issued an interim final rule (rule) to update its model forms for the summary of consumer identity theft rights and the summary of consumer rights (model forms) to incorporate the Act's new notices. This article discusses the notice changes to the summary of rights and its impact on financial institutions.

Changes to Summary of Rights

The FCRA requires CFPB to prepare two consumer disclosures: the summary of consumer rights and summary of consumer identity theft rights. The rule amends CFPB's model forms to accommodate the notice changes required by the Act.

Whenever a consumer is required to receive a summary of consumer rights, the Act's notice requirements must be included. The amendments include changes to the minimum duration of initial fraud alerts, adjustments to update contact information for certain FCRA enforcement agencies, and notice of security freeze rights. CFPB's rule amends its model forms to incorporate the Act's changes.

CFPB will regard the use of the prior model forms, being those published in Appendices I and K on November 14, 2012, to constitute compliance with the FCRA provisions requiring such forms, so long as a separate page that contains the additional required information is provided in the same transmittal.

Impact Upon Financial Institutions

As discussed above, two model forms are impacted: the summary of rights of identity theft victims and summary of consumer rights. While the rule amends what must be included in each summary of rights, it does not change when they must be provided. The summary of rights of identity theft victims must be provided by a consumer reporting agency upon contact by a consumer expressing a belief that they have been a victim of fraud or identity theft. As such, financial institutions are generally not required to provide a summary of rights of identity theft victims.

The summary of consumer rights must be provided by consumer reporting agency in a number of situations. Those situations, similar to the summary of rights of identity theft victims discussed above, generally do not apply to financial institutions. However, a summary of consumer rights must be provided by those who obtain a consumer report for employment purposes. Thus, financial institutions providing a summary of consumer rights because they obtain consumer reports for employment purposes must be aware of the notice changes.

The FCRA does not require the summary of rights to be included in adverse action notices. Thus, the Act and the rule does not affect adverse action notices.

Conclusion

Financial institutions should verify the conditions upon which they are required to provide a summary of consumer rights under the FCRA. WBA reminds financial institutions that neither the Act nor the rule changes when a summary of rights must be provided. Thus, financial institutions likely already have procedures in place to provide a summary of rights when required. Financial institutions should verify those procedures, and consider whether their summary of rights incorporates the changes required by the Act. The Act amends the notice requirements contained within the summary of rights, and the rule implements new model forms accommodating those changes.

The Act may be found here: https://www.congress.gov/bill/115th-congress/senate-bill/2155/text

The rule may be found here: https://www.gpo.gov/fdsys/pkg/FR-2018-09-18/pdf/2018-20184.pdf ■

November 2018

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

TRID 2.0 – Disclosing Inspection/Draw/Handling Fees for Construction Loans

Complying with TRID 2.0 became mandatory on October 1, 2018. TRID 2.0 represents the first set of major changes to the TILA/RESPA Integrated Disclosure Rule (TRID) since its inception back in 2015. These changes primarily addressed areas of TRID 1.0 which left a lot to be desired – disclosures for construction loans and simultaneous subordinate liens. Lucky for banks, a number of these changes (e.g. the dreaded Cash to Close table) were, in all likelihood, addressed by your vendor. However, certain changes require bank intervention or, at the very least, bank knowledge. One of those changes is the disclosure of inspection/draw/handling fees for the staged disbursement of construction loan proceeds. Under revised TRID rules, how you disclose inspection/draw/handling fees depends upon when those fees are collected from the consumer. Banks should also be aware of how these changes affect tolerance calculations.

In a construction or construction to permanent loan, banks or title companies often assess an Inspection/Draw/Handling fee (or separate, itemized fees) for the staged disbursement of construction loan proceeds. If such fees are collected from the consumer at or before closing, such fees are disclosed on the Loan Estimate and Closing Disclosure as usual – in the Loan Costs table in sections A, B, or C, as appropriate. Under revised TRID rules, however, if these fees are collected from the consumer AFTER closing (either by the bank or third party, such as a title company), the Inspection/Draw/Handling Fee(s) must be disclosed on a separate Addendum, which must accompany the Loan Estimate and Closing Disclosure. The Addendum must be titled "Inspection and Handling Fees Collected After Closing". Importantly, irrespective of how these fees are collected – before, at, or after closing – a bank must list the fees on the Written List of Providers (a.k.a. Shopping List) if the consumer has the ability to shop for the services, according to informal guidance provided by CFPB.

It appears that CFPB modified the disclosure requirements for Inspection/Draw/Handling Fees collected post-closing in order for such fees to be more accurately reflected in the disclosures on the Loan Estimate and Closing Disclosure. For example, if an Inspection/Draw/Handling Fee is collected from the consumer after closing, certainly that fee should not affect the "Cash to Close" calculation. To this end, CFPB did provide the following guidance for Inspection/Draw/Handling fees collected post-closing and disclosed on an Addendum:

- Such fees are considered "loan costs." Therefore, such fees should be included in the Total of Payments calculation and the In 5 Years calculation.

