CONSUMER FINANCIAL PROTECTION BUREAU | SEPTEMBER 2019

Supervisory Highlights

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1. Introduction

The Consumer Financial Protection Bureau (CFPB or Bureau) is committed to a consumer financial marketplace that is free, innovative, competitive, and transparent, where the rights of all parties are protected by the rule of law, and where consumers are free to choose the products and services that best fit their individual needs. To effectively accomplish this, the Bureau remains committed to sharing with the public key findings from its supervisory work to help industry limit risks to consumers and comply with Federal consumer financial law.

The findings included in this report cover examinations in the areas of automobile loan origination, credit card account management, debt collection, furnishing, and mortgage origination that were generally completed between December 2018 and March 2019 (unless otherwise stated).

It is important to keep in mind that institutions are subject only to the requirements of relevant laws and regulations. The information contained in *Supervisory Highlights* is disseminated to help institutions better understand how the Bureau examines institutions for compliance with those requirements. This document does not impose any new or different legal requirements. In addition, the legal violations described in this and previous issues of *Supervisory Highlights* are based on the particular facts and circumstances reviewed by the Bureau as part of its examinations. A conclusion that a legal violation exists on the facts and circumstances described here may not lead to such a finding under different facts and circumstances.

We invite readers with questions or comments about the findings and legal analysis reported in *Supervisory Highlights* to contact us at CFPB_Supervision@cfpb.gov.

2. Supervisory observations

2.1 Automobile loan origination

The Bureau continues to examine auto loan origination activities, including assessing whether originators have engaged in any unfair, deceptive, or abusive acts or practices prohibited by the Consumer Financial Protection Act of 2010 (CFPA).

2.1.1 Abusive act or practice when selling add-on GAP products

Under the prohibition against abusive acts or practices in Sections 1031 and 1036 of the CFPA,[1] an act or practice is abusive if, among other things, it takes unreasonable advantage of a consumer's lack of understanding of the material risks, costs, or conditions of the product or service.[2]

Some auto lenders may sell consumers a guaranteed asset protection (GAP) product to cover the difference, or "gap," between the amount the consumer owes on the auto loan and the amount received from the auto insurer in the event a vehicle is stolen, damaged, or totaled. Such a gap is more likely to occur in an auto loan with a high loan-to-value (LTV) ratio than one with a low LTV, because in a loan with a low LTV, the insurance payout for a totaled vehicle may cover the outstanding debt.

One or more examinations completed in 2018[3] found instances in which auto lenders sold a GAP product to consumers under circumstances that led to an abusive practice. Specifically, examiners observed that lenders sold a GAP product to consumers whose low LTV meant that they would not benefit from the product. By purchasing a product they would not benefit from, consumers demonstrated that they lacked an understanding of a material aspect of the product. The lenders had sufficient information to know that these consumers would not benefit from the product. These sales show that the lenders took unreasonable advantage of the consumers' lack

[1] 12 USC 5531 and 12 USC 5536.

[2] 12 USC 5531(d)(2)(A).

[3] This examination work was completed prior to the review period for this report.

of understanding of the material risks, costs, or conditions of the product. In response to these examination findings, the lenders have undertaken remedial and corrective actions, including reimbursing consumers for the cost of the product and establishing an LTV minimum for GAP product sales.

2.2 Credit card account management

The Bureau continues to examine the credit card account management operations of one or more supervised entities. These examinations may focus on all aspects of credit card origination and account servicing for compliance with various Federal consumer financial laws including the Truth in Lending Act and its implementing regulation, Regulation Z. Selected recent findings are below.

2.2.1 Triggered disclosures for online credit card advertisements

Regulation Z, 12 CFR 1026.16(b), requires credit card issuers in credit card advertisements to clearly and conspicuously provide certain disclosures if the advertisements contain certain pricing terms (“triggering terms”).

