FROM BUTLER, SNOW, O'MARA, STEVENS & CANNADA, PLLC

QUARTERLY REPORT

MISSISSIPPI REGULATORY COMPLIANCE GROUP

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AWAITING THE DEFINITION OF A "QUALIFIED MORTGAGE"

Everyone is awaiting the CFPB's final word on the definition of a "Qualified Mortgage" (QM). Most observers feel that this single regulatory development may have more of an impact on community bank profitability, the availability of housing credit and the overall economic recovery than perhaps any other aspect of the Dodd-Frank Act. Whether that is true or not may be up for debate, but that the impact of the QM will be considerable is not in doubt. So, what exactly is a Qualified Mortgage? What is the CFPB trying to accomplish here?

To understand the reasoning behind the QM definition, you first need to understand the "Ability to Pay" Rule. This rule is an amendment to the Truth in Lending Act and applies to "residential mortgage loans." That term includes virtually all consumer loans secured by a dwelling other than home equity lines of credit.

The expanded Ability to Pay Rule is similar to the Federal Reserve Rule for higher-priced mortgages adopted in 2008, but now applies to a much broader range of consumer loans.

The Ability to Pay Rule requires a creditor to consider the following underwriting criteria for each individual borrower:

- Credit history,
- Current income,
- Expected income (reasonably anticipated),
- Current obligations,
- Debt-to-income ratio or residual income,
- Employment status, and
- Financial resources (other than the equity in the dwelling).

Income must be verified using W-2 tax forms, payroll receipts, etc. (some flexibility exists here for certain government guaranteed or insured loans).

Special rules apply for "nonstandard loans" such as variable-rate loans that defer repayment of principal or interest or loans that permit interest-only payments. For those loans, a creditor must use a repayment schedule that fully amortizes the loan.

These underwriting criteria can be onerous, and there is potential liability under the Truth in Lending Act for failure to comply with the Ability to Pay Rule. Failure to comply with the Ability to Pay Rule can also be asserted as a defense to foreclosure and a possible offset should a loan become delinquent.

To lessen the potential liability, the Dodd-Frank Act created a presumption of compliance to the extent that a creditor makes a QM.

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A QM is defined as:

- A loan that features regular periodic payments which do not increase the principal balance or allow the borrower to defer the repayment of principal.
- A loan that does not result in a balloon payment.
- A loan for which the borrower's income and financial resources are verified and documented.
- Either a fixed-rate loan where underwriting is based on a fully amortizing payment schedule, or an adjustable-rate loan where underwriting is based on the maximum rate possible in the first five years and a payment schedule that would fully amortize the loan over the loan term. Taxes, insurance and assessments must be included for both types of loans.
- The loan must comply with the guidelines established by the CFPB for debt-to-income.
- Total points and fees (same definition as for "high-cost" loans) cannot exceed 3% of the "total loan amount," and
- The loan term may not exceed 30 years.

The CFPB has the authority to modify the definition of a QM to make allowances for loans of smaller amount. It also can provide for loans with balloon payments to qualify provided the loan otherwise meets all of the criteria except those applicable to the prohibition on deferred repayment of principal and the underwriting requirements for fixed- and variable-rate loans. Creditors will still have to verify that the borrower has the capacity to make all scheduled payments, other than the balloon payment, and the repayment schedule must be one that fully amortizes the loan over not more than 30 years. This exception for balloon payment loans will only be available to creditors that operate in primarily rural or underserved areas, that have annual originations that do not exceed a certain limit, that meet certain asset size criteria, and that retain the loan in portfolio. Other changes may be suggested to limit or avoid any undue impact on either the cost or availability of credit.

The CFPB is wrestling with another issue related to the QM: the question of whether making a QM should entitle a creditor to a "safe harbor" or merely a presumption of compliance. As you know, a safe harbor means you cannot be challenged on whether you have complied with the Ability to Pay Rule. A presumption of compliance would be rebuttable by a showing of contrary facts.