- Such fees are finance charges and are included as finance charges anywhere a finance charge is included on the disclosures (e.g. in the APR calculation), except these fees should be excluded from all Cash to Close calculations on the disclosures.

- If such fees are withheld from the proceeds of the credit, the fees are prepaid finance charges and the Amount Financed Calculation should reflect the fee(s). Otherwise – that is, if a post-closing Inspection/Draw/Handling fee is not a prepaid financed charge – the Amount Financed calculation should not reflect these fees.

Finally, it's important to note the impact on tolerance calculations for Inspection/Draw/Handling fees under revised TRID rules.

1. Inspection/Draw/Handling Fees Collected at or before Consummation. First, if these fees are disclosed in the Loan Costs Table because they are collected at or before closing, they are subject to tolerance just like any other fees disclosed in the Loan Costs table. That is, the tolerance standard is zero, 10%, or unlimited. No change under TRID 2.0.

2. Inspection/Draw/Handling Fees Disclosed on an Addendum and Collected Post-Closing. If an Inspection/Draw/Handling fee is disclosed on an Addendum (because it's intended to be collected post-closing) and such fees are actually collected post-closing, the best information reasonably available standard applies. Therefore, no tolerance violation will occur.

3. Post-Closing Inspection/Draw/Handling Fees Change Between Addenda. According to informal guidance provided by CFPB, if a post-closing inspection/draw/handling fee amount changes between the time an Addendum is issued with the Loan Estimate (or a revised disclosure) and the Addendum issued with the final

CD, a conservative reading of the rule is that the fees disclosed on the Addenda may not be governed by the "best information reasonably available standard". Rather, the fees will be governed by the tolerance category that would apply to those loan costs absent an Addendum. That is, the fees could be subject to 10%, 0%, or unlimited tolerance depending on whether or not the fee is an origination charge and whether or not shopping is permitted/the customer shopped. Put simply, the tolerance is based on whether the fee would be located in Loan Costs section A, B, or C if there wasn't an Addendum.

Banks should also note that if there is a change to when an Inspection/Draw/Handling Fee will be collected from the consumer, this will likely be a changed circumstances and tolerance will reset for the Inspection/Draw/Handling fee(s). For example, Bank issued a Loan Estimate and disclosed a Draw fee on an accompanying Addendum because Title Company, who was managing the draws, planned to collect the amount from the consumer post-closing. Two days after the Loan Estimate is issued and weeks before the Closing Disclosure must be issued, Bank decides it will now manage the draws itself and will be collecting the Draw fee from the consumer at closing. According to informal guidance provided by CFPB, this is likely a changed circumstance and, as such, the Bank may reset tolerance for the Draw fee with the issuance of the appropriate disclosure (here, a revised Loan Estimate). The revised disclosure should list the Draw fee in the Loan Costs section, in A, B, or C, as appropriate.

In summary, banks should familiarize themselves with these changes, as applicable to their practices. In addition, it's important to ensure that your vendor is capable of managing the bank's construction lending practices for the assessment of Inspection/Draw/Handling fees.

WBA wishes to thank Atty. Lauren C. Capitini, Boardman & Clark, llp for providing this article. ■

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December 2018

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

2019 Rate and Exemption Thresholds Set

Introduction

The new year often brings changes to a certain interest rate requirement under Wisconsin law and various exemption threshold amounts under Federal law, all of which can impact certain consumer compliance requirements. This article provides a handy list of several amounts that are changing for calendar year 2019.

2019 Interest Rate Set for Certain Required Escrow Accounts

Under 138.052(5)(am), Wis Stats., interest must be paid on required escrow accounts established in connection with residential mortgage loans that were originated before April 18, 2018. The interest rate to be paid on these accounts is established annually by the Wisconsin Department of Financial Institutions (DFI). DFI has calculated the interest rate to be paid on such accounts to be **0.18** percent beginning January 1, 2019. The interest rate shall remain in effect through December 31, 2019.

Wisconsin Bankers Association was instrumental in the passage of 2017 Wisconsin Act 340, which eliminated the requirement to pay interest on required escrow accounts established in connection residential mortgage loans that are originated on or after April 18, 2018. This was a big win for the industry. DFI's notice may be viewed at: http://www.wdfi.org/_resources/indexed/site/fi/banks/EscrowNotice.pdf.

Appraisals for Higher-Priced Mortgage Loans Exemption Threshold

The Bureau of Consumer Financial Protection (CFPB), the Board of Governors of the Federal Reserve System (FRB) and the Office of the Comptroller of the Currency (OCC) have finalized amendments to the official interpretations for their regulations that implement section 129H of the Truth in Lending Act (TILA). Section 129H establishes special appraisal requirements for "higher-risk mortgages," termed "higher-priced mortgage loans" or "HPMLs" in the agencies' regulations. When the Agencies' rules were first established, they exempted, among other loan types, transactions of $25,000 or less, and required that this loan amount be adjusted annually based on any annual percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI–W). Thus, if there is no annual percentage increase in the CPI–W, the agencies will not adjust this exemption threshold from the prior year. However, in years following a year in which the exemption threshold was not adjusted, the threshold is calculated by applying the annual percentage increase in the CPI–W to the dollar amount that would have resulted, after rounding, if the decreases and any subsequent increases in the CPI–W had been taken into account. Based on the CPI–W in effect as of June 1, 2018, the exemption threshold will increase from $26,000 to **$26,700**, effective January 1, 2019. The final rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-11-23/pdf/2018-25400.pdf.

