January 2019

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

Clearing the Air – Your Bank, the Farm Bill and Industrial Hemp

Late last year, President Donald Trump signed into law the long-awaited 2018 Farm Bill, with broad ramifications for agriculture and related industries nationwide. In its more than one thousand pages the bill covers a lot of ground, including crop insurance and farm subsidies, conservation topics and much more. There are also several provisions that affect federal regulation of the cultivation and production of industrial hemp that deserve attention from banks and some of their Ag customers.

Hemp production in the United States goes back centuries. George Washington grew hemp at Mount Vernon, and the USS Constitution used more than 120,000 pounds of hemp fiber rope in its rigging. Though the Marijuana Tax Act of 1937 raised the cost of production, hemp was used extensively through World War II in uniforms, canvas and rope. Because of efforts in efficiency and mechanization by International Harvester and the state Department of Agriculture, by the 1950s, Wisconsin was one of the leading producers of industrial hemp, just in time for the introduction of less expensive synthetic fibers that made hemp products uncompetitive. Hemp production dropped rapidly. In 1970, the Controlled Substances Act finished the industry by declaring all cannabis varieties Schedule I controlled substances, including hemp. Growers were required to obtain a rarely-granted permit from the Drug Enforcement Administration and production trailed off to essentially zero.

Despite a resurgence of interest in hemp production in the 1990s, there were no significant changes until the 2014 Farm Bill which allowed states to create agricultural pilot programs to grow hemp. The State of Wisconsin did just this in 2017 with a licensing and registration process for an industrial hemp research pilot program through the Department of Agriculture, Trade and Consumer Protection (DATCP). Hundreds of producers registered into the program for 2018 and 2019 and banks could finally consider banking these customers again. The 2014 Farm Bill also created a legal definition of industrial hemp, requiring it to contain 0.3% or less of tetrahydrocannabinol (THC), the psychoactive compound in marijuana.

The 2018 Farm Bill addresses various issues relating to industrial hemp and lowers the hurdles to legal cultivation under federal law. However, the bill legalizes industrial hemp only subject to significant conditions.

First, the requirement to maintain 0.3% THC content or less was carried forward. "Hemp" is legally defined as any part of the Cannabis sativa plant containing THC below this threshold. Any product exceeding this threshold is "marijuana" and is still a controlled substance. This replaces previous guidance under the Agricultural Marketing Act of 1946 which specified certain parts of the plant as hemp.

Testing THC concentrations will be an important qualifier for legalized hemp production. However, discussion on how this will be done, who will oversee testing (the U.S. Department of Agriculture, state departments or both), and how these results will be verified and recorded is just beginning. Banks that move forward with industrial hemp customers should look for a careful and deliberative process in measuring THC to ensure they are not inadvertently facilitating the production of a Schedule I drug.

Second, nothing in the Farm Bill invalidates the DATCP pilot program. Under the bill, states are allowed to become the primary regulators of hemp cultivation. As part of their due diligence, Wisconsin banks should look for participation and annual registration. This is still the right way in this state to become a producer in what will be a heavily regulated industry. The DATCP does not intend to publish a list of participants in the program, though they will confirm for particular customers by e-mail. DATCP is also coordinating THC testing of industrial hemp crops in Wisconsin. More information is available on their website under Programs and Services.

Third, while the Farm Bill provides clarity around non-food hemp products, it doesn't change the Food and Drug Administration's (FDA's) regulation of cannabidiol (CBD) oil. The FDA maintains that, except for some limited pharmaceutical grade production, the use of CBD as an ingredient in food or dietary supplements remains prohibited. Also, while hemp cultivation in a manner consistent with the Farm Bill will produce low-THC CBD, any that exceeds 0.3% THC remains a Schedule I controlled substance. This means that while customers that sell CBD oil have a standard to meet to avoid Drug Enforcement Agency (DEA) violations, they might still face challenges from the FDA. Banks should consider these issues when performing due diligence on any customer that sells CBD, though replace-

ment of zero tolerance for THC with 0.3% tolerance can provide some protection against the most serious, drug-related complications.

Finally, the patchwork of state laws around medicinal and recreational use of marijuana has not changed, and high-THC products are still Schedule I controlled substances according to the DEA. Despite the carve-out for hemp provided by the Farm Bill, marijuana remains illegal under state and federal law in Wisconsin. Banking marijuana-related businesses still means following Financial Crimes Enforcement Network (FinCEN) guidance and taking on some compliance risk.

With the passage of the Farm Bill, banks have opportunities to take on industrial hemp customers with more confidence than in the past. As an added benefit, the bill permits hemp researchers (under the DATCP pilot program in Wisconsin) to apply for federal grants and they are eligible for federal crop insurance. Banks may see customers looking to take advantage of hemp production as a new, potentially higher margin crop. However, the road to successfully serving those customers and meeting regulatory requirements is not without complications. In addition to the considerations above, banks that take on these customers should update their BSA policies and procedures to include any enhanced due diligence performed on industrial hemp customers. With careful planning and risk-based monitoring, industrial hemp producers could prove to be some of your best customers.

WBA wished to thank Shane B. Bauer, First Vice President - Compliance, BSA and Security Officer, Banker's Bank for providing this article. ■

Industrial Hemp in Wisconsin

WBA expects that many Wisconsin banks will soon be approached by customers engaged in the industrial hemp industry, if they have not already. Wisconsin possesses favorable weather and soil conditions for the crop, and many farmers appear to be exploring the industry. As of January 2, 2019, the Wisconsin Department of Agriculture, Trade, and Consumer Protection (DATCP) has received a total of 413 Hemp Grower, and 244 Hemp Processor applications for a license and/or 2019 annual registration to participate in Wisconsin's pilot program. Growers, processors, and retailers have already begun searching for banks offering deposit services and soon, loans. WBA has already received several calls through the WBA Legal Call Program questioning the legality of banking industrial hemp customers.

There are no rules or regulations prohibiting banks from doing business with customers legally engaged in the hemp industry. Growing, processing, and selling hemp products is legal, but it is regulated. Banks should implement policies and procedures to work with their customers accordingly. There is no regulatory guidance on the topic, but, arguably, none is necessary. Banks should follow BSA, safety and soundness, and business considerations already in place. Policies and procedures will need to be written or updated, as appropriate for this new business, but there are no new rules governing banks.

To that extent, it is important for banks to understand the hemp industry so they can understand their customers. WBA recommends considering the following matters:

- Is your customer registered with DATCP?
- Can they provide documentation that their licensing is up to date?
- Do they submit samples for regular testing?
- Who do they buy/sell to?
- If they are a grower, do they use licensed seed?
- If they're a retailer who may not be required to register with DATCP, who do they buy from (and is that seller licensed)?
- Others.

These considerations become even more important when it comes to lending, where banks must consider additional underwriting and collateralization components. Furthermore, as the hemp industry develops, the rules regulating it will change, and the business will continue

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Special Focus

to develop. Bank policies and procedures must be designed to evolve in tandem with this new industry.

Hemp has long been a cash industry, and deposit services such as checks, debit cards, and online banking are tools the industry has been without in the past. WBA has observed that farmers and growers appear eager to work with Wisconsin banks who are the experts in their community at handling money. Hemp businesses that follow Wisconsin's pilot program are legal. While this situation is new, it is analogous to others. For example, business customers that open a bar, liquor store, or own and operate ATM and gaming machines are regulated and must meet certain requirements. From a BSA, safety and soundness, and general know-your-customer standpoint, banks have policies and procedures in place to consider those requirements. Industrial hemp, while new and carrying its own unique requirements, should be no different and should be addressed by policy and procedure.

WBA encourages Wisconsin banks to learn more about hemp, what it is, how it is used, and understand its legal requirements. WBA will continue to provide resources and updates as the industrial hemp industry continues to grow. For further discussion of the hemp industry in Wisconsin and the pilot program's requirements, join us at the WBA Compliance Forum with sessions running from February 19-21 where we will be joined by a speaker from DATCP. For more information, visit our website at https://www.wisbank.com/. ■

Regulatory Spotlight

Agencies Finalize Rule on 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) are amending their Community Reinvestment Act (CRA) regulations to adjust the asset-size thresholds used to define "small bank" or "small savings association" and "intermediate small bank" or "intermediate small savings association." As required by the CRA regulations, the adjustment to the threshold amount is based on the annual percentage change in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI–W). During the 12-month period ending November 2018, the CPI–W increased by 2.59 percent. As a result, the Agencies are revising 12 CFR 25.12(u)(1), 195.12(u)(1), 228.12(u)(1), and 345.12(u)(1) to make this annual adjustment. Beginning 01/01/2019, banks and savings associations that, as of December 31 of either of the prior two calendar years, had assets of less than $1.284 billion are small banks or small savings associations. Small banks and small savings associations with assets of at least $321 million as of December 31 of both of the prior two calendar years and less than $1.284 billion as of December 31 of either of the prior two calendar years are intermediate small banks or intermediate small savings associations. The Agencies also publish current and historical asset-size thresholds on the website of the Federal Financial Institutions Examination Council at http://www.ffiec.gov/cra/. The final rule is effective **01/01/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2018-12-27/pdf/2018-27791.pdf. *Federal Register*, Vol. 83, No. 247, 12/27/2018, 66601-66604.

Agencies Finalize Rules on Examination Cycle for Certain Small Insured 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 interim final rules that were effective immediately to implement section 210 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (Economic Growth Act), which was enacted on **05/24/2018**. The agencies are now adopting the interim final rules as final without change. The interim final rules and final rules implement section 210 of the Economic Growth Act, which amended section 10(d) of the Federal Deposit Insurance Act (FDI Act) to permit the agencies to examine qualifying insured depository institutions (IDIs) with under $3 billion in total assets not less than once during each 18-month period. In addition, these final rules adopt as final the parallel changes to the agencies' regulations governing the on-site examination cycle for U.S. branches and agencies of foreign banks, consistent with the International Banking Act of 1978 (IBA). The final rules are effective **01/28/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2018-12-28/pdf/2018-28267.pdf. *Federal Register*, Vol. 83, No. 248, 12/28/2018, 67033-67035.

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Do Banks Have To Monitor Corporate Deposit Accounts To Make Sure Officers Named On Those Accounts Are Acting Lawfully?

The short answer to this question is "no," but the long answer gets more complicated. The Wisconsin Supreme Court recently delved into the long answer when it was presented with that question in Koss Corporation v. Park Bank, (2019 WI 7, dated 1/29/2019), and fortunately, it came up with the same answer to the long question, and that is "no." The Court determined that Park Bank, Milwaukee, was not liable for a massive embezzlement from Koss Corporation ("Koss") accounts at Park Bank over a period of many years thanks to the Uniform Fiduciary Act adopted by Wisconsin in 1925 ("UFA"). Under the UFA, a "fiduciary" includes an officer of a corporation as well as partners and agents of corporations, limited liability companies, partnerships, or other associations. The UFA, which is a uniform law adopted by many states, clarifies that banks are not responsible for monitoring fiduciary accounts and placed the burden of employing honest employees managing those accounts on the entities that open the deposit accounts. The UFA was enacted to "facilitate banking and financial transactions" by providing relief from consequences of the then law which was to place the duty of monitoring fiduciary accounts for wrongdoing on the bank's shoulders. Thus, under the UFA, simple negligence by a bank with respect to a corporation's deposit accounts will not lead to bank liability. However, there are certain and very limited circumstances when a bank may be found liable under the UFA for the unlawful acts of a corporate officer with respect to the corporation's deposit accounts, and that is what the Koss Corporation v. Park Bank case was all about.

In this case, a Koss senior executive officer embezzled $34 million from Koss over a nine-year period without her employer noticing. Koss attempted to shift the losses caused by its own high-level executive's criminal conduct to Park Bank by arguing that the Court should find that a bank's alleged negligence in dealing with the officer constitutes liability under the UFA. Fortunately, the Court said "no" and determined that negligence alone will not lead to bank liability. This is one of the helpful holdings of the Court in this case that will definitely benefit banks maintaining UFA accounts, and virtually every bank maintains UFA accounts for their corporate customers.