Creditors want a safe harbor; consumer advocates want only a presumption of compliance. The CFPB representatives have argued that a clear set of criteria, accompanied by a rebuttable presumption of compliance, might be the best approach since adhering to the clear criteria would mean that there is very little room to try to rebut the presumption of compliance.

The CFPB has also tossed out the idea of a two-part definition of QM. One set of criteria would be very conservative, or safe, and would be entitled to the safe harbor treatment. Another set of criteria would be more expansive and would only get a presumption of compliance. By using the two-tier definition, the CFPB would hope to overcome arguments that the QM definition is so restrictive that it would limit lending, impact earnings, impede the availability of credit, and perhaps increase the cost of mortgage loans that do get made.

We should know shortly the CFPB's thoughts. The Board is under pressure to finalize its proposal by January 21, 2013.

In the past, banks have managed to get around many of the compliance headaches associated with restrictive loan products, such as HOEPA loans, by pricing those loans in a way that took all of their loans out from under the regulatory restrictions. You will not be able to do this with respect to QMs in all likelihood. Everyone should begin now to consider what the impact will be on loan products, bank income, Community Reinvestment Act compliance, Fair Lending, etc.,

if the Bank chooses to make QMs. Many areas, in addition to the Compliance Department, will be affected.

(Ed Wilmesherr)

PERFORMING A UDAAP RISK ASSESSMENT

A little over a year ago, we told you about the potential expansion and increased emphasis on unfair, deceptive and abusive acts and practices (UDAAP) by the CFPB. In August of this year, we told you how the CFPB had lived up to its promises with its first enforcement action against Capital One assessing approximately $210 million in total penalties. We continue to see evidence that the CFPB is not taking UDAAP enforcement lightly. Since August, it has issued two more enforcement actions making examples out of Discover and American Express.

In its enforcement action against Discover, the CFPB alleged unfair, deceptive and abusive acts and practices which, as in the case against Capital One, related to the marketing and sales tactics of certain credit card add-on products. Discover's total penalty is expected to be approximately $214 million, including $14 million in civil money penalties and approximately $200 million in refunds to more than 3.5 million consumers.

Most recently, the CFPB entered into a consent order with American Express alleging, among other things, that American Express engaged in deceptive marketing practices, age discrimination, charging fees in violation of TILA, failure to report consumer disputes, and deceptive debt collection practices. American Express's penalty totaled approximately $112.5 million made up of $27.5 million in civil money penalties owed to the CFPB, the FDIC, the Federal Reserve and the OCC and an estimated $85 million in refunds to approximately 250,000 customers.

If you are beginning to think that none of this is applicable to your bank because you do not offer credit card services, please stay tuned because the lessons learned apply to all aspects of the banking business including, but not limited to, product development, marketing, lending, customer service and operations. Previously, a simple review of marketing materials, advertisements and consumer account agreements and disclosures would have been a sufficient UDAAP review, but now with the obvious increased UDAAP regulation, a more thorough review must be performed. It is important for each institution to assess and monitor all products, services, disclosures, agreements, marketing materials, scripts, employment incentive plans and third party contracts.

We encourage each of you to perform a UDAAP risk assessment to determine the level of risk that exists at your bank. The primary areas to consider when performing the risk assessment are management and polices, servicing and collections, employees and third parties, products and services, and availability of terms and services as advertised. The review should also focus on consumer complaints and the bank's processes and procedures for appropriately and timely responding to those complaints and taking corrective action. The existence of UDAAP issues can be detected through a review of trends in consumer complaints.

As you assess management's involvement, it is important to ensure that management is made aware of any potential UDAAP risks and takes immediate, corrective action upon discovery. Additionally, third party service providers are increasingly seen as a potential source of UDAAP violations. Aggressive sales tactics and incentive compensation arrangements are concerns. Fees, pricing, agreements, penalties, rates and other aspects of all of your bank's products and services should be reviewed. And, finally, all marketing and advertising should be reviewed to ensure that the availability of terms and services is as advertised. During the review, please keep in mind that disclosures and advertisements must be compliant throughout the entire lifecycle of a product or service. Products and services should be described accurately in all initial disclosures, and if the product is modified, it is important that related disclosures are also modified.

