



Compliance News...

Regulation E Compliance . . .

As the world has become more “electronic”, money can exchange hands in the blink of an eye or a click of a mouse. Plastic (credit, debit and ATM cards) is the preferred method of payment for most consumers. We have been inundated with rules for handling these electronic transactions. From Visa and MasterCard rules to NACHA it is difficult to keep things straight. Often times, the various rules even seem to contradict each other.

With all the rules that pertain to electronic transactions, it seems that the most commonly disregarded rules (the Electronic Funds Transfer Act) are the most important of all. Consider the following scenario:

Grandma Jones frantically comes into the bank with her monthly statement and informs you \$500.00 is missing from her account. In reviewing the statement, you discover two recent ATM withdrawals, one for \$200 and one for \$300. Grandma Jones insists that she did not make these withdrawals. In fact, she has her card in her purse and has never given anyone permission to use it.

Upon further questioning, Grandma Jones did remember one occasion where her Granddaughter, Kinsey, drove her to get some ice cream. They stopped at an ATM machine to get \$20 in cash. Grandma Jones’ eyesight is really poor and she was having a hard time seeing the numbers on the ATM machine. So, she told Kinsey her pin number to assist her with completing the transaction.

A review of video surveillance, showed Kinsey making the transactions in question.

The Electronic Funds Transfer Act is very clear on the how the investigation is to be conducted and how much liability the consumer will have. This brings to mind some questions that are commonly violated.

Is Grandma Jones responsible for the two ATM transactions since she gave Kinsey her PIN number?

The answer is a clear, NO. When you look at the definition of an “unauthorized electronic funds transfer” it is defined as: *an electronic fund transfer from a consumer’s account initiated by a person other than the consumer without actual authority to initiate the transfer and from which the consumer receives no benefit. [§205.2(m)]* In this scenario, Grandma Jones did not authorize the transactions and she clearly did not receive any benefit. While you may consider Grandma Jones negligent in providing her PIN number to Kinsey, gross negligence does not increase her liability.

Can the bank require Grandma to file a police report prior to continuing with the claim?

Again, the answer is NO. Requiring someone to file a police report before proceeding with the investigation of the claim or issuing provisional credit clearly violates the Regulation.

So what can the bank do?

The bank has the right to pursue legal action against Kinsey if Grandma Jones wants to continue with her claim. The bank must refund Grandma the amount in question (as well as interest and fees, if applicable). Grandma Jones liability is a maximum of \$50.

The bank does have the right to refuse anyone an ATM or debit card (or to re-issue a card). It is a privilege the bank can bestow on consumers, not the consumers right to have access to such a product. The Electronic Funds Transfer Act is clearly a “consumer protection” law and is not designed to protect the bank in all claims. Unfortunately, this is a cost of doing business when issuing ATM and debit cards. It is the financial institutions’ duty to have appropriate controls in place to protect themselves.

Trying to sift through the many rules for electronic transactions can be daunting. But the most important thing to remember is to ALWAYS ensure compliance with the Electronic Funds Transfer Act. This will guarantee maximum compliance.

Mortgage Loan Fraud . . .

The Financial Crimes Enforcement Network (FinCEN) recently updated their Mortgage Loan Fraud Assessment. The information contained in this document is compiled from filed Suspicious Activity Reports (SARs). This is an interesting read, as it details trends in mortgage loan fraud from mortgage broker fraud to appraisal fraud. You can find this report at: <http://www.fincen.gov/MortgageLoanFraudSARAssessment.pdf>

Upcoming Seminars – Mark These Dates . . .

We will be conducting our **Advanced Deposit Operations and Advanced Lending Compliance Seminars** this fall. These seminars are always very well attended. More information will be available on our website soon. For your convenience, you can register and pay by credit card on our website: <http://www.bankerscompliance.com/products/>

The dates and locations are as follows:

August 19 – 21 – Grand Island, NE

September 9 – 11 – Sioux Falls, SD

October 21 – 23 – Omaha, NE

Our annual BSA Seminar will be held in February 2009. Details will be available on our website soon.

Banker's Compliance Consulting Q & A Forum...

The following Q & A's were generated by a Escrows Webinar presented by Banker's Online and taught by David Dickinson, President of Banker's Compliance Consulting. The following website has complete information regarding past and future Bankers Online webinars: <http://www.bollearningconnect.com>.

