



# Assessing Fair Lending Compliance Risk

Todd Proebsting and Linda Morris

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- A professional services firm with three distinct business lines
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  - Audit, Tax, and Consulting
- 3,600 employees
- Offices coast to coast
- Serve more than 1,100 financial institutions



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# Speaker Introductions

## Todd Proebsting

Todd serves as a Managing Consultant in the Financial Institutions Group at CLA. Mr. Proebsting has over 10 years of experience providing attest and consulting services to financial institutions ranging in size from \$20 million to over \$12 billion. Todd's areas of expertise include internal audit, regulatory compliance, loan review, and information technology.

Bachelor of Science Degree in Business Administration, Lincoln University, Jefferson City, Missouri

## Linda Morris

Linda serves as a Regulatory Compliance Consultant in the Financial Institutions Group at CLA. Ms. Morris has more than 18 years of experience serving community banks. Prior to joining CLA Linda served as Compliance Officer at First Kentucky Bank, Mayfield Kentucky. Ms. Morris areas of expertise include fair lending, technical compliance regulations and compliance management systems.

Certified Regulatory Compliance Manager (CRCM),  
Certified Community Bank Compliance Officer (CCBCO)



# Learning Objectives

At the end of this session, you will be able to:

- Describe the current regulatory environment related to fair lending
- Recognize the importance of having a comprehensive fair lending compliance program
- Identify the risks associated to fair lending





# Assessing Fair Lending Risk



# Fair Lending Risk

**Defining risk** – The risk of fair lending violations.

## **Risk segments**

- Marketing activities
- Credit administration practices
- Controls for underwriting and pricing exceptions
- Use of third parties (i.e. loan originators or processors)
- Technical Regulation B, Fair Housing and HMDA compliance
- Current regulatory environment



# Fair Lending Risk Assessment

**Purpose of Risk Assessment** – To logically measure and communicate risk using inherent and relative risk factors

**Risk profile** – Inherent risk in your lending processes

- Pre-application processes
- Application processes
- Servicing processes



# Fair Lending Risk Assessment Factors

## Inherent risk assessment factors

Financial \* Liquidity \* Operational/Transactional  
Compliance \* Reputation/Litigation \* Foreign