We have developed a spreadsheet for the participants in the CMS Initiative that can be used in performing the UDAAP risk assessment and computing a risk rating. If you are creating your own risk assessment, we suggest closely following your regulator's examination procedures and those recently published by the CFPB which can be found online. Using that criteria, you will be able to rate the risk for each element presented as low, medium or high. A numeric value can be given to each rating. For example, low=1, medium=2, and high =3. The number resulting at the end of your risk assessment will be used to give your Bank its overall UDAAP Risk Rating.

The process of performing a risk assessment is subjective and each Bank must judge its own situation as to whether an element is low risk, medium risk, or high risk given what you know about your Bank's practices, marketing, products and services, recent examinations or reviews, etc. An overall rating average of "3" will obviously mean that your Bank is at a high risk for a UDAAP violation. Further, an explanation of each item and each risk level rating will help examiners, as well as Management and the Board of Directors, to understand.

(Memrie Fortenberry)

BASEL III'S IMPACT ON RESIDENTIAL MORTGAGES

The comment period for the Basel III proposals has passed, and the banking community now awaits the final rules. Basel III proposes some fundamental changes to the calculation of a bank's capital, and many of these changes are quite complex—threatening a potential compliance burden for many institutions. Among other things, the proposals would revamp the risk weighting of many asset classes for purposes of your bank's capital calculation.

The proposed changes to the risk weighting of one to four family residential loans could have a particularly widespread impact. Current rules weight mortgage loans at either 50% or 100% depending upon a certain factors. The proposed rules would assign one of seven risk weightings ranging from 35% to 200% for each mortgage loan depending upon several factors, most notably the loan to value ratio.

As proposed, Basel III would separate mortgage loans into two groups: Category One and Category Two. To qualify as a Category One loan, the mortgage loan must meet each of the following criteria:

- The term must not exceed 30 years;
- The loan must be secured by a first lien on real property;
- The terms must require regular payments that do not:
  - Increase the loan's principal balance,
  - Allow the borrower to defer repayment of principal, or
  - Result in a balloon payment;
- The loan's underwriting must have taken into account all of the borrower's obligations (e.g., taxes, insurance, etc.) and the borrower's ability to repay assuming the loan's maximum contractual interest rate;
- The interest rate cannot increase more than 200 basis points in any 12 month period or more than 600 basis points over the loan's life;
- The borrower's ability to repay must be based upon documented, verified income; and
- The loan must not be more than 90 days past due or on non-accrual.

One to four family mortgage loans without a government guarantee that do not qualify as a Category One loan would be considered Category Two loans, including any balloon loan.

After a loan is assigned a category, its risk weight depends upon its loan to value ratio. To calculate this ratio, the amount of the loan for a first lien

residential mortgage whose principal amount cannot increase is the current loan balance. For first lien residential mortgages whose principal balances can increase, the loan is the maximum contractual principal amount of the loan, regardless of whether the loan has been fully funded. For junior lien residential mortgages, the loan amount is determined to be the maximum contractual amount of the junior loan plus the maximum contractual amount of all senior loans outstanding at the time the junior loan was originated.

The value portion of the loan to value calculation is the lesser of (1) the acquisition cost if the loan is made in a purchase transaction and (2) the property value based upon an appraisal or evaluation at the time of origination or restructuring.

