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Regulatory Compliance Webinar Series

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Assurance • Tax • Consulting

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Agenda

- FATCA, the Foreign Account Tax Compliance Act
- Remittance Transfer Rule
 - The final rule revising the remittance rule requirements and establishing an effective date
- CFPB final rules
 - Appraisal rules
 - Ability-to-Repay: Eight underwriting factors and Appendix Q
 - Mortgage Loan Originator Compensation Rule
- Updates and reminders

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The Foreign Account Tax Compliance Act

FATCA overview

The Foreign Account Tax Compliance Act (FATCA) added Chapter 4 “Taxes to Enforce Reporting on Certain Accounts” to the Internal Revenue Code (sections 1471-1474) as part of the HIRE ACT of 2010. Additional guidance and amendments to the Act became final on January 17, 2013, when the IRS issued 544 pages of final FATCA regulations.

The principal goal of FATCA is to prevent US taxpayers from using foreign accounts and investments to hide income from the IRS and evade payment of US tax. Chapter 4 is operated via a withholding regime similar to Chapter 3, with additional reporting requirements for non-US persons.

FATCA compliance will be phased in over a period of six years (with increasing scope and complexity) beginning with withholding obligations that are effective January 1, 2014.

FATCA overview

FATCA enforces reporting by creating compliance obligations for both foreign and US persons.

- Foreign persons will have to become FATCA compliant or suffer a 30% withholding tax on certain income received from US persons.
- US persons will have to document foreign person's FATCA compliance or withhold. If US person fails to properly document compliance, the US person becomes liable for the 30% withholding (and would presumably seek to be compensated by foreign party).

Because FATCA is US law, foreign parties (foreign clients, foreign investors, etc.) are likely to be unaware or unprepared for the changes. US businesses should consider educating or notifying foreign clients regarding FATCA obligations prior to a withholding event.

FATCA timeline

2013

- January: IRS publishes final FATCA regulations
- Spring: IRS expected to publish Revenue Procedure
- July 15: IRS FFI Registration Portal to open
- October 25: FFI must enter into agreement (to avoid withholding in 2014)

2014

- January 1: FATCA withholding begins on Fixed, Determinable, Annual, Periodical (FDAP) income payments to non participating FFIs, non-compliant NFFEs, and recalcitrant account holders (i.e. foreign parties that fail to meet FATCA reporting requirements)

FATCA – US compliance requirements

To comply with FATCA regulations, US withholding agents must:

1. Identify withholdable payments to foreign persons
2. Classify foreign persons (as FFI/ NFFE) to determine if recipient is subject to FATCA obligation
3. Confirm, in advance of the payment, if FFI/NFFE is compliant with respective FATCA obligations (in order to avoid withholding)

Requires procedures in place to manage data and reporting (ability to identify certain payments, onboarding procedures to identify and classify foreign parties, ability to document compliance)

FATCA – US compliance requirements

FATCA has many key definitions introduced in the Regulations for the first time. Affected parties must understand definitions and procedures new to FATCA in order to comply.

- US withholding agents (USWAs) must withhold 30 percent tax on **withholdable payments** made to
 - **Foreign Financial Institutions (FFIs)** that do not agree to report certain information to the IRS regarding their US accounts, and
 - **Nonfinancial Foreign Entities (NFFEs)** that do not provide information on their substantial US owners to withholding agents.

FATCA – Withholdable Payments

Withholdable payments include:

- All US source FDAP income (interest, dividends, rent, other) (1/1/14)
- All US source gross proceeds from sale of property that produce interest or dividends (starting in 2015)

FDAP is same income subject to Chapter 3 Withholding Regime. Treaty benefits may operate to reduce Chapter 3 withholding. Nothing reduces FATCA withholding (even if treaty in force).

