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BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Chairman, Subcommittee On Economic Goals And Intergovernmental Policy Joint Economic Committee

Credit Insurance Disclosure Provisions Of The Truth In Lending Act Consistently Enforced Except When Decisions Appealed

GAO found that the five Federal depository institution regulators enforced the credit insurance disclosure requirements of the Truth In Lending Act in a generally consistent manner. However, in 16 cases where depository institutions appealed enforcement remedies proposed for violations of the act, the Federal Deposit Insurance Corporation and the National Credit Union Administration departed from the enforcement criteria they and the other Federal regulators agreed upon. The 16 depository institutions were granted enforcement relief from making or offering reimbursements of an estimated $1.2 million to consumers.

Consistent enforcement should be achieved in the future through the act which provides precise enforcement remedies for violations on transactions completed after March 31, 1982. However, GAO believes that for transactions completed prior to April 1, 1982, both agencies should have

--developed consistent enforcement policies to deal with appealed and unappealed cases and

--adequately informed the Federal Financial Institutions Examination Council so that it could consider revising the interagency enforcement criteria.

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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

GENERAL GOVERNMENT
DIVISION

B-206497

The Honorable Lee H. Hamilton
Chairman, Subcommittee on Economic
Goals and Intergovernmental Policy
Joint Economic Committee
United States Congress

Dear Mr. Chairman:

Your letter of December 2, 1981, asked us to determine (1) whether the Federal Deposit Insurance Corporation (FDIC) was consistently enforcing the Truth In Lending Act (15 U.S.C. 1601 et seq.) disclosure requirements for insurance (life, accident, health, or loss of income) written in connection with credit transactions and (2) whether the act's regulatory burden on the private sector could be reduced. In discussions with your office, your request was broadened to include the other four Federal financial institution regulators--the Federal Reserve System (FRS), Federal Home Loan Bank Board (FHLBB), National Credit Union Administration (NCUA), and the Office of the Comptroller of the Currency (OCC). As agreed with your office, this report discusses the enforcement of the credit insurance disclosure provisions of the act. We plan to resume work on the regulatory burden question following issuance of this report.

Our review showed that of the five Federal financial institution regulators, FDIC and NCUA

--enforced the credit insurance disclosure provisions of the act in a generally consistent manner except for a limited number of appealed cases,

--did not develop consistent enforcement policies to handle appealed and unappealed cases, and

--did not adequately inform the Federal Financial Institutions Examination Council (FFIEC) 1/ that

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1/The FFIEC was established under the authority of Title X of Public Law 95-360. Generally, its purpose is to coordinate examination and supervision activities of the five Federal regulators through the establishment of uniform principles and standards for examining financial institutions and making recommendations for uniformity in other supervisory matters.

they were using enforcement criteria not specified in the policy guide on truth in lending (TIL) enforcement and thus denied FFIEC the opportunity to revise the guide to provide for consistent enforcement among the five Federal regulators.

During April 1981 through March 1982, FDIC and NCUA headquarters granted enforcement relief to 16 depository institutions--15 banks and 1 credit union, respectively--found to be in violation of the credit insurance disclosure provisions of the act. The 16 institutions, on the basis of their appeals, were granted relief from making or offering reimbursement of an estimated $1.2 million to consumers. Relief was granted under broad discretionary authority provided by the act to decide cases on equity grounds. However, the granting of relief from reimbursement on this basis was not in strict accordance with the criteria contained in the FFIEC guide. Affording relief on equity grounds differed from the enforcement results obtained in a large number of cases in which identical violations were committed under similar circumstances but were not appealed.

The broad agency discretion under the act for enforcing credit insurance disclosure violations terminates for transactions completed after March 31, 1982. Consistent enforcement should be achieved in the future through the act which provides precise enforcement remedies for violations on transactions completed after March 31, 1982.

OBJECTIVES, SCOPE, AND METHODOLOGY

The overall objective of this review was to assess Federal regulators' enforcement of the credit insurance disclosure provisions of the act to determine whether regulators were enforcing the provisions in a consistent manner. To achieve this objective, we:

--Reviewed and discussed enforcement policies and criteria with officials of the five Federal regulators and the FFIEC.

--Analyzed FDIC's and NCUA's decisions to grant enforcement relief to 16 depository institutions found to be violating credit insurance disclosure provisions of the act. The 16 decisions comprise all appeals for enforcement relief dealing with credit insurance disclosure violations acted upon by FDIC and NCUA as of March 31, 1982.

--Analyzed unappealed enforcement remedies imposed by the Atlanta field offices of the five Federal regulators on 12 depository institutions found to be violating credit insurance disclosure provisions of the act. These were all of the unappealed enforcement remedies imposed by the Atlanta field offices for credit insurance disclosure violations identified from January 1980 to May 1982.

We conducted the majority of our work at the five Federal regulators' headquarters and at the FFIEC office in Washington, D.C. To determine how enforcement policies were being implemented, we conducted limited review work at the five Federal regulators' field offices in Atlanta, Georgia. We selected Atlanta because it is one of only two cities where all five Federal regulators have field offices. The review was conducted in accordance with GAO's current "Standards For Audit of Governmental Organizations, Programs, Activities, and Functions."

BACKGROUND

The Truth In Lending Act, as amended, was designed to ensure a meaningful disclosure of credit terms in order to allow the consumer to make intelligent, informed decisions as to the cost of available credit and to protect the consumer against inaccurate and unfair credit practices. The act attempts to accomplish this by requiring creditors to follow specific rules for disclosing credit terms, particularly in disclosing finance charges (the cost of credit) and annual percentage rates (APR)--the percentage cost of credit on a yearly basis. Through disclosure of the finance charge and APR, which are specifically defined by the act, it is intended that consumers would be provided with meaningful information with which to comparison shop and make informed decisions.

TIL CREDIT INSURANCE DISCLOSURE REQUIREMENTS

Section 106(b) of the act requires that all premiums or charges for life, accident, or health insurance written in connection with any consumer credit transaction (credit insurance) be included in the finance charge. However, charges or premiums for credit insurance may be excluded from the finance charge if the insurance is not required by the creditor and

--the optional nature of the insurance is clearly disclosed in writing to the consumer,

- --the cost of the optional insurance is disclosed in writing to the consumer, and

- --the consumer separately signs a dated written document indicating his/her desire to obtain the insurance after disclosure of the cost.

