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Office of Thrift Supervision
Department of the Treasury
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Executive Director, Supervision

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Any attachments to this document are rescinded only as they relate to national banks and federal savings associations.

MEMORANDUM FOR: Chief Executive Officers

FROM: John Downey
Executive Director, Supervision

SUBJECT: Common Compliance Violations

Many thrift institutions have asked us for information, observations, and trends about our compliance examination experiences, particularly relating to commonly cited regulatory violations. In response, and as part of our Customer Service Plan for Examinations, we thought it would be useful to provide you with a listing of common violations noted during our 1996 and 1995 compliance examinations, and describe our compliance examination approach. We also offer general observations on possible causes of regulatory violations, suggestions for correcting them, and ways to prevent future occurrences.

We believe this information can be used by your board of directors and senior management to establish or enhance an effective compliance program. It can also be used by compliance officers to pinpoint areas of particular concern, or identify significant or interesting trends.

The information on specific violations can also be a valuable tool for those individuals in your institution whose responsibilities include compliance matters. For example, an internal auditor may observe an increasing number of violations of the flood insurance purchase requirements. The internal auditor could then discuss with the compliance officer reasons for the increasing number of violations and include this particular area in compliance reviews.

Review of Common Compliance Violations

We concentrated our review of commonly cited violations (attached) on information contained in 1995 and 1996 compliance reports of examination. However, we found no material difference between the regulatory violations cited in those reports and reports completed in 1993 and 1994. Our discussion focuses on violations that were cited either a significant number of times or in a significant number of institutions.

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Possible Causes

Based on our analysis, we believe that most of the violations identified are generally attributable to one or more of the following factors:

- insufficient training of personnel;
- lack of management oversight;
- weak internal controls; and
- outmoded policies and procedures.

While these causes appear to be general in nature, they are typical of institutions in a less than satisfactory compliance position, and also may indicate that management has not devoted sufficient time and attention to its compliance responsibilities. For example, insufficient training may explain why the compliance officer does not fully understand the technical requirements to accurately complete a Currency Transaction Report, but lack of management oversight may explain why the inaccuracies were not identified prior to a compliance examination. Similarly, a well developed set of internal procedures should identify any required reports, such as those mandated by the U.S. Treasury's Bank Secrecy Act regulations.

Examination Approach

The purpose and goal of a compliance examination is to determine the extent and effectiveness of an institution's management efforts toward assuring compliance with consumer protection laws and regulations, and maintaining a solid, operational, and viable internal compliance program. Compliance examinations are conducted using a "top-down/risk-focused" approach. This approach, which is also used to perform safety and soundness examinations, places emphasis on an institution's demonstrated ability to manage its compliance responsibilities. This approach generally involves the comprehensive review and analysis of internal policies, procedures, and review programs as a basis for assessing compliance with the consumer protection and public interest laws and regulations, particularly those that fall within high risk and high sensitivity areas. After formulating an initial assessment of an institution's overall compliance efforts from a comprehensive review of policies and the like, the examiner tests the integrity of the internal compliance program thorough limited sampling of various selected transactions on a risk-basis. The examiner evaluates compliance generally by focusing on high profile areas and limits the review of other laws and regulations to the extent necessary to evaluate the compliance posture of the institution.

Solutions

Our experience shows that most thrift institutions have implemented an effective compliance program with strong board of directors and senior management support, and enjoy a satisfactory compliance position. An effective compliance program:

- defines the responsibilities and authority of a designated compliance officer;
- provides for the dissemination of compliance information to front-line personnel;

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- provides for periodic review of each compliance area with emphasis placed on high risk areas;
- addresses routine monitoring and internal controls;
- establishes a system for reporting the results of compliance reviews to the board of directors; and,
- sets forth procedures for ensuring that deficiencies are corrected.

We recognize that most institutions have made significant efforts to implement effective compliance programs. Nevertheless, we believe this information in this memorandum can be a valuable resource to educate the industry on compliance issues.

We hope this information is useful. Further information about our compliance examination program can be found in the OTS Compliance Activities Handbook which was recently revised and sent to your attention. If you have any questions or suggestions, please contact Gary C. Jackson of our Compliance Policy staff at (202) 906-5653, or Regional Compliance staff.

