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Dodd-Frank 1073: Changes to the new fabric of banking

In last year's Sibos Edition of **Momentum*****, Wells Fargo provided an overview of Section 1073 of the Dodd-Frank Act, titled "Dodd-Frank 1073 — The New Fabric of Banking," which was an overview of the then-considered "final" regulations (Rule). On April 30, 2013, the U.S. Consumer Financial Protection Bureau published a major revision of the Rule that introduced significant changes. This article provides an overview of those changes to the Rule and expected impact on the payments business.***

Section 1073 of the Dodd-Frank Act ("Dodd-Frank") introduced new regulatory requirements related to cross-border electronic payments originated by a natural person for personal, family, or household purposes through that natural person's accounts located in the U.S. ("U.S. consumer"). The aim of the regulation was to provide this class of U.S. consumer with full transparency regarding all costs and delivery terms relating to these payments.

In order to accomplish this, the Rule required that U.S. remittance transfer providers, including banks, provide certain disclosures at the time a payment was initiated. Additionally, U.S. remittance transfer providers were required to establish a strict framework for payment cancellation and error resolution. The Rule presented many challenges to providers and, as a result, the Consumer Financial Protection Bureau (CFPB) opened the Rule up for reconsideration and in order to revise certain provisions.

On April 30, 2013, the CFPB published the new Final Rule with its official interpretation. The Final Rule introduces substantial changes to the former Rule's disclosure requirements, sender liability, and the effective date.

Summary of the Final Rule's most significant changes

The primary change introduced by the Final Rule is related to information that U.S. remittance transfer providers/financial institutions (U.S. RTPs) have to include in the disclosures they provide to their U.S. consumer clients. These can be summarized as follows:

- **Disclosure of foreign taxes:** U.S. RTPs will not need to disclose foreign taxes of any kind (national or sub national). Instead, the U.S. RTP may simply provide text in the disclosure that advises the U.S. consumer that foreign taxes may apply. The conditions by which U.S. RTPs may use such text and its wording and format are detailed in the Final Rule.

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- **Disclosure of Intermediary and Recipient Institution Fees:** The changes to foreign fee disclosures can be summarized as follows:
    - o **Recipient Institution Fees:** U.S. RTPs will not need to disclose fees that are defined as "non-covered fees," which are broadly defined as fees that the recipient financial institution would charge for applying the credit to the final beneficiary.[1] Instead, the U.S. RTP may simply provide text in the disclosure that advises the consumer that recipient institution fees may apply. The conditions by which U.S. RTPs may use such text — as well as its wording and format — are detailed in the Final Rule and sample disclosures.
    - o **Intermediary Fees:** U.S. RTPs will have to disclose all intermediary lifting fees, regardless of whether the lifting fee has been charged by a contracted intermediary (in which case it has to be exact) or by any other intermediary (in which case it may, for the time being, be estimated).[2]
- **Optional disclosure of foreign fees and taxes:** In the event that the U.S. RTP does have information about recipient institution fees and foreign taxes, they may select to optionally disclose estimates of these in the "below the line" text of the disclosure. These estimates cannot be incorporated in the calculation of the total amount to be paid to the beneficiary. The U.S. RTP would not be liable from an error resolution perspective if the optionally disclosed estimates were inaccurate as long as these estimates were based upon "reasonable sources of information" which are listed in the Final Rule.

Additionally, the new Final Rule introduces changes to a U.S. RTP's liability for certain errors a sender might make in the payment instructions a sender provides to its U.S. RTP. The new Final Rule eliminates the U.S. RTP's liability in the event an error was caused because the sender gave incorrect beneficiary account number information. Additionally, the new Final Rule extends release of liability to incorrect bank identifier information the sender may provide. In both cases, the new Final Rule defines some steps and criteria the U.S. RTP needs to fulfill prior to executing the payment (including the validation of the bank identifier code the sender providers to the U.S. RTP prior to the execution of the payment).

Other aspects of the Rule related to foreign exchange and availability date disclosures, as well as cancellation and error resolution rights, were not amended by the new Final Rule and remain materially unchanged.

Impact on the banking industry

The new Final Rule generally relaxes some of the requirements over which industry participants have previously expressed concerns. Many U.S. financial institutions, which had previously thought of exiting the international U.S. consumer payments business or severely curtailing availability and service features, have an opportunity to re-evaluate those decisions. This will inevitably lead to more options for U.S. consumers, which benefits both them and their service providers.

By eliminating the need to disclose fees that the final beneficiary's bank charges its beneficiary for the processing of an incoming credit, U.S. RTPs at this stage do not need to immediately acquire this information (which is typically difficult to obtain and manage, is variable by beneficiary, and is in many countries protected by privacy laws).

