

# Compliance Corner



FEDERAL RESERVE BANK OF PHILADELPHIA

## Website Compliance for Banks, Part II

by Robin P. Myers, Team Manager

The Second Quarter 2006 issue of *Compliance Corner* contained the first of two articles reviewing the requirements for consumer regulation website compliance. Part I discussed compliance for loan products. This article will focus on the advertisement of deposit products via websites, e-mail, or banner advertisements on other third-party websites and will highlight the requirements of Regulation DD and the Federal Deposit Insurance Corporation (FDIC). The Electronic Signatures in Global and National Commerce Act (E-Sign Act), as it relates to electronic communication, will also be discussed briefly.

### Regulation DD – Truth in Savings

Regulation DD defines an advertisement as a commercial message appearing in any medium that promotes, directly or indirectly, the availability of, terms of, or a deposit in a new or existing account. Financial institutions that advertise accounts on the Internet are subject to the advertising rules outlined in Regulation DD.

**General disclosures.** All advertisements, including those in electronic format, must be clear, conspicuous, and straightforward. Additionally, advertisements cannot describe an account as “free” or “no cost” if maintenance

or activity fees may be imposed on the account.

If an advertisement states a rate of return, the rate must be stated as an “annual percentage yield,” using that term. The abbreviation “APY” may be used, provided the term “annual percentage yield” is stated at

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## *Compliance Alert:* **The Long and Short of Regulation E's Error Resolution Process and Notarized Affidavits**

Over the last several years, the United States' payment system has seen a dramatic decline in the number of checks paid. Surveys conducted by the Federal Reserve confirm that electronic payments (credit cards, debit cards, and automated clearing-house transactions) exceeded check payments for the first time in 2003. During that time, the number of electronic payment transactions totaled 44.5 billion, while the number of checks paid totaled 36.7 billion. It is predicted that the number of electronic payments will continue to increase in the coming years.

The increase in the number of electronic payments will likely be accompanied by an increase in the number of errors and unauthorized transfers. Regulation E, Electronic Fund Transfers, establishes the basic rights, liabilities, and responsibilities of consumers who use electronic fund transfer services and the financial institutions that provide these services; it also includes the resolution of errors. An electronic fund transfer is defined as any transfer of funds that is initiated through an electronic terminal, telephone, computer, or magnetic tape for the purpose of ordering, instructing, or authorizing a financial institution to debit or credit a customer's account.

Recently, bankers have asked whether it is permissible to require a consumer to provide certain documentation in support of an unauthorized electronic transfer, such as affidavits of forgery, notarized statements, police reports, etc. Additionally, some bankers have asked whether it is acceptable to have the consumer come into a branch to execute a notarized statement free of charge.

**The short answer is:** Regulation E does **not** permit a bank to require documentation such as notarized affidavits, statements, or copies of police reports. Nor does the regulation allow a bank to require a consumer to visit the branch office to sign notarized documents, regardless of whether the bank charges the consumer for the notarization process. Requiring such additional documentation, or visits to a branch office, would be burdensome and unreasonable for consumers and, at the same time, would not provide any real assistance in the investigation and resolution process.

**The long answer is:** Section 205.11(b)(2) of Regulation E allows the bank to require a “written confirmation” of error from a consumer as part of the error resolution process, within 10 business days of an oral notice of error. If the bank elects to require a consumer to put the notice of error in writing, then the bank must inform the consumer of the written requirement and provide the address where written confirmation of error must be sent when the consumer gives the oral notification.



The regulation requires the bank to start the investigation as soon as it receives an oral notice of error and to not delay the start of or the completion of the investigation pending receipt of the written confirmation. However, while the regulation requires the bank

to begin its investigation upon oral notification of an error, it allows the bank to withhold provisional credit to a consumer's account when the bank **has not** received “written confirmation” within 10 business days, if required. □

## Compliance Alert: Revised Standard Flood Hazard Determination Form Now Available

The Federal Emergency Management Agency (FEMA) recently made minor revisions to the Standard Flood Hazard Determination Form and its accompanying instructions. The revised form, FEMA Form 81-93, was distributed to Third District state member banks during the week of June 19, 2006. The revised form is also available on FEMA's website at <[www.fema.gov/business/nfip/sfhdfom.shtm](http://www.fema.gov/business/nfip/sfhdfom.shtm)>.