In one or more examinations completed in 2018,[4] examiners found that entities failed to clearly and conspicuously provide disclosures required by triggering terms in online advertisements. In some instances, the triggered disclosures were available to consumers via a hyperlink that was not labeled in a way that referred to the triggered disclosures. Consumers would have to click on the insufficiently clear or conspicuous hyperlink, and then navigate through an online application before arriving at triggered disclosures. In other instances, consumers had to click on multiple hyperlinks and could only view the triggered disclosures after completing an eight-page application. Issuers have undertaken corrective actions in these cases in response to examination findings.

2.2.2 Offset of credit card debt

Regulation Z, 12 CFR 1026.12(d), prohibits credit card issuers from offsetting credit card debt with funds the consumer has on deposit with the issuer. However, subsection 1026.12(d)(2)

[4] This examination work was completed prior to the review period for this report.

expressly permits issuers to obtain or enforce a consensual security interest in such funds, so long as certain requirements specified in the Staff Commentary are met. Such security interests must be affirmatively agreed to by the consumer and must be disclosed in the account-opening disclosures. A security interest may not simply be the functional equivalent of offset, however. Thus, routinely including a provision in a cardholder agreement indicating that consumers are giving a security interest in any deposit accounts maintained with the issuers would not qualify for the exception under subsection 1026.12(d)(2). Instead, for a security interest to qualify, the consumer must be aware that granting a security interest is a condition for the credit card (or for more favorable account terms) and must specifically intend to grant a security interest in the deposit account. Indicators of the consumers' awareness and intent include at least one of the following (or a substantially similar procedure):

- Separate signature or initials on the agreement indicating that a security interest is being given;
- Placement of the security agreement on a separate page, or otherwise separate security interest provisions from other contract and disclosure provisions; or
- Reference to a specific amount of deposited funds or to a specific deposit account number.

One or more examinations completed in 2018[5] found that issuers violated Regulation Z, 12 CFR 1026.12(d)(1), by offsetting consumers' credit card debt against funds that the consumers had on deposit with the issuers without sufficient indication of the consumer's awareness of, and intent to grant, a security interest in those funds. The issuers' policies or procedures required the issuers to have obtained a signed authorization form from consumers before attempting to enforce the security interest. However, in some instances, the issuers enforced the security interest against the funds on deposit where such forms had not been signed by the consumer or could not be located. In response to examination findings, issuers have implemented corrective action to ensure compliance with the regulatory requirements.

[5] This examination work was completed prior to the review period for this report.

2.2.3 Deceptive threats of repossession or foreclosure in credit card collections

Under the prohibition against deceptive acts or practices in Sections 1031 and 1036 of the CFPA,[6] an act or practice is deceptive when: (1) it misleads or is likely to mislead the consumer; (2) the consumer's interpretation is reasonable under the circumstances; and (3) the misleading act or practice is material. In one or more examinations completed in 2018,[7] examiners found that one or more credit card issuer(s) misled or were likely to mislead consumer credit card holders by sending collection letters that suggested that the issuer(s) could repossess consumers' automobiles, or foreclose on homes, securing loans or mortgages owned by the issuer(s). In fact, the issuer(s) did not repossess any vehicles or foreclose on any mortgages in connection with delinquent credit card accounts, and it was against the policies of the issuer(s) to do so. The representations by the issuer(s) were likely to mislead consumers into believing that they might be subject to repossession or foreclosure for delinquent credit card accounts if they had an automobile loan or mortgage with the issuer(s). The consumers' beliefs were reasonable given the representations made in the collection letters. The misrepresentations were material since they were likely to induce cardholders to change their conduct with respect to their delinquent credit card accounts. In response to these examiner findings, the issuers discontinued the use of the collection letters.

2.2.4 Deceptive marketing regarding secured credit card accounts

Under the prohibition against deceptive acts or practices in Sections 1031 and 1036 of the CFPA,[8] a practice is deceptive when: (1) it misleads or is likely to mislead the consumer; (2) the consumer's interpretation is reasonable under the circumstances; and (3) the misleading act or practice is material. In one or more examinations, examiners found that credit card issuers misled or were likely to mislead consumers by orally representing that secured credit card accounts would automatically graduate (or be upgraded) to unsecured credit card accounts on a specific timeframe, such as six or twelve months after origination, so long as cardholders maintained their accounts in good standing. In fact, the issuers did not upgrade secured card accounts on any preset timeframe, and upgrade or graduation was conditioned on additional

[6] 12 USC 5531 and 12 USC 5536.