Failure to make disclosures required by section 106(b) are referred to as credit insurance disclosure violations. These violations will result in an understated finance charge if the cost of the insurance was improperly excluded from the finance charge disclosed to the consumer. Understated finance charges and APRs are subject to the monetary restitution provisions of the act.

TIL ACT REQUIREMENTS RIGID AFTER A FLEXIBLE ENFORCEMENT PERIOD

Although one of the long-term effects of the act is to require enforcement agencies to order creditors to make restitution for disclosure violations in circumstances prescribed by the statute, the act provides the agencies with flexibility and broad discretion for dealing with credit insurance disclosure violations in the short term. Section 108(e) of the act generally requires enforcement agencies under certain conditions to order creditors to make monetary and other adjustments to the accounts of consumers in cases where the finance charge or APR was inaccurately disclosed.

Section 108(e)(2)(A) of the act grants enforcement agencies flexibility and broad discretionary authority for a prescribed period when imposing enforcement remedies for credit insurance disclosure violations. For transactions completed through March 31, 1982, monetary restitution was authorized, but not required, as an enforcement remedy, and enforcement agencies could require whatever remedial action that they determined to be equitable and that was authorized by law. For credit insurance disclosure violations involving transactions completed after March 31, 1982, section 108(e)(2)(A) eliminates this discretionary authority and generally requires monetary restitution. An exception is contained in section 108(e)(2)(D) which provides that enforcement agencies need not require monetary adjustments resulting from any unique circumstances involving clearly technical and nonsubstantive disclosure violations that do not adversely affect information provided to the consumer and that have not misled or otherwise deceived the consumer.

FEDERAL REGULATORS ADOPT FFIEC POLICY GUIDE

Although the law provided Federal regulators with broad discretionary authority in the short term, they adopted specific administrative enforcement criteria. In June 1980, the FFIEC issued a policy guide entitled "Administrative Enforcement of the Truth in Lending Act-Restitution." The guide (1) summarizes and explains the restitution provisions of the act and (2) provides enforcement remedies for Federal regulators to generally use during the prescribed period when the act gave them broad discretionary authority. The purpose of the guide was to achieve consistent enforcement by regulators and uniform compliance by depository institutions. The guide was adopted by the last of the five Federal regulators in September 1980.

The FFIEC guide provides two remedies for credit insurance disclosure violations involving transactions completed through March 31, 1982. First, for failure to disclose in writing that the insurance is optional, the creditor is generally required to refund all insurance premiums to consumers. Second, if the creditor disclosed the optional nature of the insurance but failed to obtain a proper signature (signed insurance option) or failed to disclose the cost of the insurance, the creditor is required, unless a claim was made on the insurance, to offer restitution of insurance premiums. The creditor is required to send a 45-day letter to each affected consumer disclosing the cost of the insurance and notifying the consumer that the insurance is optional and may be canceled within 45 days to obtain a full refund of all premiums paid. If the creditor receives no response from the consumer within 45 days, the insurance remains in effect and no further corrective action is required.

For transactions completed after March 31, 1982, the FFIEC guide refers to Section 108(e)(2)(A) of the act which requires that nontechnical and substantive credit insurance violations be subject to precise restitution requirements.

FDIC AND NCUA ENFORCED CREDIT INSURANCE DISCLOSURE PROVISIONS IN A GENERALLY CONSISTENT MANNER EXCEPT FOR A LIMITED NUMBER OF APPEALED CASES

For the vast majority of depository institutions violating the credit insurance disclosure provisions of the act, the Federal regulators told us they enforced the provisions consistently with the remedies specified in the FFIEC guide. However, we found in those few cases where depository institutions appealed, FDIC and NCUA departed from the remedies and enforcement criteria specified in the FFIEC guide which resulted in differing enforcement actions. Further, FDIC and NCUA did not develop adequate enforcement policies to handle appealed and unappealed cases consistently. In addition, neither agency informed the FFIEC that they were using criteria not specified in the guide and thus inconsistent actions among the five Federal regulators resulted.

Concerning FRS, FHLBB, and OCC, only OCC had appealed cases, and we determined that OCC's enforcement actions on these cases were consistent with the FFIEC guide. Specifically, OCC granted enforcement relief to two banks found to be in violation of the credit insurance disclosure provisions. However, relief was granted based on the conclusion that the violations were of a clearly technical and nonsubstantive nature, did not adversely affect information provided to the consumer, and did not mislead or otherwise deceive the consumer. The FFIEC guide specifically provided the agencies with this discretion.

Institutions which did not appeal required to make restitution

FDIC and NCUA found a large number of depository institutions violating the credit insurance disclosure provisions of the act. In 1980 and 1981 FDIC found about 3,100 banks in violation of the TIL credit insurance disclosure provisions. The bank violations uncovered were isolated violations and/or pattern or practice type violations. In commenting on this report FDIC said that all 3,100 banks were subject to the restitution provisions of the act. However, FDIC further commented that as a matter of practice, it normally requests reimbursement for pattern or practice type violations only. FDIC did not know how many of the 3,100 banks were cited for isolated violations and how many for pattern or practice type violations. In addition, FDIC did not know the dollar amount of restitution that banks made to consumers for credit insurance disclosure violations found as a result of its enforcement efforts.

NCUA in 1980 and 1981 found 84 credit unions in violation of the credit insurance disclosure provisions of the act. Thirty-three of these credit unions were subject to restitution requirements of the act. Of these, 17 credit unions reimbursed $87,000 to consumers and 16 had not yet completed reimbursement actions on NCUA's directives.

FDIC and NCUA officials told us that their field offices routinely imposed the remedies called for under the FFIEC guide. To substantiate whether the guide was being followed on unappealed cases, we reviewed examinations in the Atlanta field offices of the five Federal regulators. Specifically, we reviewed examinations that identified credit insurance violations for 12 depository institutions which did not appeal the enforcement remedy imposed. The 12 examinations (3 by FDIC, 5 by NCUA, 2 by FRS, 1 by FHLBB, and 1 by OCC) represented all examinations conducted in those offices from January 1980 to May 1982 with unappealed enforcement remedies for violations that were part of a pattern or practice. In each case the Federal regulators imposed enforcement remedies set forth by the FFIEC guide. Each institution was ordered to make or offer restitution of insurance premiums to consumers.