In greater detail, the UFA provides for three separate standards according to which a bank could be held liable for a fiduciary's embezzlement from an account or other breach of the fiduciary's duty to the corporation. Those three standards are (1) where the bank has actual knowledge of the unlawful conduct of the fiduciary, (2) where the bank has knowledge of sufficient facts to show that it acted in "bad faith" by honoring the fiduciary's withdrawals from the account, or (3) where the bank accepts its own check in payment of a personal debt of the fiduciary to the bank. In this case, no evidence was offered by Koss that Park Bank violated standards (1) and (3), and therefore Koss alleged Park Bank's transactions with the officer who engaged in the criminal acts through the account were done in "bad faith." So this case focused on whether Park Bank violated the "bad faith" standard under the UFA to determine whether Park Bank has liability to Koss, and for this purpose the Court had to define "bad faith." "Bad faith" had not previously been defined by Wisconsin courts under the UFA since 1925 when it was enacted.

The Court's effort to define "bad faith" led to certain differences of opinion among the seven Justices on the Wisconsin Supreme Court, which differences will make it difficult for attorneys going forward to make meaningful determinations for their clients. There were three different written opinions from the Court in this case. One was called the "Lead Opinion" and was rendered by two of the seven Justices, the second was called the "Concurring Opinion" and was rendered by three of the Justices, and the third was the "Dissenting Opinion" and was rendered by two of the Justices. Importantly, the "Lead Opinion" and the "Concurring Opinion" rendered by five Justices determined that the claim by Koss against Park Bank should be dismissed. That is an official holding of the Court in this case. It means that Park Bank won the case and it is good news for the banking industry. The Dissenting Opinion

determined that the case should not be dismissed and should be sent back to the trial court for a new trial by a jury, but fortunately that opinion was made by only two of the Justices and is not the decision of the Court in this case. Lawyers for banks will be assigned the task of interpreting the "Lead Opinion" and the "Concurring Opinion" to determine the legal definition of "bad faith" going forward. I will not attempt here to sort out the differences between these two opinions and indicate which might be applicable in a future case, but I will focus on the Concurring Opinion since it will be the most difficult of the two opinions for banks to comply with. Therefore, in my view, if a bank complies with the definition of "bad faith" as described in the Concurring Opinion it is likely to be able to withstand any case brought against it down the road claiming the bank acted in "bad faith."

According to the Concurring Opinion, the standard of "bad faith" is defined as follows:

> "[B]ad faith denotes a reckless disregard or purposeful obliviousness of the known facts suggesting impropriety by the fiduciary. It is not established by negligent or careless conduct or by vague suspicion. Likewise, actual knowledge of and complicity in the fiduciary's misdeeds is not required. However, where facts suggesting fiduciary misconduct are compelling and obvious, it is bad faith to remain passive and not inquire further because such inaction amounts to a deliberate desire to evade knowledge."

The lead opinion imposed a more exacting definition of "bad faith" which would make it more difficult for customers to substantiate claims for "bad faith" against banks under the UFA. I believe the bottom line is that if a bank at least meets the standard imposed by the concurring opinion it should avoid any liability to corporate customers alleging breach of "bad faith" under the UFA. Bank counsel will, of course, in the event of litigation, argue the applicability of the more exacting standard as determined by the lead opinion is applicable to bank customers making UFA claims.

Again, regardless of the standard used, neither the Lead Opinion nor the Concurring Opinion found "bad faith" on the part of Park Bank in this case. The three Justices on the Concurring Opinion concluded that even under their less onerous standard of "bad faith" than the one adopted by the "Lead Opinion" that summary judgment in favor of Park Bank was appropriate and therefore Park Bank won the case. According to the Concurring Opinion, Koss did not put forth sufficient evidence that Park Bank remained passive in the face of compelling and obvious facts suggesting fiduciary misconduct. The Court noted that even Koss itself did not notice the fraud for several years. According to the Concurring Opinion, the facts of this case did not present the "compelling and obvious" suggestion of fiduciary misconduct so as to place liability on Park Bank.

Banks may wish to include a greater focus in their training of bank personnel on claims made under the UFA and the responsibilities of the bank under the UFA in the event bank personnel become aware of facts suggesting impropriety by a fiduciary on an account. In that event, the bank may wish to inquire further given that inaction on its part could denote a deliberate desire to evade knowledge and may constitute "bad faith."

In this case, one of the methods the officer used to embezzle funds from Koss was to order cashier's checks from Park Bank for personal expenditures. She used hundreds of cashier's checks drawn on the Koss's accounts at Park Bank to pay for her purchases from luxury retailers, as well as to pay her personal credit card bills. Generally, she would instruct an assistant from Koss to call Park Bank and request a cashier's check on the officer's behalf. It was Park Bank's practice to allow non-signatories to the account to call and request cashier's checks on the officer's behalf. The officer would then send another assistant to pick up the envelopes at Park Bank with the cashier's check included in them. The officer also used "petty cash" requests to embezzle funds. She would instruct an assistant at Koss to go to Park Bank and endorse a manually written check made out to "petty cash." The officer would call and tell Park Bank the employee was coming. The officer's third method of embezzling funds was to request wire transfers from Park Bank to an out-of-state bank where Koss also maintained accounts. The officer would then make wire transfers from those accounts maintained at the out-of-state bank. The Court took the position that these wire transfers were immaterial to the case because from Park Bank's perspective, the funds remained in the control of Koss after the transfer even though Park Bank's policy required a wire transfer agreement to initiate such wire

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transfers, and Koss did not have one. Koss was unable to explain why wire transfers sent to other Koss bank accounts would have raised suspicions on the part of any Park Bank employee.

It is helpful to note that according to the Concurring Opinion neither "the amount and number of transactions carried out on an account containing fiduciary funds, nor the mere names of payees on checks drawn on that account, should be sufficient to create bad faith liability based on Bank's action in paying such checks." And in this case, over a period of ten years of the officer's embezzlement, a period during which Park Bank issued more than 60,000 cashier's checks, and 49 bank employees issued the 359 cashier's checks requested by the Koss officer, was not sufficient to establish "bad faith" and liability based on Park Bank's action in paying such checks over such a period of time.

In the end, Park Bank won this case at the trial court level, on appeal at the Court of Appeals level and at the Supreme Court level, regardless of which definition of "bad faith" was applied by the courts. The facts simply did not justify a finding under any of these definitions that Park Bank acted in bad faith and the courts therefore determined Park Bank was not liable to Koss for the embezzlement.

WBA wishes to thank Atty. John Knight, Boardman & Clark, llp for providing this article. ■

Supreme Court Issues Ruling on Koss Corp v. Park Bank Case Addressing Definition of Bad Faith Under Uniform Fiduciary Act

On January 29, 2019, the Wisconsin Supreme Court (Court) issued its opinion in the Koss Corporation v. Park Bank case (Koss Corp.). The case involved the definition of "bad faith" under Wisconsin's Uniform Fiduciary Act (UFA). Previously, there was little case law in Wisconsin interpreting "bad faith" under the UFA. WBA filed with the Wisconsin Supreme Court an amicus brief in support of Park Bank's position.

An employee embezzled approximately $34 million from Koss Corporation over a period of ten years. The employee used multiple methods to embezzle funds. Methods included obtaining cashier's checks for personal expenditures, instructing other, non-signatory employees to request checks, taking and cashing checks made payable to cash, and initiating wire transfers to out-of-state banks. After the employee pled guilty, Koss Corporation sought relief against Park Bank under the UFA, claiming Park Bank acted in bad faith in those transactions. The Milwaukee Circuit Court dismissed all claims against Park Bank. The Wisconsin Court of Appeals affirmed the lower court, and the Wisconsin Supreme Court affirmed that decision.

Two conclusions are clear from the Court's decision. First, Park Bank's conduct did not amount to bad faith. Second, negligence does not prove bad faith. However, a disagreement between the lead opinion and the concurring opinions disrupted the opportunity to clearly define "bad faith." This article will discuss what is clear from the Court's opinion, what is unclear, and how the opinion affects Wisconsin banks.

Koss Corp. involves the question of whether a bank can be held liable for the actions of a third party fiduciary. Specifically, whether a bank can be held liable for acting in "bad faith" in its transactions with an employee embezzling millions from a corporate deposit account. The UFA provides protections from such liabilities and was adopted by Wisconsin in 1925. Wis. Stats. Section 112.01(9) of the UFA provides standards whereby a bank can obtain protection from claims involving the acts of a customer's fiduciaries. In this case, that section forms the basis of Koss Corporation's claim that Park Bank acted in bad faith. The Court broke 112.01(9) down into three standards by which a bank could be liable:

1. When a bank had actual knowledge of the unlawful conduct of a fiduciary;

[1] The UFA provides protections for banks. This case was unique in that the UFA was presented as the basis for a complaint rather than as a defense. The Court's opinion is still significant in understanding that defense.

March 2019

Wisconsin Bankers ASSOCIATION

Compliance Journal

Special Focus

Private Flood Insurance

On February 12, 2019 the Federal Financial Institutions Examination Council published a final rule on loans in areas having special flood hazards (2019 final rule). The 2019 final rule amends the flood regulations for the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the National Credit Union Administration (Agencies). The Agencies issued the 2019 final rule to implement the private flood insurance provisions of the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act). The 2019 final rule was published in the *Federal Register* on February 20, 2019 and compliance is manditory on July 1, 2019; however, lenders may begin following the rule now.

Background

The Biggert-Waters Act includes a statutory definition of private flood insurance and directs the Agencies to implement acceptance through rulemaking. In 2013 the Agencies proposed a rule requiring the acceptance of private flood insurance pursuant to the statutory definition. The proposed rule generated interpretive uncertainties that ultimately resulted in the Agencies issuing a revised proposed rule in 2016. The 2019 final rule is an attempt to clarify the definition of private flood insurance under the Biggert-Waters Act.

2019 Final Rule

In addition to attempting to clarify the statutory definition of private flood insurance, the 2019 final rule includes a compliance aid to enable institutions to identify acceptable private policies. Additionally, subject to certain restrictions, it permits institutions to exercise discretionary acceptance of flood insurance policies that do not meet the definition of private flood insurance. Finally, the rule specifies how lenders may accept policies issued by "mutual aid societies" such as certain Amish Aid Plans.

Definition of Private Flood Insurance

The statutory definition of private flood insurance under the Biggert-Waters Act incorporated factors from the Federal Emergency Management Agency's Mandatory Purchase of Flood Insurance Guidelines. The 2019 final rule attempts to clarify this statutory definition. As such, institutions familiar with the statutory definition will notice slight variations when compared to the 2019 final rule's definition. For purposes of this article, the analysis will focus on the 2019 final rule's definition and not make a comparison.

Under the 2019 final rule, private flood insurance means an insurance policy that:

1. Is issued by an insurance company that is:
    - Licensed, admitted, or otherwise approved to engage in the business of insurance by the insurance regulator of the State or jurisdiction in which the property to be insured is located; or
    - Recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the State or jurisdiction in which the property to be insured is located in the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property;
2. Provides flood insurance coverage that is at least as broad as the coverage provided under a Standard Flood Insurance Policy (SFIP) for the same type of property, including when considering deductibles, exclusions, and conditions offered by the insurer. To be at least as broad as the coverage provided under an SFIP, the policy must, at a minimum:
    - Define the term "flood" to include the events defined as a "flood" in an SFIP;
    - Contain the coverage specified in an SFIP, including that relating to building property coverage; personal property coverage, if purchased by the insured mortgagor(s); other coverages; and increased cost of compliance coverage;
    - Contain deductibles no higher than the specified maximum, and include similar nonapplicability provisions, as under an SFIP, for any total policy coverage amount up to the maximum available under the National Flood Insurance Program (NFIP) at the time the policy is provided to the lender;
    - Provide coverage for direct physical loss caused by a flood and may only exclude other causes of loss that are excluded in an SFIP. Any exclusions other

than those in an SFIP may pertain only to coverage that is in addition to the amount and type of coverage that could be provided by an SFIP or have the effect of providing broader coverage to the policyholder; and

- Not contain conditions that narrow the coverage provided in an SFIP;

3. Includes all of the following:

   - A requirement for the insurer to give written notice 45 days before cancellation or non-renewal of flood insurance coverage to:

     ► The insured; and

     ► The lending institution that made the designated loan secured by the property covered by the flood insurance, or the servicer acting on its behalf;

   - Information about the availability of flood insurance coverage under the NFIP;

   - A mortgage interest clause similar to the clause contained in an SFIP; and

   - A provision requiring an insured to file suit not later than one year after the date of a written denial of all or part of a claim under the policy; and

4. Contains cancellation provisions that are as restrictive as the provisions contained in an SFIP.

Compliance Aid

Pursuant to the above definition, a national bank or Federal savings association must accept private flood insurance in satisfaction of the flood insurance purchase requirements. Thus, a financial institution is required to accept private flood insurance and must also ensure it meets the above definition. However, the 2019 final rule provides a compliance aid to assist in that mandatory acceptance. Pursuant to the compliance aid, a financial institution may determine that a policy meets the definition of private flood insurance without reviewing the policy, if the following statement is included within the policy or as an endorsement to the policy:

"This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) and the corresponding regulation."