Regulations Z & M General Exemption Thresholds

CFPB and FRB have finalized amendments to the official interpretations for the agencies' regulations that implement the Truth in Lending Act (Regulation Z) and the Consumer Leasing Act (Regulation M). The Dodd-Frank Act requires that the dollar thresholds for exempt consumer credit transactions and consumer leases be adjusted annually by the annual percentage increase in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI–W). If there is no annual percentage increase in the CPI–W, the agencies will not adjust these exemption thresholds from the prior year. However, in years following a year in which the applicable exemption threshold was not adjusted, the threshold is calculated by applying the annual percentage change in the CPI–W to the dollar amount that would have resulted, after rounding, if the decreases and any subsequent increases in the CPI–W had been taken into account. Based on the annual percentage increase in the CPI–W as of June 1, 2018, the exemption threshold for both Regulations Z and M will increase from $55,800 to **$57,200**, effective January 1, 2019. The Regulation Z final rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-11-23/pdf/2018-25398.pdf, and the Regulation M final rule may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-11-23/pdf/2018-25396.pdf.

Regulation Z's HOEPA, Ability-to-Repay, Open-end Credit, & CARD Act Threshold Amounts

CFPB has finalized amendments to the regulation text and official interpretations for Regulation Z, which implements TILA, to update the dollar amounts of thresholds regarding HOEPA, Ability-to-Repay rules, certain open-end credit plans, and the CARD Act. These thresholds are adjusted annually based on the annual percentage change in the CPI as published by the Bureau of Labor Statistics. The threshold amounts listed below are effective January 1, 2019.

Special Focus

For HOEPA loans, the adjusted total loan amount threshold for high-cost mortgages will be **$21,549**. The adjusted points-and-fees dollar trigger for high-cost mortgages will be **$1,077**.

For qualified mortgages, which receive certain protections from liability under the Ability-to-Repay rule, the maximum thresholds for total points and fees in 2019 will be 3 percent of the total loan amount for a loan greater than or equal to $107,747; $3,232 for a loan amount greater than or equal to $64,648 but less than $107,747; 5 percent of the total loan amount for a loan greater than or equal to $21,549 but less than $64,648; $1,077 for a loan amount greater than or equal to $13,468 but less than $21,549; and 8 percent of the total loan amount for a loan amount less than $13,468. The final rule may be viewed at: https://www.govinfo.gov/content/pkg/FR-2018-08-27/pdf/2018-18209.pdf.

For open-end consumer credit plans under 1026.6(b)(2)(iii) and 1026.60(b)(3), the threshold that triggers requirements to disclose minimum interest charges will remain unchanged at **$1.00** in 2019.

For open-end consumer credit plans under the CARD Act amendments to TILA, the adjusted dollar amount in 2019 for the safe harbor for a first violation penalty fee will increase by $1 to **$28** and the adjusted dollar amount for the safe harbor for a subsequent violation penalty fee will increase by $1 to **$39**.

Conclusion

As noted above, these various amounts are effective beginning January 1, 2019. Therefore, creditors should ensure that any and all applicable adjustments to systems are in place on the effective date. ■

Regulatory Spotlight

Agencies Propose Reduced Reporting for Covered Depository Institutions.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) issued a proposed rule that would implement section 205 of the Economic Growth, Regulatory Relief, and Consumer Protection Act by: Expanding the eligibility to file the agencies' most streamlined report of condition, the FFIEC 051 Call Report, to include certain insured depository institutions with less than $5 billion in total consolidated assets that meet other criteria; and, establishing reduced reporting on the FFIEC 051 Call Report for the first and third reports of condition for a year. OCC and FRB also are proposing similar reduced reporting for certain uninsured institutions that they supervise with less than $5 billion in total consolidated assets that otherwise meet the same criteria. Comments are due **01/18/2018**. The notice may be viewed at: https://www.gpo.gov/fdsys/pkg/FR-2018-11-19/pdf/2018-24587.pdf. *Federal Register*, Vol. 83, No. 223, 11/19/2018, 58432-58458.

Agencies Propose Amendments to Real Estate Appraisals Regulations.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), and the Office of the Comptroller of the Currency (OCC) issued a proposed rule to amend the agencies' regulations requiring appraisals for certain real estate-related transactions. The proposed rule would increase the threshold level at or below which appraisals would not be required for residential real estate-related transactions from $250,000 to $400,000. Consistent with the requirement for other transac-

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