The only changes reflected in the new Standard Flood Hazard Determination Form are an updated Office of Management and Budget (OMB) control number and an updated form expiration date. Minor changes were made to the instructions that accompany the form to reflect new FEMA contact information (i.e., website addresses and telephone numbers) to be used for information requests when completing the form.

A screenshot of the FEMA website navigation bar. It features the FEMA logo on the left, followed by navigation links: Home, Get Disaster Info, Plan Ahead, Apply for Assistance, Recover &amp; Rebuild, See All Audiences, and About Us. On the right, there are links for Contact Us, Site Map, Frequently Asked Questions, and Español, along with an Advanced Search box with a Go button.

Business and Professionals

### National Flood Insurance Program

- About Flood Insurance
- Ask the Expert
- Flood Insurance Library
- Flood Insurance Publications

## Standard Flood Hazard Determination Form and Instructions

### Required Use of the Standard Flood Hazard Determination Form

FEMA Form 81-93, Standard Flood Hazard Determination Form (SFHDF) has a revised expiration date of October 31, 2008 and was approved for use, effective December, 2005. There were no changes to the format or content of the Form.

To allow users of the Form time to update their systems to the new version, the effective date for mandatory use of the new Form is July 1, 2006. Although the old version (expiration date October 31,

## Compliance Alert: Recent Cases on the Right of Rescission

A recent decision from the United States Court of Appeals for the Sixth Circuit in *Barrett v. JP Morgan Chase Bank*, 445 F.3d 874 (6th Cir. 2006), is of interest to banks in the Third District. The issue in this case is whether a consumer's right of rescission under the Truth in Lending Act (TILA) and Regulation Z is eliminated when a consumer refinances a loan and the bank releases its security interest. TILA allows borrowers three days to rescind certain secured loan transactions, but if the creditor fails to deliver the required material disclosures or makes errors in those disclosures, the right of rescission is extended for three years.<sup>1</sup> Residential mortgage transactions to finance the acquisition or construction of a consumer's principal dwelling are exempt from rescission, but the right of rescission does apply to second or third mortgages or the refinancing of an existing mortgage.

Prior to *Barrett*, the only other federal appeals court to address the issue in a published decision was the Ninth Circuit in *King v. California*, 784 F.2d 910 (9th Cir. 1986), which concluded that the right of rescission is eliminated once a loan is repaid and the security interest is released. But the Sixth Circuit rejected

<sup>1</sup> Section 226.15(a)(3) of Regulation Z defines "material disclosures" as "the information that must be provided to satisfy the requirements in §226.6 with regard to the method of determining the finance charge and the balance upon which a finance charge will be imposed, the annual percentage rate, the amount or method of determining the amount of any membership or participation fee that may be imposed as part of the plan, and the payment information described in §226.5b(d)(5)(i) and (ii) that is required under §226.6(e)(2)."

the reasoning in *King* and concluded, after a thorough analysis of TILA and Regulation Z, that consumers can still invoke the right of rescission for a refinanced loan for eligible violations within the three-year period. In the aftermath of *Barrett*, banks should consider the possibility that loans subject to the right of rescission, which are later refinanced, are still potentially subject to rescission for up to three years from the closing of the original loan if the bank violated TILA and Regulation Z with respect to the required material disclosures.

The right of rescission allows consumers to obtain a refund of certain charges and fees—including finance charges, penalties, loan transaction fees, appraisal fees, closing costs, and attorneys' fees for the rescission lawsuit—which could be costly.

It is important to note that decisions from the Sixth Circuit are only binding in the states of Ohio, Kentucky, Michigan, and Tennessee. However, a decision from a federal appeals court is persuasive authority. If this issue reaches the Third Circuit, whose decisions are binding in Pennsylvania, New Jersey, and Delaware, the court would take a careful look at the Sixth Circuit case, which contains

an exhaustive and persuasive analysis of this issue. Moreover, both the federal district and bankruptcy courts in Philadelphia have previously ruled in the following three cases that the right of rescission can still be exercised after a refinancing: *Abele v. Mid-Penn Consumer Disc.*, 77 B.R. 460, 464–65 (E.D. Pa. 1987); *Nichols v. Mid-Penn Consumer Disc. Co.*, 1989 WL 46682 (E.D. Pa. Apr. 28, 1989); and *In re Wright*, 127 B.R. 766, 770–71 (Bankr. E.D. Pa. 1991). In addition, a state appeals court in California recently followed *Barrett* in holding that a refinancing does not eliminate the right of rescission: *Pacific Shore Funding v. Lozo*, 42 Cal.Rptr.3d 283, 289, 138 Cal.App.4th 1342 (Cal.App. 2 Dist. 2006).