While the compliance aid provides a safe harbor to financial institutions that accept policies containing the above language, there is no requirement for insurers to include the compliance aid language. Furthermore, because the 2019 final rule prescribes mandatory acceptance of private flood insurance that meets the above definition, financial institutions must accept policies that meet the above definition whether it includes the compliance aid or not. Meaning, a financial institution cannot reject a policy for the sole reason that it does not contain the compliance aid language.

Discretionary Acceptance

The 2019 final rule provides financial institutions the discretionary ability to accept or reject policies that do not meet the above definition of private flood insurance. Lenders may accept such policies, at their own discretion, if the policy:

1. Provides coverage in the amount required by the NFIP;

2. Is issued by an insurer that is licensed, admitted, or otherwise approved to engage in the business of insurance by the insurance regulator of the State or jurisdiction in which the property to be insured is located; or in the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, is issued by a surplus lines insurer recognized, or not disapproved, by the insurance regulator of the State or jurisdiction where the property to be insured is located;

3. Covers both the mortgagor(s) and the mortgagee(s) as loss payees, except in the case of a policy that is provided by a condominium association, cooperative, homeowners association, or other applicable group and for which the premium is paid by the condominium association, cooperative, homeowners association, or other applicable group as a common expense; and

4. Provides sufficient protection of the designated loan, consistent with general safety and soundness princi-

March 2019
Volume 23, Number 10

Wisconsin Bankers Association
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Subscription Rate:
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ples, and the national bank or Federal savings association documents its conclusion regarding sufficiency of the protection of the loan in writing.

Mutual Aid Societies

In order to meet the mandatory acceptance provisions for private flood insurance, the 2019 final rule permits lenders to accept policies written by mutual aid societies if:

1. The applicable supervisory agency has determined that such plans qualify as flood insurance for purposes of the Act;

2. The plan provides coverage in the amount required by the NFIP;

3. The plan covers both the mortgagor(s) and the mortgagee(s) as loss payees; and

4. The plan provides sufficient protection of the designated loan, consistent with general safety and soundness principles, and the national bank or Federal savings association documents its conclusion regarding sufficiency of the protection of the loan in writing.

In addition, the rule defines mutual aid society to mean an organization:

1. Whose members share a common religious, charitable, educational, or fraternal bond;

2. That covers losses caused by damage to members' property pursuant to an agreement, including damage caused by flooding, in accordance with this common bond; and

3. That has a demonstrated history of fulfilling the terms of agreements to cover losses to members' property caused by flooding.

Conclusion

With the 2019 final rule becoming effective July 1, 2019, and optional compliance available under the 2019 final rule now, WBA recommends financial institutions review their policies on acceptance of private flood insurance. Financial institutions will need to understand the definition of private flood insurance policies pursuant to the rule, even if they had previously adhered to the statutory definition, as the 2019 final rule implements slight changes. Furthermore, institutions should be prepared to understand the relation of the compliance aid to the mandatory acceptance requirements.

The 2019 final rule may be found here: https://www.govinfo.gov/content/pkg/FR-2019-02-20/pdf/2019-02650.pdf ■

Regulatory Spotlight

Agencies Finalize Current Expected Credit Losses Methodology for Allowances.

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) are adopting a final rule to address changes to credit loss accounting under U.S. generally accepted accounting principles, including banking organizations' implementation of the current expected credit losses methodology (CECL). The final rule provides banking organizations the option to phase in over a three-year period the day-one adverse effects on regulatory capital that may result from the adoption of the new accounting standard. In addition, the final rule revises the agencies' regulatory capital rule, stress testing rules, and regulatory disclosure requirements to reflect CECL, and makes conforming amendments to other regulations that reference credit loss allowances. The final rule is effective **04/01/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-02-14/pdf/2018-28281.pdf. *Federal Register*, Vol. 84, No. 31, 02/14/2019, 4222-4250.

Agencies Extend Comment Period for Standardized Approach for Calculating the Exposure Amount of Derivatives Contracts.

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) published a proposal in the *Federal Register* on **12/17/2018** to amend the agencies' capital rule to implement the Standardized Approach for Calculating the Exposure Amount of Derivatives Contracts. The agencies have decided to extend the comment period for the proposal. The new comment due date is **03/18/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-02-26/pdf/2019-03249.pdf. *Federal Register*, Vol. 84, No. 38, 02/26/2019, 6107.

CFPB Proposes Rescinding Parts of Payday, Vehicle Title, and Certain High-Cost Installment Loans Rule.

The Bureau of Consumer Financial Protection (CFPB) is proposing to rescind certain provisions of the regulation

Wisconsin Bankers ASSOCIATION

April 2019

Compliance Journal

Special Focus

What Are Brokered Deposits and What Is the Significance of FDIC Reform?

Brokered deposits are relatively simple in concept but subject to complex regulatory restrictions. By concept, "brokered deposit" is a term used to describe a source of funding for financial institutions. That is, funds managed by a deposit broker, being an individual who accepts and places funds in investment instruments at financial institutions, on behalf of others. This concept has evolved over the years, grown controversial, and subjected to regulatory restriction. To that extent, the question is: what deposits are considered brokered for purposes of regulatory coverage?

According to section 29 of the Federal Deposit Insurance Act (FDI Act) and Section 227 of the Federal Deposit Insurance Corporation's (FDIC) rules and regulations, brokered deposit means any deposit that is obtained, directly or indirectly, from or through the mediation or assistance of a deposit broker.[1] A deposit broker is:

1. Any person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with insured depository institutions, or the business of placing deposits with insured depository institutions for the purpose of selling interests in those deposits to third parties; and

2. An agent or trustee who establishes a deposit account to facilitate a business arrangement with an insured depository institution to use the proceeds of the account to fund a prearranged loan.

This broad language gives FDIC significant discretion to determine whether a deposit is brokered, making the above question difficult to answer.

Emerging technologies continue to create innovative deposit opportunities. For example, internet and mobile banking did not exist when the rules were written. Brokered deposits were born from new technologies, but those technologies continue to evolve, and with them, the concept of what a brokered deposit is.

Background

The inception of brokered deposits came with the ability to transfer funds electronically. These technologies made it quick, easy, and cheap to access before unreached markets, which enabled greater bank liquidity and growth. Controversy exists as to whether such growth contributed to the 1980 financial crisis, an examination of which is outside the scope of this article. However, the 1980 financial crisis did result in FDIC launching a study into brokered deposits which led the agency to write rules in 1989 and amend them in 1991.

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 added Section 29 of the FDI Act, titled "Brokered Deposits" (Section 29). Section 29 places certain restrictions on "troubled" institutions. Specifically, Section 29 provides:

1. Acceptance of brokered deposits is restricted to well-capitalized insured depository institutions.

2. Less than well-capitalized institutions may only offer brokered deposits under certain circumstances, and with restricted rates.

In 1991 Congress enacted the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA). The FDICIA resulted in threshold adjustments to the brokered deposit restrictions under Section 29 and gave FDIC the ability to waive those restrictions under certain circumstances.

More recently, the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) amended Section 29 which excepted certain reciprocal deposits from treatment as brokered deposits. As seen above, Section 29 does not define the term "brokered deposit." Rather, it defines the term "deposit broker." Following EGRRCPA, on February 6, 2019, FDIC published an advance notice of proposed rulemaking and request for comment on unsafe and unsound banking practices: brokered deposits and interest rate restrictions (ANPR). The ANPR announces FDIC's comprehensive review of its regulatory approach to brokered deposits and their interest rate caps. As part of its re-evaluation FDIC seeks comment on how it should revamp its definition of brokered deposits and interest rate restrictions.

While the EGRRCPA implementation is specific to reciprocal deposits, FDIC's ANPR is broader in scope, and presents

1 2 C.F.R. § 337.6(a)(2)

an opportunity to re-examine the definition and treatment of brokered deposits as a whole.

Impact

How Brokered Deposits are Used

Brokered deposits are a relatively new mechanism to the financial service industry. They provide:

1. A quick, cheap, alternative sources of funding from national markets.

2. An additional tool for institutions to maintain liquidity and interest rate risk analysis for balance sheet management.

3. A potential tool for community banks to expand their deposits and maintain funds that do not move away when the local market shifts.

4. Flexibility in availability of funds to institutions with varying demands in regional markets for deposits vs. loans.

5. Greater opportunities to match deposit terms to loan funding.

6. Alternative, competitive rates for investors.

7. An additional tool for investing institutions to manage funds.

Significance of Regulation under Current Rules

As discussed above, Section 29 restricts acceptance of brokered deposits and limits deposit interest rates. A well-capitalized institution is, generally, unrestricted. However, an undercapitalized institution may not accept, renew, or roll over any brokered deposit. An adequately capitalized institution may not accept, renew, or roll over any brokered deposit unless FDIC grants a waiver. Even though a well-capitalized institution is unrestricted, examiners consider the presence of core[2] and brokered deposits when evaluating liquidity management programs and assigning liquidity ratings.

Furthermore, brokered deposits are a significant source of assets for some institutions. Institutions also seek to meet their customers deposit needs in an age of constantly evolving technologies. This creates uncertainty as to whether a particular deposit qualifies as a brokered deposit. The answer to that question is complex, as it lies not only in statute, but FDIC issued studies, interpretations, advisory opinions, regulations, and an FAQ on identifying, accepting, and reporting brokered deposits.

Brokered deposit determinations are fact-specific and influenced by a number of factors. FDIC has broad discretion in application of its rules, which involves complex methodologies for determining and adjusting rates, and considers brokered deposit determinations on a case-by-case basis. For example, the term deposit broker has been applied to social media platforms, fintech, homeowners associations, and employee benefits providers. How FDIC views brokered deposits is also up to interpretation. Fortunately, FDIC states its view of brokered deposits in its 2016 FAQ:[3]

> "Brokered deposits can be a suitable funding source when properly managed as part of an overall, prudent funding strategy. However, some banks have used brokered deposits to fund unsound or rapid expansion of loan and investment portfolios, which has contributed to weakened financial and liquidity positions over successive economic cycles. The overuse of brokered deposits and the improper management of brokered deposits by problem institutions have contributed to bank failures and losses to the Deposit Insurance Fund."

FDIC still appears to view brokered deposits as volatile and scrutinizes them accordingly. One direct result is rate cap limitations. By rule, rate caps only apply to less-than well capitalized banks. However, regulators have looked to the limits during exams, regardless of capital levels, pointing to potential volatility. Furthermore, under its 2009 calculation method, current rate caps are artificially low and hardly reflect what a customer can get from other sources. For example, as of April 22, 2019, a 12-month CD had a national average rate of 0.66% and a cap at 1.141%.[4] On

2 Core deposits are distinct from brokered deposits in that they are considered "stable," including checking, savings, and CD accounts made by individuals rather than a deposit broker.

3 FIL-42-2016, Identifying, Accepting and Reporting Brokered Deposits: Frequently Asked Questions (Updated June 30, 2016; Revised July 14, 2016).

4 https://www.fdic.gov/regulations/resources/rates/

April 2019
Volume 23, Number 11

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April 22, 2019, the Treasury yield was at 2.46%.[5]

So, the current rules require financial institutions to identify deposits that are brokered, mind the rate cap limitations, and consider liquidity rating implications, in anticipation of regulatory examination. As technologies continue to evolve, and the financial industry follows those trends, the brokered deposit regulations designed before the age of online banking are outdated. For example, such broad coverage means banks seeking deposits through the internet could be subject to rate caps.

Significance of FDIC's ANPR

The ANPR is an opportunity to comment and guide FDIC's future approach to brokered deposits. Issues to comment on include:

1. Clarify the definition of brokered deposit and deposit broker for the modern era of technology.
2. Create a methodology to calculate a rate cap that appropriately reflects the cost of deposits.
3. Provide examples of what brokered deposits mean to your institution with today's modern technologies (ex: internet deposits such as online, mobile banking, and social media).
4. Refocus of policy goals: original intent was to restrict large volumes of volatile funds. Brokered deposits were suspect of this category of deposit, but did not, and do not, necessarily continue to merit fierce restrictions.
5. Reconsider limitations on brokered deposit offerings for well-capitalized institutions.