Based upon a loan's category assignment and loan to value ratio, each loan would be assigned a risk weight pursuant to the following table:

Loan to Value Ratio	Risk Weight for Category 1 Loans	Risk Weight for Category 2 Loans
60% or less	35%	100%
Greater than 60% and less than or equal to 80%	50%	100%
Greater than 80% and less than or equal to 90%	75%	100%
Greater than 90%	100%	200%

While the final rules may deviate from these proposals, the proposals could significantly impact some banks' capital positions by changing the risk weighting of assets. Banks should carefully consider the final rules to determine their impact on their institution, and banks whose capital positions may be negatively impacted by these proposed rules should consider whether to take proactive steps to soften Basel III's blow to their capital account.

(Jeff Stancill)

MISSISSIPPI MEDICAID ASSET VERIFICATION PROGRAM

A number of banks in the state have received letters from the Mississippi Division of Medicaid (DOM) enclosing a form of contract with the DOM for the bank to participate in an asset verification/data match program for Medicaid applicants. The letter implied that the Mississippi Bankers Association (MBA) had worked with DOM on the program and contract and asked that banks sign and return the contract and agree to participate in the program. When it learned of the DOM letter, the MBA notified its members that while it had worked with the DOM on the legislation, it had not reviewed the form of the contract, and the MBA suggested that its member banks may want to hold off signing the contract or participating in the program until the contract could be reviewed and the MBA could make sure the form of the contract addressed several issues it believed to be important to participating banks.

The impetus for the DOM letter was House Bill 1391 which was approved by the Mississippi legislature during the 2012 session. That bill directed the DOM to implement a program for verifying assets of those persons applying for Medicaid benefits, their spouses and certain other persons whose resources are required to be considered in determining eligibility for Medicaid benefits. The bill also authorized DOM to enter into agreements with financial institutions in the state to develop and operate a data match system under which DOM would send to participating financial institutions on a quarterly basis a an electronic file containing names, Social Security numbers and other identifying information of Medicaid applicants, spouses and other persons whose resources must be considered for eligibility, and the financial institution would compare the list against its records and respond with account

numbers and balances for any names that matched. The DOM, then, can follow up with a request for additional information about those persons' accounts if necessary. The process would work much like the existing child support collection data match program.

Butler Snow was engaged by the Mississippi Bankers Association to assist the association on the bill, and we were successful in getting a number of amendments made which clarified that participation in the program is voluntary, provided for reimbursement of expenses to participating financial institutions in accordance with the cost reimbursement provisions of the federal Right to Financial Privacy Act, and granted participating financial institutions immunity from liability for participating and responding to the DOM information requests without any responsibility for notifying customers that their information had been provided, among other changes.

It was also necessary to amend Miss. Code Section 81-5-55 which generally prohibits a bank from revealing the name of a depositor or amount of his or her deposit, except in certain specified circumstances. An exception was added to permit disclosures in connection with verifications of qualification for public assistance where the Department of Human Services or the Division of Medicaid certifies to the bank that it has on file an effective written authorization from the depositor authorizing the disclosure.

As things stand today, the MBA has obtained comments on the form contract from its Bank Attorneys Committee. Those comments will be delivered to the DOM and MBA will seek to get the DOM to agree to the changes. Once that is complete, we expect MBA will advise its members so that each bank can then review the contract (with its counsel), consider what its responsibilities might be under the agreement and decide for itself whether or not to participate in the program.

Mississippi and all other state Medicaid programs are under a federal mandate to implement an automated asset verification program. The U.S. Department of Health and Human Services initially set a timetable for implementation which contemplated that Mississippi would implement a program before f.y.e. 2010, with Tennessee by f.y.e. 2012 and Alabama, Arkansas and Louisiana by f.y.e. 2013. While it appears that Mississippi is the only one of those five states to take legislative action thus far and only a few states nationwide have actually implemented a program, banks in all states should be alert to the issue.

As the Mississippi law stands today, participation in the asset verification program is entirely voluntary on the part of Mississippi banks. There is some possibility, however, that if the DOM doesn't get sufficient participation, it may seek to amend the law to make bank participation mandatory. Of course, there is a good reason for banks to participate where possible. The data match program may save the state and its taxpayers a great deal of money in the long run by helping to ensure that recipients of Medicaid benefits are truly qualified.