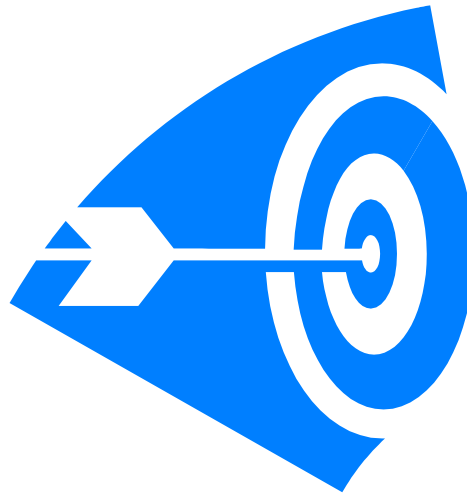


# Fair Lending Risk Assessment Factors

## Relative risk assessment factors

Internal Controls \* Management & Staff

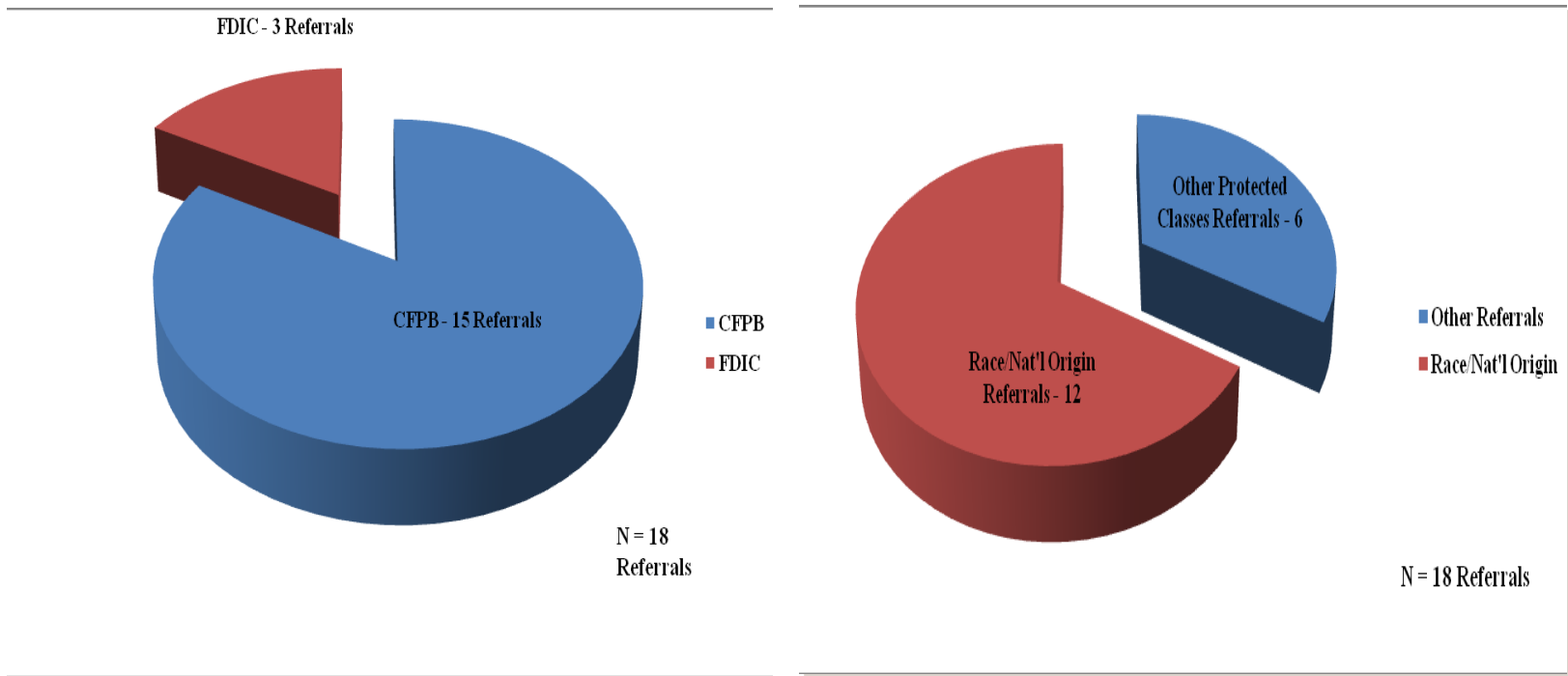
Dollar Exposure \* Products & Systems





# Current Regulatory Environment

# 2014 Lending Referrals to DOF by Agency and Protected Class\*



\* The Attorney General's 2014 Annual Report to Congress Pursuant to the Equal Credit Opportunity Act Amendments

# MOST FREQUENTLY CITED REGULATION B VIOLATIONS BY FFIEC AGENCIES: 2014\*

\* FAIR LENDING REPORT OF THE  
CONSUMER FINANCIAL PROTECTION  
BUREAU, APRIL 2014

## FFIEC Agencies Reporting

CFPB, FDIC, FRB, NCUA, OCC

## Regulation B Violations: 2014

12 C.F.R. § 1002.4(a): Discrimination on a prohibited basis in a credit transaction.

12 C.F.R. §§ 1002.5(b), (d): Improperly requesting information about an applicant's race, color, religion, national origin, sex, marital status or source of income.

12 C.F.R. § 1002.7(d)(1): Improperly requiring the signature of an applicant's spouse or other person.

12 C.F.R. §§ 1002.9(a)(1), (a)(2), and (b)(2): Failure to timely notify an applicant when an application is denied; failure to provide sufficient information in an adverse action notification, including the specific reasons the application was denied.

12 C.F.R. §§ 1002.13(a) and (b): Failure to request and collect information about the race, ethnicity, sex, marital status, and age of applicants seeking certain types of mortgage loans.



# Recent Federal Reserve Referrals

In recent years the Federal Reserve has referred a number of matters to the DOJ, including matters regarding:

## ✓ Redlining

## ✓ Pricing

- Mortgages
- Direct and Indirect Auto Loans
- Unsecured loans

## ✓ Underwriting

- Maternity Leave Discrimination
- Disability /Public Assistance Discrimination





# Redlining

“Redlining is a form of illegal disparate treatment in which a lender provides unequal access to credit, or unequal terms of credit, because of the race, color, national origin, or other prohibited characteristic(s) of the residents of the area in which the credit seeker resides or will reside or in which the residential property to be mortgaged is located.”

[Interagency Fair Lending Examination Procedures](#)



# Referrals

## **9/24/2015 Hudson City Savings Bank, NJ, penalty for mortgage redlining**

This referral was the result of investigations by DOJ and CFPB into the Bank's lending practices in certain majority-Black and Hispanic areas within the metropolitan statistical areas served by the Bank from 2009 to 2013.

The proposed consent order includes a loan subsidy fund of \$25 million for future lending in the redlined areas, \$5.5 million in civil monetary penalties, \$2.25 million in advertising, outreach, and community partnerships and two new full-service branches to serve the redlined areas.