FDIC's ANPR means a potential to modernize and even narrow the designation of a deposit as brokered, given the current wide scope of interpretation, stigmatization, limitation, and regulatory burden over a broad categorization of deposits. An update to Section 29 could mean new opportunities for banks to seek funding from new sources and explore new technological applications to deposits.

Conclusion

In 2019, many consumers bank from their phone. Various internet technologies give access to funds quickly, and new technologies are surely on the horizon. As businesses, banks need to accommodate these technologies in order to stay competitive. The ANPR is an opportunity to explore how brokered deposits are treated and can be better utilized. Comments can direct FDIC's regulatory framework to enhance the functionality of brokered deposits as another deposit tool.

Comments on the ANPR are due May 7, 2019. After the ANPR, FDIC will issue a proposed rule, with another opportunity for comment prior to a final rule. The ANPR can be found here: https://www.fdic.gov/news/board/2018/2018-12-18-notice-sum-i-fr.pdf ■

5 https://www.macrotrends.net/2492/1-year-treasury-rate-yield-chart

Regulatory Spotlight

Agencies Issue Interim Final Rule on Margin and Capital Requirements for Covered Swap Entities.

The Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the Federal Housing Finance Agency (FHFA), and the Farm Credit Administration (FCA) are adopting and invite comment on an interim final rule amending the Agencies' regulations that require swap dealers and security-based swap dealers under the Agencies' respective jurisdictions to exchange margin with their counterparties for swaps that are not centrally cleared (Swap Margin Rule). The Swap Margin Rule takes effect under a phased compliance schedule stretching from 2016 through 2020, and the dealers covered by the rule continue to hold swaps in their portfolios that were entered into before the effective dates of the rule. Those swaps are grandfathered from the Swap Margin Rule's requirements until they expire according to their terms. There are currently financial services firms located within the United Kingdom (U.K.) that conduct swap dealing activities subject to the Swap Margin Rule. The U.K. has provided formal notice of its intention to withdraw from the European Union (E.U.) on 03/29/2019. If this transpires without a negotiated agreement between the U.K. and E.U., these entities located in the U.K. may not be authorized to provide full-scope financial services to swap counterparties located in the E.U. The Agencies' policy objective in developing the interim final rule is to address one aspect of the scenario likely to ensue, whereby entities located in the U.K. might transfer their existing swap portfolios that face counterparties located in the E.U. over to an affiliate or other related establishment located within the E.U. or the United States. The Agencies seek to address industry concerns about the status of grandfathered swaps in this scenario, so the industry can focus on making preparations for swap transfers. These transfers, if carried out in accordance with the conditions of the interim final rule, will not trigger the application of the Swap Margin Rule to grandfathered swaps that were entered into before the compliance dates of the Swap Margin Rule. The interim final rule is effective **03/19/2019**, comments are due **04/18/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-03-19/pdf/2019-05012.pdf. *Federal Register*, Vol. 84, No. 53, 03/19/2019, 9940-9950.

Wisconsin Bankers ASSOCIATION

May 2019

Compliance Journal

Special Focus

Who Must Sign The Mortgage?

When originating a mortgage loan, banks often find themselves asking "who needs to sign the mortgage". It's a great question and the trite, lawyerly answer, is "it depends"! Given the fact that Wisconsin is a community property state and has a marital property act which includes homestead protections, the answer is not necessarily easy.

There are, of course, certain straightforward scenarios that follow the "General Rule". The General Rule is this: only those parties in title to the property securing the loan are required to sign the mortgage. Of course, there is an exception to the General Rule – when you have a *married* person(s) in title to the property securing the loan, the spouse of the titled individual *may* be required to sign the mortgage.

The following hypotheticals demonstrate application of the General Rule.

1. Mom and Daughter, both unmarried individuals, are borrowers on a loan. The loan will be secured by Mom's home, for which Mom is the sole titleholder. Though Mom and Daughter are both borrowers, only Mom must sign the mortgage as the sole titleholder.

2. Same facts as (1) above, except both Mom and Grandma are in title to the property. Grandma is unmarried. In this case, though Mom and Daughter are borrowers, Mom and Grandma must sign the mortgage because they are both titleholders.

3. Son and Son's Wife are borrowers on the loan and Dad is a Guarantor. The loan will be secured by a home in which Son and Son's wife permanently reside, but Dad and Uncle are the titleholders. Dad and Uncle are both unmarried. In this case, Dad and Uncle must sign the mortgage. Son and Son's Wife are not required to sign the mortgage despite the fact that they are married and the property is their permanent residence – in this case, neither spouse is in title to the property and thus no exceptions to the General Rule apply, as described in further detail below.

Of course, every good rule has exceptions. In this case, the exception to the General Rule is as follows: If a *married* person is in title to the property securing the loan, the spouse of that individual will also be required to sign the mortgage if the conveyance alienates either or both spouses' homestead interest, even if the spouse is not in title. *See* Wis. Stats §706.02(1)(f). This requirement to obtain the spouse's signature (the "exception"), however, does not apply to purchase money mortgages. *See* Wis. Stats §706.02(1)(f). In other words, if the mortgage is a purchase money mortgage, you're back to the General Rule and the spouse of the married titleholder will not be required to sign the mortgage if the spouse is not going to be listed as an owner of the property, even if the property is homestead property or either or both spouses.

Thus, assuming the bank is not originating a purchase money mortgage, the bank must require signatures of all titleholders PLUS the spouse of a married titleholder if the property is the homestead property of either or both spouses.

Banks should note that a "homestead" is defined under Wis. Stats. § 706.01(7) as "the dwelling, and so much of the land surrounding it as is reasonably necessary for use of the dwelling as a home, but not less than one-fourth acre, if available, and not exceeding 40 acres." Customers should indicate to the Bank whether the property is homestead property and such information should be contained on the mortgage itself.

If the bank does not obtain the signature of the married titleholder and the spouse of the titleholder, the mortgage is void and unenforceable. This interpretation of Wis. Stats. § 706.02(1) and (1)(f) was recently confirmed in a 2017 court case – *U.S. Bank National Association v. Charles E. Stehno III*, 2017 WI App. 57 (August 30, 2017). In *Stehno*, the Bank attempted to foreclose on mortgages signed by Charles Stehno in December 2002 and April 2003. The property was Stehno's homestead at the time he signed the mortgages. However, the mortgages were not signed by his then-spouse, Candice Wells. Therefore, according to the court, the mortgages were invalid from the start against both spouses because only Stehno signed them.

The following hypotheticals demonstrate application of the Exception to the General Rule:

1. Husband and Wife are refinancing their homestead property. They are both listed as borrowers on the loan. Husband is the sole titleholder on the property. Both Husband and Wife must sign the mortgage because it's conveying an interest in the homestead property of both spouses on a non-purchase money loan.

Special Focus

2. Daughter and Daughter's Husband are borrowers on second mortgage loan. The property securing the loan is titled in Dad's name only and it's Dad's homestead property. Dad is married to Stepmom who does not live in the property. Both Dad and Stepmom must sign the mortgage because this is a non-purchase money loan which conveys the homestead interest of one spouse.

3. Daughter and Son are refinancing their parents' homestead property and are borrowers on the loan. Dad is married to Mom and the property securing the loan is both Dad's and Mom's homestead. Dad and Grandma are in title to the property. Grandma is unmarried. Dad, Mom, and Grandma must sign the Mortgage. Dad and Grandma must sign because they are titleholders. Mom must sign because this is a non-purchase money loan which conveys the homestead interest of Mom and Dad.

4. Husband and Wife are looking to originate a purchase money mortgage loan for which they will both be borrowers. The loan will be secured by property held by husband only. Husband only will live in the property as his homestead. In this case, only husband must sign the mortgage because this is a purchase money loan and, therefore, the Exception to the General Rule does not apply.

In summary, taken altogether, the signatures needed on a mortgage are as follows: (1) All titleholders and (2) if the loan is not secured by a purchase money mortgage, the spouse of any married titleholder to the extent the property is the homestead of one or both spouses.

Finally, it's best to obtain a title insurance policy that lists the owners of the property being mortgaged. Title insurance companies will also list the names of all individuals required to sign the mortgage so banks may have additional comfort that the correct individuals are signing the mortgage.

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

Learn more about the Wisconsin Marital Property Act at the June session of the WBA Compliance Forum. ■

Regulatory Spotlight

Agencies Propose Revisions to the Supplementary Leverage Ratio To Exclude Certain Central Bank Deposits of Banking Organizations Predominantly Engaged in Custody, Safekeeping and Asset Servicing Activities.

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 proposal to implement section 402 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. Section 402 directs these agencies to amend the supplementary leverage ratio of the regulatory capital rule to exclude certain funds of banking organizations deposited with central banks if the banking organization is predominantly engaged in custody, safekeeping, and asset servicing activities. Comments are due **07/01/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-04-30/pdf/2019-08448.pdf. *Federal Register*, Vol. 84, No. 83, 04/30/2019, 18175-18186.

Agencies Request Comment on Information Collections.

- 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 Consolidated Reports of Condition and Income for a Bank with Domestic and Foreign Offices. The Agencies also gave notice that they sent the collection to OMB for review. Comments are due **06/18/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-04-19/pdf/2019-07841.pdf. *Federal Register*, Vol. 84, No. 76, 04/19/2019, 16560-16567.

- The Board of Governors of the Federal Reserve System

May 2019
Volume 23, Number 12

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Subscription Rate:
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Wisconsin Bankers ASSOCIATION

June 2019

Compliance Journal

Special Focus

Wisconsin Consumer Act FAQs

The Wisconsin Consumer Act (WCA) continues to be a frequent topic for the WBA legal call program. We have compiled some of the most frequently asked WCA questions and present them in the article below. Note that this article is not, nor intended to be, a recital of all applicable State and Federal laws and regulations for specific transactions.

What transactions does the WCA cover?

The WCA applies to loans and credit sales to individuals for personal, family, or household purpose when the amount financed is $25,000 or less and the loan is not secured by a first lien real estate mortgage or equivalent security interest.

Note the exception for an "equivalent security interest," sometimes referred to as a "1st lien equivalent." The concept of a "1st lien equivalent" is unique to Wisconsin. For example, Bank A takes a 1st lien mortgage on a purchase. The customer returns to Bank A for a line of credit, and Bank A secures the line with another lien on the same property. If there is no intervening creditor, that additional lien is effectively a 1st lien equivalent. On the other hand, if that customer comes back to Bank A for a line of credit, and at that time there is an intervening creditor who has taken a lien on the same property sometime after Bank A took the 1st lien on the purchase, Bank A's new lien for the line of credit would be "true junior mortgage" rather than a 1st lien equivalent.

Does the WCA give the ability to prepay?

Yes. The WCA provides the consumer the right to prepayment in full or part at any time without penalty.

Are deferral fees permitted by the WCA?

Not for simple-interest transactions. Under the WCA deferral fees are permitted for precomputed transactions but they are not permitted for simple-interest transactions.

Does the WCA impose maximum rates of finance charges?

No. The creditor and customer may agree to a maximum finance charge per the terms of the contract. However, the rate may not be unconscionable.

Does the WCA restrict how interest is calculated?

No. However, if the 1/360th method is utilized, it must be disclosed conspicuously.

Does the WCA restrict rates after default?

Yes. The interest rate after the final scheduled maturity date may not exceed the greater of 12% per year or the annual rate of finance charge assessed on the transaction.

Does the WCA require a right to cure default?

Yes. The WCA prohibits a bank from taking any action with respect to default until notice requirements have been met. The notice must be given to the customer, and inform them how to cure the default.

Does the WCA have requirements for delinquency charges?

Yes. For closed-end transactions, late charges are restricted to the lesser of $10 or 5% of the unpaid amount of the installment.

The Wisconsin Department of Financial Institutions has explained that an installment is considered current when a payment is made on its due date or within the 10 days following its due date, creating a grace period.

If an installment is received on or before its scheduled or deferred due date, no delinquency charge may be assessed for that payment even though an earlier installment or delinquency charge has not been paid in full.

A delinquency charge may be collected only once on any installment.

When assessing late charges, the WCA requires payments be applied first to current installments and then to delinquent installments.

Finally, if interest is charged after the final scheduled maturity date, no delinquency charge may be assessed on the final scheduled payment.