This also means the new Final Rule focuses transparency efforts on those fees which do affect the sender and the beneficiary and which may not have been traditionally known to them. These are lifting or deduction fees agreed to by banks for the intermediation of payments. Since the sender and beneficiary are not party to these correspondent commercial agreements, up to now they have not had insight into the fees these agreements imposed onto their payments.

Payments executed using the BEN or SHA charge instruction code created a reduction in the principal amount and often led to inquiries by either the sender or beneficiary about which party deducted a fee and why. By providing more transparency around these fees, U.S. consumers will be able to make a more informed choice when selecting payment providers. This will ensure that U.S. financial institutions also more competitively evaluate the correspondent lifting fee or charging agreements they engage in with their foreign partner banks.

U.S. RTPs may seek to adjust the routing of their payments in order to better manage intermediary fees and their ability to disclose them. This may cause the following trends:

- U.S. RTPs with extensive global correspondent networks will likely increase the use of split advised cover payments. These banks will send an MT103 directly to the beneficiary's bank and only route bank-to-bank funding through intermediaries. By doing this, U.S. RTPs can attempt to eliminate intermediary lifting fees. This would directly benefit the U.S. consumer and beneficiary since the principal amount of the payment would be preserved. Contrary to payments sent with OUR charge instructions, cover payments provide U.S. RTPs with a relatively cost-effective way of meeting the requirements of the regulation while providing U.S. consumers the value add of principal preservation up to the beneficiary's bank. Since the new Final Rule does not require the disclosure of fees the beneficiary bank charges on behalf of their commercial relationship with the beneficiary, the direct MT103 resulting from these payments can be

Dodd-Frank 1073 Toolbox 2.0

FX and USD payment tools	Fee tools	Disclosure production support	Error resolution tools
FX payments	**Wells Fargo's fees:** Beneficiary deduction fees, Account analysis fees	Country-level intermediary bank fee estimates with availability date factors	*CEO*® portal *CyberInquiry*℠
USD payments	**Foreign intermediary fees:** Book transfers, GP.Intraday, FX OUR payments	Direct look-up and disclosure production tools (work in progress)	International customer care
Foreign currency nostros			FX investigations

Not legal advice. Consult your counsel for advice unique to your institution.

executed with BEN or SHA charge instructions, allowing the beneficiary's bank to freely charge their fee without the increased cost and burden of MT191 charge backs associated with OUR payments.

- The ability of U.S. RTPs to comply with the regulation in this manner is dependent on the size of their global correspondent network and, more specifically, the number and reach of SWIFT RMAs their institution maintains. In addition, executing payments (especially those not denominated in USD) with OUR charge code instructions may continue to be an option for payments to beneficiary banks with which the U.S. RTP does not maintain an RMA. Smaller U.S. RTPs that do not have an extensive SWIFT RMA footprint, or are not SWIFT participants, might consider partnering with larger banks who can downstream this service or might consider estimating intermediary fees.
- Requirements related to the disclosure of foreign currency exchange rates at which payments may be converted remain unchanged in the new Final Rule. Because of the need to disclose the rate at which the payment will be converted, regardless of which bank performs the conversion, U.S. RTPs will attempt to convert more U.S. consumer payments at the point of sale.

Wells Fargo's approach within the new Final Rule

With more than 9,000 stores and 12,000 ATMs in the United States, Wells Fargo is one of the largest providers of U.S. consumer banking services in the U.S. Additionally, Wells Fargo's domestic correspondent banking business services over 1,600 U.S. financial institutions, most of which also provide payment services to U.S. consumers executing cross-border payments from their U.S.-domiciled accounts. Given such a broad footprint, efforts to comply with the provisions of Dodd-Frank are of primary strategic importance to Wells Fargo.

Based upon the requirements of the new Final Rule, Wells Fargo has adjusted the solutions it will be implementing within its own retail lines of business, as well as those it will be offering to its domestic U.S. financial institution clients.

From a disclosure and fee perspective, the focus of these solutions is on those routing mechanisms Wells Fargo can implement to manage intermediary fees. A key component in Wells Fargo's efforts to build Dodd-Frank compliant tools is our Global Financial Institutions line of business, which maintains more than 2,000 relationships in 135 countries around the world.

With extensive routing capabilities supported by 34,000 enterprise-wide SWIFT RMAs and a routing database containing over 56,000 bank records, our correspondent network effectively creates Wells Fargo's global distribution system for U.S. consumer payments.

[1] Please note that industry consensus has not yet been established as to the exact definition of non-covered recipient institution fees. We will continue to seek clarification from the CFPB on this matter and will advise you accordingly.

[2] The Official Interpretation of the Final Rule clearly states that the CFPB will continue to monitor the industry's ability to disclose recipient institution fees and taxes and that they may amend the Final Rule in the future if they believe the industry has created the ability to disclose those accurately.