

# Client Alert

September 2017

## HMDA Amendments and Agency Guidelines Provide Critical Framework for Examination Procedures

Financial institutions working toward the January 1, 2018, effective date of many key provisions of the 2015 Home Mortgage Disclosure Act (HMDA) Final Rule<sup>1</sup> should take note of two recent HMDA developments from the Consumer Financial Protection Bureau (the CFPB) and Federal Financial Institutions Examination Council (FFIEC). On August 24, 2017, the CFPB issued a final rule (the 2017 HMDA Amendment)<sup>2</sup> amending and clarifying certain requirements of the 2015 HMDA Final Rule, including an adjustment to the HELOC reporting threshold. Simultaneous with the 2017 HMDA Amendment, the FFIEC issued HMDA Examiner Transaction Testing Guidelines (the Guidelines)<sup>3</sup> for all financial institutions that report HMDA data, making it the first time that there will be uniform HMDA guidelines for all federal HMDA supervisory agencies.

### Key Aspects of the 2017 HMDA Amendment

The 2017 HMDA Amendment temporarily changes the HELOC reporting threshold and also makes various clarifications and technical corrections. Specifically, the Amendment:

- Temporarily increases the threshold for collecting and reporting data with respect to open-end lines of credit from 100 to 500 for the 2018 and 2019 calendar years. Financial institutions, such as community banks and credit unions, originating between 100 and 499 open-end lines of credit in either of the two preceding years will benefit from this temporary exemption by not being required to begin collecting HMDA data for open-end lines of credit until January 1, 2020. In the meantime, the CFPB will consider whether another rulemaking is necessary to address the appropriate open-end threshold for data that is collected beginning January 1, 2020;
- Establishes transition rules for two data points, loan purpose and the unique identifier for the loan originator, in connection with reporting purchased loans that were originated prior to certain regulatory requirements' taking effect;
- Establishes a new reporting exclusion and optional reporting for New York Consolidation, Extension and Modification Agreements (CEMA). Covered financial institutions generally will not be required to report any preliminary transaction where a consumer borrower receives additional funds prior to consolidation into a CEMA. However, financial institutions will still be required to report the CEMAs;

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<sup>1</sup> The 2015 HMDA Final Rule may be found on the CFPB website at <http://www.consumerfinance.gov/regulatory-implementation/hmda>.

<sup>2</sup> The 2017 HMDA Amendment may be found on the CFPB website at <http://www.consumerfinance.gov/regulatory-implementation/hmda>.

<sup>3</sup> The Guidelines may be found at <https://www.consumerfinance.gov/about-us/blog/heres-what-you-need-know-about-new-ffiec-hmda-examiner-transaction-testing-guidelines/>.

- Provides clarification surrounding two categories of transactions that are excluded as temporary financing and not reported in HMDA data: (1) a construction-only loan or line of credit that is extended to a consumer borrower solely to construct a dwelling for sale; and (2) a loan or line of credit designed to be replaced by separate permanent financing extended by any financial institution to the same consumer borrower at a later time;
- Makes clear certain key terms defined in the 2015 HMDA Final Rule, including multifamily dwelling and automated underwriting system, among others; and
- Sheds light on three aspects of collecting and reporting race and ethnicity information, including: (1) that an applicant is not required to select an aggregate race or ethnicity category as a precondition to selecting one of the race or ethnicity subcategories; (2) that an applicant may provide a particular other ethnicity or race in the free-form field, whether or not the applicant selects the “Other” ethnicity or race subcategory; and (3) how a financial institution should report ethnicity if an applicant selects more than five ethnicity categories and subcategories combined.

### **Key Aspects of the Guidelines**

The FFIEC, which includes the CFPB, the Board of Governors of the Federal Reserve System (Federal Reserve), the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), the Office of the Comptroller of the Currency (OCC) and the State Liaison Committee, issued its HMDA Examiner Transaction Testing Guidelines on August 22, 2017. The Guidelines, which apply for examinations under the new HMDA data collection requirements effective January 1, 2018, describe how to validate the accuracy of the HMDA data and the circumstances in which the examiners may ask financial institutions to correct and resubmit HMDA data. For example, the Guidelines:

- Remove the file error resubmission threshold under which a financial institution would be asked to correct and resubmit its entire Loan Application Register (LAR) if the number of sample files with one or more errors equaled or was more than a specific threshold;
- Create, for the purpose of counting errors toward the field error resubmission threshold, allowable tolerances for certain data fields; and
- Provide a less stringent 10 percent field error resubmission threshold for financial institutions, such as community banks or credit unions, with LAR counts of 100 or less.

### **HMDA Data in Regulatory Actions**

The FFIEC’s Guidelines are critical for financial institutions as they will serve as a roadmap for future examination procedures and the basis for potential regulatory actions. Beginning in January 2018, the 2015 HMDA Final Rule requires financial institutions to report 48 different data fields on each consumer borrower. Undoubtedly, the enhanced HMDA data that will be required as part of the 2015 HMDA Final Rule and 2017 HMDA Amendment will be actively used by regulators to conduct more robust analyses of potential fair lending and Community Reinvestment Act (CRA) risks, with additional requirements on collecting information about the applicant’s or borrower’s ethnicity, race and sex, including “visual observations” by institutions. Indeed, we have already seen a steady uptick in regulatory focus on redlining issues, and with the trove of new data that will soon be available for regulators, we expect regulators to aggressively analyze this data for potential redlining indicators, monitor housing trends and evaluate lending patterns. As such, it is essential that financial institutions are well aware of these recent amendments and make every effort to adapt their policies, procedures and monitoring practices to the Guidelines, as the regulators certainly will be expecting them to do so.

## Takeaways

While the CFPB's HMDA amendments and FFIEC's Guidelines certainly reflect regulators' continuing focus on ferreting out potentially unfair or discriminatory lending patterns or practices, institutions also now have the opportunity to proactively use the Guidelines to prepare for their next examination. Institutions should incorporate the Guidelines into their routine procedures to validate the accuracy of their HMDA data. Institutions should further alter their routine monitoring practices to conduct HMDA transaction testing in line with the Guidelines or retain outside consultants to do so. By doing so, institutions then have the opportunity to promptly and voluntarily take corrective action or address potential concerns—potential mitigating factors in future regulatory exams. In sum, while these changes reflect a framework for potential regulatory action, they also, for the first time, provide a uniform and transparent framework that institutions can use to proactively mitigate against future regulatory risk.

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