Note: In some of the answers below we may refer you to look at a certain page in the manual. The manual we are referring to is Banker's Compliance Consulting's Advanced Lending Manual. If you do not have this manual and would like to purchase it, please contact our office.

Escrow Account Cushion

Question 1. At closing, can we collect more than the two months cushion? For example, 2 months cushion plus the first month due.

Answer: RESPA states that you can have enough money in the escrow account to make all the payments (taxes, insurance, etc) in the upcoming twelve months plus a two month cushion. That is it. You cannot have a penny more than the amount determined by the aggregate analysis.

Question 2. If we don't require a cushion, are we ok if we have up to two months cushion in the escrow account?

Answer: RESPA allows you to have a 2 month cushion regardless of whether you require a cushion or not. However, you are required to disclose the amount of cushion to the borrower on the initial escrow statement. So, while you are within your rights of the law, you might be in violation of the initial disclosure requirements.

Question 3. Going back to the state cushion requirements, is it the state the property is located in, or the state the lender is in that determines the requirements?

Answer: I am not a tax expert but generally it would be the location of the property. I would check with a tax attorney in your area to be sure.

Escrow Payments

Question 4. Our tax service First American, reports taxes due in Texas in November, but they are actually due 1/31, is this a violation if we pay them in November?

Question 5. Many Texas counties offer discounts for early tax payments. Does that means it has to be paid early?

Question 6. In Texas, you get a discount for paying taxes early in November. Isn't there a rule that we must take advantage of any discount available to the customer and pay in November rather than January?

Question 7. Our tax bill is a lien on the property as of December 1, but the late charge is not assessed until February 15. Most borrowers want to deduct the tax bill in the year it is assessed. Should we be analyzing with a due date of December or February?

Question 8. In reference to the statement regarding paying taxes before the due date, what is the difference between that and paying insurance before it is due?

Question 9. Shouldn't the due date of the taxes, insurance etc. be the month they are being disbursed not the due date? For example, if taxes are due April 1st then the analysis should show March as the month the taxes are paid?

Answer: For the answer we must look to a couple different sections of RESPA. Section 3500.17(c)(2) of RESPA states: *"Before establishing an escrow account, the servicer must conduct an escrow account analysis to determine the amount the borrower must deposit into the escrow account (subject to the limitations of paragraph (c)(1)(i) of this section), and the amount of the borrower's periodic payments into the escrow account (subject to the limitations of paragraph (c)(1)(ii) of this section). In conducting the escrow account analysis, the servicer must estimate the disbursement amounts according to paragraph (c)(7) of this section. Pursuant to paragraph (k) of this section, **the servicer must use a date on or before the deadline to avoid a penalty as the disbursement date for the escrow item and comply with any other requirements of paragraph (k) of this section.** Upon completing the initial escrow account analysis, the servicer must prepare and deliver an initial escrow account statement to the borrower, as set forth in paragraph (g) of this section. The servicer must use the escrow account analysis to determine whether a surplus, shortage or deficiency exists and must make any adjustments to the account pursuant to paragraph (f) of this section."*

3500.17(k)(1) and (k)(3) of RESPA state, (1) *If the terms of any federally related mortgage loan require the borrower to make payments to an escrow account, the **servicer must pay the disbursements in a timely manner, that is, on or before the deadline to avoid a penalty,** as long as the borrower's payment is not more than 30 days overdue. (3) For the payment of property taxes from the escrow account, if a taxing jurisdiction offers a servicer a choice between annual and installment disbursements, the servicer must also comply with this paragraph (k)(3). **If the taxing jurisdiction neither offers a discount for disbursements on a lump sum annual basis nor imposes any additional charge or fee for installment disbursements, the servicer must make disbursements on an installment basis.** If, however, the taxing jurisdiction offers a discount for disbursements on a lump sum annual basis or imposes any additional charge or fee for installment disbursements, the servicer may at the servicer's discretion (but is not required by RESPA to), make lump sum annual disbursements in order to take advantage of the discount for the borrower or avoid the additional charge or fee for installments, as long as such method of disbursement complies with paragraphs (k)(1) and (k)(2) of this section. HUD encourages, but does not require, the servicer to follow the preference of the borrower, if such preference is known to the servicer.*

Section 3500.17(k)(3) above makes it clear that if there are no discounts for paying early and the borrowers will avoid any fees for paying early, then the servicer **MUST** pay before the imposition of a penalty but not earlier. The "spirit of the law" is intended to do what is in the best interest of the customer. And paying later (unless there is a discount) is always in the best interest of the customer.

