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Community Bankers Association of Georgia

Regulatory Update

November 12, 2009

We wanted to provide you with a brief update on four regulatory issues on which there have been developments this week.

FDIC Approves Three-Year Prepayment Plan

On Thursday, November 12, 2009, the FDIC Board of Directors voted unanimously to approve the three-year prepaid assessment plan for deposit insurance premiums, essentially as it had been proposed.

As best I can determine from a quick review of the final rule, only relatively minor changes were made to the original proposal. First, the final rule indicates that any prepayment amounts not exhausted after collection of the amount due on June 30, 2013, will be refunded to the institution. In the original proposal, any refunds would not have been paid until December 30, 2014. Secondly, perhaps in response to our comment letter, the **FDIC provided some greater clarity in the final rule regarding the process for institutions to be exempted from the prepayment requirement due to safety and soundness issues, including liquidity issues**, both in regard to those institutions that the FDIC will exempt without an application and those institutions who will be considered for exemption only after filing an application. Also, the FDIC moved the deadline back from December 24, 2009, to November 23, 2009, by which they plan to notify any institution that they plan to exempt without application. Even those banks filing an application for exemption (which must be filed by December 1, 2009) will now be notified no later than December 15, 2009, if they are being exempted.

A detailed summary of the final rule and the way the prepaid assessment is intended to operate is included at the end of this Update. [Read Final Rule on Prepay.](#)

Federal Reserve Guidance Provides Some Regulation Z Relief/More Relief Needed

On November 9, 2009, the Federal Reserve issued a Question and Answer document regarding the July 2008 revisions to Regulation Z related to "higher-priced" mortgages. **The Q & A document clarifies that the repayment ability requirements for "higher priced" mortgage loans were not intended to prohibit community banks from offering balloon residential mortgages that mature in less than seven years.**

The FRB indicated that while creditors have an affirmative duty to engage in prudent underwriting, they are not required to verify that borrowers have the assets or income when a mortgage is issued that would be sufficient to pay the balloon payment when it is due. The guidance also expressly states that the bank "is not required to predict the consumer's future financial circumstances, interest rate environment or home value."

The issuance of this guidance follows a meeting a week ago between Independent Community Bankers of America (ICBA) and senior FRB officials on the July 2008 Regulation Z revisions. This meeting was scheduled at the urging of the CBA of GA, other community bankers associations and community bankers from around the country.

This guidance does not, however, address the burden of creating escrow accounts for mortgage loans that meet the definition of "higher-cost," a requirement of the 2008 Regulation Z revisions which goes into effect April 1, 2010. CBA of GA will continue

to work toward an agreeable solution to the escrow problem and will continue to urge ICBA to work with policymakers to limit this requirement for community banks. [Read Fed Guidance.](#) [Read ICBA Release.](#)

Federal Reserve Adopts Final Overdraft Protection Rule

The Federal Reserve Board adopted **final rules – effective July 1, 2010** – on Thursday, November 12, 2009 that **prohibit financial institutions from charging consumers fees for paying overdrafts on automated teller machine and one-time debit card transactions, unless a consumer opts in to the overdraft service for those types of transactions.** The Federal Reserve issued this regulation under Regulation E, the Electronic Funds Transfer Act.

Before opting in, the consumer must be provided a notice that explains the financial institution's overdraft services, including the fees associated with the service, and the consumer's choices. The final rules include a model opt-in notice.

The Federal Reserve Press Release regarding the rule indicates that in order to ensure the consumer has a true choice, the rule prohibits financial institutions from discriminating against consumers who do not opt in, meaning they must provide these consumers with the same account terms, conditions, and features -- including pricing -- that they provide to consumers who do opt in.

The Board Press Release stated that its consumer testing showed most consumers prefer not to be enrolled in overdraft services for ATM and one-time debit card transactions unless they have opted in. The testing also affirmed, however, that most consumers want overdraft services to cover important bills such as house payments, utility bills, etc.