[7] This examination work was completed prior to the review period for this report.

[8] 12 USC 5531 and 12 USC 5536.

factors, as some subsequent disclosures and online and print solicitations suggested. The oral representations misled or were likely to mislead consumers about both the timing and likelihood of upgrade or graduation, and subsequent written disclosures were inadequate to cure the oral representations. The consumers' interpretation of the preset graduation or upgrade was reasonable based on the oral representations. The representations were also material to the consumers' decisions to apply for a secured card account with the issuers.

In one or more examinations, examiners found that credit card issuers misled or were likely to mislead consumers by representing in prescreened offers of credit that secured credit card accounts subject to an annual fee would be "periodically" reviewed for graduation (or upgrade). In fact, the issuers did not review such accounts for a year or more but did not provide additional disclosures to accountholders or modify their marketing materials. Such representations were likely to mislead consumers about the timing for a potential upgrade. Consumers' interpretations of such representations were reasonable under the circumstances. The issuers' misrepresentations were material to consumers' decisions to apply for a secured card account and to existing cardholders' decisions to maintain their secured card accounts.

In all the above cases, the issuers have developed action plans to identify and compensate impacted consumers, and updated their policies and procedures to prevent future violations.

2.3 Debt collection

Supervision continues to examine consumer debt collection for compliance with various Federal consumer financial laws, including the Fair Debt Collection Practices Act (FDCPA). Below are findings resulting from these supervisory activities.

2.3.1 False representation of the amount and legal status of debt

Section 807 of the FDCPA prohibits the use of any false, deceptive, or misleading representation or means in the collection of any debt. Specifically, Section 807(2)(A) of the FDCPA prohibits the false representation of the character, amount, or legal status of any debt. Examiners found that one or more debt collectors claimed and collected from consumers, interest not authorized by the underlying contracts between the debt collectors and the creditors. In doing so, one or more debt collectors falsely represented to consumers the amount due and authorized in violation of Section 807(2)(A) of the FDCPA. In response to these examination findings, one or more debt collectors conducted or are conducting a full accounting of these charges and providing remediation for affected consumer accounts, including accounts in which consumers paid in full, settled in full, or made partial payments.

2.4 Furnishing

Entities that furnish information relating to consumers to consumer reporting companies for inclusion in consumer reports (furnishers) play a vital role in the consumer reporting process. They are subject to several requirements under the Fair Credit Reporting Act (FCRA)[9] and its implementing regulation, Regulation V,[10] including accuracy and dispute handling requirements.

In one or more recent furnishing reviews, examiners found deficiencies in furnisher compliance with FCRA accuracy and dispute investigation requirements.

2.4.1 Duty to timely complete dispute investigations

The FCRA requires that when a furnisher receives notice of a dispute from a credit reporting company (CRC) pursuant to FCRA Section 623(b)(1),[11] the furnisher must complete its investigation of disputes "before the expiration of the period under section 611(a)(1). . ." within which the CRC must complete its own dispute investigation.[12] This period of time is normally 30 days from the date the CRC receives a dispute and can be extended to 45 days in certain limited circumstances.[13] Examiners found that one or more furnishers failed to complete dispute investigations within the required time period. At one or more furnishers, examiners found certain disputes of which the furnisher(s) received notice from the CRC but failed to conduct an investigation or respond to the CRC. In response to these findings, one or more furnishers are

[9] 15 USC 1681s-2(a)-(e).

[10] 12 CFR 1022.40-43.

[11] 15 USC 1681s-2(b)(1).

[12] 15 USC 1681s-2(b)(2).

[13] 15 USC 1681i(a)(1)(B).

establishing and implementing enhanced monitoring activities, and policies and procedures regarding compliance with furnisher-specific requirements of the FCRA.