Attachment

COMMON COMPLIANCE VIOLATIONS CITED DURING 1995 AND 1996 OTS COMPLIANCE EXAMINATIONS

A. Equal Credit Opportunity Act (Regulation B, 12 CFR 202)

The most commonly cited violations of Regulation B involve the adverse action notification provisions in §202.9, and the monitoring information collection requirements in §202.13.

Common violations of the adverse action notification provisions include late or incomplete notices. Under §202.9(a)(1)(i), a creditor must notify an applicant of action taken within 30 days of receiving a completed application for credit. Also, under §202.9(a)(2), the notification of adverse action must contain a statement of the action taken, the name and address of the creditor, the ECOA notice under section 701(a) of the act, and the name and address of the creditor's enforcement agency (in the case of thrift institutions, the Office of Thrift Supervision).

Common violations of the monitoring information collection requirements involve the failure to request, as part of the application, information pertaining to the race, sex, marital status, and age of the applicant(s). Under §202.13(a), this information is to be requested in connection with applications for credit primarily for the purchase or refinancing of a dwelling occupied or to be occupied as a principal residence by the applicant(s), and that will be secured by the dwelling. This violation also has carry-over effects to regulations implementing the Home Mortgage Disclosure Act, which requires creditors to record this information on loan/application registers.

B. OTS Non-discrimination Regulations (12 CFR 528)

The most commonly cited violations of the OTS Nondiscrimination regulation include the nondiscriminatory advertising requirements in §528.4, and the nondiscriminatory loan underwriting standards in §528.2a(b).

Common violations of the nondiscriminatory advertising requirements involve the failure to include the equal housing lender logotype and legend on advertisements other than for savings. Section 528.4 details these regulatory requirements.

Common violations of the nondiscriminatory loan underwriting standards include the failure to make clearly written, nondiscriminatory loan underwriting standards available to the public upon request under §528.2a(b). Also, under §528.2a(b), a creditor must, at least annually, review its standards and business practices to ensure equal opportunity in lending.

C. Home Mortgage Disclosure Act (Regulation C, 12 CFR 203)

The most commonly cited violation of Regulation C pertains to the loan application register (LAR) provisions in §203.4.

Common violations of the LAR provisions include incomplete and inaccurate data. For example, information pertaining to property location and applicant information may have been omitted, or the type and date of action taken may be incorrect. Under §203.4(a), a creditor must collect data regarding applications for, and originations and purchases of, home purchase and home improvement loans (including refinancings of both) for each calendar year. Section 203.4(a) also requires that the data collected be presented on a register in a certain format.

D. Fair Credit Reporting Act (15 USC 1681)

The most commonly cited violation of the Fair Credit Reporting Act pertains to incomplete notification requirements.

Under §615(a), whenever credit or insurance for personal, family or household purposes is denied or the charge for such credit or insurance is increased either wholly or partly because of information contained in a consumer report from a consumer reporting agency, the user of the consumer report must notify/advise the consumer against whom such adverse action has been taken and supply the name and address of the consumer reporting agency making the report.

E. Truth in Lending Act (Regulation Z, 12 CFR 226)

The most commonly cited violations of Regulation Z pertain to the finance charge and APR disclosure requirements in §§226.18(d) and 226.22(a); respectively.

Common violations of the finance charge and APR disclosures include inaccurate or understated disclosures. While there seem to be a number of causes for these violations, common causes include failure to properly treat PMI premiums, erroneous treatment of interim interest on construction loans, not making proper credit life disclosures, or not handling discounted ARMs correctly. Typically, some of these errors lead to other disclosure errors. For example, an incorrect finance charge may affect the amount financed and the repayment schedule.

F. OTS Mortgage Regulation (12 CFR 560.210)

The most commonly cited violations of the OTS Mortgage regulation involve the adjustment notice requirements in §560.210(c), and the initial disclosure requirements for adjustment rate loans in §560.210(b).

Common violations of the adjustment notice requirements include incomplete notices (e.g., information regarding the current and prior index values, and interest rates). Under §560.210(c), an adjustment notice must include the following:

- the current and prior interest rates;
- the index values upon which the current and prior interest rates are based;
- the extent to which the creditor has forgone any increase in the interest rate;
- the contractual effects of the adjustment, including the payment due after the adjustment is made, and a statement of the loan balance; and,
- the payment that would be required to amortize fully the loan at the new interest rate over the remainder of the loan terms.