Exceptions: Payments made in the ordinary course of trade or business, for use of property, or for nonfinancial services or goods (e.g., wages, employment compensation, rents, licenses, transportation, gambling winnings, interest on accounts payable), interest on short term obligations, and income effectively connected to a US trade or business

FATCA – Foreign Financial Institution

Foreign Financial Institutions (FFI) include foreign entities that:

- Accept deposits in the ordinary course of a banking
- Hold financial assets for others as a substantial portion of its business
- Engage primarily in the business of investing, reinvesting or trading in securities and similar items
- Manage portfolios
- Hold itself out as a hedge fund, private equity fund, mutual fund, or private investment fund
- Regulatory examples show that investment advisors, and fund managers are FFIs

Exceptions: Start-up company, group treasury/hedging center, companies emerging from bankruptcy, entities tax-exempt under section 501(c), foreign real estate funds

FATCA - FFI compliance

- An FFI will not be subject to withholding if it enters into an FFI
- agreement directly with the IRS.
- The agreement must meet the requirements of section 1471(b), under which the FFI must:
 - Identify the holders of all “U.S. accounts”
 - Report ID of account holder, value of account, gross withdrawals to the IRS annually and other information
 - Withhold at 30 percent on any payments to “recalcitrant” holders
 - Obtain waiver from holder of any rights under any bank secrecy/nondisclosure law, or close the account
- FFIs entered into agreements are called participating FFIs or “PFFIs”

FATCA - Intergovernmental Agreements (IGAs)

- In many cases, foreign laws prevent FFIs from reporting directly to the IRS. To remedy this, the IRS has collaborated with foreign governments to develop two alternative model intergovernmental agreements (IGAs).
- Goals of the IGAs
 - Allows FFIs to report directly to their home country authorities
 - Foreign government will transmit information directly to IRS automatically
 - Reciprocal information exchange
 - U.K. , Denmark, Mexico, Switzerland, and Norway have signed agreement
 - Over 50 countries are in discussions with IRS

FATCA overview

Non- Financial Foreign Entities (NFFE) includes any foreign entity that is not a FFI

- Tax applies unless NFFE provides information regarding its substantial U.S. owners (i.e., 10 percent owners) or certifies that it has none (similar to direct agreements made between FFIs and IRS)
- Potentially huge expansion of FATCA

Exceptions: Public companies and certain affiliates, entities based in U.S. territories/possessions, active NFFEs with less than 50% passive income and 50% passive assets.

FATCA overview – Compliance evaluation

- Legal entity structure confirmation and classification of entities as FFIs and NFFEs
- Assess/Amend organizational/shareholder agreements if necessary
- Review investor data to classify investors into appropriate FATCA categories
- Review of current on-boarding processes and determination of whether the know-your-customer- processes are adequate
- Review of payment systems impacted by FATCA
- Determine if FFI agreement necessary? FFI must enter into agreement by 10/25/2013 to avoid withholding in 2014
- Identify compliance officer
- What functions can be outsourced?
- Amend due diligence checklist for new transactions

Appendix: FATCA Timeline

2014

January 1

- Must implement new account onboarding procedures for U.S. Withholding Agents, participating FFIs, and Registered Deemed Compliant FFIs.
- FATCA withholding on Fixed, Determinable, Annual, Periodical (FDAP) income payments to non participating FFIs, non-compliant NFFEs, and recalcitrant account holders begins
- Last date to qualify for grandfathered obligations and exempt from FATCA withholding (still subject to reporting)

June 30

- USWAs, Participating FFIs, and Registered Deemed Compliant FFIs must document preexisting entity accounts identified as Prima Facie FFIs. If the FFI signed agreement after 1/1/14, the deadline is six months from the effective date of the FFI agreement.

December 31

- Participating FFIs must document preexisting high value individual accounts by December 31, 2014. If the FFI signed an agreement after January 1, 2014, the deadline is one year from the effective date of the FFI agreement.