2.4.2 Duty to provide results of dispute investigations to CRCs

The FCRA requires that if a furnisher's dispute investigation finds that disputed information is incomplete or inaccurate, the furnisher must report the results not only to the CRC that sent the dispute to the furnisher but also to all nationwide CRCs to which the furnisher provided the information.[14] Examiners found that one or more furnishers failed to report updates or corrections to information found to be incomplete or inaccurate following a dispute investigation to all applicable CRCs. At one or more furnishers, examiners found the systematic failure of reporting dispute investigation results to a particular CRC. In response to these findings, one or more furnishers are establishing and implementing enhanced monitoring activities, as well as policies and procedures regarding compliance with furnisher-specific requirements of the FCRA, and providing validation of corrective action.

2.4.3 Duty to promptly correct and update previously furnished information

The FCRA requires that if a furnisher determines that previously furnished information is not complete or accurate, the furnisher must promptly notify the CRC of that determination and provide the CRC with any corrections to that information, or any additional information, that is necessary to make the information complete and accurate.[15] In addition, a furnisher cannot thereafter furnish to the CRC any of the information that remains incomplete or inaccurate.[16]

Examiners found that one or more furnishers failed to promptly send corrections or updates to all applicable CRCs after making a determination, as reflected in the relevant system of record, that previously furnished information about certain accounts was no longer accurate. As a result, one or more furnishers are establishing and implementing enhanced monitoring activities, as well as policies and procedures regarding compliance with furnisher-specific requirements of the FCRA, and providing validation of corrective action.

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[14] 15 USC 1681s-2(b)(1)(D).

[15] 15 USC 1681s-2(a)(2)(B).

[16] 15 USC 1681s-2(a)(2)(B).

Examiners found that one or more furnishers of deposit account information failed to furnish updated information regarding accounts that were paid-in-full or settled-in-full. When one or more furnishers removed their company identification from account number fields at the request of a nationwide specialty CRC, and the removal of the identification changed the search key that the furnishers used for matching when making account updates, the furnishers discovered that almost two thousand accounts were not corrected to reflect the paid-in-full or settled-in-full status. Examiners observed that one or more furnishers did not promptly notify the nationwide specialty CRC after having determined that the accounts were not corrected and updated, in violation of the FCRA. In light of these findings, one or more furnishers have taken action to update and correct information that it previously furnished when they determined that the information was not complete or accurate.

2.4.4 Duty to provide notice of dispute

The FCRA prohibits furnishers from furnishing information to any CRC without notice that such information is disputed if the completeness or accuracy of the information furnished is disputed by a consumer.[17] Examiners found that one or more furnishers of deposit account information received consumer disputes and then continued furnishing information about the disputed accounts for several months without notifying a nationwide specialty CRC that the information furnished was disputed, in violation of the FCRA. As a result of these examination findings, one or more furnishers have taken action to provide timely notice to CRCs upon receipt of a direct dispute from a consumer who has disputed information previously furnished.

2.4.5 Regulation V duty to establish and implement policies and procedures

Regulation V requires furnishers to establish and implement reasonable written policies and procedures regarding the accuracy and integrity of the information relating to consumers that it furnishes to a CRC.[18] Examiners found that one or more furnishers of deposit account information failed to implement reasonable written policies and procedures regarding the accuracy and integrity of deposit account information it furnished to nationwide specialty CRCs. Such policies and procedures were also not appropriate to the nature, size, complexity, and scope of the furnishing activities. For example, there were no written policies and procedures for

[17] 15 USC 1682s-2(a)(3).

[18] 12 CFR 1022.42(a).

handling disputes regarding account information from certain files. The existing policies also did not address compliance with FCRA dispute requirements, such as the duty to conduct a reasonable investigation. There were also no policies and procedures for training, monitoring, or conducting internal audits regarding a business unit's responsibilities to forward disputes of furnished information. Finally, one or more furnishers failed to have policies and procedures for one business unit to conduct investigations of consumer disputes alleging account abuse caused by fraud. As a result of these observations, one or more furnishers have taken action to comply with the Regulation V requirements to establish and implement reasonable written policies and procedures regarding the accuracy and integrity of information furnished to nationwide CRCs.