For open-end credit, there is no limit on the amount nor a grace period, but the charge must still be agreed to by contract.

What are some of the requirements for variable rate loans under the WCA?

There are two types of variable rate transactions under the WCA: approved index loans and non-approved index loans.

For approved index loans:

- Adjustments in rate are based upon changes in an approved index (e.g. Wall Street Journal Prime).
- Index approved by the Secretary of WDFI.
- Index must be beyond control of creditor.
- Index must be verifiable by consumer.
- Limitations on decreases allowed only if similar limitations placed on increases.
- No carry-over provision.

For non-approved index loans:

- Index is set by the creditor and is not tied to an approved index.
- Additional limitations and disclosure requirements, including:
    - May not increase rate during first 3 months following consummation of transaction.
    - Rate increases may not exceed 2% per year.

Are there subsequent notice requirements for variable rate closed-end loans under the WCA?

Yes. A creditor must mail or deliver a written notice of every rate change at least 15 days prior to the change in rate if implemented by a change in periodic payment, other than the final payment. The notice must be given no later than 30 days after any other change.

Notice is not required, however, for closed-end loans if the rate change is based on an approved index and there is no change in the periodic payment (other than the final payment).

Are there subsequent notice requirements for variable rate open-end loans under the WCA?

No notice is required if the adjustment is made in a variable rate transaction pursuant to an open-end credit plan that is based upon changes in an approved index.

Does the WCA require any notices to customers, co-signers, and guarantors?

Yes. The creditor must furnish the customer with an exact copy of each instrument, document, agreement and contract signed by the customer and which evidences the customer's obligation before any payment is due to the creditor. The creditor must also provide the customer with copies of every writing evidencing the customer's obligation to pay upon request of the customer. One such copy must be furnished at no charge to the customer. Subsequent copies must also be furnished, but the creditor may charge a reasonable fee for production and delivery.

Each person signing the guaranty or as co-signer in addition to signing the guaranty or note must receive either: copies of each instrument, document, agreement, and contract signed by the customer and which evidences the customer's obligation, or an explanation of personal obligation. A sample notice appears in the WCA and is reproduced on the WBA 156 or 156A (for open-end credit) Explanation of Personal Obligation forms.

In connection with open-end credit, if any subsequent change would increase or extend contingent liability of the guarantor or co-signer, an explanation of change must be provided conspicuously disclosing that if such person wishes to terminate liability with respect to future transactions, that person must notify the creditor in writing.

Conclusion

While this article is not comprehensive in its consideration of all WCA issues, WBA hopes it will serve as a helpful guide to some of the more common questions we receive. For a full understanding of the applicable rules WBA recommends consulting Chapters 421 through 427 of the Wisconsin Statutes for the full scope of the WCA. ■

June 2019
Volume 24, Number 1

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Wisconsin Bankers ASSOCIATION

July 2019

Compliance Journal

Special Focus

Regulation CC Dollar Amount Adjustment Rule Finalized

On July 3, 2019, the Board of Governors of the Federal Reserve System (FRB) and the Bureau of Consumer Financial Protection (CFPB) published a jointly issued final rule (rule) amending Regulation CC that implements a requirement to periodically adjust dollar amounts under the Expedited Funds Availability Act (EFA Act). This requirement stems from a Dodd-Frank Act amendment to the EFA Act a number of years ago.

The rule also extends Regulation CC's coverage to American Samoa, the Commonwealth of the Northern Mariana Islands, and Guam, and makes certain other technical amendments. This article will only focus on the dollar amount adjustment provisions of the rule.

Specified Dollar Amounts Subject to Adjustment

Subpart B of Regulation CC implements the requirements set forth in the EFA Act regarding the availability schedules within which institutions must make funds available for withdrawal, exceptions to those schedules, disclosure of funds availability policies, and payment of interest.

The EFA Act and subpart B of Regulation CC contain the following specified dollar amounts concerning funds availability which are subject to adjustment: (1) The minimum amount of deposited funds that institutions must make available for withdrawal by opening of business on the next day for certain check deposits ("minimum amount") under 229.10(c)(1)(vii); (2) the amount an institution must make available when using the EFA Act's permissive adjustment to the funds availability rules for withdrawals by cash or other means ("cash withdrawal amount") under 229.12(d); (3) the amount of funds deposited by certain checks in a new account that are subject to next-day availability ("new account amount") under 229.13(a); (4) the threshold for using an exception to the funds availability schedules if the aggregate amount of checks on any one banking day exceed the threshold amount ("large deposit threshold") under 229.13(b); (5) the threshold for determining whether an account has been repeatedly overdrawn ("repeatedly overdrawn threshold") under 229.13(d); and (6) the civil liability amounts for failing to comply with the EFA Act's requirements under 229.21(a).

Frequency of Adjustments; Initial and Subsequent Adjustment Dates

The rule specifies that amounts for the six enumerated categories listed above must be adjusted every five years in accordance with a calculation set forth in the rule, with the first adjustment taking effect on July 1, 2020. Thus, each subsequent adjustment following July 1, 2020 will take effect every fifth July 1, (e.g. July 1, 2025; July 1, 2030, etc.).

Calculation Methodology of the Adjustment Amount

The adjustment amount will be calculated across an "inflation measurement period" (defined in the regulation) by the aggregate percentage change in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W), rounded to one decimal, and then multiplied by the applicable existing dollar amount, the result of which being rounded to the nearest multiple of $25. However, no dollar amount adjustment will be made if the aggregate percentage change is zero or is negative, or when the aggregate percentage change multiplied by the applicable existing dollar amount and rounded to the nearest multiple of $25 results in no change.

When there is an aggregate negative percentage change over an inflation measurement period, or when an aggregate positive percentage change over an inflation measurement period multiplied by the applicable existing dollar amount and rounded to the nearest multiple of $25 results in no change, the aggregate percentage change over the inflation measurement period will be included in the calculation to determine the percentage change at the end of the subsequent inflation measurement period. That is, the cumulative change in the CPI–W over the two (or more) inflation measurement periods will be used in the calculation until the cumulative change results in publication of an adjusted dollar amount in the regulation.

Adjustments will likely be published in the *Federal Register* at least one year in advance of their effective date. The Agencies stated they anticipate publishing in the first half of 2024 the adjustment amounts that will take effect on July 1, 2025.

Initial Adjustment Amounts

The following is a list of current dollar amounts that apply prior to July 1, 2020, and the set of first adjustment amounts that will take effect on July 1, 2020.

1. For purposes of the minimum amount under § 229.10(c)(1)(vii), the dollar amount in effect prior to July 1, 2020 is $200; effective July 1, 2020, the amount will be $225;

2. For purposes of the cash withdrawal amount under § 229.12(d), the dollar amount in effect prior to July 1, 2020, the amount is $400; effective July 1, 2020, the amount will be $450;

3. For purposes of the new account amount, large deposit threshold, and the repeatedly overdrawn threshold under §S 229.13(a), (b), and (d) respectively, the dollar amount in effect prior to July 1, 2020, the amount is $5,000; effective July 1, 2020, the amount will be $5,525; and

4. For purposes of the civil liability amounts under § 229.21(a), the dollar amounts in effect prior to July 1, 2020, are $100, $1,000, and $500,000 respectively; effective July 1, 2020, the amounts will be $100, $1,100, and $552,500 respectively.

Updating Disclosures & Notices

Institutions will need to update funds availability policies, disclosures, and notices (including change-in-terms notices for existing accounts) that will be provided on and after the applicable effective date to reflect the appropriate adjusted amount(s). It should be noted that rule has not changed the timing or content requirements for such policies, disclosures, and notices.

Revised and New Commentary Examples in the Regulation

The rule has revised and added certain examples in the commentary to reflect the July 1, 2020 adjustment amounts, and to address the new adjustment amount calculation methodology. However, the rule neither addresses nor modifies model hold notice verbiage or format, as a separate rulemaking is underway for that purpose.

Conclusion

Fortunately, the rule provides a substantial period of time before the first set of adjusted amounts is effective on July 1, 2020. Institutions should read the rule and begin reviewing their funds availability policies, disclosures, and notices to identify needed changes, and devise an implementation strategy for accounts opened prior to July 1, 2020, and those opened on or after that date. In addition, the plan should address procedures for future adjustments. The final rule may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-07-03/pdf/2019-13668.pdf ■

July 2019
Volume 24, Number 2

Wisconsin Bankers Association
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Wisconsin Bankers ASSOCIATION

August 2019

Compliance Journal

Special Focus

No Big Wins, No Big Losses in This Legislative Session

On July 3, 2019, Governor Tony Evers signed the State 2019-2021 Budget Bill (budget) into law after 78 line-item vetoes. WBA has been tracking the budget since it was introduced earlier this year and now offers this report on some of its more prominent features.

Budget Summary

The budget was presented to Governor Evers on June 28, 2019 and approved with partial veto on July 3, 2019. This version of the budget was just the final stop on a long process that began in the fall of 2018 when state agencies began to formulate their budget requests. The Executive Budget, the budget recommendations provided initially by the governor, was released in February and then Republicans in charge of the Joint Committee on Finance began to pick it apart. Deal-making throughout the summer between Governor Evers and the Legislature got a budget bill to the governor's desk, which became 2019 Wisconsin Act 9 after the governor's partial vetoes and signature. Considering this is the first time since the 2007-2009 budget that such a bill was passed under split government, the process went surprisingly smoothly.

WBA's advocacy team campaigned for the interests of our members and reported on many key issues leading up to the passing of the budget as a way to keep members informed, as well as generate media and public support (in some cases). This long process saw many versions of the budget as different provisions were added and removed. Ultimately, Evers's initial 1,100-page Executive Budget was whittled down to 500 pages by the Legislature. This article presents the results of the WBA's efforts in the final budget.

Highlights

The budget contains no major legislative victories, but also no major losses. While not exciting news, it demonstrates the importance of advocacy for our industry in the coming years. The WBA advocacy team worked hard and long hours on defense to achieve this "neutral" result by preventing many negative items from being added to the budget.

Highlights include provisions from the Tax Cut and Jobs Act (TCJA) proposed to conform Wisconsin's tax code to the Internal Revenue Code. Those changes, which were ultimately removed from the final budget, would have increased taxation on Wisconsin business by over $362,000,000.* In addition to what was deleted from the final budget, a $500 million income tax cut was ultimately passed.

Select items that WBA followed closely and lobbied on are included in the table below. The table describes the provision, its ultimate outcome in the final budget, and the net impact this has on banking.

Provision	Description	Outcome	Impact on Banking
Updating References to the Internal Revenue Code for Corporate Income and Franchise Taxes	$12M tax on the banking industry by incorporating federal changes to Federal Deposit Insurance Corporation premium deductibility for banks with asset sizes from $10B to $50B	REMOVED	POSITIVE
Tax Credit Changes	Several tax credit changes were proposed	REMOVED	NEUTRAL

Provision	Description	Outcome	Impact on Banking
Gas Tax	Proposed 8 cents per gallon gas tax	Replaced by $10 increase in registration fees	NEUTRAL
Loss Limitation Provision for Taxpayers Other Than Corporations	Proposed excess business loss limitation (a $166M increase). Meaning, those business losses by which the total deductions attributable to business exceed total gross income plus $250,000. Affects business gains and loss reporting.	REMOVED	POSITIVE
Limitation on the Deduction for Business Interest ($156 million increase)	This provision would apply to all who have business interest expenses. Taxpayers may generally deduct interest expense paid over a taxable year. However, this limitation restricts the amount of deductible business interest expense to not exceed: 1) The taxpayer's business interest income for the year; 2) 30% of the taxpayer's adjusted taxable income for the year; and 3) The taxpayer's floor plan financing interest expense for the year	REMOVED	POSITIVE
Accounting Rules for Accrual Method Taxpayers ($20M increase)	Certain converting S corporations required to change from the overall cash method to an overall accrual method of accounting (as a result of revocation of S corporation election)	REMOVED	POSITIVE
Limitation on the Deduction of FDIC Premiums	For banks with assets greater than $10B, phases out FDIC premium deduction ($12M increase)	REMOVED	POSITIVE
Limitation on the Deduction for Highly Paid Individuals	Proposed modification to limit the deduction that can be taken with respect to compensation for "covered employees" to $1M per year. "Covered employees" are those who: 1) served as principal executive officer; 2) were in the top three highest-paid officers for the year; 3) were a covered employee during a prior tax year beginning in 2016	REMOVED	NEUTRAL
Limitation on the Deduction for Entertainment, Amusement, and Recreation Expenses	Proposal to eliminate the deduction for any expense related to activities generally considered entertainment, amusement, or recreation	REMOVED	POSITIVE
Amortization of Research and Experimental Expenditures	Proposal to require specific research and experiment expenditures to be capitalized and amortized over a five-year period	REMOVED	POSITIVE
Wisconsin Economic Development Corporation (WEDC) Changes	14 different changes to WEDC	REMOVED	NEUTRAL