FDIC granted relief to banks on appealed cases

On the basis of FDIC examinations conducted primarily in 1980 and 1981, 15 banks appealed to FDIC and requested relief from making consumer reimbursements for violations of the credit insurance disclosure provisions of the act. The banks, for the most part, acknowledged they were in violation of the act but requested relief from enforcement remedies proposed.

The FDIC examinations showed that for the 15 banks

--3 failed to disclose the optional nature of the credit insurance,

--7 failed to disclose the optional nature of the credit insurance and also failed to obtain a separately signed and dated written statement that consumers desired the insurance,

--1 failed to disclose the optional nature of the insurance and also failed to disclose the dollar cost of the insurance,

--3, while disclosing the optional nature of the insurance, failed to disclose the dollar cost of the insurance, and

--1, while disclosing the optional nature of the insurance, failed to obtain a separately signed and dated written statement that consumers desired the insurance.

As a result of these disclosure violations, the 15 banks understated the finance charges disclosed to consumers by improperly excluding the insurance premiums from the finance charges.

In deciding the appeals, FDIC headquarters granted full relief to 12 banks and partial relief to 3 banks. FDIC headquarters acknowledged that the banks had committed apparent violations of the credit insurance disclosure provisions. The relief granted was not in strict accordance with the enforcement criteria specified in the FFIEC guide. The 15 banks were granted relief from making or offering restitution of an estimated $1.2 million in insurance premiums to customers. FDIC officials told us that they reviewed the facts and circumstances of each case to arrive at an equitable remedy.

The three banks which were granted partial relief had requested it in lieu of full relief. Instead of requiring restitution as provided in the FFIEC guide for failure to disclose the optional nature of the insurance, FDIC directed the banks to offer consumers restitution through 45-day letters. One of the banks was given partial relief for violations involving transactions completed prior to a particular examination and no relief for violations involving subsequent transactions.

NCUA granted relief to one credit union

NCUA granted enforcement relief to one credit union using criteria not specified in the FFIEC guide. The granting of relief to the credit union was important because it was used by NCUA as a basis to revise its policy for enforcing credit insurance disclosure violations.

On the basis of an examination conducted in October 1980, NCUA identified a credit union that was in violation of the credit insurance disclosure provisions of the act. The credit union, while disclosing that the insurance was optional, failed to disclose the cost of the insurance and failed to obtain separately signed statements of the consumers' desire to buy the insurance. In March 1981 the responsible NCUA regional office imposed the enforcement remedy called for under the FFIEC guide. The credit union was told to offer restitution by notifying affected consumers that they had the option to continue the insurance or obtain a full refund of premiums paid. The credit union refused to comply with the enforcement remedy and appealed the case. After much deliberation, NCUA in December 1981 granted the credit union full relief. The credit union was granted relief from offering an estimated $11,000 in insurance premiums to customers. NCUA told us that there was a preponderance of evidence to justify enforcement relief to the one credit union.

On the basis of the decision to grant relief to the one credit union, NCUA revised its policy to allow an enforcement remedy on appealed cases which was not specifically provided for in the FFIEC guide. At the time of our review, NCUA had several appeals in process at the regional level which, if decided under its revised policy, could also result in enforcement remedies not provided for in the FFIEC guide.

Basis for FDIC and NCUA departure from FFIEC guide

Our review of the case files showed that the two agencies granted relief on the basis of the broad discretionary authority contained in section 108(e)(2)(A) of the act. One key factor often used to justify relief was the depository institutions' insurance penetration rates--the percentage of consumers taking the insurance--which indicated that the insurance was optional. After nearly a year of experience in administering the FFIEC guide, FDIC and NCUA reviewed the appealed cases from a broader perspective and considered other criteria such as insurance penetration rates not addressed in the FFIEC guide.

FDIC AND NCUA DID NOT DEVELOP CONSISTENT ENFORCEMENT POLICIES

Both FDIC and NCUA allowed dual enforcement criteria to exist at the same time--one for enforcement remedies that were appealed and another for enforcement remedies that were not appealed. Both agencies allowed insurance penetration rates to be used in deciding enforcement remedies that were appealed but did not consider their use when routinely imposing enforcement remedies prior to appeal. This approach to deciding cases and granting relief was not specified in the guide.

In contesting enforcement remedies, depository institutions often cited their insurance penetration rate as evidence that their credit insurance was in fact optional. In this regard, a depository institution might argue that although it has not disclosed the optional nature of its insurance in writing as required by the act, the fact that a small percentage of its customers have taken the insurance indicates that it is in fact optional. Further, a large percentage of customers not taking the insurance would indicate that some type of disclosure was made, oral or otherwise, of the optional nature of the insurance.

FDIC should have developed a consistent policy

FDIC's Office of the General Counsel recognized a need to develop standards for deciding appeals for relief from reimbursement for TIL violations, but no standards were developed.

In an October 20, 1981, memorandum, an Assistant General Counsel advised the Division of Bank Supervision that there was a potential problem of inconsistent enforcement. The memorandum commented that requests for relief have been forwarded from FDIC regions on a piecemeal basis. The memorandum further commented that although there has been effort at the headquarters level to ensure consistent enforcement, there is concern that inconsistent enforcement could result leading to charges of arbitrary and capricious conduct.

The memorandum concluded by suggesting that:

> "One way to alleviate this problem may be to articulate, based on prior experience, some standards for internal use in deciding whether to grant relief from reimbursement. As a beginning point, it might be useful to analyze those cases in which relief has been granted and for what reasons, and those cases in which relief has been denied, and for what reasons."

Contrary to the suggestion, FDIC did not develop a standard or written criteria that could be used in deciding future appeals for relief from reimbursements.

Not only was there a need for FDIC to develop a policy with respect to appealed cases, this policy should have been designed to articulate the enforcement criteria that would be applied to cases decided before and after appeal. Although FDIC headquarters developed a pattern of granting enforcement relief based in part on insurance penetration rates, it did not advise its regional offices that insurance penetration rates were being used to grant enforcement relief.