Regulation V requires furnishers to consider and incorporate, as appropriate, the guidelines in Appendix E of Regulation V.[19] Examiners found that one or more furnishers of deposit account information failed to consider the guidelines in Appendix E of Regulation V. For example, such guidance states that a furnisher's policies and procedures should consider and incorporate, as appropriate, conducting "reasonable investigations of consumer disputes and take appropriate action based on the outcome of such investigations." However, the policies of one or more furnishers did not consider and incorporate such guidance. Based on examiner findings, one or more furnishers have taken action to consider and incorporate, as appropriate, the guidance in Appendix E of Regulation V.

2.5 Mortgage origination

Supervision continues to examine both forward and reverse mortgage origination activities for compliance with various Federal consumer financial laws, including the Truth in Lending Act and its implementing regulation, Regulation Z.

2.5.1 Inaccurate APR and TALC disclosures in reverse mortgage transactions

Regulation Z requires creditors to disclose the annual percentage rate (APR) in accordance with either the actuarial method or the U.S. Rule method.[20] The explanations, equations, and

[19] 12 CFR 1022.42(b), Appendix E.

[20] 12 CFR 1026.22(a)(1).

instructions for determining the APR in accordance with the actuarial method are set forth in Appendix J to 12 CFR Part 1026.[21]

Appendix J provides that the unit-period for a single advance, single payment transaction, for the purposes of determining the APR, shall be the term of the transaction, but shall not exceed one year.[22] In all other transactions, the unit-period shall be the common period that occurs most frequently in the transaction unless an exception applies.[23]

Generally, by its terms, a closed-end reverse mortgage is a single advance, single payment transaction because it includes a single lump-sum advance at origination and a single payment due at the end of the loan term. Thus, per Appendix J and Regulation Z, the unit-period for the purposes of determining the APR for such a closed-end reverse mortgage, with a term greater than a year, is one year.

In addition to a single lump-sum advance at origination, some closed-end reverse mortgages may have multiple advances throughout the loan term. For example, a closed-end reverse mortgage with a life-expectancy set-aside (LESA) typically has a set number of semiannual advances for the payment of property taxes, and flood and hazard insurance premiums. Thus, per Appendix J and Regulation Z, the unit-period for the purposes of determining the APR for such a loan would be six months because that would be the common period that occurs most frequently in the transaction.

In addition, Regulation Z states that the APR shall be considered accurate for a regular transaction if it is not more than 1/8 of one percentage point above or below the APR determined in accordance with section 1026.22(a)(1).[24] Likewise, the APR shall be considered accurate for an irregular transaction if it is not more than 1/4 of one percentage point above or below the APR determined in accordance with section 1026.22(a)(1).[25]

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[21] *Id.*

[22] 12 CFR Part 1026, App. J(b)(4)(ii).

[23] 12 CFR Part 1026, App. J(b)(4)(i).

[24] 12 CFR 1026.22(a)(2).

[25] 12 CFR 1026.22(a)(3).

In one or more examinations, examiners observed that creditors were disclosing inaccurate APRs for closed-end reverse mortgages. Specifically, while conducting loan file reviews, examiners observed creditors using a unit-period of one month instead of one year to calculate the APR, leading to inaccurate calculations outside of Regulation Z's permissible tolerances.[26] In response to this finding, the creditors have revised their calculation methodology to reflect the correct unit-period and provided affected consumers with reimbursements.

Examiners also found creditors disclosing inaccurate APRs for closed-end reverse mortgages with a LESA. While conducting loan file reviews, examiners observed creditors using a unit-period of one month instead of six months to calculate the APR, leading to inaccurate calculations outside of Regulation Z's permissible tolerances.[27] In response to this finding, the creditors have revised their calculation methodologies to reflect the correct unit-period.

