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THE HOME MORTGAGE DISCLOSURE ACT: COMMON COMPLIANCE CHALLENGES

In their discussion of common challenges in HMDA reporting, the authors focus on transactions with multiple parties, business purpose loans, required reportable actions, and automated underwriting systems. They also discuss the combined loan-to-value ratio, and the collection and reporting of demographic data. They conclude by describing how the Bureau of Consumer Financial Protection evaluates the compliance management systems of the institutions it supervises.

By Sherry-Maria Safchuk and Frida Alim *

Since 2015, financial institutions have been inundated with reviewing and implementing numerous changes to the Home Mortgage Disclosure Act ("HMDA") as required by the Dodd-Frank Act. The act transferred HMDA rulemaking authority to the Bureau of Consumer Financial Protection ("Bureau"), added new data points, and authorized the Bureau to require additional information from covered institutions.[1] Specifically, in 2015, the Bureau issued the 2015 HMDA Final Rule implementing the Dodd-Frank Act amendments to HMDA through Regulation C.[2] In 2017, the Bureau amended Regulation C to clarify certain requirements adopted by the Final Rule and to temporarily increase the loan threshold that is used to determine which financial institutions must collect and report loan data under HMDA.[3]

In May 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act (S. 2155) was signed into law, which modifies certain provisions of the Dodd-Frank Act, including HMDA. S. 2155 provides that banks and credit unions that originate fewer than 500 open-end lines of credit in each of the two preceding calendar years or 500 closed-end mortgage loans in each of the two preceding calendar years are exempt from

[1] *See generally* Bureau of Consumer Fin. Prot., New Rule Summary: Home Mortgage Disclosure (Regulation C) (Oct. 15, 2015), https://files.consumerfinance.gov/f/201510_cfpb_hmda-executive-summary.pdf/.

[2] Bureau of Consumer Fin. Prot., Home Mortgage Disclosure (Regulation C), Final Rule, 80 Fed. Reg. 66128 (Oct. 28, 2015).

[3] Bureau of Consumer Fin. Prot., Home Mortgage Disclosure (Regulation C), Final Rule, 82 Fed. Reg. 43088 (Sept. 13, 2017).

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HMDA's expanded data disclosures, although the exemption does not apply to nonbanks and does not exempt institutions from HMDA reporting altogether.[4] In July of 2018, the Bureau, the Federal Reserve Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the National Credit Union Administration issued similar statements to clarify that S. 2155 only provides partial exemptions to certain insured depository institutions and insured credit unions.[5] The agencies explained that the partial exemptions would be generally available to such institutions for closed-end mortgage loans and open-end lines of credit when the institutions' transactions did not meet the thresholds specified above.[6] They further clarified that while the requirements of HMDA section 304(b)(5) and (6) (expanded data disclosure requirements) would not apply to these transactions, the institutions would still need to report some of the data points specified in Regulation C.[7] The Bureau stated that it plans to provide further guidance later in the summer on the applicability of S. 2155 to HMDA data collected in 2018.[8]

HMDA was originally enacted to help "citizens and public officials . . . determine whether depository institutions are filling their obligations to serve the housing needs of the communities and neighborhoods in which they are located" and help officials allocate public-sector investments by providing information to the public about lending patterns.[9] HMDA's development since it was originally enacted in 1975 has been driven by dramatic changes in the mortgage industry, and criticism of how the mortgage industry serves low-income communities and members of minority groups.[10] And while the basic objectives and structure of HMDA have largely stayed the same, the types of data and institutions subject to HMDA reporting requirements have expanded substantially since its enactment.[11] The result is a statute the Bureau has recognized as serving the following key functions: (i) providing information regarding whether institutions — both depository institutions and other mortgage lenders — are serving the housing needs of communities where they are located, (ii) assisting with the distribution of public sector investments to improve the public investment environment, (iii) identifying discriminatory lending, and (iv) providing a source of information for

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[4] *See* 12 U.S.C. § 2083(i).

[5] *See* Bureau of Consumer Fin. Prot., Bureau of Consumer Financial Protection Issues Statement on the Implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act Amendments to the Home Mortgage Disclosure Act (July 5, 2018), https://www.consumerfinance.gov/about-us/newsroom/bureauconsumer-financial-protection-issues-statement-implementation-economic-growth-regulatory-relief-and-consumer-protection-act-amendments-home-mortgage-disclosure-act/; Fed. Reserve Board, CA 18-6, Statement on the Implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act Amendments to the Home Mortgage Disclosure Act (July 5, 2018), https://www.federalreserve.gov/supervisionreg/caletters/caltr1806.htm; Off. of the Comptroller of the Currency, OCC Bull. 2018-19, Statement on the Implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act Amendments to the Home Mortgage Disclosure Act (July 5, 2018), https://www.occ.treas.gov/newsissuances/bulletins/2018/bulletin-2018-19.html; Fed. Deposit Ins. Corp., FIL-36-2018, Statement on the Implementation of the Economic Growth, Regulatory Relief and Consumer Protection Act Amendments to the Home Mortgage Disclosure Act (July 5, 2018), https://www.fdic.gov/news/news/financial/2018/fil18036a.pdf; Nat'l Credit Union Admin., Information About the Recent Changes to the Home Mortgage Disclosure Act (July 5, 2018), https://www.ncua.gov/regulation-supervision/Documents/recent-changes-hmda-july-2018.pdf.