Without specific guidance as to why relief was granted, FDIC regions enforced credit insurance violations as instructed under the FFIEC guide, while FDIC headquarters granted relief using criteria not included in the guide. The guide is silent on insurance penetration rates and, as such, these rates would not be considered by FDIC regions when routinely imposing enforcement remedies. However, from April 1981 through March 1982, FDIC headquarters used insurance penetration rates to justify granting relief, on appeal, to nine banks.

<u>FDIC relied on high penetration rates</u>

In addition to limiting consideration of insurance penetration rates only to appealed cases, FDIC headquarters in some of those cases justified enforcement relief based in part on insurance penetration rates that appeared high. These high rates may have indicated that the insurance was not optional.

FDIC headquarters cited a wide range of insurance penetration rates in justifying enforcement relief to nine banks. FDIC headquarters cited insurance penetration rates ranging from 12 to 94 percent as support for its conclusions that the banks' insurance penetration rates indicated that the credit insurance was optional. FDIC headquarters granted relief to four of the nine banks on the basis of insurance penetration rates over 50 percent. An example of FDIC's use of a high penetration rate to support enforcement relief can be seen in an excerpt from an August 24, 1981, Division of Bank Supervision memorandum on one case.

> "Given the penetration rate for credit life insurance (between 77 and 80%) and the fact that violations are isolated to the real estate loan category, the Division of Bank Supervision recommends that the bank be granted relief and that no further action be required for these violations."

<u>NCUA developed an inconsistent policy</u>

Unlike FDIC, NCUA formally revised its policy to include insurance penetration rates as enforcement criteria, but it restricted the use of such rates to only appealed cases. In November 1981, on the basis of a decision to grant enforcement relief to one credit union and with other similar appeals for relief in process at the regional level, NCUA revised its policy for enforcing credit insurance disclosure violations. NCUA recognized that the revised policy called for remedial action other than that specified in the FFIEC guide.

NCUA's revised policy, contained in a November 19, 1981, memorandum to NCUA regional directors, allowed relief from reimbursement for certain credit insurance violations under certain conditions when the insurance penetration rate was 10 percent or less.

While NCUA's objective in revising its policy was to ensure consistent and equitable enforcement remedies on appealed cases, this policy revision, which allowed for a more lenient remedy than specifically provided in the FFIEC guide, was not extended to unappealed cases. Rather, the use of insurance penetration rates was specifically excluded from consideration in cases prior to appeal. In a December 9, 1981, memorandum clarifying the policy revision, NCUA regional directors were provided the following additional guidance.

"Consumer examiners are not to conduct any penetration rate determinations as a standard examination procedure. Penetration rates will be reviewed only if the FCU [Federal Credit Union] requests a waiver of reimbursement."

NCUA DID NOT INFORM THE FFIEC

NCUA did not inform the FFIEC of its November 1981 decision which revised its policy for enforcement remedies in appealed cases. Also, NCUA did not inform the FFIEC (1) of its December 1981 decision to grant a credit union enforcement relief using criteria not specified in the FFIEC guide and (2) that at the regional level, there were other similar appeal cases which could be decided contrary to the guide.

FDIC'S EFFORTS TO INFORM THE FFIEC WERE INADEQUATE

FDIC's Division of Bank Supervision in July 1981 recognized that FDIC headquarters had granted enforcement relief to a number of banks for credit insurance disclosure violations which seemed not to be in strict accordance with the FFIEC guide. Recognizing that something needed to be done to ensure consistent enforcement among the five Federal regulators, FDIC decided to propose a change to the guide before the FFIEC Consumer Compliance Task Force.

At the August and September 1981 meetings of the FFIEC Consumer Compliance Task Force, FDIC representatives (1) discussed the problems and inequities that FDIC was experiencing in administering the credit insurance disclosure section of the FFIEC guide and (2) proposed that the guide be revised. In short, FDIC's proposal called for an easing of the enforcement remedies. The representatives on the task force from the four other Federal regulators were not in favor of FDIC's proposal. The task force recommended that FDIC's proposal be taken to the full FFIEC, i.e., the heads of each of the five Federal regulators, for consideration.

In accordance with the task force's recommendation, FDIC's proposal to amend the guide was placed on the agenda for the September 1981 FFIEC meeting. At that meeting, however, the Chairman of FDIC asked that the FDIC proposal be withdrawn from the agenda because FDIC was not fully prepared to bring the proposal before the FFIEC. No further consideration was given to FDIC's proposal by the full FFIEC or its task force.

CONCLUSIONS

FDIC and NCUA found a number of depository institutions violating the credit insurance disclosure provisions of the act. For these violations the two agencies generally imposed the enforcement remedies called for under the FFIEC guide. For 16 institutions that appealed their enforcement remedies, FDIC and NCUA granted relief from reimbursement after the appeals. The two agencies used the broad discretionary authority contained in the act to arrive at what they believed were equitable decisions to grant the 16 institutions relief from reimbursement. As a result of the relief on the appealed cases, inconsistent enforcement occurred.

Consistent enforcement of the act was an important objective that all five Federal regulators agreed to when adopting the FFIEC guide. We believe that FDIC and NCUA could have done more to obtain consistent enforcement. Both agencies should have (1) dealt with appealed and unappealed cases in a more consistent manner and (2) adequately informed the FFIEC so that it could make policy revisions to ensure application of consistent enforcement criteria among the five Federal regulators.

Inconsistent enforcement occurred because FDIC and NCUA used the broad discretionary authority in the act when deciding appealed cases, but used the more restrictive FFIEC guide on unappealed cases to impose enforcement remedies. Because the broad discretionary authority does not apply to transactions completed after March 31, 1982, there appears to be little opportunity for further inconsistent enforcement. Transactions completed after March 31, 1982, are subject to the precise restitution requirements of the act. Consequently, consistent enforcement should be achieved in the future.

AGENCY COMMENTS AND OUR EVALUATION

We furnished drafts of this report to the five Federal regulators and the FFIEC for their review and comment. The FRS and FHLBB had no comments. FFIEC responded by stating that it would be more appropriate for the concerned regulators to comment on our report. OCC stated that the report did not directly pertain to it and provided no specific report comments. FDIC and NCUA provided detailed comments as discussed below. The full text of all comments received appears in appendixes I through IV.