This issue is significant for banks because the right of rescission allows consumers to obtain a refund of certain charges and fees—including finance charges, penalties, loan transaction fees, appraisal fees, closing costs, and attorneys’ fees for the rescission lawsuit—which could be costly. Moreover, a federal district court in Massachusetts, in *McKenna v. First Horizon Home Loan Corp.*, 429 F.Supp.2d 291 (D.Mass. 2006), recently certified a class action for the right of rescission and held that a refinancing does not eliminate the right of rescission. Prior to this decision, courts had uniformly held that rescission lawsuits could not be certified as class actions because liability for rescission relies on the facts of each individual

case and thus could not be adjudicated on a class-wide basis. The United States Court of Appeals for the First Circuit recently agreed to review this decision to determine whether rescission lawsuits can be certified as class actions and whether the refinancing of a loan eliminates the right of rescission.

The lessons of both *Barrett* and *McKenna* is that rescission errors can be costly and that banks should therefore be very diligent in ensuring that their loan disclosures fully comply with TILA and Regulation Z. When these disclosures are timely and made properly, a loan cannot be rescinded after the initial three-day rescission period expires. □

## Website Compliance for Banks, Part II ... *continued from page 1*

least once in the advertisement.

Additionally, the advertisement cannot state any other rate except the interest rate, using that term. The interest rate may be stated in conjunction with the annual percentage rate, but it may not be more conspicuous than the APY to which it relates.

**Additional disclosures.** When the APY is stated in an electronic advertisement, the following additional information is required: (1) the period of time the APY will be offered or a statement that the APY is accurate as of a specified date; (2) the minimum balance required to obtain the advertised APY; (3) the minimum deposit required to open the account, if it is greater than the minimum balance to obtain the advertised APY; and (4) a statement that fees (if charged) could reduce the earnings on the account.

For variable-rate accounts, a statement that the rate may change after the account is opened must be included. For tiered accounts, the minimum balance required for each tier must be stated in close proximity and with equal prominence to the applicable APY. Finally, for time accounts, additional required disclosures include: (1) the term of the account, (2)

a statement that a penalty will or may be imposed for early withdrawals, and (3) the required interest payouts for certain accounts.<sup>1</sup>

If a bonus<sup>2</sup> is stated in an electronic advertisement, the advertisement must also state the following information: (1) the annual percentage yield, using that term; (2) the time requirement to obtain the bonus; (3) the minimum balance to obtain the bonus, including the minimum balance required to open the account if it is greater than the minimum balance necessary to obtain the bonus; and (4) when the bonus will be available.

According to the Official Staff Commentary, if the additional disclosures are not listed on the same page as the advertisement, the advertisement must clearly

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<sup>1</sup> Refer to Section 230.8(c)(6)(iii) of Regulation DD for more details on required interest payouts at <[www.federalreserve.gov/regulations/default.htm#dd](http://www.federalreserve.gov/regulations/default.htm#dd)>.

<sup>2</sup> Regulation DD defines a bonus as a premium, gift, award, or other consideration worth more than \$10 (whether in the form of cash, credit, merchandise, or any equivalent) given or offered to a consumer during a year in exchange for opening, maintaining, renewing, or increasing an account balance.

refer the consumer to the location where the additional required information begins (e.g., website link).

**Disclosure requirements for institutions advertising the payment of overdrafts.** When an advertisement promotes the payment of overdrafts, the following information is required: (1) the fee or fees for the payment of each overdraft, (2) the categories of transactions for which a fee for paying an overdraft may be imposed, (3) the time period by which the consumer must repay any overdraft, and (4) the circumstances under which the bank will not pay an overdraft.