Provision	Description	Outcome	Impact on Banking
Increase and Subsequent Indexing of Minimum Wage	Increase of statutory minimum wage by $1.00 beginning Jan. 1, 2020, to increase $0.75 each subsequent year for three years	REMOVED	POSITIVE
Family and Medical Leave Act (FMLA) Expansion	Expanded coverage of FMLA in terms of applicability, permitted use, and qualifications	REMOVED	NEUTRAL
Increased Concentrated Animal Feeding Operations (CAFO) Fees	Increased annual fee assessed to operators of CAFOs and added an application and renewal fee for the operation of a CAFO	REMOVED	NEUTRAL
Legalization of Medicinal Marijuana	Funding to establish a medical marijuana program	REMOVED	NEUTRAL
Codifying Obamacare Into State Statute	Accepts the federal Affordable Care Act's provision for Medicaid	REMOVED	NEUTRAL
Property Taxes Increase	Proposal to increase property taxes by a minimum of 2% per year	REMOVED	POSITIVE
Repeal of State Pre-Emption of Certain Employment Local Ordinances	Repeal prohibition on local governments enacting ordinances regarding: 1) Minimum family and medical leave requirements; 2) Wage claims and collections; 3) Employee hours and overtime; 4) Required employment benefits; and 5) Solicitation of a prospective employee's salary history	REMOVED	NEGATIVE
Creation of a Tax-Advantaged First-Time Homebuyer Savings Account	Proposal to create savings accounts that permit certain contributions as exempt from state taxation	REMOVED	NEGATIVE
Historic Rehabilitation Tax Credit Changes	Proposals to apply awards under the rehabilitation credit program on a per project basis rather than a per parcel basis and repeal the state's supplement (given the repeal at the federal level)	REMOVED	POSITIVE
Repeal of Net Operating Loss Carryback	Proposed repeal of state net operating loss carryback provisions to parallel the federal repeal	REMOVED	NEGATIVE
Amend Calculation of Low-Income Housing Tax Credit	Proposal to add back low-income housing credits to taxable income of the entity claiming the credit	REMOVED	NEUTRAL
Limit Capital Gains Exclusion	Proposal to eliminate the long-term capital gains exclusion for filers above certain income levels	REMOVED	NEUTRAL

Provision	Description	Outcome	Impact on Banking
Real Estate Transfer Fee Exemption	Exemption for transfers from a subsidiary corporation to its parent corporation does not apply in cases where a non-corporate entity owns a majority of shares in the corporation. Specifies that the exemption does not apply to conveyances between different owners	REMOVED	POSITIVE
Student Loan Refinancing Study	Creation of an advisory group to study the development of an authority for the refinancing of student loans	REMOVED	NEUTRAL
Dark Store Legislation	Reforms to assessment practices to clarify the assessment of leased property to specify that real property be assessed for property tax purposes at its highest and best use and that real property includes leases, rights and privileges pertaining to the property	REMOVED	NEUTRAL
Undocumented Immigrant Driver's License Creation	Extension of eligibility to receive driver's licenses and identification cards for undocumented individuals if they comply with the driver knowledge and skills requirement	REMOVED	NEUTRAL
Bonding for New Water Lines	Clean water fund program expanded to include bonding for safe drinking water loan program	PASSED	NEUTRAL
DATCP Industrial Hemp Program	Funding for three additional agency positions	PASSED	POSITIVE
Wisconsin Forestry Practice Study	Funding for the implementation of recommendations made in the Wisconsin Forestry Practices Study	PASSED	NEUTRAL

Conclusion

The budget process was surprisingly tame this year. Although the banking industry did not gain anything major, it also did not suffer any major loss. WBA was on the front line throughout the process, working to ensure the voice of Wisconsin's banks was heard by decision-makers, even on topics that would only indirectly affect banks. Regardless of its impact on Wisconsin's banks, the state budget is an important process that provides insight into what the governor and the Wisconsin Legislature currently consider important.

For more information on WBA's Advocacy efforts contact Mike Semmann at msemmann@wisbank.com.

**All figures derived from the Wisconsin Legislative Fiscal Bureau.* ■

Wisconsin Bankers ASSOCIATION

September 2019

Compliance Journal

Special Focus

Welcome Back, Old Friend – Section 8 of RESPA is a Hot Topic Again

Section 8 of the Real Estate Settlement Procedures Act (RESPA)[1] – the prohibition against kickbacks and unearned fees – is back and compliance officers are taking note. In the last year, we have seen a significant increase in RESPA section 8 questions, many of which involve a determination as to whether certain marketing activities are permissible. This is due, in part, to evolving technology which provides a platform to facilitate marketing relationships between settlement service providers, along with recent regulatory and case law developments. Some of these arrangements are simple, while others extraordinarily complex. Either way, I sense bit of panic from compliance officers any time there's a new opportunity to market the institution's mortgage area that may implicate RESPA (and for good reasons – penalties and reputation to name a couple!). Not all these arrangements are problematic, especially in light of the recent PHH decision and developments out of the Consumer Financial Protection Bureau (CFPB), but some arrangements should still make your ears perk up.

So, how do we analyze whether a marketing opportunity presents a RESPA Section 8 issue? Let's discuss.

When we consider marketing activities under RESPA, there are two primary provisions of RESPA Section 8 that are relevant to our analysis: (1) Section 8(a) which delineates prohibited activity,[2] and (2) Section 8(c) which prescribes permissible activities.

Sections 8(a)– Prohibited Activity

The first is Section 8(a) of RESPA which prohibits illegal kickbacks – the giving or receiving of a "thing of value" for referrals made between settlement service providers. Specifically, Section 8(a) prohibits any person from giving or accepting any fee, kickback, or thing of value pursuant to an agreement or understanding for the referral of a settlement service involving a federally related mortgage loan (a.k.a. consumer mortgage loans).[3] There are three elements to an illegal kickback under Section 8(a):

1. A "thing of value" – for example, money, defrayed costs, special contract terms, a promise to provide future referrals, and things (such as sporting event tickets or office supplies);

2. An "agreement or understanding", whether oral, written, or established by practice; and

3. A "referral", which is defined in two ways: (a) oral or written action that has the effect of affirmatively influencing selection of a settlement service provider, or (b) when a person is required to use a particular settlement service provider.

All of these components must be present to be considered a prohibited activity under RESPA. Thus, when a potential RESPA-implicating opportunity presents itself, each of these components must be analyzed in detail.

Section 8(c) of RESPA – Permissible Activity

Notwithstanding the prohibitions in Sections 8(a), the second relevant provision, contained in Section 8(c) of RESPA, sets forth *permissible* activity. Relevant here, RESPA specifically permits the following:

1 12 U.S.C. § 2607. Implementing Regulation X is codified at 12 C.F.R. § 1024.14.

2 Note that section 8(b) prohibits the giving or accepting of a "portion, split, or percentage of any charge made or received" for rendering settlement services other than for services actually performed. In other words, institutions cannot share a portion of or split fees with other settlement service providers when rendering settlement services unless the payment given/received is for "services actually performed". Though a very important component of RESPA to understand, this provision is not often relevant in the marketing context.

3 12 U.S.C. § 2607(a) and 12 C.F.R. § 1024.14(b).

- "normal promotional or educational activities that are not conditioned on the referral of business and that do not involve the defraying of expenses that otherwise would be incurred…";[4] and

- "payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or for services actually performed." [5]

These permissible activity exceptions are generally relied upon in order to create relationships between settlement services providers (e.g. the institution and a realtor).

Importantly, there are some general principles that have developed over time, via administrative interpretations, case law, and enforcement actions that must be true in order for the marketing activity to be permissible pursuant to one of these exceptions:

- Services must *actually* be performed or goods must *actually* be provided. For example, advertising must actually be provided. Any payment for advertising that does not actually occur will be considered an unlawful kickback.

- The payment for such services or goods must be bona fide. That is, payment must be reasonable market value. Any excess payment above reasonable market value will be seen as an illegal kickback.[6]

Now, assuming the marketing activity meets the parameters of one of the Section 8(c) exceptions, the activity receives a "safe harbor" from a RESPA Section 8 violation. Note, however, that the "safe harbor" rule was not the prevailing opinion of the CFPB under the reign of Director Richard Cordray, which was a significant departure from previous, longstanding interpretations of RESPA under the Department of Housing and Urban Development (HUD). However, in perhaps one of the most contentions of RESPA cases in recent history, *PHH Corporation v. Consumer Financial Protection Bureau*,[7] the Court of Appeals for the D.C. Circuit confirmed that Section 8(c) of RESPA provides a safe harbor so long as the activity meets the parameters of the Section 8(c) exceptions.

Analysis When Considering Marketing Opportunities

With that RESPA background in mind, if your institution is considering a marketing opportunity involving federally related mortgage loans, I suggest engaging in the following analysis:

(1) Might this be deemed a prohibited activity under RESPA Section 8(a) or 8(b)?

   a. That is, could this be considered an illegal kickback under Section 8(a) in that all three elements are present, as described above and restated here:
      i. A "thing of value";
      ii. An "agreement or understanding"; and
      iii. A "referral"

   b. Or, is this impermissible fee splitting under 8(b)?
      i. Though not often arising in the marketing context and, consequently, not thoroughly discussed herein, the institution should consider applicability

   If NO, that's the end of your analysis – no Section 8 concern
   If MAYBE or YES, continue to (2) and (3).

4 12 C.F.R. § 1024.14(g)(1)(vi).
5 12 C.F.R. § 1024.14(g)(1)(iv).
6 See PHH Corporation v. Consumer Financial Protection Bureau, 839 F.3d 1 at 41 (D.C. Cir. 2016).
7 839 F.3d 1 (D.C. Cir. 2016). The court's interpretation of RESPA was upheld by a petition for rehearing en banc by the D.C. Circuit Court of Appeals. PHH, No. 15-1177 (Jan. 31, 2018).

September 2019
Volume 25, Number 4

Wisconsin Bankers Association
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(2) Is the activity "saved" by the Section 8(c) educational and marketing exception; or

(3) Is the activity "saved" by the Section 8(c) "bona fide payment for services actually performed" exception?

Let's take a couple of common marketing opportunities and run through the analysis:

Hosting a Complementary Educational Seminar for Settlement Service Providers

If an institution chooses to host a complementary educational seminar for real estate professionals, such an event may be considered to violate Section 8(a) of RESPA because it's certainly the provision of a "thing of value" provided in hopes of generating business (or, in other words, referrals from those settlement service providers). In fact, previous HUD Guidance states that such educational events implicitly positions settlement service providers to refer business to the institution. We can question whether there is an "agreement or understanding", but let's just assume that the conduct is indicative of such. The question then becomes whether this can be redeemed by the "normal promotional and marketing" exception under 8(c).

Whether an educational seminar meets the safe harbor exception is very much dependent upon the facts and circumstances at hand. Consider the following:

- Is the event in any way conditioned on past, present, or future referrals of business? For example, does the institution provide an incentive for attendees to refer business back to the institution? Or, does the institution only invite settlement service providers that have previously referred business to the institution? If so, the safe harbor is unlikely to be met.
    - *Note that who is invited can make a difference here. The more "open" the attendance list (e.g. not just settlement services providers located near your branches or those who have previously referred business your way), the more likely the seminar is to pass muster.*
- Does the seminar defray costs of the attendees? For example, if the seminar provides a course required to receive or maintain licensure, that would be defraying a cost ordinarily incurred and would be, consequently, unlawful.

The most challenging aspect here is to remain referral-neutral. Pay careful to this component in your analysis.

Advertising with a Realtor

Recently, a number of institutions have been given the opportunity to advertise their services on a realtor's website or jointly advertise with a realtor on a separate platform (e.g. Zillow). I think we could all agree that this is prohibited activity under Section 8(a). Thus, we turn to whether it can be saved under either of the relevant Section 8(c) exceptions delineated above.