NCUA, while generally concurring with our conclusions, suggested that the inconsistent enforcement that we attribute to it was not significant. NCUA stated that its deviation from the policy guide was not significant enough to warrant notifying the FFIEC. We disagree. We believe that because NCUA thought it was important enough to revise its own policy by adding new enforcement criteria, then it was significant enough to advise the FFIEC.

Concerning our conclusion that NCUA had developed an inconsistent enforcement policy, NCUA explained that the policy would not, in fact, result in inconsistent enforcement. NCUA pointed out that the Credit Union Membership Insurance Society (CUMIS) insures 95 percent of all Federal credit unions against the financial impact of failing to comply with the act. NCUA further commented that CUMIS was advised of the NCUA policy decision to allow consideration of insurance penetration rates as a defense on appealed cases. CUMIS in its own interest, NCUA commented, would raise the penetration rate issue in any case in which it might be applicable.

We do not believe that NCUA should rely on CUMIS to implement consistent enforcement of NCUA policy. NCUA should have informed credit unions directly of the enforcement criteria to be used before and after appeal. It should also be emphasized that CUMIS does not represent all credit unions. The question arises as to whether the unrepresented 5 percent, or about 585 Federal credit unions, were aware that penetration rates could be used as a defense on appealed cases.

Nonetheless, we concur with NCUA that it established very strict limitations on the use of insurance penetration rates as a defense on appealed cases. These strict requirements would tend to limit the extent of inconsistent enforcement actions.

To ensure more consistent enforcement in the future, NCUA said that it is currently developing procedures which will be followed in all appeals. The procedures, NCUA commented, will be furnished to all credit unions and should ensure that NCUA enforces the act in a uniform manner.

FDIC agreed that inconsistency occurred as a result of its enforcement of the credit insurance disclosure provisions of the act but stated that the inconsistency was limited. FDIC acknowledged that there was inconsistency between the appealed cases and the unappealed cases. However, FDIC stated that our conclusion that it did not enforce the credit insurance disclosure provisions in a thoroughly consistent manner was an over generalization. Our conclusion, FDIC stated, suggested that the FDIC did not cite credit insurance violations consistently, applied the remedies in the policy guide in an erratic and inconsistent manner, and decided appeals in an arbitrary and inconsistent manner.

We believe that FDIC is reading into the report conclusions that have not been made. The report does not state or suggest that FDIC cited credit insurance violations inconsistently, applied remedies erratically, decided appeals arbitrarily, or did not follow the policy guide on unappealed cases. Our stated conclusions are based on detailed facts as presented in the body of the report, and we have implied nothing beyond these stated conclusions.

To briefly restate our point, we found that FDIC granted, on appeal, enforcement relief amounting to an estimated $1.2 million to 15 banks found to be in violation of the credit insurance disclosure provisions of the act. The enforcement results, i.e., the granting of relief, differed from the enforcement results obtained in a much larger number of cases in which identical violations were committed under similar circumstances but which were not appealed. Further, we stated in several sections of the report that FDIC's enforcement of the credit insurance disclosure provisions of the act was, in the majority of cases, consistent with the remedies it agreed to in the FFIEC guide. However, on the basis of FDIC's comments, we understand its concerns about our characterization of the instances of inconsistent enforcement that did occur. Accordingly, we made additional changes to reflect throughout the report that FDIC's enforcement was generally consistent except for a limited number of appealed cases.

Concerning our conclusion that FDIC did not develop a consistent enforcement policy, FDIC stated that there was a certain amount of truth to our conclusion but that it must be placed in context. FDIC stated it determined early in implementing the policy guide that the guide frequently produced unreasonable and unfair enforcement results for credit insurance violations. FDIC commented that it attempted to develop a consistent policy for dealing with credit insurance violations on an interagency basis within the context of the FFIEC.

We believe that for FDIC to more fully address its concern about the fairness of the policy guide, it could have taken additional actions. Specifically, FDIC could have devised a policy to ensure that the equity it was extending to appealed cases through enforcement relief was also extended to unappealed cases or, alternatively, advised banks of the different criteria applicable to the handling of appealed and unappealed cases. We agree with FDIC that it decided on the best approach to maintain consistent enforcement actions on appealed and unappealed cases by initiating steps to get the policy guide revised on an interagency basis within the FFIEC. However, FDIC did not follow through with its initial steps to revise the guide on an interagency basis. Even if FDIC had followed through and was unsuccessful, we believe that it could have taken action on its own to ensure fair and consistent enforcement within FDIC.

FDIC disagreed with our conclusion that it failed to adequately inform the FFIEC that it was deviating from the policy guide on appealed cases. FDIC commented that it discussed the difficulties it was having with the policy guide with the Consumer Compliance Task Force of the FFIEC, proposed a solution, was prepared to discuss it in good faith, and stood ready to provide whatever additional information the FFIEC might find useful. The staff members from the other agencies represented on the task force opposed FDIC's proposed solution.

We clearly pointed out in the report that FDIC notified the Consumer Compliance Task Force of the FFIEC and proposed a change to the policy guide. However, we question whether FDIC stood ready to provide whatever information the FFIEC might have needed in considering a change to the policy guide. As FDIC is fully aware, the Consumer Compliance Task Force, although not in favor of FDIC's proposal, recommended that the proposal be considered by the full FFIEC. As we stated in the report, FDIC's proposal was placed on the agenda for consideration at the September 1981 FFIEC meeting. At that meeting, the Chairman of FDIC withdrew the FDIC proposal stating that the agency was not prepared to discuss it. FDIC did not introduce the issue in subsequent FFIEC meetings. Because FDIC did not permit the proposal to change the policy guide to be considered by the full FFIEC as recommended, we concluded that FDIC's notification attempts were inadequate.

Concerning our conclusion that FDIC should have developed a consistent policy, FDIC commented that the report did not recognize FDIC's efforts to inform its regional offices of the appeal decisions and to encourage banks to file appeals if appropriate. During our review, we inquired at FDIC's headquarters and Atlanta regional office about any guidance on appealed cases provided to FDIC field offices. We were provided with a November 2, 1981, memorandum from the Associate Director, Division of Bank Supervision to Regional Directors transmitting a summary of actions on appealed cases. The memorandum, in our opinion, was of little value as guidance. For each appeal decision the memorandum merely listed the bank, the violation committed, and the decision by FDIC headquarters to grant or deny enforcement relief. The memorandum contained no explanation as to why relief was granted or denied nor were there any comments about encouraging banks to appeal.

