InfoBytes

September 9, 2011

Topics In This Issue

Federal Issues

Consumer Financial Protection Bureau Issues Request for Information on Consumer Financial Products and Services Offered to Servicemembers. On September 6, the Consumer Financial Protection Bureau (Bureau) issued a Request for Information on Consumer Financial Products and Services Offered to Servicemembers. The request was consistent with the Bureau's responsibilities under Section 1013(e) (1) of the Consumer Financial Protection Act of 2010, which requires the Bureau to "educate and empower servicemembers and their families to make better informed decisions regarding consumer financial products and services...." The Bureau's Office of Servicemember Affairs (Office), which is seeking the requested information, is particularly interested in data on products and services (as well as associated programs and policies) "that are tailored to the unique financial needs of servicemembers and their families." The Office will use the information provided to it to develop a "knowledge base" of consumer financial products and services used by servicemembers. That "knowledge base" will inform the Office's planning regarding education and outreach initiatives, the monitoring of consumer complaints, and "other consumer protection measures." The Bureau has encouraged comments from consumers, financial services providers, organizations and other members of the public. Comments are due by September 20, 2011. Click here for the text of the Bureau's *Federal Register* Notice of the Request for Information.

FINRA Fines Broker-Dealers for Excessive Handling Fees. On September 7, the Financial Industry Regulatory Authority (FINRA) announced that it has fined five broker-dealers for mischaracterizing commission charges as fees for handling services. The five firms had charged handling fees between $65 and $99 per trade in addition to commission and FINRA found that these fees far exceeded the actual cost of the handling-related services. The firms were each fined between $60,000 and $300,000. Click here for a copy of FINRA's press release.

SEC Adjusts Registration Fee Rates. On August 31, the Securities and Exchange Commission (SEC) ordered the annual adjustment of securities registration fees for fiscal year 2012, as required by the Dodd-Frank Act. The SEC determined the fee rate for fiscal year 2012 to be $114.60 per million. This fee rate is effective October 1, 2011 and applies to the collection of fees in connection with the registration of securities, specified repurchases of securities, and proxy solicitations and statements in corporate control transactions. Click here for a copy of the Order.

Courts

Ninth Circuit Affirms Dismissal of Class Action Challenging MERS. On September 7, the U.S. Court of Appeals for the Ninth Circuit affirmed the dismissal of a putative class action against the Mortgage Electronic Registration System (MERS). *Cervantes et al. v. Countrywide Home Loans, Inc., et al.*, No. 09-17364 (9th Cir. Sept. 7, 2011). Among other things, plaintiffs alleged that MERS, several mortgage lenders (some who originated the named plaintiffs' loans; others who were alleged "shareholders in MERS" or "members of the MERS System"), and Fannie Mae and Freddie Mac engaged in a conspiracy to commit fraud through the use of MERS. At loan closing, each named plaintiff executed a deed of trust designating MERS as a nominee for the lender and the lender's "successors and assigns," and as the deed of trust's "beneficiary." According to plaintiffs, MERS is a "sham entity" and the use of MERS "impermissibly 'splits' the note and deed by facilitating the transfer of the beneficial interest in the loan among lenders while maintaining MERS as the nominal holder of the deed." Defendants moved to dismiss, primarily arguing that plaintiffs had failed to (and could not) allege the elements of their causes of action. The district court granted the motions, and rejected as futile plaintiffs' request to amend the complaint to add a claim for "wrongful foreclosure" based on the operation of MERS. Plaintiffs appealed, and the Ninth Circuit affirmed. First, the court agreed with the district court that plaintiffs had failed to adequately set forth several elements of a civil conspiracy to commit fraud claim. To the contrary, the court found that the MERS deeds of trust, which plaintiffs signed at closing, fully disclosed the nature of MERS' interest in their loans. Second, the court ruled that the district court did not abuse its discretion by denying plaintiffs the opportunity to amend their complaint, noting that this refusal was particularly appropriate where Arizona state courts have not yet recognized a wrongful foreclosure cause of action. Finally, the court rejected plaintiffs' conclusion that no party has the power to foreclose. As the court recognized, the foreclosure trustees in this case initiated foreclosure as agent of and in the name of the lenders, who were the parties entitled to payment on the loans. Even accepting plaintiffs' theory, the court held, the notes and deeds of trust were not "irreparably split" because any such "split only renders the mortgage unenforceable if MERS or the [foreclosure] trustee, as nominal holders of the deeds [of trust], are not agents of the lenders." Click here for a copy of the opinion.

Bankruptcy Court Refuses to Lift Automatic Stay for Want of Standing. Debtor homeowner filed for Chapter 7 bankruptcy in the U.S. Bankruptcy Court for the Southern District of New York, triggering an automatic stay under the bankruptcy code. Creditor U.S. Bank moved to lift the stay so that it might pursue foreclosure on debtor's home in state court. *In re Lippold*, No. 11-12300 (Bankr. S.D.N.Y. Sep. 6, 2011). The mortgage was originally made to MERS as nominee of Aegis, but the note was made to Aegis. MERS thereafter purported to transfer the note and mortgage to U.S. Bank. Scrutinizing the chain of transfer, the court noted that MERS never received any rights to the note

itself, such that its subsequent transfer to U.S. Bank (which purported to confer all rights under the mortgage and note) was ultra vires because MERS never had rights under the note. As such, U.S. Bank had no interest under the note and was powerless to enforce it, thus divesting it of the standing necessary to lift an automatic stay. Click here for a copy of the opinion.