[6] *Id.*

[7] *Id.*

[8] Bureau of Consumer Fin. Prot., Bureau of Consumer Financial Protection Issues Statement on the Implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act Amendments to the Home Mortgage Disclosure Act (July 5, 2018).

[9] 80 Fed. Reg. at 66166.

[10] Joseph M. Kolar and Jonathan D. Jerison, *The Mortgage Disclosure Act: Its History, Evolution, and Limitations*, ("*HMDA History, Evolution, and Limitations*"), 59 Consumer Fin. L.Q. Rep. 189 (2005).

[11] For an overview of the history of HMDA, *see* Fed. Fin. Inst. Examination Council, History of HMDA (*last modified* Sept. 1, 2017), https://www.ffiec.gov/hmda/history2.htm; *HMDA History, Evolution, and Limitations,* note 5 *supra*.

those that analyze mortgage markets for HMDA or other purposes.[12]

In 2016 alone, 6,762 financial institutions reported data under HMDA on approximately 14 million home mortgage applications they received, of which 8.4 million resulted in origination.[13] The data provided by these HMDA disclosures offer valuable insight into mortgage outcomes by income, race, and ethnicity, including the distribution of home loans across demographic groups, the reasons for loan denials, and the frequency of loan denials.[14]

This article discusses common challenges to HMDA implementation and suggests measures financial institutions should take to comply with HMDA.

HMDA IMPLEMENTATION CHALLENGES[15]

Transactions involving multiple parties

When evaluating whether a financial institution has reporting obligations in a multi-party transaction, the institution must consider its relationship with the other parties, as well as each of their duties in the transaction. In a multi-party transaction, only one financial institution reports the originated covered loan as an origination.[16] On the other hand, more than one financial institution may report an application that does not result in an origination depending on the action taken by each institution.[17]

The 2015 Dodd-Frank Act amendments to Regulation C clarify and expand on the previous "broker rule," which explained the responsibilities of each institution in a multi-party transaction. Where multiple financial institutions are involved in loan origination, only the financial institution that made the credit decision "approving the application before closing or account opening, reports that loan as an origination."[18] Where multiple financial institutions are involved in a loan application that does not result in an origination, "a financial institution reports the action it took on that application if it made a credit decision on the application or was reviewing the application when the application was withdrawn or closed for incompleteness."[19] Regulation C provides an exception to this rule where the financial institution "ma[kes] the credit decision on a covered loan or application through the actions of an agent," as determined under state law.[20] In this situation, the financial institution, not the agent that made the credit decision on behalf of the financial institution, reports the loan as an origination.[21]

The Bureau's comments to section 1003.4 provide helpful illustrations for understanding reporting obligations in multi-party transactions where the financial institutions have no agency relationship.[22] Financial institutions should review the examples carefully to determine how to report applications and originations in multi-party transactions.

However, the Bureau commentary does not address all multi-party transactions that may occur. For example, a financial institution may work with other entities (*e.g.*, state housing agencies) that review the loans at issue prior to closing. Whether the financial institution has reporting responsibilities for these loans may depend upon several factors, including whether the review results in a credit decision being made on the loan and whether there is an agency relationship between the financial institution and the reviewing entity.[23] The guiding principle is that the financial institution that makes a credit decision — even when the credit decision

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[12] 80 Fed. Reg. at 66130.

[13] Bureau of Consumer Fin. Prot., FFIEC Announces Availability of 2016 Data on Mortgage Lending (Sept. 28, 2017), https://www.consumerfinance.gov/about-us/newsroom/ffiec-announces-availability-2016-data-mortgage-lending/.

[14] For a discussion of trends in the 2016 HMDA data, *see* Neil Bhutta et al., *Residential Mortgage Lending in 2016: Evidence from the Home Mortgage Disclosure Act Data*, Federal Reserve Bulletin, Vol. 103, No. 6 (2017).

[15] This article does not address HMDA implementation challenges for all the data points. Rather, it focuses on the implementation challenges that we have seen with some frequency.

[16] Supplement I to Part 1003, comment 4(a)-2.i.

[17] *See, e.g.*, *id.* at comment 4(a)-3.vii.

[18] *See, e.g., id.* at comment 2(g)-5 (providing thresholds for loan originations); *id.* at comment 4(a)-2 through -4. Note that in a multi-party transaction, determining which institution is considered the loan originator is also important to determine whether the party has originated sufficient loans to trigger the reporting thresholds based on the number of closed-end mortgage loans or open-end lines of credit originated by the institution. *See, e.g.,* 12 C.F.R. § 1003.2(g).

[19] Supplement I to Part 1003, comment 4(a)-2.ii.

[20] *Id*. at comment 4(a)-4.

[21] *Id*.

[22] *Id*. at comments 4(a)-2 through -3.

[23] *See, e.g., id*. at comments 4(a)-2 through -4.

is based on the criteria of a third-party insurer or guarantor — reports the application or loan origination.[24]

This is an area financial institutions should review closely to determine who should be reporting a transaction when many parties are involved. This is especially true for financial institutions in agency relationships, and/or relationships where multiple parties are reviewing the loan application and making a credit decision.