Concerning insurance penetration rates, FDIC took issue with the example that we used to show that FDIC was relying on high penetration rates in granting enforcement relief. In the example cited, FDIC granted enforcement relief based in part on an insurance penetration rate of between 77 and 80 percent. FDIC commented that an 80 percent insurance penetration rate is not high and is more indicative of voluntary rather than mandatory insurance because it shows that one out of five borrowers did not take the insurance.

We questioned FDIC's use of high penetration rates and suggested that they may indicate the insurance was mandatory rather than voluntary for several reasons. First, while FDIC was relying in some cases on penetration rates as high as 80 percent, NCUA was limiting its consideration of penetration rates to 10 percent or less. Second, FDIC told us that it had not established any limits or criteria on the use of insurance penetration in determining the voluntariness of credit insurance. The wide difference between FDIC's and NCUA's consideration of insurance penetration rates is a clear illustration of why we believe that both agencies should have more adequately informed the FFIEC of their deviations from the policy guide.

FDIC also commented on a number of statements in the report apart from our principal conclusions. Most of these comments were technical in nature, and we made appropriate changes in the report as we deemed necessary.

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As arranged with your office, unless you publicly announce its content earlier, we plan no further distribution of this report until 14 days from its issue date. At that time, we will send copies to interested parties and make copies available upon request.

Sincerely yours,

W. J. Anderson

William J. Anderson
Director

Federal Financial Institutions **Examination Council**, Washington, D.C. 20219

September 13, 1982

Mr. William J. Anderson
Director
United States General
Accounting Office
Washington, DC 20548

Dear Mr. Anderson:

Thank you for your letter of August 31 transmitting the General Accounting Office's draft report entitled, "Truth in Lending Act Consistently Enforced Except When Decisions Appealed." The Examination Council appreciates being given the opportunity to comment on the report.

After reviewing the draft report, the Council feels it would be more appropriate for the individual agencies that wish to provide comment to address the conclusions directly.

Sincerely,

Robert J. Lawrence
Executive Secretary

Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Federal Home Loan Bank Board, National Credit Union Administration, Office of the Comptroller of the Currency

Comptroller of the Currency
Administrator of National Banks

Washington, D.C. 20219

September 22, 1982

Mr. William J. Anderson
Director
General Government Division
U. S. General Accounting Office
441 G Street, NW
Washington DC 20548

Dear Mr. Anderson:

We appreciate the opportunity to comment on the General Accounting Office's (GAO) draft report entitled "Truth In Lending Act Consistently Enforced Except When Decisions Appealed." The overall objective of GAO's review was to assess the effectiveness and consistency of Federal regulators' enforcement of the credit insurance disclosure provisions of the Truth in Lending Act. The draft report, which was distributed to the five Federal financial institution regulators, contains no specific recommendations to the Office of the Comptroller of the Currency (OCC).

We were pleased to see that the OCC was not mentioned as having any deficiencies in the enforcement of the Truth in Lending Act. The OCC will continue to work for and promote consistent enforcement of credit insurance disclosure provisions.

We look forward to GAO resuming work on the regulatory burden question following issuance of this report.

Sincerely,

C. T. Conover

C. T. Conover
Comptroller of the Currency

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

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Mr. William J. Anderson, Director
General Government Division
U. S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Anderson:

As requested in your August 31, 1982 letter, we are forwarding our comments on your draft report entitled "Truth in Lending Act Consistently Enforced Except When Decisions Appealed."

As a matter of information we would like to provide two items of information regarding conclusions reached in the report.

First, the report concludes that NCUA's "revised" enforcement policy would be applied in an inconsistent manner since only those credit unions which appealed would be afforded penetration rate consideration. While this may appear to be the case, such inconsistency would not, in fact, occur.

CUMIS Insurance Society offers insurance to protect credit unions from the financial impact of failing to comply with the provisions of the Truth in Lending Act. According to information we have received from CUMIS, in excess of 95% of all credit unions have purchased this protection. Pursuant to the insurance agreement, the credit union must notify CUMIS whenever violations requiring reimbursement are identified. This notification provides CUMIS the opportunity to review the credit union's documents prior to making the reimbursement. CUMIS reviews the credit union documents to determine whether they agree with NCUA's determination that reimbursable violations exist. Accordingly, CUMIS has prior knowledge of and is involved in almost all credit union reimbursements.

CUMIS was furnished a report detailing NCUA's policy decision and specifying how and when NCUA would consider penetration rates as a defense against reimbursement. CUMIS, in its own interest, would raise the penetration rate issue in any case in which it might be applicable. Therefore, as a practical matter, almost all credit unions had the opportunity to request waiver consideration on the basis of penetration rates.

Very few credit unions would meet the extremely low penetration rate standard imposed by NCUA. Additionally, verification of penetration rates could be a very time consuming task. Considering these two factors and the fact that CUMIS has a vested interest in determining penetration rates, NCUA examiners were instructed not to conduct penetration rate determinations as a standard

NATIONAL CREDIT UNION ADMINISTRATION
WASHINGTON, D.C. 20456

examination procedure. This instruction was issued in order to better allocate limited examiner resources since we knew that in virtually every case in which it would be pertinent, CUMIS would review the penetration rate.

Second, page 12 of the report states that both NCUA and FDIC officials agreed that their agencies should have reported their "inconsistent" actions to the FFIEC. While our staff agrees that "significant deviations from the policy guide" should be reported to the FFIEC, our staff did not concur that the one situation involving NCUA represented a significant deviation. *

We concur with your conclusion that consistent enforcement among the agencies and within each agency is vital. In an effort to better achieve this goal, our staff is presently developing appeal procedures which will be followed in all appeals. These procedures will be furnished to our regional offices and to all Federal credit unions. This will ensure that NCUA enforces the statute in a uniform manner and that all credit unions are afforded equal access to appeal procedures. Additionally, we will continue to inform the FFIEC if significant departures from the adopted policy guide occur.

Thank you for the opportunity to comment on your draft report. If you have any questions regarding our comments, please let me know.