Appendix: FATCA Timeline

2015

March 15

- Form 1042-S reporting on withholdable income payments begins (with respect to 2014 calendar year)

March 31

- USWAs begin Form 8966 U.S. Owner reporting
- FFIs begin Form 8966 U.S. Account information and balance reporting (with respect to the 2013 and 2014 calendar years)
- FFIs begin Form 8966 recalcitrant account reporting (for 2014 calendar year)

December 31

- U.S. Withholding Agents, Participating FFIs, and Registered Deemed-Compliant FFIs must document preexisting entity accounts not identified as Prima Facie FFIs. If the FFI signed an agreement after 1/1/14, the deadline is two years from the effective date of the FFI agreement.
- Participating FFIs must document all remaining preexisting non-high value individual accounts by December 31, 2015. If the FFI signed an agreement after January 1, 2014, the deadline is two years from the effective date of the FFI agreement.

Appendix: FATCA Timeline

2016

January 1

- Deadline for limited FFIs or limited branches (due to local regulations prohibiting FATCA compliance) to become participating FFIs and avoid other participating FFIs within the expanded affiliated group from losing their participating FFI status

March 15

- FFI begin temporary Form 1042-S aggregate reporting on payments made to non-participating FFIs (with respect to 2015 calendar year)

March 31

- Form 8966 reporting on U.S. Account income by participating FFIs begins in addition to account information and balance (with respect to the 2015 calendar year)

Appendix: FATCA Timeline

2017

January 1

- FATCA withholding on gross proceeds payments to non-participating FFIs and recalcitrant payees begins
- Withholding on foreign pass-thru payments begins not before January 1, 2017

March 15

- Last year for FFI temporary Form 1042-S aggregate reporting on payments made to non-participating FFIs (with respect to 2016 calendar year)
- Form 8966 reporting on U.S. Account gross proceeds by participating FFIs begins in addition to account information, balance, and income (for 2016 calendar year)

2018

March 15

- Form 1042-S reporting on gross proceed payments begins (with respect to the 2017 calendar year)

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Regulation E Remittance Transfer Rule

Remittance Transfer Rule

Where are we with this rule?

- May 23, 2011: Proposed rule
- February 7, 2012: Final rule
- February 7, 2012: Proposed rule (companion to final rule)
 - safe harbor and refinements to disclosures and cancellation requirements
- July 10, 2012: Technical correction to final rule
- August 20, 2012: Final Remittance Rule
 - Adoption of safe harbor and other revisions from the companion proposal
- December 31, 2012: Proposed rule
 - Addresses issues within the final rule (foreign tax disclosure issues and error resolution provisions)
- January 22, 2013: Final rule
 - Temporarily delays effective date
- **April 30, 2013: Rule finalizing the December 31st proposed rule. This final rule established the effective date: October 28, 2013**

Regulation E: Remittance Transfer Rule

Three issues addressed

Final rule addresses three issues:

First

- Rule modifies the 2012 final rule to make optional the requirement to disclose fees imposed by a designated recipient's institution.

Second

- Rule also makes optional the requirement to disclose taxes collected by a person other than the remittance transfer provider.

Third

- Rule revises the error resolution provisions (when sender provided incorrect or insufficient information such as an incorrect account number)

Regulation E: Remittance Transfer Rule

Fees and taxes disclosure

Final rule creates optional requirement to disclose fees and taxes imposed by a person other than the remittance transfer provider.

- Disclaimers on disclosure to sender
- May disclose fees and taxes as estimates

Regulation E: Remittance Transfer Rule

Error provisions – sender info wrong account

2013 Final Rule creates exemption from 2012 Final Rule error provisions - sender provides incorrect information and deposit ends up in wrong account. For exemption to apply, provider must:

Provide notice to the sender prior to transfer

Implement recipient institution identifier verification measures

Make reasonable efforts to retrieve mis-deposited funds

Regulation E: Remittance Transfer Rule

Error provisions – Sender info other situations

- Final rule streamlines error resolution procedures in other situations where sender provides incorrect or incomplete information (situations other than incorrect recipient account information).
- Contrary to requests by commenters that the Bureau extend the proposed exception for sender mistakes regarding account numbers to mistakes regarding all types of information, the Bureau is limiting the exception to sender mistakes regarding account numbers and recipient institution identifiers