[Read the Fed's press release.](#) [Read the final rule.](#) [Read the model disclosure form.](#)

FDIC Approves Rule Implementing SAFE Act

On Thursday, November 12, 2009, the FDIC Board also approved a **joint final rule implementing the Secure and Fair Enforcement Mortgage Act (SAFE Act), which would require employees of banks, savings associations, credit unions and other depository institutions, and institutions regulated by the Farm Credit Administration to register with the Nationwide Mortgage Licensing System and Registry,** obtain a unique identifier and maintain this registration.

Non-bank loan originators will not only be required to register; they must also be licensed.

[Read Draft Final Rule on SAFE Act.](#)

ICBA's Detailed Summary of the FDIC's Prepaid Assessment Rule

Under the final rule on the prepaid assessment, banks would prepay their estimated regular quarterly assessments for the fourth quarter of 2009 and all of 2010-2012 on Dec. 30, when the regular third-quarter assessment payment is due.

The prepay plan would allow exemptions for banks if prepaying assessments would threaten the bank's safety and soundness or liquidity or would otherwise create a significant hardship. The FDIC will work with banks' primary federal regulators to proactively exempt banks based on regulatory data. The agency will notify banks it determines should be exempt by Nov. 23.

Additionally, banks that believe paying the advanced premiums would be an undue hardship or pose liquidity issues may apply to the FDIC for an exemption. The FDIC will consider exemption requests on a case-by-case basis and expects that only a few institutions will find an exemption necessary.

Applications are due to the Director of the Division of Supervision and Consumer Protection by Dec. 1. E-mail applications to prepaidassessment@fdic.gov or fax them to (202) 898-6676.

Any application for exemption will be deemed to be denied unless the FDIC notifies the applying institution by Dec. 15. The FDIC

will notify banks that they are exempt or the agency has postponed determination of the application for exemption until no later than Jan. 14, 2010. The FDIC expects that it will postpone few, if any, determinations of applications for exemption. In the event, however, that the FDIC postpones such determinations, the institution will not have to pay its prepaid assessment on Dec. 30.

The prepayment would be based on an institution's assessment rate and assessment base for the third quarter of 2009, assuming a 5 percent annual growth in deposits each year. While the FDIC plan would maintain current assessment rates through 2010, effective Jan. 1, 2011, the rates would increase by three basis points across the board (e.g., Risk Category I banks paying 12-16 basis points for 2010 would pay 15-19 basis points). Additionally, the agency voted to extend the DIF restoration plan from seven to eight years, with a target of returning the fund to a 1.15 percent reserve ratio (the minimum required by law) by the first quarter of 2014.

Banks would book the total prepayment as a "prepaid expense" asset and draw it down as each quarterly payment comes due. In that respect, the prepayment option has the virtue of drawing from available cash and liquidity in the industry while not immediately reducing industry capital and continues to keep the DIF funded by the industry. The prepaid assessment will qualify for a zero risk weight under the risk-based capital requirements.

Under the final rule, any prepayment amounts not exhausted after collection of the amount due on June 30, 2013, will be refunded to the institution, rather than on Dec. 30, 2014, as originally proposed. If the FDIC determines its liquidity needs allow, it may return any remaining prepaid assessment to the institution sooner. However, the FDIC considers an earlier refund unlikely given its current projections.

In its comment letter to the FDIC, ICBA urged the agency to shorten its three-year prepayment plan to two years, with the option to impose a third year at the end of 2010 if Deposit Insurance Fund liquidity needs have not been met. ICBA also recommended that the FDIC use a significantly lower estimated annual deposit growth rate for banks located in parts of the country with historically slower deposit growth rates.

ICBA also strongly recommended that the assessment base used for the prepayment calculation be the same used for the second-quarter special assessment—total assets minus Tier 1 capital. For the second-quarter special assessment, 98 percent of community banks paid less than if the assessment had been based on domestic deposits, and \$300 million in costs were shifted to the nation's largest banks.

The plan would bring in an estimated \$45 billion for the DIF. The FDIC projects \$100 billion in failure costs from 2009 to 2013, with most occurring in 2009 and 2010. Without an infusion of liquidity, the FDIC believes its liquidity needs will exceed its liquid assets early next year. **[Read Final Rule on Prepay.](#)**

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