Of course, facts matter here. The following should be considered:

- Is the advertising conditioned on past, present, or future referrals of business? For example, if the institution and the realtor enter into a contractual arrangement for direct advertising, does the agreement discuss future business or incentives for referrals? Pay close attention to contract language, if a contract exists, and remain referral-neutral in order to meet the exception.
- Is the institution paying for the advertising? If the advertising is free, this will not meet the exception as the institution's costs will be defrayed.
- Is the institution paying reasonable market value for the advertising? Assuming the institution is paying for the advertising, is the institution paying reasonable market value? Remember, any payment above reasonable market value will be seen as an illegal kickback.

One of the challenges with meeting these relevant Section 8(c) exceptions is to get the fee structure exactly right. If the institution is obtaining free advertising or is receiving "below market rate" advertising, you run the risk of receiving "defrayed costs" or not making a bona fide payment for the advertising. In contrast, if you pay above market rate, the portion of the payment above market rate kicks you back into prohibited activity under Section 8(a). To this end, we always suggest drafting a business justification to demonstrate that the fee paid is fair market value and maintaining it in your files. To determine market value, we suggest considering the following:

a. Look internally for evidence of similar transactions (e.g. is the price similar to the institution's other advertising costs for the type of media, duration, etc.);

b. Look externally to determine if the price is consistent with the price third parties would incur for similar services (e.g. other financial institutions in the area); and

c. Management should exercise its best judgment based on the internal and external evidence.

Furthermore, you should be especially careful when navigating joint marketing arrangements when a third party is involved. For example, Zillow offers lenders and real estate agents the opportunity to jointly advertise via the Zillow online platform. In this program, Agent invites up to five lenders to jointly market with Agent. Lender then pays Zillow for the opportunity to advertise with Agent. The advertising fees paid by lender, in turn, reduce the amount the Agent pays Zillow for Agent's advertising. The more the lender spends, the more often the lender is featured (versus other lenders with whom the Agent advertises). Though this program was being investigated by CFPB for violations of RESPA Section 8 and UDAAP, the investigation quietly concluded and Zillow announced in a June 2018 SEC filing that the company had received a letter from the Bureau indicating that it would not be pursuing enforcement action.

The Zillow case is comforting to institutions insomuch as the CFPB validated that these types of marketing arrangements can lawfully exist. However, they do not come without scrutiny. In these types of arrangements, institutions should pay considerable attention to how the fee structure flows through the parties, in addition to the considerations above. In my experience, these arrangements can be incredibly complex and always invite risk. It's prudent to get legal counsel involved before agreeing to participate in this kind of arrangement.

To conclude, RESPA Section 8 questions can be complex, rife with competing interpretations from HUD, CFPB and the courts, and require wading through unchartered waters with ever-changing leadership at the CFPB. Given that penalties are steep, as permitted by statute – recent RESPA CFPB enforcement actions have imposed penalties ranging from $35,000 to $265,000 and the amount at issue in the PHH case was $109 million – these questions deserve attention, thorough analysis, and often times, involvement of counsel.

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

Regulatory Spotlight

Agencies Request Comment on Information Collection.

- The Board of Governors of the Federal Reserve System (FRB), and the Federal Deposit Insurance Corporation (FDIC) announced they seek comment on the information collection titled Regulation I: Disclosure Requirements for Depository Institutions Lacking Federal Deposit Insurance. The agencies also gave notice that they sent the collection to OMB for review. Comments are due **10/28/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-08-29/pdf/2019-18606.pdf. *Federal Register*, Vol. 84, No. 168, 08/29/2019, 45491-45494.

- 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 Country Exposure Report and Country Exposure Information Report. The agencies also gave notice that they sent the collection to OMB for review. Comments are due **10/09/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-09-09/pdf/2019-19369.pdf. *Federal Register*, Vol. 84, No. 174, 09/09/2019, 47264.

CFPB Requests Comment on Information Collections.

- CFPB announced it seeks comment on the information collection titled Regulation I: Disclosure Requirements for Depository Institutions Lacking Federal Deposit Insurance. CFPB also gave notice that it sent the collection to OMB for review. Comments are due **09/23/2019**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-08-23/pdf/2019-18249.pdf. *Federal Register*, Vol. 84, No. 164, 08/23/2019, 44289-44290.

Wisconsin Bankers ASSOCIATION

October 2019

Compliance Journal

Special Focus

Can Wisconsin Banks Lawfully Bank Marijuana-Related Businesses?

On January 1, 2020, recreational marijuana becomes lawful in Illinois, making it the eleventh state in the country to legalize marijuana for recreational use. When Illinois Public Act 101-0027 was enacted this past June, Illinois also became the second state bordering Wisconsin to legalize marijuana for recreational use, second to Michigan where licenses will begin being issued next month. Marijuana legalization in neighboring states raises the following question: Can a Wisconsin bank lawfully bank marijuana-related businesses (MRB)[1] that operate in states where recreational marijuana is legal?

State v. Federal Legality

To answer that question, it requires an understanding of the current legal landscape. At a state level, individuals and businesses acting consistent with state law requirements (e.g. licensure, age restrictions) will be deemed lawful actors within the state. However, current federal law muddies the waters regarding whether those individuals and business are acting entirely lawfully. This is because marijuana is still unlawful on the federal level – the Controlled Substances Act (CSA) characterizes marijuana as a Schedule I Controlled Substance and makes it illegal under federal law to manufacture, distribute, dispense, or possess marijuana. Technically speaking, then, individuals acting consistent with state marijuana laws are violating federal law. But, you ask, why don't we often hear of lawful state actors being penalized by federal law enforcement officials?

Enter the Cole Memo. On August 29, 2013, then-Attorney General James Cole issued a Memorandum (the "**Cole Memo**") in response to several states legalizing marijuana. The memo, in so many words, defers enforcement of marijuana-related activity to the states that have enacted laws legalizing marijuana in some form. The Cole Memo sets forth a number of federal enforcement priorities pertaining to marijuana including, for example, preventing the distribution of marijuana to minors, preventing violence and use of firearms in the cultivation and distribution of marijuana, and preventing revenue from the sale of marijuana from going to criminal enterprises, gangs, and cartels. Outside of the enforcement priorities delineated in the Cole Memo, the federal government will rely, as it has traditionally relied, on "states and local law enforcement agencies to address marijuana activity through enforcement of their own narcotics laws."

After the issuance of the Cole Memo, individuals and businesses could act pursuant to state marijuana laws without fear of prosecutorial action from the feds, assuming their actions did not implicate an enforcement priority indicated in the Cole Memo. That "relief" was short-lived, however, as on January 4, 2018, then-Attorney General Jeff Sessions rescinded the Cole Memo. The Cole Memo remains rescinded today. In practice, however, the spirit of the Cole Memo appears to live on, as the rescission issued by Attorney General Sessions continued to provide "prosecutorial discretion."

Thus, in summary, though recreational marijuana may be lawful at the state level, it remains unlawful and subject to enforcement action at the federal level. In practice, however, it is clear that federal law enforcement officials do not necessarily prioritize taking enforcement action against individuals and businesses acting consistent with state marijuana laws.

BSA Responsibilities

Of course, the legality question is a relevant one for banks because of Bank Secrecy Act (BSA) obligations. As banks, it's imperative that you meet your (BSA) obligations, consistent with your Customer Due Diligence (CDD) program. In short, the bank must ensure

1 A marijuana-related business (MRB) is not a defined term, though it has been used in various guidance issued by federal agencies. Questions remain regarding whether a business needs to "touch the plant" to be considered an MRB (e.g. grower, processor, or retailer) or if MRB would include parties accepting monies from MRBs (e.g. landlords, vendors, or suppliers). This definitional question is one for the bank to grapple with, possibly in consultation with regulators, until additional clarification is provided.

that the transactions conducted through the bank are not derived from illegal activity. As described above, however, transactions flowing through an MRB are, very clearly, derived from illegal activity.

Recognizing the precarious position of financial institutions and the practical realties of having an unbanked yet burgeoning MRB population, the Financial Crimes and Enforcement Network (FinCEN) issued guidance entitled "BSA Expectations Regarding Marijuana-Related Businesses" on February 14, 2014 ("**FinCEN Guidance**"). The FinCEN Guidance, which is still alive and well today, leaves direction to banks to determine whether to provide financial services to MRBs, but indicates that customer due diligence is a "critical aspect" of this determination. To this end, the FinCEN Guidance delineates financial institutions' due diligence responsibilities when banking MRBs. Specifically, it outlines requirements including, for example, verifying state licensure and registration and reviewing associated documentation, requesting information about the MRB and related parties from state licensing and enforcement authorities, developing an understanding of the normal and expected activity of the business, and conducting ongoing monitoring.

In addition, the FinCEN Guidance outlines the obligation of financial institutions to file Suspicious Activity Reports (SARs) on activity involving MRBs, which, according to the Guidance "is unaffected by any state law that legalizes marijuana-related activity." If a bank is providing financial services to an MRB, the bank must file one of the following types of SARs, consistent with FinCEN's suspicious activity reporting requirements and related thresholds:

- "Marijuana Limited"
- "Marijuana Priority"
- "Marijuana Termination"

Determining which type of SAR to file is described within the FinCEN Guidance. In summary, the determination is based on whether or not Cole Memo priorities are implicated (despite its rescission) and if the account activity leads the bank to terminate the relationship with the customer.

Finally, the FinCEN Guidance notes that a bank's Currency Transaction Reporting (CTR) responsibilities are unaffected by the fact that a customer is deemed an MRB.

Banks planning to provide financial services to MRBs should familiarize themselves with the obligations outlined in the FinCEN Guidance.

Regulator Considerations

In addition to the criminal liability risks and practical considerations that a bank must consider in weighing the decision to bank MRBs, the regulator risk must also be weighed. Based on our current understanding the various regulators' position on banking MRBs, the direction is to "follow FinCEN Guidance." Thus, assuming the bank is following the FinCEN Guidance and has followed applicable policies and procedures, one would assume enforcement action would be avoided.

To the extent your bank is considering providing financial services to MRBs, I suggest getting in touch with your regulator for guidance.

So, What Do I Do?

The head-in-the-sand approach to banking MRBs is not a good one, as the issue will eventually present itself if it hasn't already. Thus, I suggest banks take the following actions:

- Consider whether your answer to "will you bank an MRB?" is a "yes (under certain circumstances)" or "no". Develop policies and procedures accordingly and as necessary.

October 2019
Volume 25, Number 5

Wisconsin Bankers Association
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- Regardless of your policy, it's important to know if your customer is an MRB; thus, you should ask. If the customer is an MRB and your policy says you won't bank them, don't bank them. If your policy is that "yes" (you will consider banking the MRB), you need additional information before you should bank or continue banking the self-identified MRB.

- That additional information is information and documentation that allows the bank to determine whether or not the customer is in compliance with state law. Such collection will typically take the form of a Questionnaire and Certification and will require supporting documentation from the customer. Information will vary from state to state and any such information collection documentation should be developed in consultation with counsel who is familiar with the marijuana laws of the state.

    - If, based on the bank's reasonable due diligence, the customer appears to be in compliance with state law at account-opening or when the bank confirms compliance of an existing customer, I suggest the following:

        - Designate the customer as "High Risk". Consistent with such designation, continue to monitor your MRB customer for compliance with state law on an ongoing basis; and

        - Follow FinCEN Guidance. This includes monitoring the account for the presence of red flags identified in the FinCEN Guidance and filing SARs as appropriate.

    - In contrast, if, based on the bank's reasonable due diligence, the customer appears to NOT be in compliance with state law, the activity is unlawful and inconsistent with FinCEN Guidance. Accordingly, I do not suggest banking the customer.

The Future

The good news is that we only anticipate greater clarity as time marches on. Such clarity could come with enactment of the Secure and Fair Enforcement Banking Act of 2019 ("SAFE Banking Act"), which has already cleared the Senate and is now in the hands of the House. In summary, the Act would provide protections for financial institutions that provide financial services to legitimate cannabis-related businesses and services providers. The Act would allow banks to serve cannabis-related businesses without fear of adverse action from the regulators or criminal liability. The Act would not eliminate the need for banks to make policy decisions and draft implementing policies and procedures pertaining to MRBs, but it would certainly reduce ambiguity and provide protections that bankers need to feel comfortable serving this clientele. Stay tuned on the SAFE Banking Act and/or other possible legislative fixes to the precarious relationship between the banker and the MRB.

