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Financial Services Report

Staying Ahead of the Summons

Award Winning Newsletter

Vol 5, No 1. Spring 2009

Inside

Editor's Note

Stuff happened this quarter, lots of it. Unless you have on-board GPS or are two proofs away from solving Fermat's Last Theorem, you need a decent docent. That's where we come in.

As we went to press, we got our hands on an early draft of the press release in which Treasury Secretary Geithner will announce the latest condition on entities that receive government TARP funds. Banks failing the new stress tests will be forced to relocate to FEMA trailers, and execs who receive excessive compensation will have to diaper the octuplets. In another breaking story we're following even though no one else will (funny, that), the government denies having a secret plan to cap-and-trade American banks' toxic assets and ship them to Iran in steamer trunks labeled "yellowcake."

It was an exciting three months. Our local bartenders have given up on Happy Hour and have started offering Pepto Bismol on tap. In pint glasses.

There was more news than these modest pages can support, so once again we have called upon reinforcements. For just about every item in this newsletter, there is a corresponding lengthier and more detailed Client Alert or posting that you can access through links found on our web page, www.mofo.com.

Strap on your stimulus package. We are shovel-ready. ■

William L. Stern, Editor

MoFo Metrics

14	Average worker's vacation days per year, U.S.
37	Average worker's vacation days per year, France
149	Average hours spent at work per month, U.S.
151	Average hours of TV watched per month, U.S.
59	Percentage of employees who steal confidential employer information upon termination
246	Annual cost of U.S. tort system, in billions
2.2	That amount expressed as a percentage of GDP, United States
0.7	Equivalent percentage for France, UK

Beltway Report

If these Reader's Digest recaps leave you breathless and wanting more, go to www.mofo.com. You will find detailed Client Alerts for many of these items, baked fresh daily.

DRUM ROLL, PLEASE

On February 10, Treasury Secretary Geithner released an outline of his Financial Stability Plan, a six-pronged approach to once again "help restart the flow of credit, clean up and strengthen our banks, and provide critical aid for homeowners and for small businesses" with "new, higher standards for transparency and accountability." His only mention of TARP was a passing reference to the "current program" being replaced. The new plan calls for the Treasury Department, FDIC, Federal Reserve Board, and other government agencies to work together. You can keep tabs on them through a new website at www.financialstability.gov. For additional details, see our Client Alert at: http://www.mofo.com/news/updates/files/090210Treasury.pdf.

Meanwhile, the FDIC announced plans to extend the Temporary Liquidity Guarantee Program (TLGP) final debt issuance date from June 30, 2009, to October 31, 2009. The TLGP is a guarantee program for certain banking institution liabilities established in October 2008 and designed to unfreeze inter-bank lending and encourage lending more broadly. To learn more, see our Client Alert at: http://www.mofo.com/news/updates/files/20090219TLGP_Extended.pdf.

For more information, contact Amy Baumgardner at abaumgardner@mofo.com.

LINING UP AT THE GOVERNMENT WINDOW

Consumers and small business cried "me too!," the government listened, and there was much improved lending to be had by all. The Federal Reserve Board recently announced updated terms for the Term Asset-Backed Securities Loan Facility, or TALF, a joint program with the Treasury. In a one-two punch, the FRB signaled its willingness to increase its commitment from $200 billion to as much as $1 trillion, with Treasury announcing the expansion of TALF beyond its original asset classes (credit cards, auto loans, student loans, and small business loans) to include commercial mortgage-related asset-based securities (ABS). The FRB announced consideration of greater expansion to cover private label residential mortgage-related ABS and assets collateralized by corporate debt. For more details, see our Client Alert at: http://www.mofo.com/news/updates/files/090210TALF.pdf.

For more information, contact Amy Baumgardner at abaumgardner@mofo.com.

THE PARTY'S OVER … OR IS IT?

On February 4, Treasury announced a new set of executive compensation guidelines applicable to companies receiving government bailout funds. This announcement comes on the heels of an increasing number of press reports and public outcries over excesses at bailed-out institutions. Responding to public unrest over the existing compensation limitations, too few limitations on the use of public funds, and, according to President Obama, a growing sense that "executives [are] being rewarded for failure," Treasury announced prohibitions on executive compensation. Now for the small print: the new guidelines only apply to financial institutions that receive government assistance to address the current financial crisis after the date of the guidelines and to those institutions that receive "exceptional financial recovery assistance." For additional details, see our Client Alert at: http://www.mofo.com/news/updates/files/090205ExecutivePay.pdf.

For more information, contact David Lynn at dlynn@mofo.com.