Question 10. What should a bank do if they paid taxes 1 month early?

Answer: You cannot correct a timing error. I would suggest documenting the error, training the appropriate personnel and move on.

Question 11. If the due date of the taxes is April 1st (last day before penalty is assessed) and we disburse in March, what month should we use in the escrow analysis - April or March?

Answer: If payments can still be made on April 1st without being delinquent, then the payment should be made on April 1st and the escrow analysis should show a disbursement in April. If the payments are considered delinquent on April 1st then payment should be made on March 31st and the escrow analysis should show a disbursement in March.

Question 12. We find that the insurance companies are changing their due dates to two weeks prior to the borrower's policy coverage dates. When should we be paying these bills and what date should we use for analysis?

Question 13. We are finding insurance companies that are changing the 'DUE DATE'.....i.e., the due date has been 4/30/08 but now the company is saying the due date is 4/15/08 but the 'POLICY PERIOD' is still 4/30.....when should we pay the bill and what should the analysis date be (especially IF IT CHANGES FROM MAY 1 TO APR 15?

Answer: I understand that there is a need for "mail time", but in today's environment of electronic payments, I see this argument getting weaker. I would contact the insurance company and see if the borrower will incur any fees, policy cancellation, etc. if not paid by the due date. If not, I would wait to make payment until as close to the policy date as possible (without going over to avoid cancellation, of course). However, if the insurance company insists that payment must be received by the "due date" then that is when they need to be paid and the escrow analysis should reflect that date.

Question 14. In Oregon, we pay out taxes on November 15th and pay in full to take advantage of an early discount. Is this an issue with the 12 month payout, if we are paying again the following year on the same day? As you said, the computation year is November to October. Or have I confused two different areas?

Answer: I need some more clarification. I don't understand the question.

Escrow Surplus

Question 15. Are we required to refund a surplus if the customer requests that we retain it due to anticipated increased taxes?

Question 16. Are we breaking any laws by netting the escrow balance during a payoff?

Question 17. What do you do with the surplus if the loan is in past due, or in foreclosure?

Answer: Anytime you have a surplus of \$50 or more you **must** refund it to the customer. You can give it to them by check or by depositing it into an account under their control. If the customer wants the bank to retain the surplus, they can endorse the check or give the money back to the bank to retain in their escrow account. A bank cannot automatically apply the refund to the loan balance. The bank also cannot apply an escrow surplus to a loan payoff balance. If the borrower is delinquent, the bank may retain the surplus until the delinquency is resolved.

Question 18. Also we currently include the escrows in the payoff. If we turned this off and cut checks back to the customer for their overages how is it handled if the escrow is short?

Answer: If the escrow is short at the time of loan payoff, it is acceptable to include this shortage in the loan payoff. This is money that you paid out on the borrower's behalf for which they are responsible.

Question 19. If the loan had two borrowers, do we have to refund the surplus to both borrowers? Can the refund go to just the primary borrower?

Answer: There is no guidance on this. I would consult an attorney on this issue. My guess would be that the check should be made payable to both Borrower 1 AND Borrower 2.

Question 20. Does required funding of surplus pertain to commercial loans?

Answer: The RESPA requirements discussed in this webinar only pertain to consumers. Some states have chosen to apply these rules or variations of them to commercial/ag loans as well. I would check your state law.

Escrow Fees

Question 21. What kind of fees can we pass on to the customer in reference to Escrow accounts?

Answer: RESPA does not prohibit a bank from charging fees for escrow accounts. A bank may pass along charges for establishing the account, monitoring the account, etc. RESPA does; however, prohibit charging a customer for RESPA related documents. So be sure your charges do not include your time for producing escrow disclosures, statements, etc.

Question 22. Can you also pass on the sales tax from fees charged for monitoring taxes? And what would we need to substantiate the fees for monitoring?

Answer: I would try to substantiate your tax service fee based on the time and process involved in monitoring, etc. As long as the fee is reasonable and comparable to other institutions, you should not have any issues. Sales tax is a state law issue. I would check with your examiners on this issue.