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Final Appraisal Rules

Appraisal Rules

Regulation B

- Consumer access to appraisal report

Regulation Z

- Higher-priced mortgage loans

Appraisal rule: Regulation B

Current rule:

- Application for credit secured by a lien on a dwelling
- May routinely provide a copy of appraisal or provide a copy at consumer's written request.
- If the latter, must give a notice of the right to receive a copy of the appraisal during application process but no later than notice of action taken

New rule:

- Application for credit secured by a **first** lien on a dwelling
- Notify within three business days of right to receive copy of appraisal.
- Provide copy of each appraisal or **valuation** three business days before consummation (C/E credit) or at account opening (O/E credit)

Appraisal rule: Regulation B

Other Provisions

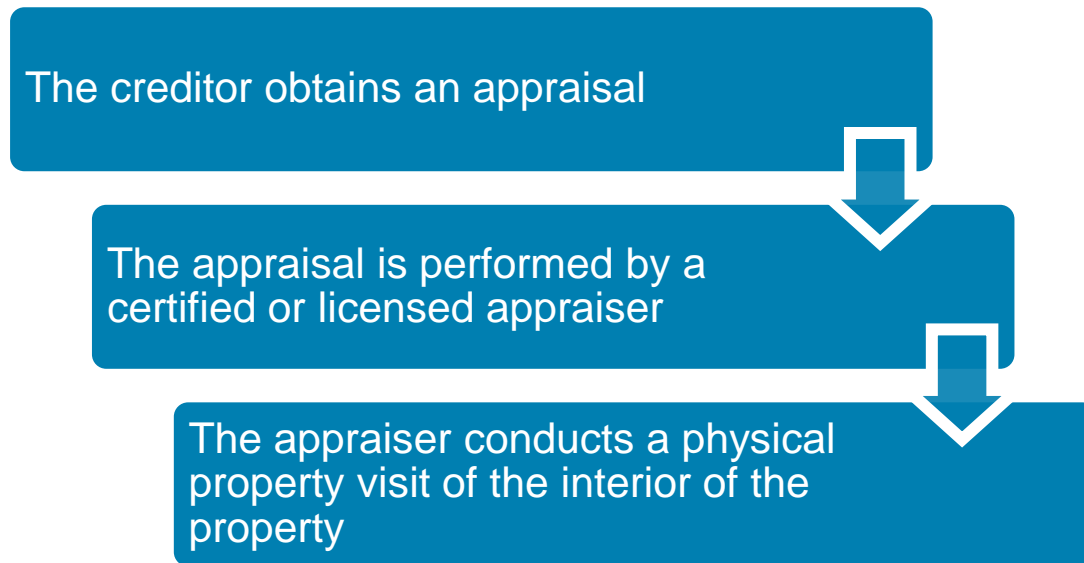
Applicants can waive timing requirements – must still receive copy of appraisal or valuation

Prohibits creditors from charging a fee for the copy of appraisal or valuation

This appraisal notice can be used to satisfy the appraisal rule for HPMLs (TILA rule)

Appraisal rule: Regulation Z HPML main requirement

- “A creditor shall not extend a higher-priced mortgage loan to a consumer without obtaining, prior to consummation, a written appraisal performed by a certified or licensed appraiser who conducts a physical visit of the interior of the property that will secure the transaction.” **Cannot extend an HPML unless:**



Definition of Higher-Priced Mortgage Loan

- Higher-Priced Mortgage Loans (HPMLs) apply to **closed-end** consumer credit secured by principal dwelling with an annual percentage rate that exceeds the average prime offer rate by:
 - 1.5% 1st lien
 - 2.5% Jumbo
 - 3.5% Subordinate lien

Exemptions for HPML appraisal rule

- A qualified mortgage
- A transaction secured by a new manufactured home
- A transaction secured by a mobile home, boat, or trailer.
- A transaction to finance the initial construction of a dwelling
- A loan with maturity of 12 months or less, if the purpose of the loan is a “bridge” loan connected with the acquisition of a dwelling intended to become the consumer’s principal dwelling
- A reverse-mortgage transaction