Reporting commercial transactions

Regulation C excludes certain transactions from coverage.[25] One such exclusion is for a closed-end mortgage loan or open-end line of credit that is or will be made primarily for a business or commercial purpose, unless the closed-end mortgage loan or open-end line of credit is a home improvement loan, a home purchase loan, or a refinancing.[26]

The first point of inquiry is whether the primary purpose of the loan or line of credit is for a business or commercial purpose under Regulation Z, 12 C.F.R. 1026.3(a).[27] If that is the primary purpose, the loan may be reportable if it meets the definition of a home improvement loan, a home purchase loan, or a refinancing.[28] The following are examples of loans or lines of credit that are primarily for a business or commercial purpose, but are covered by Regulation C:

- "A closed-end mortgage loan or an open-end line of credit to purchase or to improve a multi-family dwelling or a single-family investment property, or a refinancing of a closed-end mortgage loan or an open-end line of credit secured by a multi-family dwelling or a single-family investment property;"[29]
- "A closed-end mortgage loan or an open-end line of credit to improve a doctor's office or a daycare center that is located in a dwelling other than a multi-family dwelling;"[30] and
- "A closed-end mortgage loan or an open-end line of credit to a corporation, if the funds from the loan or line of credit will be used to purchase or to improve a dwelling, or if the transaction is a refinancing."[31]

If the commercial transaction is not a home improvement loan under section 1003.2(i), a home purchase loan under section 1003.2(j), or a refinancing under section 1003.2(p), it is not reported under Regulation C even if it is secured by a dwelling.[32] Note that if the commercial transaction meets the definition of a home purchase loan, a home improvement loan, or a refinancing, it still may be excluded under other provisions in section 1003.3(c), such as temporary financing in section 1003.3(c)(3).[33] Therefore, financial institutions should review their various product lines carefully to determine whether certain transactions are covered by HMDA and should be reported. Institutions should also pay close attention to the purpose of the transaction when applicants apply for a loan, and create policies and procedures to ensure that all the loans that are HMDA-reportable are accurately categorized and the information required for reporting is captured.

Once a financial institution determines that a particular commercial loan or line of credit is covered under Regulation C, it should be aware of the data points that must be reported. While some data fields are specific to commercial purpose loans or lines of credit, others do not need to be reported for these loans or lines of credit.[34] Institutions should review each data point to

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[24] *Id.*

[25] 12 C.F.R. § 1003.3(c) (listing excluded transactions).

[26] *Id.* at § 1003.3(c)(10).

[27] *Id.*; Supplement I to Part 1003, comment 3(c)(10)-2; 12 C.F.R. § 1026.3(a) (exempting an extension of credit primarily for a business, commercial, agricultural, or organizational purpose).

[28] 12 C.F.R. § 1003.3(c)(10); Supplement I to Part 1003, comment 3(c)(10)-1.

[29] Supplement I to Part 1003, comment 3(c)(10)-3.i.

[30] *Id.* at comment 3(c)(10)-3.ii.

[31] *Id.* at comment 3(c)(10)-3.iii.

[32] For examples of excluded business- or commercial-purpose transactions, *see id.* at comment 3(c)(10)-4.

[33] 12 C.F.R. § 1003.3(c)(3).

[34] *See, e.g.*, Supplement I to Part 1003, comment 4(a)(34)-1 (NMLSR reporting requirement not applicable to commercial-purpose loans in certain cases); *id.* at comment 4(a)(17)(i)-1 (total loan costs reporting requirement not applicable to commercial-purpose loans); *id.* at comment 4(a)(17)(ii)-1 (total points and fees reporting requirement not applicable to commercial-purpose loans); *id.* at comment 4(a)(19)-1 (discount points reporting requirement not applicable to commercial-purpose loans); *id.* at comment 4(a)(22)-1 (pre-payment penalty term reporting requirement not applicable to commercial-purpose loans).

determine how it will respond depending on the commercial transaction at issue.

Determining whether an action is reportable

A financial institution must be aware of the various application and transactional permutations that can give rise to reporting obligations. Financial institutions must report data from applications that did not result in an origination but on which actions were taken – *e.g.*, applications that were denied, applications that were approved but not accepted by the applicant, applications that were closed for incompleteness, or applications that were withdrawn by the applicant.[35] When a financial institution reports these actions, it must accurately characterize the particular action taken along with the date the action was taken, among other data points.[36] When the application is approved and results in an origination, the financial institution reports the loan as an origination rather than an application, along with the data points specified in Regulation C.[37]

Certain preliminary assessments of applicants may be reportable. For example, requests for pre-approval under a pre-approval program are considered applications under Regulation C.[38] Specifically, a pre-approval program is a program in which the financial institution performs a "comprehensive review" of the creditworthiness of the applicant that involves verification of income, resources, and other information.[39] Through this program, the institution may issue, as is typically done by the institution as part of its normal credit evaluation program, a written commitment to the applicant valid for a specific period of time to extend a home purchase loan up to a specified amount.[40] On the other hand, pre-qualification requests do not meet the definition of "application" and are not HMDA-reportable.[41] A pre-qualification request is defined as a request by a prospective loan applicant seeking a "preliminary determination on whether the prospective loan applicant would likely qualify for credit under an institution's standards, or for a determination on the amount of credit for which the prospective applicant would likely qualify."[42]

A financial institution's actions on an existing loan may trigger additional reporting requirements. For example, a financial institution may replace a customer's existing line of credit in a way that would be considered a new "extension of credit," which would trigger reporting obligations under HMDA.[43] Some transactions completed under installment sales contracts, such as some land contracts, may involve extensions of credit depending on the facts and circumstances, making these transactions closed-end mortgage loans for HMDA reporting purposes.[44] Whether the actions taken by the financial institution in these scenarios are reportable may depend on whether these actions result in new debt obligations.[45] On the other hand, an extension of credit that simply modifies, renews, extends, or amends the terms of an existing debt obligation will typically not be reportable because the existing debt obligation is not satisfied and replaced.[46] But, a transaction that satisfies and replaces an existing debt obligation of a borrower will be a reportable action.[47] It is important for financial

[35] 12 C.F.R. § 1003.4(a); Supplement I to Part 1003, comment 4(a)-1.ii.