CLOSING THE BARN DOOR

Under its TARP authority, the Treasury Department has relied on expedited procedures to award all kinds of contracts ranging in value from $5,000 to $2.5 million and in length from six months to several years. The GAO has now called for increased oversight of the contractors operating under these contracts. A Client Alert discusses the details: http://www.mofo.com/news/updates/files/15013.html.

For more information, contact Richard Vacura at rvacura@mofo.com.

HEDGE FUNS

The House and Senate introduced legislation designed to greatly increase the regulatory oversight of hedge funds and their investment advisers. Although the stated objective of the proposed legislation is to regulate the hedge fund industry, its reach extends to private equity and venture capital funds and their respective investment advisers. Think of it as "Extreme Makeover: Home Edition." For more, see our Client Alert at: http://www.mofo.com/news/updates/files/15232.html.

For more information, contact Barbara Mendelson at bmendelson@mofo.com.

ARE YOU WELL CAPITALIZED?

If the FDIC adopts a regulatory change recently proposed for comment, the small minority of banks that are less than "Well Capitalized" will face increased restrictions on interest rates they can offer on deposits. "Prompt Corrective Action" requires the FDIC to prevent banks that are less than Well Capitalized from soliciting deposits at interest rates that significantly exceed prevailing rates. The FDIC's current regulation ties permissible interest rates paid by these banks on deposits solicited nationally to the comparable maturity Treasury yield, and ties permissible interest rates on deposits solicited locally to undefined prevailing local interest rates. The proposed regulation would define nationally prevailing deposit rates as a direct calculation of those national averages, as computed and published by the FDIC. It would also establish a presumption that locally prevailing deposit rates equal the national rates published by the FDIC.

For more information, contact Rick Fischer at rfischer@mofo.com.

SIGN OF THE TIMES

The FDIC issued two final rules aimed at failing and failed institutions. The first, effective July 1, 2009, establishes practices for determining deposit and other account balances at a failed depository institution for purposes of deposit insurance and receivership. To a large extent, this rulemaking codifies the FDIC's long-standing policies and procedures for bank closings. It applies to all FDIC-insured institutions. The second adds certain recordkeeping requirements designed to improve the FDIC's ability to monitor and evaluate risks in certain insured depository institutions with qualified financial contracts (QFCs), as well as ensure preparedness if such institutions fail. The rule will make it easier for the FDIC to meet its statutory obligations regarding the treatment of QFCs in the event of its appointment as receiver of a failed insured depository institution.

For more information, contact Obrea Poindexter at opoindexter@mofo.com.

REPLENISHING THE WELL

You won't be surprised to hear that the FDIC's Deposit Insurance Fund used for handling bank failures has dipped below the statutorily mandated minimum. But who should pay? For now, the FDIC will make up the shortfall through an emergency special assessment of 20 basis points on all banks. FDIC Chairman Sheila Bair explained that FDIC staff considered tapping the FDIC's credit line with Treasury but rejected this option in the face of likely congressional skepticism, and that the industry risked having all banks painted with the "bailout brush."

For more information, contact Obrea Poindexter at opoindexter@mofo.com.

NEW AMLF RULES

The Federal Reserve Board recently announced two final rules pertaining to the Asset-Backed Commercial Paper Money Market Fund Liquidity Facility (AMLF), which extends loans to banking organizations to finance their purchases of high-quality asset-backed commercial paper from money market mutual funds. The first rule provides a temporary limited exception from the Board's leverage and risk-based capital rules for bank holding companies and state member banks. The sec-

Continued on Page 12

Credit Card Report

Note: We have issued detailed Client Alerts for many of these items. For more information, go to http://www.mofo.com.

ALL ABOARD THE UDAP TRAIN

On December 18, the Federal Reserve, the Office of Thrift Supervision, and the National Credit Union Administration approved a joint final rule (Regulation AA) addressing unfair or deceptive acts or practices (UDAP) relating to credit cards. The implementation of the UDAP rule will have a dramatic impact on both credit card issuers and consumers and will be the most substantial overhaul of disclosure rules and restrictions on lender practices in decades. It will also shift the regulators' historical focus on individual enforcement efforts to broader rules-based enforcement, with numerous specific prohibitions on particular practices. The rule takes effect on July 1, 2010, and expressly authorizes banks to continue until the date to take actions that will be prohibited once the final rule is effective.

There's a lot more to the new rule than we can do justice to here. For more information, contact Obrea Poindexter at opoindexter@mofo.com.