Appraisal proposal vs. final rule

- Proposal included an option for a metric to use for comparison to the APOR instead of the APR (transaction coverage rate or TCR).
- Unlike the APR, the TCR would exclude all prepaid finance charges not retained by the creditor, a mortgage broker, or an affiliate of either.
- Final rule did not adopt the proposed alternative to the APR. Rule may be modified if the Bureau adopts practice in the TILA/RESPA Proposal.

Appraisal rule: Regulation Z HPML requirements

Disclosure within three business days of application:

- Purpose of the appraisal
- Copy of written appraisal will be provided
- Charge for appraisal may be assessed
- Applicant can choose to have a separate appraisal conducted at their own expense

Give copy (free of charge) of the appraisal at least three business days before consummation

Additional appraisal requirement for “flipped” properties

Creditor must obtain, at creditor’s expense, an additional appraisal from a different certified or licensed appraiser if the HPML will finance the purchase or acquisition of the mortgaged property from a seller within 180 days of the purchase or acquisition of such property by the seller at a price that was lower than the current sale price of the property if:

- Price exceeds seller’s acquisition price by:
 - 10% if seller acquired property within past 90 days
 - 20% if acquired 91 to 180 days earlier

Exemptions from additional appraisal

Rule does not apply to extensions of credit that finance a consumer's acquisition of property from a:

- Local, state or federal government agency;
- Person who acquired title to the property through foreclosure,
- Non-profit entity as part of a local, state, or federal government program
- Person who acquired title to the property by inheritance or pursuant to a court order of dissolution of marriage, civil union, or domestic partnership
- Relocation agency in connection with an employee relocation
- Servicemember who received a deployment or permanent change of station order after the property was purchased
- Area designated by the President as a federal disaster area
- Rural county

Appraisal rule: Regulation Z HPML second appraisal

If two appraisals are required, one must include:

- Difference between the price at which the seller acquired property and the price consumer is obligated to pay
 - Changes in market conditions between the date the seller acquired property and the date of the consumer's purchase agreement
- Any improvements made to the property between the date the seller acquired the property and date of the consumer's purchase agreement

Appraisal rule: Regulation Z HPML Safe Harbor

For the safe harbor, the creditor needs to:

1. Order the appraiser to perform the appraisal in conformity with USPAP and FIRREA
2. Verify through the National Registry the appraiser has a valid appraisal license or certification in the property state.
3. Confirm that nine elements are addressed in the written appraisal
4. Acknowledge there is nothing to the contrary in the facts or certifications contained in the written appraisal.

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Ability-to-Repay Rule Underwriting Factors

Ability-to-Repay

- Section 1026.43: Minimum standards for transactions secured by a dwelling:
 - For residential mortgages, creditors must determine that the consumer has the ability to repay the loan using verified documentation of the consumer's income and debt obligations.
- Appendix Q establishes Standards for Determining Monthly Debt and Income

Coverage

- Any consumer credit transaction secured by a dwelling
- Excludes: HELOCs, timeshare plans, reverse mortgages, temporary (bridge) loans with a term of 12 months or less, construction loans and business/commercial purpose loans.

Ability-to-Repay minimum requirements

At a minimum, creditors generally must consider eight underwriting factors:

- (1) Current or reasonably expected income or assets;
- (2) current employment status;
- (3) the monthly payment on the covered transaction;
- (4) the monthly payment on any simultaneous loan;
- (5) the monthly payment for mortgage-related obligations;
- (6) current debt obligations, alimony, and child support;
- (7) the monthly debt-to-income ratio or residual income; and
- (8) credit history

Minimum requirements in detail

- (1) Current or reasonably expected income or assets
 - Income from employment or other sources
 - Assets other than the dwelling securing the transaction

Only have to consider income/assets to support ability to repay.