Sincerely,

E. F. Callahan

E. F. CALLAHAN
Chairman

*GAO note: This section of the report was deleted.

FDIC

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, D.C. 20429

OFFICE OF DIRECTOR · DIVISION OF BANK SUPERVISION

September 24, 1982

Mr. William J. Anderson, Director
General Government Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Anderson:

Your August 31 letter requested comment on an attached GAO draft report entitled "Truth in Lending Act Consistently Enforced Except When Decisions Appealed."

At the outset, we would question the accuracy and possibly misleading character of the title since the report itself focuses rather narrowly on the credit insurance disclosure provisions of the Act and not the entire Truth in Lending Act as the title implies.

Looking more importantly at the conclusions reached, however, we agree with the principal point made in the report that our Board of Directors, in the exercise of its equitable discretion, chose not to apply the remedies prescribed in the interagency Truth in Lending Enforcement Policy Guide in a number of appealed cases involving credit insurance disclosure violations. The decision of our Board in each case was based on the specific facts and circumstances. To the extent the results obtained in these relatively few appealed cases differed from the results obtained in the field where the remedies prescribed in the Policy Guide were being routinely applied in accordance with outstanding instructions, inconsistency in enforcement results occurred. By and large, the relatively few banks that appealed from Regional Office requests that they reimburse their customers for credit insurance violations fared better (i.e., were granted relief from reimbursement in whole or in part) than the large majority of banks that complied with such requests and followed the remedies prescribed in the Policy Guide. To keep matters in perspective, however, it should be noted that there were no inconsistencies in the application of the Policy Guide remedies in the field or in the decisions of our Board in the relatively few cases that were appealed. Consequently, in light of the character and limited extent of the inconsistent enforcement results that did occur, we believe the conclusion (page 1 of the report) that the "FDIC . . . did not enforce the credit insurance disclosure provisions of the act in a thoroughly consistent manner," over generalizes and suggests, in a very misleading way, that the FDIC did not cite credit insurance violations consistently, applied the remedies in the Policy Guide in an erratic and inconsistent manner or decided appealed cases in an arbitrary and inconsistent manner, none of which is supported in the report.

The second major conclusion reached (page 1) was that the FDIC failed to "develop consistent enforcement policies to deal with appealed and unappealed cases."

As with the first conclusion, there is a certain amount of truth here which must be placed in context. In analyzing the specifics of the appealed cases and considering the arguments advanced, it soon became apparent to staff and the FDIC Board that the remedies for credit insurance violations prescribed in the Policy Guide would frequently produce unreasonable or unfair results. Consequently, our Board in these cases properly refused to follow the Policy Guide and opted instead for an equitable remedy which was generally complete or partial relief from reimbursement. This development, in turn, raised serious questions as to the fairness and reasonableness of the remedies prescribed in the Policy Guide which had been developed on an interagency basis by staff based on an analysis of the nature of credit insurance violations and the purposes of the credit insurance disclosure requirements of the Truth in Lending Act. Since the decided cases suggested the remedies prescribed in the Policy Guide were inappropriate for routine application in the field, the Director of FDIC's Division of Bank Supervision sought to have the Policy Guide remedies reconsidered by the Consumer Compliance Task Force of the FFIEC. A copy of his letter to this effect is enclosed (Exhibit I).* This was done not only in the interest of consistency, both within the FDIC and with the other enforcement agencies, but more importantly in the interest of fair and sensible regulation. When the issue of revising the Policy Guide remedies was presented to the Consumer Compliance Task Force, there was no sentiment among the other agencies for reopening the issue since they reportedly were not experiencing the problems the FDIC was having and the issue would become moot in any event on April 1, 1982, when the authority of the agencies to apply an equitable remedy for credit insurance violations would expire. Consequently, it is clear from this sequence of events that the FDIC did attempt to develop a consistent enforcement policy for dealing with credit insurance violations but felt constrained to do so on an interagency basis within the context of the FFIEC since the Policy Guide itself was an FFIEC product.

The conclusion that the FDIC failed to develop consistent enforcement policies also ignores efforts to inform our Regional Offices of our Board's decisions on reimbursement appeals and encourage banks under our supervisory jurisdiction to file an appeal if they believed they qualified under some statutory exception.

We disagree categorically with the third major conclusion (page 1) that the FDIC failed to adequately inform the FFIEC that they were using criteria not specified in the Policy Guide and thus denied the FFIEC an opportunity to revise the Policy Guide to provide for consistent enforcement.

*GAO note: Not included for the sake of brevity.

At the outset, we reject the premise implicit in this conclusion that in order to permit the FFIEC to adequately consider an issue, an agency must go beyond raising the issue, offering a proposed solution and being prepared to discuss and consider it in good faith while standing ready to provide whatever additional information the FFIEC might find necessary or useful. This is exactly what the FDIC did. As the enclosed letter (Exhibit I) indicates, the FDIC explained the difficulties it was having with the Policy Guide remedies and also the differences in case results being obtained. This was done at the practical working level (Consumer Compliance Task Force) at which any changes must be initiated given the organizational structure and operating scheme of the FFIEC. The other agencies represented on the Task Force opposed revision.

Insofar as informing the FFIEC of FDIC criteria for granting relief, the issue in our view has never been penetration rates per se but whether the offering of credit insurance was optional in fact apart from any disclosure errors that may have occurred. Penetration rates were used simply as important indicators of whether credit insurance was optional in fact rather than required as a condition of each loan. The FFIEC was informed of our criterion of voluntariness in fact in the FDIC proposal for revising the Policy Guide remedies. This proposal was submitted to the FFIEC and opposed by the other agencies (Exhibit II).* Under these circumstances, we believe the FDIC had quite adequately informed FFIEC of the FDIC's criterion for granting relief from reimbursement for credit insurance violations and the FFIEC could well have pursued revision of the Policy Guide remedies were it disposed to do so.

Apart from the principal conclusions in the report, there are a number of other statements with which we disagree. These are dealt with serially as follows:

1. The penultimate paragraph on page 4 states that the Policy Guide "provides enforcement remedies for Federal regulators to use during the prescribed period when the act gave them broad discretionary authority."