MORE REVISIONS TO THE ALPHABET SOUP

In addition to approving amendments to Regulation AA, the Board also approved final amendments to Regulation Z, including:

- revisions to the five main types of open-end credit disclosures governed by Regulation Z, including application and solicitation disclosures, account-opening disclosures, periodic statement disclosures, change-in-terms notices, and advertising disclosures;
- substantive revisions in the change-in-terms requirements, including increasing the amount of time a change-in-terms notice must be sent before a change takes effect and requiring a 45-day advance notice before a rate is increased due to consumer delinquency or default; and
- additional consumer protections for credit card accounts to complement the final amendments to Regulation AA, such as cut off-hour restrictions for mailed payments to be considered timely.

For additional details and links to the final rules, please refer to our Legal Update at http://www.mofo.com/news/updates/files/15057.html.

For more information, contact Obrea Poindexter at opoindexter@mofo.com.

MISLEADING ISN'T ENOUGH

The Ninth Circuit held that loss of a promotional interest rate for reasons disclosed in the balance transfer offer did not violate TILA even if the bank knew or should have known of the default triggering the interest rate change when plaintiff accepted the offer. *Hauk v. JP Morgan Chase Bank USA*, 552 F.3d 1114, 2009 WL 153236 (9th Cir. 2009). The court rejected the Third Circuit's holding that a disclosure that complies with the requirements of Regulation Z could still give rise to a TILA violation, focusing instead on the specific disclosure requirements in Regulation Z and whether the disclosures reflected the legal obligations of the parties. While the creditor's undisclosed intent was not relevant to evaluating a TILA violation, the court found that the bank's knowledge of the triggering event could give rise to a state UDAP claim.

For more information, contact Bob Stern at rstern@mofo.com.

SUBPRIME SETTLEMENT

You can outsource, but you can't hide. The FDIC recently announced a settlement with CompuCredit Corporation, a company charged with deceptive marketing of subprime credit cards with three banks in violation of the FTC Act. The FDIC alleged that the solicitations failed to adequately disclose that significant upfront fees would leave consumers with initial available credit of much less than the disclosed credit limit. The settlement will result in an order that will correct the FTC Act violations, impose a civil penalty, and provide restitution to consumers in the form of credits for certain fees arising from the deceptive marketing practices. CompuCredit did not admit or deny any liability. The FDIC used the settlement announcement to warn institution boards of directors and senior management that they are responsible for managing activities conducted through third-party relationships and for the resulting risks. ■

For more information, contact Steve Colangelo at scolangelo@mofo.com.

Operations Report

Note: We have issued detailed Client Alerts for many of these Operations Report items, which we update daily. For more information, go to http://www.mofo.com.

GET ON THAT TREADMILL

Treasury recently announced details of the new Capital Assistance Program (CAP). At the same time, federal regulators announced plans to conduct "stress tests" on banks with assets above $100 billion. These assessments are designed to determine how banks can withstand unanticipated and severe losses in coming periods. Banks identified as needing additional capital can participate in CAP or raise private funds. Capital provided under CAP will be in the form of preferred securities, which will convert to common stock after seven years and will be Tier 1 securities. Institutions will likely use CAP to exchange their existing preferred shares, which are of higher quality than the securities issued to Treasury under the prior program. For more information, see our Client Alert at www.mofo.com/news/updates/files/090225NewFederalPrograms.pdf.

For more information, contact Amy Baumgardner at abaumgardner@mofo.com.

FASB ISSUES GUIDANCE ON "OTHER THAN TEMPORARY IMPAIRMENT"

The Financial Accounting Standards Board (FASB) issued final staff guidance on accounting for "other than temporary impairment" for certain debt securities. The guidance is effective for interim and annual reporting periods ending after December 15, 2008. New Emerging Issues Task Force (EITF) 99-20-a is based more on a "reasonable judgment" by management of the probability that the holder will be unable to collect all amounts due, than on a "market participant's" view of cash flows. Thus, the guidance will be more consistent with Financial Accounting Standard No. 115. FASB's announcement follows earlier SEC recommendations against suspending fair value accounting standards and in favor of improving existing practices, including reconsidering accounting for impairments and developing additional guidance for determining fair value of investments in inactive markets. The SEC's report was mandated by the Emergency Economic Stabilization Act of 2008.

For more information, contact Ollie Ireland at oireland@mofo.com.