We will be watching for developments and will pass on any information we receive in future newsletters.

(Cliff Harrison)

UPDATE: REGULATION E REMITTANCE TRANSFER RULES

The February 7, 2013 effective date for the CFPB's final rule regarding new disclosure, error resolution rights and cancellation policies for international remittance transfers is fast approaching. There remains a good deal of uncertainty surrounding the rule and many questions linger. In fact, there are so many questions that in August thirty-two members of Congress wrote the CFPB requesting a two year delay in implementing the rule. This request was denied, and efforts continue to clarify the scope and requirements of the rule. On October 16, the CFPB conducted a webinar during which the requirements of the rule were discussed and many questions addressed. During the webinar, a website and phone number were also provided through which the Bureau will attempt to answer

questions. We have provided that contact information below.

Is Your Bank Acting as a "Remittance Transfer Provider"?

In order to comply with the rule, one should first determine whether the bank is a "remittance transfer provider" as defined in the rule. A remittance transfer provider is any person who conducts remittance transfers for a ***consumer*** to a foreign location "in the normal course of business" whether or not the consumer holds an account with the remittance provider. Banks that conduct only a small number of foreign remittance transfers per year will be exempt from the rule as this service will not be considered to be provided "in the normal course of business".

To make this initial determination, if a bank provided 100 or fewer covered remittance transfers during the previous calendar year, then the bank will not be considered to be a provider of covered transfers during the normal course of business and will not be required to comply with the rule. However, if subsequently it is discovered that more than 100 remittance transfers were provided in the current calendar year, a bank will have a period of six months or less to begin complying with the rule. The 100 total remittance transfers is a total of all remittance transfers provided; it is not separated by transfer type.

What Is a Remittance Transfer?

A remittance transfer covered by the rule is ***any*** transfer of electronic funds made in an amount greater than $15 by a consumer in the United States and sent to a recipient in a foreign country by a remittance transfer provider. This is a very broad definition and has created some confusion. Specific facts attendant to each specific foreign transfer are important to consider. Select examples of transfers covered by the rule include: (1) any request to send money from a bank to an account located in a foreign country; (2) international consumer wire transfers; (3) certain addition of funds to a reloadable prepaid card by a participant in a prepaid card program if the bank sends the prepaid card or funds to a foreign country; (4) international ACH transactions; and (5) certain pre-scheduled online bill payments or other electronic payments.

If the transfer is requested by a business, then such transfer would not be covered because the rule applies only to transactions initiated by a consumer. It is important to note, however, that a transfer initiated by a consumer and sent to a foreign business recipient would be covered. Prepaid cards will only be covered if the bank is directly involved in sending the card or the funds to a foreign country. If a consumer buys a prepaid card from your bank in the United States and your bank gives or mails the card directly to the consumer located in the United States, then that prepaid card will not be covered as it is not sent to a foreign country and the bank would have no way to know whether the consumer will send the card abroad.

Suggestions

In order to determine whether your bank falls under the definition of a remittance transfer provider, we suggest that you create a list of all of the services offered, provided by, or processed through your bank that could potentially fall under the category of an international remittance transfer. Then, determine the transaction volume per month for each type of transaction.

If, based upon the transaction analysis above, the conclusion is reached that your bank falls under the definition of remittance transfer provider, the next step you should take is to review your current disclosures and contact your vendors for assistance in preparing or modifying your disclosures in accordance with the rule. Modify your Reg E policies and procedures and record keeping requirements to reflect the new rules and associated changes. We will be providing members with an update for your MRCG or MSRCG Compliance Manual. This template can

be tailored to reflect each bank's actual practices. The next step will be to conduct training for all appropriate employees and prepare the notices

required to be displayed at physical locations and on your website.

CFPB Contact Information

The telephone number to the CFPB's Office of Regulation is (202)-435-7700 and the email address for questions is RemittanceRule@CFPB.gov. At the annual meetings, we will further discuss options for compliance and answer any questions you may have.