Ninth Circuit Holds Discretionary Increase in Cardholder's Interest Rate Does Not Violate the Delaware Banking Act. On August 9, the U.S. Court of Appeals for the Ninth Circuit held that Section 944 of the Delaware Banking Act (DBA) permitted a creditor to make a discretionary increase in a cardholder's interest rate following a default due to the cardholder's late payment. *McCoy v. Chase Manhattan Bank, USA, National Association*, No. 06-56278 (9th Cir. Aug. 19, 2011). In this matter, the plaintiff cardholder brought a putative class action against the defendant bank, alleging the bank unlawfully increased his interest rate retroactively to the beginning of his payment cycle as the result of a late payment. The cardholder claimed that the interest rate increase violated the Truth in Lending Act (TILA) because the bank failed to give him notice of the increase until it had already taken effect, and that it violated the DBA § 944 because the DBA did not authorize a discretionary post-default rate increase, but only a rate increase that was "in accordance with a schedule or formula." The Ninth Circuit had previously reversed the dismissal of the plaintiff's TILA claim and the state law claim under DBA § 944. That decision was appealed to the Supreme Court, which overturned the Ninth Circuit's TILA decision but left the state law claims untouched. On remand, the Ninth Circuit also reversed its previous decision regarding the DBA and affirmed the district court's dismissal of the action. First, the court noted, two other circuit courts had since weighed in and held that Section 944 authorized the discretionary rate change as long as it was authorized in the cardholder agreement. Second, and more importantly, the Delaware legislature enacted a clarifying amendment to Section 944 which stated that the bank had the discretionary authority to increase the interest rate, at a rate lower than the maximum rate, pursuant to "any event or circumstance specified in the plan, which may include borrower default." Here, the discretionary rate increase was up to the maximum rate specified in the cardholder agreement and thus allowable under the DBA. The court rejected the cardholder's argument that the statutory amendment should not be applied retroactively, noting that the amendment makes clear that it is simply a clarifying statement on the statute and not a substantive change to the law. Click here for a copy of the opinion.

Miscellany

Individuals Plead Guilty in Mortgage Fraud Scam. On September 6, United States Attorney for the Eastern District of California Benjamin B. Wagner announced that two individuals pled guilty to conspiring to commit mail fraud and making false statements in loan applications. The two individuals were charged in June 2010 with eight other defendants in a conspiracy that involved two companies - Liberty Real Estate and Investment Company and Liberty Mortgage Company - that purchased at least 30 homes in the Sacramento area in 2006 and 2007, typically through 100 percent financing, obtained as the result of false information regarding the buyers' employment, income, and intent to live in the properties. At the close of the transactions, and unbeknownst to the lenders, cash payments were made back to the buyers out of the loan proceeds. Of the 30 transactions, at least 28 have gone into foreclosure, resulting in a loss to lenders in excess of $5 million. One defendant admitted to purchasing three homes in a two-month period, submitting false loan applications to

finance the purchases, and receiving approximately $75,000 at the close of these transactions. The other defendant admitted to buying two homes in a two-month period, submitting false loan applications and receiving approximately $64,000 at the close of the transactions. The defendants face a maximum penalty of five years in prison, and are scheduled for sentencing on November 15, 2011. Click here for a copy of the announcement.

Firm News

James Shreve will speak at the International Association of Privacy Professionals' Privacy Academy in Dallas on September 14-16. Mr. Shreve will lead the "Protecting and Securing a Moving Target: NFC, RFID and Mobile Payments" panel and participate in the panel "Who Am I? Understanding Multi-Factor Authentication in Online Environments."

Jeff Naimon will be participating in a panel titled "The Future of Lending" at the National Mortgage News Mortgage Regulatory Forum which will be held at the Washington Marriott in Washington, DC from September 19-20. Mr. Naimon will be discussing the effect of recent regulatory and enforcement developments on the direction of the mortgage market, including QM/QRM, Loan Officer Compensation rules, and Federal Housing Administration and fair lending enforcement efforts.

Benjamin Klubes will be moderating a panel focusing on Preparing for and Responding to New and Emerging Federal and State Enforcement Actions at the ACI's Residential Mortgage Litigation and Regulatory Enforcement Conference on Tuesday, September 20 in Dallas, Texas.

Andrew Sandler, **Benjamin Klubes**, and **Jonice Gray Tucker** will be speaking at the Mortgage Bankers Association's Regulatory Compliance Conference which will be held in Washington, D.C. from September 25-27. Mr. Sandler will be addressing enforcement priorities. Mr. Klubes will address litigation and enforcement trends relating to loan originations and Ms. Tucker will speak on developments in mortgage servicing.

James Parkinson will be speaking at two International Bar Association training sessions as part of the IBA's Anti-Corruption Strategy for the Legal Profession (http://www.anticorruptionstrategy.org/) on September 27 (Sao Paulo, Brazil), and on September 29 (Caracas, Venezuela).

Benjamin Klubes will be speaking at the 2011 PCI CRA and Fair Lending Colloquium on November 7 in Baltimore, MD on "Hot Compliance Topics: Reform Impact, Oversight Trends, Enforcement Actions and More!"

Margo Tank and **John Richards** will participate in the ESRA Fall Conference in Washington, D.C. on November 9 and 10. For details on registration, accommodations and agenda, please see http://esignrecords.org/events/.

David Krakoff will be participating in a panel at the International Association of Defense Counsel program on worldwide anti-corruption laws in Palm Springs in February 2012.

Mortgages

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Criminal Enforcement Action

Stay current on U.S. FCPA enforcement actions and international anti-corruption news by visiting our **FCPA & Anti-Corruption Score Card**.

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