Additionally, such advertisements trigger periodic statement disclosures. The bank must separately disclose the following on periodic statements: (1) the total dollar amount for all fees or charges imposed on the account for paying checks or other items to cover insufficient funds and (2) the total dollar amount for all fees imposed on the account for returning items unpaid. The disclosures should be provided for the statement period and the calendar year-to-date for any accounts to which the advertisement applies.

The requirements for the above disclosures cease to apply two years after the date of the bank's last advertisement promoting the payment of overdrafts.

### **FDIC Requirements**

The FDIC membership statement or symbol must be listed on the financial institution's homepage and all other pages that reference deposits. If a financial institution also advertises nondeposit investment products on its website, via e-mail, or via banner advertisements on other third-party websites, the FDIC insurance statement and logo must be removed from those pages.

### **Electronic Communication**

Financial institutions have the option of providing account disclosures electronically. Regulation DD defines electronic communication as a message transmitted electronically between a depository institution and a consumer in a format that allows visual text to be displayed on equipment (e.g., a personal computer). All disclosures that Regulation DD requires to be in writing may be provided to the consumer via electronic communication. However, the disclosures must be in accordance with the E-Sign Act and Regulation DD.

Under the E-Sign Act, a depository institution is required to obtain a consumer's affirmative consent when providing disclosures electronically that are related to a transaction. Disclosures requested by consumers and those required for advertisements are not considered to be related to a transaction.

The electronic communication must be sent to the consumer's e-mail address or made available at another location, such as a website. When a disclosure provided by electronic communication is returned to a depository institution as undeliverable, the depository institution shall take reasonable steps to attempt redelivery using all available customer information from its files.

### **Closing Comments**

While the Internet provides financial institutions with an additional medium in which to market products and services, there are also additional laws, regulations, and compliance requirements. Banks should review their websites on a regular basis to ensure compliance with all applicable laws and regulations. If you have any questions about this article, please contact Supervising Examiner John D. Fields (john.d.fields@phil.frb.org) through the Regulations Assistance Line at (215) 574-6568. □

The FDIC membership statement or symbol must be listed on the financial institution's homepage and all other pages that reference deposits.



# Who to Call

Your institution may need to contact an officer, manager, or staff member in the Supervision, Regulation, and Credit Department, but you may not know whom to call. The following list should help you find the correct contact person to call. Financial institutions that have an appointed central point of contact should generally contact that individual directly.

Contact names appearing in bold are the primary contacts for their areas.

## Community, Regional, and Global Supervision

John J. Deibel, VP	574-4141
Elisabeth V. Levins, AVP	574-3438
<b>Joseph J. Willcox, Manager</b>	574-4327
<b>William T. Wisser, Manager</b>	<b>574-7267</b>
Eric A. Sonnheim, AVP	574-4116
<b>Glenn A. Fuir, Manager</b>	<b>574-7286</b>
<b>Adina A. Himes, Manager</b>	<b>574-6443</b>
H. Robert Tillman, Special Advisor	574-4155

## Capital Markets

John J. Deibel, VP	574-4141
Elisabeth V. Levins, AVP	574-3438
<b>Avi Peled, Manager</b>	<b>574-6268</b>

## Consumer Compliance & CRA Examinations

John J. Deibel, VP	574-4141
Constance H. Wallgren, AVP	574-6217
<b>Robin P. Myers, Manager</b>	<b>574-4182</b>
<b>David A. Center, Manager</b>	<b>574-3457</b>

## Consumer Complaints

John J. Deibel, VP	574-4141
Constance H. Wallgren, AVP	574-6217
John D. Fields	574-6044
<b>Denise E. Mosley</b>	<b>574-3729</b>

## Regulations Assistance

**Regulations Assistance Line** **574-6568**

## Enforcement

A. Reed Raymond, VP 574-6483  
**Cynthia L. Course, AVP** **574-3760**

## Regulatory Applications

A. Reed Raymond, VP 574-6483  
William L. Gaunt, AVP 574-6167  
**James D. DePowell, Manager** **574-4153**

## Retail Risk Analysis

William W. Lang, VP 574-7225  
Todd Vermilyea, AVP 574-4125  
Christopher C. Henderson,  
Special Advisor 574-4139

## Discount Window and Reserve Analysis

Vish P. Viswanathan, VP 574-6403  
**Gail L. Todd, Manager** **574-3886**

NOTE: All phone numbers have the area code (215).



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