[36] 12 C.F.R. § 1003.4(a)(8)(i)-(ii). For example, additional data points that a financial institution may be required to report include: (i) the interest rate applicable to the approved application, or to the covered loan at closing or account opening; (ii) the pre-payment penalty term in months; and (iii) the ratio of the applicant's or borrower's total monthly debt to the total monthly income relied on in making the credit decision. *Id.* at § 1003.4(a)(20)-(22).

[37] *Id.* at § 1003.4(a)(8)(i)(A).

[38] *Id.* at § 1003.2(b)(2).

[39] *Id.*

[40] The written commitment may not be subject to conditions other than: (i) conditions that require the identification of a suitable

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property; (ii) conditions that require that no material change has occurred in the applicant's financial condition or creditworthiness prior to closing; and (iii) limited conditions that are not related to the financial condition or creditworthiness of the applicant that the financial institution ordinarily attaches to a traditional home mortgage application. 12 C.F.R. § 1003.2(b)(2)(i)-(iii). For additional guidance on reporting requests for pre-approval, *see* Supplement I to Part 1003, comment 1003.2(b)-3.

[41] Supplement I to Part 1003, comment 2(b)-2.

[42] *Id.*

[43] *Id.* at comment 2(d)-2.

[44] *Id.*

[45] *Id.*

[46] *Id.*

[47] *Id.* ("In general, extension of credit under § 1003.2(d) refers to the granting of credit only pursuant to a *new debt obligation*. Thus, except as described in comments 2(d)–2.i and .ii, if a transaction modifies, renews, extends, or amends the terms of an existing debt obligation, but the existing debt obligation is

institutions to review their policies and procedures regarding the definition of "extension of credit" because the phrase is defined differently under Regulation C and Regulation B (the implementing regulation for the Equal Credit Opportunity Act ("ECOA")).[48]

Reporting the Automated Underwriting System name and result

Financial institutions must report the name of the automated underwriting system ("AUS") used in evaluating the application and the result generated by that AUS.[49] An AUS is defined as an "electronic tool developed by a securitizer, Federal government insurer, or Federal government guarantor of closed-end mortgage loans or open-end lines of credit that provides a result regarding the credit risk of the applicant and whether the covered loan is eligible to be originated, purchased, insured, or guaranteed by that securitizer, Federal government insurer, or Federal government guarantor."[50]

The Bureau's commentary to section 1003.4(a)(35) provides clarification on when AUS information must be reported:

- A financial institution must report the name and results of an AUS used to evaluate an application, regardless of whether the AUS was used before the underwriting process or during the underwriting process.[51]

- A financial institution must report the name and results of an AUS used to evaluate an application regardless of whether the financial institution intends to hold the covered loan in its portfolio or sell the covered loan.[52]

- A financial institution that uses an AUS that is developed by a securitizer to evaluate an application must report the name and results of the AUS regardless of whether the *securitizer* intends to hold the covered loan it purchased from the financial institution in its portfolio or securitize the covered loan.[53] The Bureau provides the following example: "[I]f a financial institution uses an AUS developed by a securitizer to evaluate an application and the financial institution sells the covered loan to that securitizer but the securitizer holds the covered loan it purchased in its portfolio, the financial institution complies with § 1003.4(a)(35) by reporting the name of the securitizer's AUS that the institution used to evaluate the application and the result generated by that system."[54]

- The Bureau further provides that a financial institution, which is also a securitizer, that uses its own AUS to evaluate an application, must report the name and results of the AUS regardless of whether the financial institution intends to hold the covered loan it originates in its portfolio, purchase the covered loan, or securitize the covered loan.[55]

The Bureau offers additional guidance for financial institutions that use one or more AUSs and/or the systems generate multiple results. For these scenarios, the Bureau provides the following four principles to help financial institutions determine which AUS and result(s) to report under section 1003.4(a)(35).[56]

1. Where a financial institution obtains two or more AUS results and the AUS generating one of those results corresponds to the loan types reported pursuant to section 1003.4(a)(2), the financial institution reports only the name and result of the AUS corresponding to the loan type.[57] The Bureau provides the following example: "[I]f a financial institution evaluates an application using the Federal Housing Administration's ("FHA") Technology Open to Approved Lenders ("TOTAL") Scorecard and subsequently evaluates the application with an AUS used to determine eligibility for a non-FHA loan, but ultimately originates an FHA loan, the financial institution complies with § 1003.4(a)(35)

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not satisfied and replaced, the transaction is not a closed-end mortgage loan under § 1003.2(d) because there has been no new extension of credit.") (emphasis added).

[48] *Id*.

[49] 12 C.F.R. § 1003.4(a)(35)(i).