Question 23. What authorizes charging a fee to avoid establishing an escrow account?

Answer: There is no requirement that a fee needs to be charged to avoid establishing an escrow account. This is not addressed in RESPA. I will assume that this was a management decision or required by your secondary market providers.

Question 24. Does RESPA prohibit charging a tax service fee part of which we will pay to a third party vendor and part of which we will retain? We will disclose the full amount on the TIL as paid to lender.

Answer: There is no prohibition for charging a fee to establish an escrow account. But, I do see an issue with how you are disclosing the fee. Fee splitting is prohibited by REPSA.

Payment Shock

Question 25. If we “can only inflow for what you are out-flowing in the next 12 months” like– property taxes for a house built in 2008 for example – how do we avoid payment shock?

Answer: You don't avoid payment shock. You should advise the customer of the upcoming payment increase by giving them the disclosure on page 17 of the packet. If they want to voluntarily pay in extra they can, but are not required to do so.

Question 26. We have some lo's (loan officers) that know the taxes will be higher in the coming years than at closing. So, they collect more and the escrow payment is more than is really needed. Then when they go through analysis, they have a big surplus and they want us to hold the money in the account until the taxes go up. We cannot do that, right?

Answer: You are exactly right. First, RESPA prohibits collecting more than determined using aggregate analysis. Second, you cannot hold a surplus. It must be refunded to the customer if it is \$50 or more. This is a big deal and this practice should be changed immediately.

Short-Year Statements

Question 27. A customer escrows for homeowner's insurance, it has been paid out of escrow in August. Then we receive a cancellation. We now have no coverage and no one to pay, so we force place coverage. Do we continue to collect payments based on the last analysis until the next analysis is performed or do we close that portion of the escrow account and reanalyze and make changes for that portion of the escrow account? We do not escrow for force placed insurance. What is the proper procedure in handling this?

Answer: You could wait to adjust the escrow until the annual escrow analysis is due. Most likely, the new insurance will be more expensive so you will probably have a deficiency if you wait. You could issue a short year statement and run a new analysis with the changed information. This is what I would recommend.

Question 28. In response to not escrowing force placed insurance - we add the insurance to the principal balance of the loan. We do not know why we do not escrow force placed insurance, but it has been like that for 12 years. Maybe it is because we used to be a credit union - don't know, but we are going to look into it.

Answer: Since you are adding the cost of the force placed insurance to the principal balance of the loan and continue to escrow for insurance based on the current escrow analysis, you will accumulate a surplus very quickly. You can issue a short year statement and run a new escrow analysis with the updated information.

Question 29. We have a customer that has been delinquent so we have not been able to perform the analysis. The account was brought current today and we need to perform the analysis. All of our accounts are normally analyzed at the same time in December. Do we analyze this account for June 1st-May 31st and then can I analyze in December to keep this account on track with the others or will the account go to a 12 month analysis based on 6/1 -5/31 dates?

Answer: You can wait until the end of the escrow account computation year. Or, you can conduct a short year statement at anytime. This will allow you to keep this escrow account on the same schedule as your other escrow accounts.

Question 30. Our system is set up to do the annual analysis on January 15th of every year regardless of when the loan was put on the system. Are we doing this wrong? Should every loan have a different analysis date?

Answer: No. Many banks "cycle" their escrow accounts in the same month. You just need to ensure that to get an escrow account on your "cycle" that you are providing short-year statements to end one account computation year and starting another.

Voluntary Escrow Accounts

Question 31. We have had a customer request to start a new escrow account for Jan-Dec computation year (all our escrow accounts are voluntary) and instead of paying a 2 month cushion up front, used Nov & Dec to complete the 2 month cushion and continued with his monthly payments for Jan-Dec. The voluntary disclosure we provided actually showed 14 months instead of 12 months. Is this a violation?

Question 32. Our escrow accounts are all voluntary. We still try to abide by all the regs. Are we overdoing something?

Question 33. If all escrow accounts are voluntary, do RESPA and HUD escrow rules apply?

Question 34. Since our escrow accounts are voluntary, we send the check to the customer and tax agency. If we don't send them early, the customer may not have time to get taxes paid timely. Is this a problem?