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

Wisconsin Bankers ASSOCIATION

November 2019

Compliance Journal

Special Focus

USDA's New Hemp Program and What it Means for Wisconsin

The United States Department of Agriculture (USDA) published an interim final rule on October 31, 2019 specifying regulations to produce hemp. The rule is effective October 31, 2019 through November 1, 2021.

Introduction

The rule establishes a Federal program for producers in States that do not have their own USDA-approved plan. The program includes provisions for maintaining information on the land where hemp is produced, testing of THC levels, disposing of plants not meeting certain requirements, and licensing requirements. USDA has also outlined provisions under which States may submit their own plans for approval.

It is WBA's understanding that the Wisconsin Department of Agriculture, Trade and Consumer Protection (DATCP) will submit a Hemp Program Plan to USDA. However, DATCP will continue under the 2014 Farm Bill provisions, and existing Wisconsin regulation at time of this article's publication, in 2020. As of November 1, 2019, DATCP has begun its hemp licensing for the 2020 hemp season. At this time, DATCP is is preparing to write rules to align Wisconsin law with the 2018 Farm Bill, and expects to begin the new program under the 2018 Farm Bill, and USDA's rule, in 2021.

This article discusses the procedural aspects for submission of a State plan to USDA under its interim final rule. It also discusses the Federal program requirements placed upon hemp producers. While these procedures and the program requirements do not directly apply to banks, they will affect how hemp businesses operate in Wisconsin, and thus, bank customers seeking to engage in hemp-related activity. This article presents selected aspects of the interim final rule for banks to better understand what to expect in the coming years and the requirements that may apply to their customers.

Procedural Aspects

From a procedural standpoint, WBA reminds readers that as of publication of this article, much remains to be decided. November 26, 2019 Governor Tony Evers signed 2019 Senate Bill 188 establishing a new hemp program. It requires DATCP to write and submit a plan to USDA for approval. After USDA receives the plan, it will either approve or disapprove the plan no later than 60 calendar days after receipt.

If DATCP proposes a plan and it is rejected by USDA, the interim final rule provides for amended plan procedures. Under those procedures, hemp production continues under the existing plan. For example, production in Wisconsin would continue under current rules while DATCP and USDA work out amendments to the proposed plan. However, if an amended plan is not submitted within one year from the effective date of the rejected new law or regulation, the existing plan is revoked.

Note that as of publication of this article, the current DATCP program under ATCP 22 and 2017 Wisconsin Act 100 is still in effect. As discussed above, DATCP is currently issuing licenses for the 2020 season. If DATCP writes new rules under the new law, WBA will report on what banks need to know about the process.

USDA Plan Requirements

Because hemp production at the time of this article's publication continues under existing Wisconsin law, and the future rule governing production is unknown, a full discussion of USDA's rule and the Wisconsin bill would be premature. As such, this article will not discuss the Wisconsin bill which has yet to be signed by the governor. It will discuss USDA's rule below, but from a conceptual standpoint rather than a full discussion. Note that the requirements as presented below have been edited to help banks understand their broader implications. As such, most technical requirements have been removed. For a full reading of the rule, please refer to the link at the end of this article.

A State plan must meet information collection requirements, to be reported to The Secretary of Agriculture of the United States regarding:

(1) Contact information for licensed producers;

- (i) A legal description of the land on which the producer will produce hemp including its geospatial location; and
- (ii) The status and number of the producer's license or authorization.

(2) A State plan must include a procedure for accurate and effective sampling of all hemp produced, requiring the following:

- (i) Samples must be collected within 15 days prior to the anticipated harvest.
- (ii) The method used for sampling must be within a level of 95% accuracy, that no more than 1% of the plants in the lot would exceed the acceptable hemp THC level.
- (iii) During a scheduled sample collection, the producer or an authorized representative of the producer shall be present at the growing site.
- (iv) Representatives of the sampling agency shall be provided with complete and unrestricted access during business hours to all hemp and other cannabis plants, whether growing or harvested, and all land, buildings, and other structures used for the cultivation, handling, and storage of all hemp and other cannabis plants, and all locations listed in the producer license.
- (v) A producer shall not harvest the cannabis crop prior to samples being taken.

(3) The State plan must include procedures for testing that can accurately identify delta-9 tetrahydrocannabinol content concentration levels to specified levels and meet a specific methodology.

- (i) Any test resulting in higher than acceptable THC levels is considered conclusive evidence that the lot represented by the sample is not in compliance. Lots tested and not certified may not be further handled, processed or enter the stream of commerce and the producer shall ensure the lot is disposed of.
- (ii) Samples of hemp plant material from one lot shall not be commingled with hemp plant material from other lots.
- (iii) Analytical testing for purposes of detecting the concentration levels of THC shall meet standards that are not presented in this summary.

(4) The State shall promptly notify USDA by certified mail or electronically of any occurrence of cannabis plants or plant material that do not meet the definition of hemp in this part and attach the records demonstrating the appropriate disposal of all of those plants and materials in the lot from which the representative samples were taken.

(5) A State plan must include a procedure to comply with certain enforcement procedures.

(6) A State plan must include a procedure for conducting annual inspections of, at a minimum, a random sample of producers to verify that hemp is not produced in violation of this part.

November 2019
Volume 25, Number 6

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(7) A State plan must include a procedure for submitting a monthly report to USDA. All such information must be submitted to the USDA in a format that is compatible with USDA's information sharing system.

(8) The State must certify that it has the resources and personnel to carry out the practices and procedures necessary to comply.

(9) The State plan must include a procedure to share information with USDA.

(i) The State plan shall require producers to report their hemp crop acreage to the Farm Service Agency.
(ii) The State government shall assign each producer with a license or authorization identifier in a format prescribed by USDA.
(iii) The State government shall require producers to report the total acreage of hemp planted, harvested, and, if applicable, disposed. The State government shall collect this information and report it to USDA.

Final Takeaways

As expected, the rule requires testing, reporting, and monitoring to accurately identify whether hemp samples contain a delta-9 tetrahydrocannabinol (THC) content concentration level that does not exceed the acceptable level. To that extent, hemp is defined as the plant species Cannabis sativa L. and any part of that plant, including the seeds thereof and all derivatives, extracts, cannabinoids, isomers, acids, salts, and salts of isomers, whether growing or not, with a THC concentration of not more than 0.3 percent on a dry weight basis.

Another aspect to note is the rule's use of the word "producer." A producer is someone who is licensed or authorized to produce hemp, meaning to grow hemp plants for market, or for cultivation for market, in the United States. The rule does not distinguish between grower, producer, retailer, or any other type of hemp-related business. As such, it will remain important to see what DATCP proposes for categories of regulation in its rule.

Conclusion

While hemp businesses in Wisconsin still operate under DATCP's current rule at time of this article's publication, it is important to understand the track Wisconsin is currently on, and what possibilities the future holds, in order to prepare accordingly. WBA will continue to monitor and report on future hemp regulation as it continues to develop.

Click here to view USDA's interim final rule. ■

Regulatory Spotlight

Agencies Finalize 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) are finalizing amendments to the official interpretations for their regulations that implement section 129H of the Truth in Lending Act (TILA). Section 129H of TILA establishes special appraisal requirements for "higher-risk mortgages," termed "higher-priced mortgage loans" or "HPMLs" in the agencies' regulations. The Agencies issued joint final rules implementing these requirements, effective 01/18/2014. The Agencies' rules 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). If there is no annual percentage increase in the CPI–W, OCC, FRB, and CFPB 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 **06/01/2019**, the exemption threshold will increase from $26,700 to $27,200, effective **01/01/2020**. The notice may be viewed at: https://www.govinfo.gov/content/pkg/FR-2019-10-30/pdf/2019-21559.pdf. *Federal Register*, Vol. 84, No. 210, 10/30/2019, 58013-58017.

Wisconsin Bankers ASSOCIATION

December 2019

Compliance Journal

Special Focus

Mergers and Acquisitions: A Compliance Officer's Perspective

by Jeffrey Schmid, Director-Compliance & Management Services, FIPCO

In early 2019, I served as the Compliance Officer of a small-community bank that was in the early stages of an acquisition. While both institutions performed necessary due-diligence, including review of the Compliance Management System I managed, certain compliance and regulatory aspects began to emerge that never previously hit my radar. After all, M&A activity is not an area of focus for the typical Compliance Officer. What I came to realize is that emerging trends in our industry are beginning to change the dynamics of where our responsibilities lie, while prevention of consumer harm rises to a new level.

So, what is a Compliance Officer to do? First, I turned toward my regulator for guidance. The Summer 2013 edition of Supervisory Highlights from the FDIC was a great starting point. The article, *Mergers and Acquisitions: A Compliance Perspective*, written by **Matthew Z. Zamora**, Senior Compliance Examiner, Division of Depositor and Consumer Protection, reminded me of the importance of maintaining a good Compliance Management System (CMS) during and after the merger. It helped me recognize that the ability of the surviving institution to establish and maintain its CMS would be subject to regulatory scrutiny and non-compliance could lead to punitive damages.

Equipped with this new-found knowledge, I confronted the next challenge of putting it to practical use. To further complicate matters, areas and issues not addressed when merger discussions first began started to crop-up. For example, if management decided to merge any products, services, and software, it would undoubtedly create a vacuum of new disclosures, changed processes, enhanced procedures, and potentially limit resources.

So, what is a compliance officer to do?

First, I analyzed which regulations brought the most risk, including reputational and regulatory. I identified several regulations that presented potential punitive damages for non-compliance which, if not addressed early, could result in negative consequences to shareholder value. To tackle this, I created a chart of the regulations applicable to both institutions, along with potential civil monetary penalties. What I found was staggering.

Next, I created a checklist. I know, I know, Compliance Officers live by these. But a well-documented checklist of which regulations needed to be considered, which tasks needed to be performed, and who was be responsible for performing them helped me to keep this aspect of M&A in the forefront. I then communicated this information with management of both institutions so that proper resources could be allocated.

Then, much like the first steps in introducing a new product or service, I engaged my experiences as a Compliance Officer. For instance, in the case of mapping loan and deposit accounts, a Compliance Officer should perform a side-by-side comparison of account related disclosures, including Truth in Savings, TRID and contracts, looking for commonality in terms and fees to help find the right products that bring synergy. By applying this method I found that, in some cases, it made more sense to build a new product on the acquirer's system to mirror the product of the merged institution. The key was to find as much commonality as possible to avoid additional disclosures and customer confusion. As I worked with the merger and acquisition team, we found differences and tracked them in a table format so we could use this information when it came time to inform our customers well in advance of the actual merger.

Next, I worked with management to determine what the departments would look like following the formal merger of both institutions. I found that because of how the merged institution serviced its mortgage loans, a simple name change triggered RESPA requirements

on providing Notice of Servicing Rights to all mortgage customers, even though payments, address and phone number remained the same. Once the merger was announced and a legal closing date was determined, I worked with our mortgage processing department to properly disclose the likelihood that servicing would be transferred to the new bank and prepared a mass mailing for existing customers.

And what about that thing they call HMDA? This can be disastrous for an institution if done wrong, so the team began by analyzing if one or both institutions were required to file. If one institution did not file, we knew it would be a major change for the other institution, especially for collecting necessary information. We started by asking questions about Pre-approval and Pre-qualification programs and if ether institution reported HELOC's, knowing that how these are defined and reported could be different for each bank and might lead to missed applications. Until the end of the year, we found that keeping and filing separate HMDA LAR's could be advantageous, but not efficient. Referencing A Guide to HMDA Reporting Getting It Right! was my greatest tool as a compliance officer. I also found that a conversation with our reporting vendor about license fees and implementation helped prepare for another calendar year of reporting. Planning a new collection, reporting, and review process before the next calendar year helped put both banks on the right path.

Finally, as one who handled multiple responsibilities, I didn't forget to dust off my CRA Officer hat and update our public file. I had to redraw our CRA assessment area, update our list of products and services for the combined institution, and re-post the corresponding lobby notice. I also prepared for the possibility of customer complaints that might follow after the merger.

Conclusion

While these are just a few examples of what I encountered during a merger and acquisition, through them I found that the role of the Compliance Officer is a critical component, before, during, and after the merge. Keeping abreast of these challenges introduced a new dynamic in managing the newly formed CMS program. To prepare your bank for these or other types of challenges, please contact **Jeffery Schmid**, Director of Compliance and Management Services through FIPCO at jschmid@fipco.com to see how our experience can assist your bank. ■

December 2019
Volume 25, Number 7

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