- (2) Current employment status
 - Need not be full time or at regular intervals as long as seasonal, part-time or irregular characteristics are considered in repayment ability determination
 - Can verify employment status verbally by calling employer, but the call must be documented

Minimum requirements in detail

(3) Monthly payment on the covered transaction

- Must be calculated in accordance with 1026.43(c)(5)
 - Fully indexed rate
 - Monthly fully amortized payment
- If balloon loan:
 - Not HPML, must consider the maximum payment due in the 1st 5 yrs
 - HPML, must consider the maximum payment due in the 1st 5 yrs, including the balloon
 - Special provisions for balloon-payment Qualified Mortgages held in portfolio by small creditors operating in rural or underserved areas.

http://files.consumerfinance.gov/f/201303_cfpb_preliminary-list_rural-or-underserved-counties.pdf

Balloon Payment Qualified Mortgage - defined

May originate balloon payment qualified mortgage if you're a small creditor operating in rural or underserved areas:

- More than 50% of your 1st lien mortgages in prior year were secured by properties in rural or underserved areas
- Assets below \$2 billion
- Originated no more than 500 1st lien mortgages in prior year

Balloon Payment Qualified Mortgage - defined

To be a balloon payment qualified mortgage:

- Loan must have a fixed interest rate
- Loan must have periodic payments
- Loans may not have negative amortization features
- Loan must have a term of five years or longer
- Loan must not be subject to a forward commitment
- Must determine that the consumer's ability to repay
- Must consider and verify the consumer's income or assets, and debts, alimony, and child support.
- Must consider the consumer's DTI or residual income,
- Must comply with the points/fees limits for qualified mortgages

Minimum requirements in detail

- (4) Monthly payment on any simultaneous loan secured by the same property
- HELOCs – calculate the monthly HELOC payment based on the amount of credit to be drawn at or before consummation of the main loan
 - For simultaneous loans transactions that are not HELOCs, use the monthly payment for the loan calculated in the same manner as we discussed on the prior slide depending on the type of loan

Minimum requirements in detail

- (5) Monthly payment for mortgage-related obligations
 - Property taxes and insurance you require the consumer to buy, and other costs related to the property such as homeowners association fees or ground rent
- (6) Current debt obligations, alimony, and child support;
 - Do not have to include debt obligations or credit history of someone who is merely a guarantor or surety on the loan.

Minimum requirements in detail

(7) Monthly debt-to-income ratio or residual income;
and

- No specified DTI for general ability to repay rule, but it should be reasonable

(8) Credit history

- May consider non-traditional credit if no file (i.e. rental history or utilities)
- May ignore certain items with a reasonable belief the information is inaccurate (i.e. disputed accounts).
- May accept, without further verification, debt obligations disclosed by the consumer that are not on the credit report

Potential penalties

- If you originate a mortgage loan and do not follow the ability to repay rules, you could be liable for up to three years of finance charges and fees the consumer paid as well as the consumers' legal fees
- There is a three-year statute of limitations on ability to repay claims brought as affirmative cases. After three years, consumers can bring ability to repay only as setoff/recoupment claims in a defense to foreclosure

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Final Mortgage Loan Originator Compensation Rule

Important dates, definitions and applicability

- Effective dates:
 - June 2013 – Prohibition on mandatory arbitration of disputes and financing credit insurance
 - January 2014 – all other provisions
- Mortgage Loan Originator (MLO) = loan officer/mortgage broker
- Rule applies to any consumer credit transaction secured by a dwelling
- Recordkeeping = 3 years

Requirements/prohibitions

- Written policies and procedures
- Prohibits steering incentives (refined)
 - Pay cannot vary based on loan terms (higher rate, prepayment penalty or higher fees)
 - MLO not paid more if consumer buys settlement services from lender, broker or affiliates
 - Pay cannot vary based on “proxy” terms
 - Can contribute to 401(k) or bonus plan based on profitability
- Prohibits dual compensation (refined)
 - MLO cannot be paid by both the consumer and the creditor (includes seller paid closing costs as consumer payment)
 - Exception – mortgage brokers can pay commissions to employees as long as they aren’t based on loan terms