[50] A person is a securitizer, Federal government insurer, or Federal government guarantor of closed-end mortgage loans or open-end lines of credit, respectively, if it has ever securitized, provided Federal government insurance, or provided a Federal government guarantee for a closed-end mortgage loan or open-end line of credit. *Id*. at § 1003.4(a)(35)(ii).

[51] Supplement I to Part 1003, comment 4(a)(35)-1.i.

[52] *Id*. at comment 4(a)(35)-1.ii.

[53] *Id*. at comment 4(a)(35)-1.iii.

[54] *Id*.

[55] *Id*. at comment 4(a)(35)-1.iv.

[56] *Id*. at comment 4(a)(35)-3.

[57] *Id*. at comment 4(a)(35)-3.i.

by reporting TOTAL Scorecard and the result generated by that system."[58] If a financial institution obtains two or more AUS results and more than one of those results is generated by a system that corresponds to the loan type, then the financial institution looks to the next principle to determine the information to report.[59]

2. Where a financial institution obtains two or more AUS results and the AUS generating one of those results corresponds to the purchaser, insurer, or guarantor, if any, the financial institution reports that AUS name and result.[60] The Bureau provides the following example: "[I]f a financial institution evaluates an application with the AUS of Securitizer A and subsequently evaluates the application with the AUS of Securitizer B, but the financial institution ultimately originates a covered loan that it sells within the same calendar year to Securitizer A, the financial institution complies with § 1003.4(a)(35) by reporting the name of Securitizer A's AUS and the result generated by that system."[61] If a financial institution obtains two or more AUS results and more than one of those AUS results is generated by a system that corresponds to the purchaser, insurer, or guarantor, if any, then the financial institution looks to the next principle to determine the information to report.[62]

3. Where the financial institution obtains two or more AUS results and the systems generating those results do not correspond to the purchaser, insurer, or guarantor, if any, or if the financial institution is following this principle because more than one AUS result is generated by a system that corresponds to either the loan type or the purchaser, insurer, or guarantor, the financial institution reports the AUS name and result generated closest in time to the credit decision.[63] The Bureau provides the following examples: (i) "[I]f a financial institution evaluates an application with the AUS of Securitizer A, subsequently again evaluates the application with Securitizer A's AUS, the financial institution complies with § 1003.4(a)(35) by reporting the name of Securitizer A's AUS and the second AUS result" and (ii) "[I]f a financial institution obtains a result from an AUS that requires the financial institution to underwrite the loan manually, but the financial institution subsequently processes the application through a different AUS that also generates a result, the financial institution complies with § 1003.4(a)(35) by reporting the name of the second AUS that it used to evaluate the application and the AUS result generated by that system."[64]

4. If none of the first three principles applies, the financial institution reports all of the names and results of the AUSs used to evaluate the application.[65] In any event, the financial institution does not report more than five AUSs and five results.[66] If more than five AUSs and results were obtained, the financial institution chooses any five among them to report.[67]

If a financial institution follows the foregoing principles, the instances when it will report more than one AUS and result obtained will be the exception and not the rule, unless the financial institution's policies and procedures do not align with the first three principles.

Calculating the combined loan-to-value ratio

When reporting an application or origination of a covered loan other than a purchased loan, Regulation C requires the financial institution to report the ratio of the total amount of debt secured by the property to the value of the property relied on in making the credit decision.[68] This ratio is known as the combined loan-to-value ("CLTV") ratio.

Determining whether and how to report the CLTV ratio can depend on a number of factors, including whether multiple CLTV ratios were used in making a credit decision and the number of properties secured by a loan.[69] The guiding principle when considering how to report the CLTV ratio is which CLTV ratio was *relied on* in making the credit decision.[70] Even if a CLTV ratio

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[58] *Id*.

[59] *Id*.

[60] *Id*. at comment 4(a)(35)-3.ii.

[61] *Id*.

[62] *Id*.

[63] *Id*. at comment 4(a)(35)-3.iii.

[64] *Id*.

[65] *Id*. at comment 4(a)(35)-3.iv.

[66] *Id*.

[67] *Id*.

[68] 12 C.F.R. § 1003.4(a)(24).

[69] *See, e.g.*, Supplement I to Part 1003, comment 4(a)(24).

[70] *Id*. at comment 4(a)(24)-1 ("Section 1003.4(a)(24) requires a financial institution to report, except for purchased covered loans, the ratio of the total amount of debt secured by the

was only one of many factors considered in making the credit decision, the financial institution must still report the CLTV ratio relied on, even if it was not dispositive.[71]

The Bureau's comments to section 1003.4(a)(24) provide insight on how a financial institution should report CLTV ratios:

- If a financial institution calculates a CLTV ratio twice — once according to the financial institution's own requirements and once according to the requirements of a secondary market investor — but the financial institution only relied on one of these CLTV ratio calculations, the financial institution reports the CLTV ratio relied on.[72]
- If the CLTV ratio was one of multiple factors relied upon by a financial institution in making a credit decision, but the financial institution denied an application because of the applicant's failure to satisfy one or more underwriting requirements *other* than the CTLV ratio, the financial institution still reports the CLTV ratio it relied on, even if it was not a dispositive factor.[73]
- If a file was closed for incompleteness, or if an application was withdrawn before a credit decision was made, a financial institution reports that the requirement to report the CLTV ratio is not applicable, even if the financial institution calculated the CLTV ratio.[74]
- If the financial institution does not rely on the CLTV ratio in making a credit decision, it reports that the requirement to report the CLTV ratio is not applicable.[75]