# Pricing Risks for Indirect Auto Lending

## CFPB Bulletin 2031-02 – Indirect Auto Lending and Compliance with the Equal Opportunity Act

- Three-party transaction: consumer, auto dealer, bank
- Fair lending risks arise where:
  - Bank and dealer have financial incentives to mark up the contract interest rate above the buy rate
  - Bank grants the dealer discretion to set the contract interest rate
  - Bank does not monitor the pricing across its portfolio



# Referrals

## **09/28/2015 Fifth Third Bank - Auto-Lending Discrimination and Illegal Credit Card Practices**

The joint CFPB and Department of Justice (DOJ) auto-lending enforcement action requires Fifth Third to change its pricing and compensation system to minimize the risks of discrimination, and to pay \$18 million to harmed African-American and Hispanic borrowers.

## **7/16/15 U.S. vs. American Honda Finance Corp.**

Complaint alleges lender charged minority borrowers higher interest rate markups on indirect auto loans  
\$24 million settlement fund –administered jointly with CFPB  
\$1 million financial literacy fund –only with DOJ



# Maternity Leave Discrimination

The U.S. [Department of Housing and Urban Development](#) states that since 2010, there has been a steady stream of complaints alleging discrimination against borrowers who are on maternity leave. In these cases, lenders allegedly denied or delayed loans to working women because they were pregnant or on maternity leave.

In some instances, a lender allegedly treated women differently by requiring women to end their maternity leave and return to work in order to be approved for a loan.



# Referrals

## 9/12/14 FirstBank to Pay \$35,000 in Maternity Leave Discrimination Case

FirstBank Mortgage Partners in Jackson, Tenn., agreed to pay \$35,000 to settle allegations that it violated the Fair Housing Act by denying a mortgage loan to an applicant on maternity leave.

The Agreement resolves a discrimination complaint filed with HUD by a married couple that alleged FirstBank approved their mortgage application, scheduled the loan closing, and then within 24 hours of learning the wife was on maternity leave, notified them the loan was denied, according to HUD.



# Mortgage Loan Origination referrals

## 6/4/2015 RPM Mortgage to pay \$18 million in consumer redress for steering borrowers into costlier mortgages

The CFPB took action against RPM Mortgage, Inc. and its CEO, Erwin Robert Hirt, for illegally paying bonuses and higher commissions to loan originators to incentivize them to steer consumers into costlier mortgages. RPM is required to pay \$18 million in redress to consumers and a \$1 million civil penalty, and Hirt is required to pay an additional \$1 million civil penalty.



# 2015 Civil Money Penalties by Bank Agencies/ DOJ / FTC

Number of CMPs	Penalty Type	Dollar Amount	Issued By
4	BSA/AML	\$40,500,000	FinCen, FDIC DOJ, SEC
1	Fair Lending	\$32,750,000	CFPB, DOJ
22	Flood	\$1,603,560	FRB FDIC, OCC
6	UDAP/UDAAP	\$547,100,000 (plus restitutions)	CFPB, DOJ FDIC, FTC







# Fair Lending Compliance Program

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## Common features of a well-developed fair lending compliance program:

- Current fair lending policy
- Comprehensive fair lending training
- Monitoring for compliance with policies and procedures including underwriting and pricing/terms exception tracking



# Fair Lending Compliance Program

## Common features of a well-developed fair lending compliance program:

- Periodic review of lending policies and procedures
- Regular statistical analysis of loan data
- Assessment of marketing materials



# Fair Lending Compliance Program

## Common features of a well-developed fair lending compliance program:

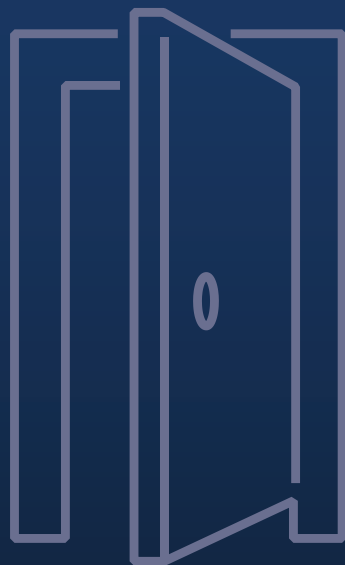
- Strong board and management oversight
- Effective reporting
- Independent testing



# Resources

- [CFPB Supervisory Highlights](#)
- [Department of Justice Housing and Civil Enforcement Cases](#)
- [U.S. Department of Housing and Development Fair Housing Act Enforcement Activity](#)
- Federal Reserve's Step-By-Step Guide to Coding for Gender and Ethnicity:  
<https://consumercomplianceoutlook.org/outlook-live/2013/indirect-auto-lending/>





# Thank you!

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