Additional requirements

- Sets qualification and screening standards (new)
 - Levels playing field for MLOs - Currently different standards for federally regulated vs. state licensed
 - Character and fitness requirements (credit report)
 - Criminal background checks
 - Training requirements
 - MLO name and NMLS ID number must be included on application, note/loan contract and security instrument

Additional prohibitions

- Prohibits mandatory arbitration of disputes and waivers of consumer rights (new)
- Prohibits increasing loan amount to cover credit insurance premiums (new)
- Look for additional implementation guidelines from the CFPB as effective date approaches

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Updates and Reminders

Updates and reminders

- Interagency guidance regarding the Biggert-Waters Flood Insurance Reform Act:
<http://www.fdic.gov/news/news/financial/2013/fil13014.html?source=govdelivery>.
- Proposed rule clarifying and making technical amendments to the 2013 Escrow Rule:
http://files.consumerfinance.gov/f/201304_cfpb_amendment_escrows-final-rule.pdf
- Proposed rule to address questions regarding the 2013 Mortgage Servicing Rules and the Ability to Repay Rule:
http://files.consumerfinance.gov/f/201304_cfpb_proposed-rule_amending-atr-qm-and-servicing-mortgage-rules.pdf

Updates and reminders

- 2013 Guide to HMDA Reporting: Getting It Right is now available on the FFIEC's HMDA website:
<http://www.ffiec.gov/hmda/guide.htm>
- FDIC and OCC proposed guidance on deposit advance products:
<http://fdic.gov/news/news/press/2013/pr13031a.pdf?source=govdelivery> and <http://www.occ.gov/news-issuances/bulletins/2013/bulletin-2013-11a.pdf>
- FDIC guidance on payday loans and subprime lending:
<http://fdic.gov/news/news/press/2013/pr13031a.pdf>

Updates and reminders

- Final rule amending the Credit Card Act (timeframe the fee limitation applies):
<https://www.federalregister.gov/articles/2013/03/28/2013-07066/truth-in-lending-regulation-z>
- CFPB final rule amending the Credit Card Act (amends applicants' ability to repay based on independent income):
http://files.consumerfinance.gov/f/201304_cfpb_credit-card-ability-to-pay-final-rule.pdf
- Final rule amending Regulation E (ATM fee notice):
<https://www.federalregister.gov/articles/2013/03/26/2013-06861/disclosures-at-automated-teller-machines-regulation-e>

Updates and reminders

CFPB's Small Entity Compliance Guides:

- http://files.consumerfinance.gov/f/201304_cfpb_compliance-guide_atr-qm-rule.pdf: Guide for Ability to Repay Rule (Qualified Mortgages)
- http://files.consumerfinance.gov/f/201304_cfpb_compliance-guide_2013-escrows-rule.pdf: Guide for TILA Escrow Rule
- http://files.consumerfinance.gov/f/201305_compliance-guide_home-ownership-and-equity-protection-act-rule.pdf: Guide for High-Cost Mortgage Rule
- http://files.consumerfinance.gov/f/201305_compliance-guide_ecoa-appraisals-rule.pdf: Guide for ECOA Appraisal/Valuation Rule.
- http://files.consumerfinance.gov/f/201305_compliance-guide_higher-priced-mortgage-loan-appraisals-rule.pdf: Guide for HPML Appraisal Rule

Updates and reminders

- June 1, 2013: Regulation Z's MLO Compensation Rule for extensions of credit secured by the consumer's principal dwelling:
 - restricts mandatory arbitration in mortgage loan agreements (including HELOCs) and prohibits barring a consumer from bringing forth a claim in Federal court.
 - Prohibits financing single-premium credit insurance
- June 1, 2013: Escrow requirements for HPMLs – maintain escrow for 5 years on first lien loans

Thank you for joining us today!

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