Common violations of the initial disclosure requirements include incomplete disclosures. Under §560.210(b), a creditor must provide a loan program disclosure for each adjustable-rate home loan program in which a consumer expresses an interest.

G. Real Estate Settlement Procedures Act (HUD Regulation X, 24 CFR 3500)

The most commonly cited violations of Regulation X involve the mortgage servicing transfer disclosure provisions in §3500.21, and the Good Faith Estimate (GFE) requirements in §3500.7.

Common violations of the mortgage servicing transfer disclosure provisions include the failure to provide the required disclosure statement. Under §3500.21(b)(1), at the time an application for a mortgage loan is submitted, or within 3-business days after submission of the application, the lender or mortgage broker who anticipates using table funding, or dealer who anticipates a first-lien dealer loan must provide to each person who applies for such a loan a servicing disclosure statement.

Common violations of the GFE requirements involve the failure to include information on a particular provider of a settlement service. Under §3500.7(e), if a creditor requires the use of a particular provider for a settlement service, other than the creditor's own employees, and also requires the borrower to pay any portion of the cost of such service, then the GFE must:

- clearly state that use of the particular provider is required and that the estimate is based on the charges of the designated provider;
- give the name, address, and telephone number of each provider; and,
- describe the nature of any relationship between each such provider and the creditor.

H. Electronic Fund Transfer Act (Regulation E, 12 CFR 205)

The most commonly cited violation of Regulation E pertains to the error resolution procedures in §205.11.

Common violations of the error resolution procedures involve adherence to the timing requirements for investigation of errors.

Section 205.11(c) contains the procedures and timing rules an institution must follow to resolve an alleged error.

I. Truth in Savings (Regulation DD, 12 CFR 230)

The most commonly cited violation of Regulation DD pertains to the advertising requirements in §230.8(a).

Common violations of the advertising requirements involve misleading or inaccurate advertisements.

Under §230.8(a), an advertisement must not be misleading or inaccurate and must not misrepresent an institution's deposit contract. For example, an institution may not use the term "profit" (which implies a return on investment) in its advertisements, or the terms "free" or "no cost" to describe an account if a maintenance or account fee might be imposed on the account.

J. Expedited Funds Availability (Regulation CC, 12 CFR 205)

The most commonly cited violations of Regulation CC involve the exception notice requirements in §229.13(g)(1), and the large deposit exception provisions in §229.13(b).

Common violations of the exception notice requirements include late or incomplete notices. Under §229.13(g)(1), whenever a creditor exceeds the maximum hold periods in the availability schedules, it must notify the customer in writing. Also, under §229.13(g)(1), a creditor has two options for sending notices. The first allows a creditor to send a notice that includes the following:

- the account number of the customer;
- the date and amount of the deposit;
- the amount of the deposit that is being delayed;
- the reason the exception was invoked; and,
- the time period within which the funds will be available for withdrawal.

The second option allows a creditor to provide the notice at the same time the deposit is made at a staffed facility. If the deposit is not made at a staffed facility, then the notice may be mailed to the customer no later than the business day following the banking day of deposit. However, if a creditor discovers a reason to delay the funds subsequent to the time the notice should have been given, the creditor must notify the customer as soon as possible, but no later than the business day after the facts become known.

K. Bank Secrecy Act (31 CFR 103)

The most commonly cited violation of the Bank Secrecy Act regulation pertains to the Currency Transaction Report (CTR) requirements in §103.27(d).

Common violations of the CTR requirements include incomplete and inaccurate CTRs. For example, an institution may have omitted information pertaining to the person(s) involved in the transaction(s) or the amount and type of the transactions(s). Under §103.27(d), CTRs must be filed on forms prescribed by the Secretary of the U.S. Treasury. Also, under §103.27(d), all information called for in such forms must be furnished.

L. Bank Protection Act (12 CFR 568)

The most commonly cited violation of the Bank Protection Act regulation pertains to the annual security report provision in §568.4.

Common violations of the security report provision include the failure to report the status of an institution's security program to the board of directors.

Under §568.4, a security officer must report at least annually to the institution's board of directors on the implementation and effectiveness of the security program.