Additional issues with reporting the CLTV ratio may arise beyond the scenarios contemplated by the Bureau's comments. Ascertaining debt for purposes of a CLTV ratio calculation may be difficult where an application is submitted or a loan is originated to improve a multi-family dwelling and the loan is to be secured by two other multi-family dwellings, each of which has an existing mortgage held by another financial institution, or by non-real property, such as securities. In such a situation, the rules and accompanying commentary do not specify whether a financial institution is required to investigate any existing liens on the dwellings and include them in calculating the "total amount of debt" required under section 1003.4(a)(24). Further, Regulation C neither requires use of a CLTV ratio in making a credit decision, nor does it specify a particular method of calculating the CLTV ratio.[76] Rather, Regulation C merely requires the financial institution report the CLTV ratio that it relied on to make the credit decision.[77]

Collecting demographic data

HMDA and Regulation C require that financial institutions collect and report the ethnicity, race, and sex of an applicant or borrower for covered loans and applications, and report whether the information was collected on the basis of visual observation or surname.[78] Regulation C imposes specific requirements for the method of data collection and the time at which the data may be collected. Beginning January 1, 2018, Regulation C sets forth specific ethnicity and race categories and subcategories that must be presented to applicants, but also prohibits the financial institution from requiring that the applicant provide such information.[79] Financial institutions should not ask for information about ethnicity and race unless authorized by law, including Regulation C and ECOA/Regulation B.[80] If information is collected about ethnicity, race, and sex of an applicant under Regulation C but not reported as required by Regulation C, and the collection is not permissible under ECOA/Regulation B, there is a risk of violating Regulation C and ECOA/Regulation B.[81]

Regulation C provides specific guidelines for the collection of data on the ethnicity, race, and sex of an applicant if collected in person. The applicant must be informed that: (i) federal law requires the collection of

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property to the value of the property (combined loan-to-value ratio) *relied on* in making the credit decision.") (emphasis added).

[71] *Id*. at comment 4(a)(24)-2.

[72] *Id*. at comment 4(a)(24)-1.

[73] *Id*. at comment 4(a)(24)-2.

[74] *Id*. at comment 4(a)(24)-3.

[75] *Id*. at comment 4(a)(24)-4.

[76] *Id*. at comment 4(a)(24)-6.

[77] *Id*.

[78] 12 C.F.R. § 1003.4(a)(10)(i).

[79] 12 C.F.R. § 1003, Appx. B, -1, -8, -9.

[80] Fed. Fin. Inst. Examination Council, A Guide to HMDA Reporting: Getting It Right! at Appx. C (2018).

[81] *Id*.

this information for consumer protection purposes and to monitor compliance with federal anti-discrimination statutes and (ii) if the information is not provided during an in-person application, the financial institution is required to note the information on the basis of visual observation or surname.[82] The Bureau has created a sample collection form with the required disclosure.[83] When the application is taken by phone, the financial institution must state the substantive information in the collection form orally and omit the portions of the disclosure that relate exclusively to written applications.[84]

When reporting demographic information, the financial institution must report the ethnicity, race, and sex of an applicant as provided by the applicant.[85] An applicant may select an ethnicity or race subcategory even if the applicant does not select an aggregate ethnicity or aggregate race category.[86] For example, when the applicant provides the requested information for some but not all fields, the financial institution must report the information that was provided by the applicant, even if the applicant provided partial information.[87] The applicant also has the option of selecting more than one ethnicity or race.[88] If the applicant selects more than one ethnicity or race, the financial institution must report each selected designation (with some limitation).[89] Institutions should review Appendix B carefully to determine how it should report certain ethnicity and race designations.

If the applicant chooses not to provide any information for an application taken in person, the financial institution must note that fact, collect the applicant's ethnicity, race, and sex on the basis of visual observation or surname, and report whether such information was collected on the basis of visual observation or surname.[90] Further, while an applicant generally has the option of selecting disaggregated ethnicity and race categories, a financial institution collecting ethnicity, race, and sex on the basis of visual observation or surname must select only from the aggregate categories.[91]

If the applicant affirmatively declines to answer these questions by checking the "I do not wish to provide this information" box on an application that is taken by mail or on the internet, or orally declines to provide this information during an application that is taken by telephone, the financial institution must report "information not provided by applicant in mail, internet, or telephone application."[92] If the applicant begins an application by mail, internet, or telephone and does not provide the requested information on the application, but does not select the "I do not wish to provide this information" box on the application, the financial institution must request the applicant's ethnicity, race, and sex during a subsequent in-person meeting.[93] Again, if the applicant declines to provide the requested information during the in-person meeting, the financial institution must collect the information based on visual observation or surname.[94] However, note that the financial institution is not required to collect this information if the in-person meeting occurs *after* the application process is complete, such as at closing or account opening.[95]

Financial institutions must also be aware of requirements for collecting information from co-applicants and from non-natural persons. If there are no co-applicants, the financial institution reports that fact.[96] If there is more than one co-applicant, the financial institution is required to provide the demographic information for the first co-applicant listed on the collection form.[97] For absent co-applicants, there are two options: (i) a co-applicant may provide an absent co-applicant's ethnicity, race, and sex on behalf of the absent co-applicant or (ii) if the information is not provided for an absent co-applicant, the financial institution must report "information not provided by

[82] 12 C.F.R. § 1003, Appx. B, -2.