(Memrie Fortenberry and Michael Sheridan)

MRCG MEETING TO BE HELD ON NOVEMBER 15, 2012

The MRCG will hold its November Annual Meeting on November 15, 2012, at the Mississippi Sports Hall of Fame & Museum Conference Center, 1152 Lakeland Drive, Jackson, Mississippi. Registration will begin at 9:00 a.m. with the meeting to begin at 9:30 a.m..

During the November meeting, we will feature speakers from the FDIC and the Mississippi Department of Banking and Consumer Finance. Mitchell Pittman (FDIC) will speak on Fair Lending and will also address recent and anticipated regulatory developments, as well as a list of questions that various ones of you have sent to us. A team of examiners from the State Department of Banking will give us an update from the perspective of the Department of Banking. In addition to a brief business meeting, we will have discussion topics devoted to the anticipated "Qualified Mortgage" definition, the Reg. E Remittance Transfer Rule, and UDAAP Assessment procedures, among others.

As always, the dress code for this occasion is casual, and lunch will be provided. We ask that you fax or e-mail your registration to Liz Crabtree no later than Friday, November 9, 2012 so that arrangements for lunch can be finalized. We look forward to seeing you there.

(Ed Wilmesherr)

MRCG COMPLIANCE CALENDAR

01/16/09 – RESPA Servicing Transfer Disclosure revised	10/01/10 – Escrow requirements effective for mobile homes
07/30/09 – Reg. Z early disclosures for dwelling secured loans effective	10/01/10 – S.A.F.E. Act regulations effective
08/20/09 – Reg. Z changes on time to make payments on open-end accounts effective	01/01/11 – Risk-based pricing rules effective
08/20/09 – Reg. Z changes on notices of changes in terms on credit card accounts effective	01/31/11 – S.A.F.E. Act Registration Begins
10/01/09 – Reg. Z higher priced mortgage loan regulations effective	02/28/11 – Post Revised Notice to IOLTA Customers
10/01/09 – Reg. Z servicing practices regulations effective	04/01/11 – Appraisal Independence Final Rule Effective
10/01/09 – Reg. dwelling secured advertising disclosures changes effective	07/21/11 - Anticipated Effective Date for changes to Risk-based pricing notices
10/01/09 – HMDA changes for reporting rate spreads on higher priced mortgage loans effective	07/29/11 - S.A.F.E. Act Registration Expires
10/01/09 – Reg. Z HOEPA changes on verification of repayment ability effective	11/15/12 – MRCG Annual Meeting
11/20/09 – Reg. Z disclosures on transfer of mortgage loans effective	1/21/13 – Mortgage Loan Servicing Regulations take effect
01/01/10 – RESPA GFE and HUD-1 disclosure changes effective	1/21/13 – Combined RESPA/TILA disclosure rule final
01/01/10 – Reg. DD changes on disclosure of OD fees and providing balance information effective	01/17/13 – MRCG Steering Committee Meeting
02/14/10 – Reg. Z disclosures on private education loans effective	02/21/13 – MRCG Quarterly Meeting
02/22/10 – Reg. Z implementing changes to open-end credit and credit card accounts under Credit Card Act effective	04/18/13 - MRCG Steering Committee Meeting
02/27/10 – Reg. CC disclosure changes effective	05/23/13 - MRCG Quarterly Meeting
04/01/10 – Escrow requirements effective for site-built homes	07/18/13 - MRCG Steering Committee Meeting
06/01/10 – Unlawful internet gambling enforcement regulation compliance date.	08/15/13 - MRCG Quarterly Meeting
07/01/10 – Reg. E changes for ATM and debit card overdrafts	09/19/13 - MRCG Steering Committee Meeting
07/01/10 – FFIEC Accuracy and Integrity Guidelines effective	11/21/13 - MRCG Quarterly Meeting
08/22/10 – Reg. E rules on gift certificates and gift cards effective	