Examiners observed similar issues in relation to the calculation of the total annual loan cost (TALC). Regulation Z requires that, in a reverse mortgage transaction, the creditor provide a good-faith projection of the total cost of credit, determined in accordance with paragraph (c) of this section and expressed as a table of "total annual loan cost rates," in accordance with Appendix K of 12 CFR Part 1026.[28]

Per Appendix K, the unit-period for a single advance, single payment transaction, for the purposes of determining the TALC rate, shall be the term of the transaction, but shall not exceed one year.[29] Both a closed-end reverse mortgage and an open-end reverse mortgage with a line of credit are single advance, single payment transactions, even though the latter may have multiple advances over the loan term.[30] Accordingly, the appropriate unit-period for such transactions when determining the TALC rate and the future value of all advances, a variable of the TALC equation, is one year. While conducting loan file reviews, examiners observed creditors using a unit-period of one month instead of one year to calculate the TALC rate and the future value of all advances, leading to inaccurate TALC disclosures. In response to these findings, the creditors have revised their calculation methodologies to reflect the correct unit-period.

[26] 12 CFR 1026.22(a)(2) and (3).

[27] *Id.*

[28] 12 CFR 1026.33(b)(2).

[29] 12 CFR Part 1026, App. K(b)(4)(ii).

[30] 12 CFR Part 1026, App. K(b)(9) (Regulation Z treats such open-end reverse mortgages with a line of credit as single advance, single payment transactions for purposes of calculating the TALC).

3. Supervision program developments

3.1 Recent Bureau rules and guidance

3.1.1 Small entity compliance guide

On June 28, 2019, the Bureau updated the small entity compliance guide summarizing the Payday Lending Rule's payment-related requirements. The guide has been updated to incorporate the changes that the Delay Final Rule made to the 2017 Payday Lending Rule.[31]

3.1.2 Memorandum of Understanding with the Federal Trade Commission

On February 26, 2019, the CFPB and the Federal Trade Commission (FTC) announced a new memorandum of understanding (MOU) between the agencies that went into effect on February 25, 2019.[32] The MOU, which facilitates cooperation and coordination on supervision, enforcement and consumer response activities, renews a previous MOU between the agencies, and is required by the CFPA.[33]

3.1.3 Amendment to the annual privacy notice requirement under the Gramm-Leach-Bliley Act (Regulation P)

On August 10, 2018, the CFPB published a final rule to implement a December 2015 statutory amendment to the Gramm-Leach-Bliley Act.[34] The rule provides an exception under which financial institutions that meet certain conditions are not required to provide annual privacy notices to customers. To qualify for this exception, a financial institution must not share

[31] There is currently a stay on the compliance date for the 2017 Payday Lending Rule.

[32] The MOU can be found here: https://www.consumerfinance.gov/documents/7302/cfpb_ftc_memo-of-understanding_2019-02.pdf.

[33] 12 USC 5514(c)(3)(A).

[34] The final rule can be found here: https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/amendment-annual-privacy-notice-requirement-under-gramm-leach-bliley-act/.

nonpublic personal information about customers except as described in certain statutory exceptions. In addition, the rule requires that the financial institution must not have changed its policies and practices with regard to disclosing nonpublic personal information from those that the institution disclosed in the most recent privacy notice it sent. As part of its implementation, the Bureau is also amending Regulation P to provide timing requirements for delivery of annual privacy notices in the event that a financial institution that qualified for this annual notice exception later changes its policies or practices in such a way that it no longer qualifies for the exception. The Bureau is also removing the Regulation P provision that allows for use of the alternative delivery method for annual privacy notices because the Bureau believes the alternative delivery method will no longer be used in light of the annual notice exception. The final rule went into effect on September 17, 2018.

4. Conclusion

The Bureau will continue to publish *Supervisory Highlights* to aid Bureau-supervised entities in their efforts to comply with Federal consumer financial law. The report shares information regarding general supervisory and examination findings (without identifying specific institutions, except in the case of public enforcement actions), communicates operational changes to the program, and provides a convenient and easily accessible resource for information on the Bureau's guidance documents.