[83] *Id*. at Appx. B.

[84] *Id*. at Appx. B, -1.

[85] *Id*. at Appx. B, -8.

[86] *Id*.

[87] *Id*. at Appx. B, -13.

[88] *Id*. at Appx. B, -9.

[89] *Id*.

[90] *Id*. at Appx. B, -10.

[91] *Id*.

[92] *Id*. at Appx. B, -11.

[93] *Id*. at Appx. B, -12.

[94] *Id*.

[95] *Id*.

[96] *Id*. at Appx. B, -5.

[97] *Id*.

applicant in mail, internet, or telephone application" for the absent co-applicant.[98]

On the other hand, if the applicant or co-applicant is not a natural person, then the financial institution must report that the requirement to report the applicant's or co-applicant's ethnicity, race, and sex is not applicable.[99] For example, for a transaction involving a trust, the institution reports that these fields are "not applicable" if the trust is an applicant.[100] However, if the applicant is a natural person and the beneficiary of a trust, the financial institution must report the applicant's ethnicity, race, and sex.[101]

While the Bureau's commentary addresses situations where a trust is a co-applicant, various other scenarios may involve applicants that are not natural persons. For example, a natural person may initiate the application process with the intent of closing the loan in the name of a corporate entity that has not yet been created. If the application is withdrawn before a corporate entity is created, the financial institution may still be obligated to provide the natural person's ethnicity, race, and sex, even if the intent was for the application to close in the name of the corporate entity.

The collection of demographic information is an area where financial institutions could easily make mistakes. Therefore, it is important for financial institutions to review Regulation C and Appendix B often to ensure compliance and to provide frequent training to loan originators regarding the collection of demographic information.

ENSURING ACCURATE REPORTING OF HMDA INFORMATION

As part of a HMDA review, the examination teams of supervising agencies conduct HMDA transaction tests by selecting a random sample of entries from the reporting institution's HMDA loan/application register ("LAR") and comparing the entries with the loan or application files held by the institution.[102] The size of the LAR sample generally corresponds to the size of the institution's LAR.[103] Further, the threshold error rate is lower for financial institutions with greater than 100,000 entries on the LAR than it is for financial institutions with fewer than 100,000 entries.[104] If the total number of errors in the sample exceeds the Bureau's Resubmission Threshold, the financial institution may be required to correct and resubmit its entire LAR — not just those files that contained errors.[105]

In addition to evaluating data submissions for accuracy, the Bureau also evaluates the compliance management system of the institutions it supervises.[106]

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[98] *Id*.

[99] *Id*. at Appx. B, -7.

[100] *Id*. By contrast, an extension of credit to a trust created for tax or estate planning purposes for personal, family, or household purposes may be considered an extension of credit to the beneficiaries under Regulation Z, the implementing regulation for the Truth in Lending Act. Supplement I to Part 1026, comment 3(a)-10(i).

[101] 12 C.F.R. § 1003, Appx. B, -7 ("[…] if the applicant is a natural person, and is the beneficiary of a trust, you must report the applicant's ethnicity, race, and sex.").

[102] Bureau of Consumer Fin. Prot., Examination Procedures: HMDA Resubmissions Guidelines at Procedures 2 (Oct. 2013); *see* Fed. Fin. Insts. Examination Council, FFIEC HMDA Examiner Transaction Testing Guidelines, https://www.federalreserve.gov/supervisionreg/caletters/CA%2017-2%20Attachment%20HMDA%20Resubmission%20Guidelines%20Final%2008-10-17.pdf.

[103] Bureau of Consumer Fin. Prot., Examination Procedures: HMDA Resubmissions Guidelines at Procedures 2 (Oct. 2013).

[104] *Id*.

[105] *Id*. at 2. Note that HMDA provides procedures for correcting bona fide errors, or errors that were "unintentional or occurred despite the maintenance of procedures reasonably adapted to avoid such errors." 12 C.F.R. § 1003.6(b). Further, "[i]f an institution makes a good-faith effort to record all data concerning covered transactions fully and accurately within 30 calendar days after the end of each calendar quarter, and some data are nevertheless inaccurate or incomplete, the error or omission is not a violation of the act or this part provided that the institution corrects or completes the information prior to submitting the loan/application register to its regulatory agency." 12 C.F.R. § 1003.6(b)(3).

[106] Note that in 2017, in light of the 2017 amendments to HMDA that may pose "significant systems and operational challenges" to implementation, the Bureau announced that it does not intend to require data resubmission "unless data errors are material." Bureau of Consumer Fin. Prot., Statement with Respect to HMDA Implementation (Dec. 21, 2017), *available at* http://files.consumerfinance.gov/f/documents/cfpb_statement-with-respect-to-hmda-implementation_122017.pdf. The Bureau also flagged its intention to engage in rulemaking to amend aspects of the 2015 HMDA rule, including the institutional and transactional coverage tests, and the rule's discretionary data points. *Id.* In assessing initial compliance with the newly amended rule, the Bureau will consider "whether companies have made good-faith efforts to come into

The Bureau describes its examination process as the following steps:

1. **Initial procedures**: The Bureau first evaluates whether the institution meets the definition of a "financial institution" under Regulation C.[107] The Bureau then evaluates any mergers or acquisitions that occurred in previous years to determine whether data collection and reporting duties are affected.[108]

2. **Evaluation of compliance management**: The Bureau examines the financial institution's compliance management system to determine whether the policies, procedures, trainings, and internal review procedures are adequate to ensure ongoing compliance with HMDA and Regulation C.[109] The Bureau determines whether effective corrective action is taken to respond to deficiencies.[110] It also evaluates whether the financial institution performs LAR volume analysis from year-to-year to detect fluctuations in activity for possible omission of data.[111]

3. **Evaluation of policies and procedures**: The Bureau evaluates whether the institution's informal procedures and internal controls are adequate to ensure compliance with HMDA and Regulation C.[112] This includes an evaluation of compliance with specific Regulation C requirements governing pre-approval programs, reporting of certain categories of loans, methods for determining and reporting lien status for all originated loans and applications, procedures for collection of demographic data, and proper training of personnel.[113]

4. **Transaction testing**: The Bureau tests a sample of loans and applications to verify that the financial institution accurately compiled home mortgage disclosure information in the format prescribed by Regulation C.[114]

5. **Disclosure and reporting**: The Bureau examines certain disclosure and reporting procedures, including whether the financial institution: (i) submits its LAR to the appropriate supervisory agency in a timely manner; (ii) makes available certain disclosures to the public; (iii) makes available certain LAR data to the public; and (iv) employs the proper tools to compile the necessary geographic information.[115]

Failure to comply with HMDA can result in administrative sanctions or civil money penalties.[116] In 2016 alone, the Bureau's fair lending supervisory and public enforcement actions (which include HMDA actions) resulted in $46 million in remediation to harmed consumers.[117]

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compliance with the rule in a timely manner." Bureau of Consumer Fin. Prot., Supervisory Highlights 41, Issue 16 (2017), *available at* https://www.consumerfinance.gov/documents/5386/201709_cfpb_Supervisory-Highlights_Issue-16.pdf. In July 2018, the Bureau reaffirmed that it does not intend to require data resubmission for HMDA data collected in 2018 and reported in 2019, "unless data errors are material," and would not assess penalties with respect to errors in data collected in 2018 and reported in 2019. Bureau of Consumer Fin. Prot., Bureau of Consumer Financial Protection Issues Statement on the Implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act Amendments to the Home Mortgage Disclosure Act (July 5, 2018), https://www.consumerfinance.gov/about-us/newsroom/bureau-consumer-financial-protection-issues-statement-implementation-economic-growth-regulatory-relief-and-consumer-protection-act-amendments-home-mortgage-disclosure-act/.

[107] Bureau of Consumer Fin. Prot., Supervision and Examination Manual, Part II, C. at Procedures 1 (Oct. 2012), https://www.consumerfinance.gov/documents/4568/102012_cfpb_home-mortgage-disclosure-act-hmda_procedures.pdf.

[108] *Id*. at Procedures 1-2.

[109] *Id*. at Procedures 2.

[110] *Id*. at Procedures 3.

[111] *Id*.

[112] *Id*. at Procedures 4.

[113] *Id*. at Procedures 4-5.

[114] *Id*. at Procedures 6.

[115] *Id*. at Procedures 6-8 (Oct. 2012).

[116] 12 C.F.R. § 1003.6(a).

[117] This number represents estimates of monetary relief for consumers resulting from supervisory or enforcement actions for fair lending violations, in addition to monetary payments such as loan subsidies, increased consumer financial protection, and civil money penalties. Bureau of Consumer Fin. Prot., Fair Lending Report of the Consumer Financial Protection Bureau 8 (Apr. 2017). With respect to violations of HMDA, among other types of relief, institutions may be ordered to pay civil money penalties. 12 U.S.C. § 5565(c); *see also In re Washington Federal*, No. 2013-CFPB-0005 (Oct. 9, 2013), *available at* http://files.consumerfinance.gov/f/201310_cfpb_consent-order_washington-federal.pdf. The Bureau deposits civil money penalties into the Consumer Financial Civil Penalty Fund, which the Bureau uses to pay victims for activities for which the civil penalties have been imposed. 12 U.S.C. § 5497(d)(1)-(2). When victims cannot be

THE TAKEAWAY

Given the risk of inaccuracies or omissions inherent in the magnitude of data requested under HMDA, financial institutions should take a number of steps to ensure compliance and minimize faulty reporting, including the following:

- Consider implementing regular quality-control reviews both before and after reporting to ensure that information is accurately collected and reported.
- Understand the effective dates for loan-volume thresholds for purposes of determining whether a financial institution and its loan transactions are covered under Regulation C.
- Analyze the financial institution's relationship with other institutions that originate or purchase loans, or provide services related to the evaluation of loan applications. Understanding these relationships is integral to anticipating HMDA and Regulation C requirements for collection of information on loan applications and originations. If the financial institution purchases loans or uses third-party service providers to approve loans, the institution should ensure that accurate and complete data are collected at the loan application and loan origination levels.
- Ensure that personnel understand the requirements surrounding collection of demographic data in-person, including statements that must be made to applicants and the appropriate time to request demographic data. ■

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located or payments are otherwise impractical, the Bureau may put these funds towards consumer education and financial literacy programs. 12 U.S.C. § 5497(d)(2).