The categorical nature of this statement overlooks the introduction to the Policy Guide which states that it "also explains corrective actions the financial regulatory agencies generally intend to take in those situations in which the Act gives the agencies the authority to take equitable remedial action." (Emphasis supplied.) In other words, the Policy Guide itself contemplates some flexibility and judgment in fashioning remedies in particular cases and recognizes that it may be neither appropriate nor desirable to always apply the remedies prescribed in the Policy Guide in an automatic, inflexible manner in the interest of consistency.

2. The last paragraph on page 5 mentions that the "OCC granted enforcement relief to two banks found to be in violation of the credit insurance disclosure provisions." However, the report concludes that these actions were consistent with the Policy Guide since "relief was granted based on the conclusion that the violations were of a clearly technical and nonsubstantive nature, did not adversely affect information provided to the consumer, and did not mislead or otherwise deceive the consumer."

*GAO note: Not included for the sake of brevity.

Apart from the merits of these cases (i.e., how the understated APR's and finance charges that resulted from the insurance disclosure errors can properly be characterized as nonsubstantive and not adversely affecting information provided the consumer), we fail to perceive the logic by which an inconsistent enforcement result (i.e., relief) is suddenly rendered consistent because a statutory provision is relied upon different from that relied upon by the FDIC. Obviously, we have not had access to or analyzed these two cases, but we very much doubt that these two cases are factually very different from those in which the FDIC granted relief. In truth, we are inclined to believe that all three agencies that had appealed cases deviated from the Policy Guide remedies and for good reason; namely, that application of the remedies to the specifics of these cases would produce unfair or unreasonable results.

As an aside, it is interesting to note that the report ventures no opinion on the Policy Guide remedies but only on the question of consistency. While we realize that consistency was the only issue raised by Congressman Hamilton, an analysis of the fairness and reasonableness of the Policy Guide remedies could well help to explain the deviations from those remedies that did occur.

As a final comment on the OCC cases, in the interest of accuracy, the last sentence on page 5 states that the "FFIEC guide specifically provided the agencies with this discretionary authority" (the authority relied upon by the OCC to grant relief).

In point of fact, the Policy Guide provides none of the agencies with any authority to grant relief, all of which is derived from section 108(e) of the Truth in Lending Act.

3. The discussion in the first paragraph on page 6 is inaccurate and misleading in several respects. It states that because the "FDIC did not know how many of the 3,100 banks were cited for isolated violations and how many for pattern or practice type violations . . . the total number of FDIC supervised banks subject to the restitution provisions of the act is also unknown." In point of fact, all 3,100 banks were subject to the restitution provisions of the act since the Act authorizes restitution for isolated violations as well as for pattern or practice type violations although the agencies, as a matter of practice, have normally requested reimbursement for pattern or practice type violations only. Furthermore, the characterization of violations in the FDIC's statistical system as being "systemwide" represents for analytical purposes a reasonable proxy for pattern or practice type violations and yet the report overlooks this data which was furnished to it and explained.

The statement "[I]n addition, FDIC did not know the dollar amount of restitution that banks made to consumers as a result of its enforcement effort" is incorrect since reimbursement figures were furnished the GAO. If what is meant is that the statistical system alone does not reveal the amount of reimbursement obtained as a result of credit insurance violations alone, this should be stated as such. In addition, it is not even correct to say the FDIC does not "know" the dollar amount of restitution attributable to credit insurance violations since the statistical system identifies individual bank files and the GAO, if it chose to and believed the information significant enough, could compile the data by reviewing individual bank files. Not having information conveniently available is very different in our view from not knowing or having the information at all.

4. The statement at the bottom of page 8 and the top of page 9 to the effect that the FDIC "denied" the use of penetration rates when routinely requesting remedial action prior to appeal is a mischaracterization. The FDIC didn't "deny" anything but rather permitted the field organization to continue to use the Policy Guide remedies after abandoning its effort to change those remedies at the FFIEC level. To characterize this as a "denial" of the use of penetration rates distorts the facts. Moreover, as discussed above, the issue was never penetration rates anyway but rather voluntary purchase.

5. The discussion in the first paragraph under the heading "FDIC should have developed a consistent policy" (page 9) misses the point. There was no inconsistency among appealed cases which, as the GAO's comments themselves indicate, the Assistant General Counsel's proposal was designed to address, but rather between the Board's decisions and routine field enforcement action. Moreover, insofar as the appealed cases are concerned, our Board has generally preferred to decide cases on their own merits with due regard for its own precedents but without necessarily being constrained by articulated policy standards for every type of case.

The first sentence of the last paragraph on page 9 continues to reflect this misunderstanding regarding the inconsistency that occurred when it continues to allude to the "need for the FDIC to develop a policy for more consistent enforcement with respect to appealed cases." It is not apparent from the GAO's report where inconsistent enforcement occurred with respect to appealed cases.

6. The statement at the bottom of page 9 to the effect that the FDIC "did not advise its regional offices that insurance penetration rates were being used to grant enforcement relief" is not entirely accurate. While it is true that the FDIC did not issue an official directive to the field modifying the FFIEC Policy Guide, penetration rates were discussed orally from time to time with Regional staff in connection with pending cases.

7. It is difficult to address the issue of high penetration rates (page 10) as a basis for relief without more particulars. Certainly, in the one example given, the 77 to 80 percent penetration rate cited was not high since it indicates that at least one in five borrowers did not take credit insurance, a result much more consistent with voluntary purchase rather than mandatory purchase as a condition of each loan.

Mr. William J. Anderson - 6 - September 24, 1982

8. As indicated above, we disagree with the discussion on pages 10 and 11 to the effect that the FDIC's efforts to inform the FFIEC were inadequate. The FFIEC staff was well aware that the FDIC deviated from the Policy Guide on credit insurance appeals since the matter was often discussed at meetings of the Consumer Compliance Task Force. Moreover, in deciding appealed cases, we regarded voluntariness in fact in the purchase of credit insurance as the important criterion (and not penetration rates per se), and quite adequately informed the FFIEC of this criterion by structuring our proposed revision of the Policy Guide remedies to make voluntary purchase a critical factor. Under the circumstances, we believe the FFIEC had ample opportunity to make informed revisions to the Policy Guide if it had been disposed to do so.

Sincerely,

James L. Sexton
Director

Enclosures *

*GAO note: Not included for the sake of brevity.

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