Answer: Truly voluntary escrows are not subject RESPA. A bank can establish what ever method they prefer. However, check your state laws.

Miscellaneous

Question 35. Since we pay 2% interest on our escrow accounts, and we do so on a monthly basis, do we need to make an additional column or add that interest to the escrow computation when calculating the initial escrow deposit required? During the seminar it was stated that if we pay interest, we need to collect less than what is calculated to account for the interest.

Answer: You will need to factor in the interest in the aggregate analysis. You cannot have a penny more than is allowed by law (enough for the next 12 months payments and 2 months cushion).

Question 36. On FHA loans, is it a requirement to escrow hazard insurance?

Answer: This is not an area that I am familiar with.

Question 37. When will a spreadsheet for biweekly loans be available?

Answer: As I joked during the webinar, "when someone invents one". I have seen many attempts and have even attempted myself. None have been 100% accurate.

Question 38. Upon a loan sale, are we responsible for notifying customers of negative escrow balances?

Answer: No. A sold loan is not your responsibility. Generally the new servicer will run a new analysis and notify borrowers accordingly.

Question 39. If a loan payment is received without the escrow included but satisfies the principle and interest, are we required to bump the due date or is it still considered past due until escrow payment is received?

Answer: The answer depends on how your bank has set up its payment application. This is usually addressed in your loan contract. If the payment is applied first to escrow, then late fees, then interest, then principal, etc. I would say that the customer is in default. But if your payment application is late fees/interest/principal/escrow, they may not be in default.

Question 40. Would there be any issue with sending a loan payoff statement to loans that do not have escrows, in addition to the notes that do have an escrow?

Answer: I am not sure I completely understand the question. There is no regulatory prohibition against this. This could potentially be a large expense for the bank for something that is not required

Question 41. My understanding is if the customer owes money and we owe the customer money we have the right to set off; is this correct?

Answer: Right of set off is a state issue. Check your state law. But, under RESPA this would not be acceptable.

Question 42. If we currently have several mortgage loans that are being paid out annually, must we notify the borrower if we make a change to disburse semi-annually?

Answer: I assume that taxes are going from annual to semiannually. If the change would create a deficiency in the escrow account you should send a new analysis. If not, there are no notification requirements that I am aware of.

Question 43. Can escrow be force placed if taxes are two years delinquent?

Answer: Absolutely. You can establish an escrow account at any time. The initial escrow disclosure would be required to be provided within 45 days of establishing the account.

Question 44. Instead of changing the assessed value of homes for the last three years, our county simply changed the equalization rate, to represent a 5% increase each year in market value (from 2005-07 we went 95%, 90%, 85%). This year, they are equalizing to 100%, which is a 15% increase in assessed value. Can we set up escrows based on the current assessed value with the tax rates from the most recent year's taxes, or do we have to use the dollar value of the most recent taxes available on the assumption that while all property assessments went up 15%, the tax base is larger, and, therefore; the rate should actually drop (assuming of course that the taxing municipalities are not smart enough to create a budget that decreases by a smaller margin than the assessments increased, and make out like bandits)?

Answer: If taxes are paid in arrears (after the fact), you don't need to anticipate any increases, as tax payments will always be known. If taxes are not paid in arrears, you can base your aggregate analysis on what you anticipate the taxes to be for the next 12 months.

Question 45. When doing an in-house refinance, are we in compliance if we collect for the new escrow account and give the borrower a credit for the old escrow account on the HUD for the new loan?

Answer: Yes I think this is the correct way to disclose this. Show a credit to the borrower in the 200 series of the HUD (for the old escrow account) and show the amount collected for the new escrow account in the 1000 series.

Question 46. What happens when you analyze on the 12th month and you find a major error in the escrow account that requires maintenance and it causes the analysis to run on the 13th month?

Answer: Once the account computation year ends you basically have 30 days to analyze and get the new analysis out to the borrower. If you discover the error really late in to this 30 day timeframe, I suggest you get it done as quickly as possible.

NOTE: During the webinar, references were made to a HUD Q & A. You can access it at:

<http://www.hud.gov/offices/hsg/sfh/res/resindus.cfm>

Also, the website to find the HUD public guidance documents that have been removed from the regulation is:

<http://www.hud.gov/offices/hsg/sfh/res/respagui.cfm>