CAPP: SUBCHAPTER S CORPORATIONS

Last month, Treasury released a standard form term sheet detailing the terms and conditions for its direct investment in banking institutions organized as subchapter S corporations (S-Corps) pursuant to the TARP CaPP. For those catching up on all the acronyms, TARP CaPP is the program through which Treasury intends to make capital investments in private and public banking institutions. The material differences in the CaPP for S-Corps are based primarily on the statutory structure of S-Corps, not on the nature of the offering. For example, the securities to be offered are subordinated debentures and warrants as opposed to preferred stock and warrants. Under the Internal Revenue Code, S-Corps may issue only one class of stock. In addition, the government is not an eligible stockholder of an S-Corp. For additional details, please refer to our Client Alert at http://www.mofo.com/news/updates/files/090115CaPP.pdf.

For more information, contact Amy Baumgardner at abaumgardner@mofo.com.

BLAME THE ACCOUNTANTS

Existing fair value accounting and mark-to-market standards have dodged a bullet. The SEC has recommended that these standards, including Financial Accounting Statement 157 (FAS 157), should not be suspended. Instead, the SEC recommends improvements to existing accounting practices, including reconsidering the accounting for impairments. Critics have blamed mark-to-market accounting rules for exacerbating the liquidity problems caused by the subprime mortgage crisis. For additional details, see our Client Alert at http://www.mofo.com/news/updates/files/090107SECStudy.pdf.

For more information, contact Amy Baumgardner at abaumgardner@mofo.com.

Continued on Page 6

Operations Report

Continued from Page 5

OVERDRAFT OVERHAUL

Until now, it's been pretty much a game of Russian roulette when it comes to whether a bank will deny a transaction that puts the consumer over the credit limit or will process the transaction and collect hefty fees for the privilege. The Federal Reserve has put in its two cents, publishing proposed changes to Regulation E (Electronic Funds Transfer Act) intended to give consumers more of a say in whether the bank will pay overdrafts for ATM withdrawals and debit card transactions. If the rules go into place as proposed, banks will have the choice to implement either an "opt-in" system, requiring consumers to affirmatively authorize overdraft fees, or an opt-out system, which would require additional notice in each periodic statement cycle in which the institution assessed an overdraft fee or charge for those consumers who did not opt out of the bank's overdraft payment policies. The comment deadline is March 30.

For more information, contact Obrea Poindexter at opoindexter@mofo.com.

MORE PAPERWORK FOR CREDIT RATING AGENCIES

On February 2, 2009, the SEC issued final rules relating to Nationally Recognized Statistical Rating Organizations (NRSROs) and proposed additional NRSRO rules. The final rules are intended to increase the transparency of rating methodologies of the NRSROs, strengthen disclosures of ratings performance, prohibit certain practices that create conflicts of interest, and enhance recordkeeping and reporting obligations. The Final Rules are effective after publication in the Federal Register, which should be around April 2009. Our Client Alert contains additional details: http://www.mofo.com/news/updates/files/090204SECAdoptsandProposesReforms.pdf.

For more information, contact Amy Baumgardner at abaumgardner@mofo.com.

"IX NAY" ON INSURANCE COVERAGE FOR LINKED ACCOUNTS

You can see the wheels turning – an unnamed banker asked the FDIC if an accountholder could negotiate an interest rate on an account (possibly in exchange for keeping a large minimum balance in the non-interest-bearing transaction account), secure FDIC deposit insurance coverage for the total amount deposited, and still earn interest on the total. The FDIC shot him down, warning that "linked-account" arrangements with depositors designed to obtain unlimited deposit insurance coverage for interest-bearing accounts are illegal. Any arrangement between a bank and a depositor in which the interest amount "paid on a time deposit will increase with the amount of money deposited in another non-time deposit account is not legally permissible because it would be a violation of the federal prohibition against the payment of interest on demand deposits." And if that's not bad enough, the FDIC also considers these arrangements to be an attempt to circumvent the FDIC's Transaction Account Guarantee Program participation eligibility requirements.

For more information, contact Rick Fischer at rfischer@mofo.com.

WE KNOW IT'S BROKE, BUT HOW DO WE FIX IT?

According to a GAO report, regulation is to blame for what it called the worst financial crisis in more than 75 years. Specifically, the GAO pointed to the fragmented, complex, and overlapping regulatory structures, developed over a period of 150 years as a result of discrete responses by individual governmental authorities to perceived isolated market problems. But don't despair, the report also offers a framework to evaluate any proposed revised regulatory system. Want to learn more? See our Client Alert at: http://www.mofo.com/news/updates/files/090122GAO.pdf.

For more information, contact Barbara Mendelson at bmendelson@mofo.com.

GROWING PAINS

Bank regulators have changed the definitions of small and intermediate small institutions.

"Small bank" or "small savings association" means an institution that, as of December 31 of either of the prior two calendar years, had assets of less than $1.109 billion. "Intermediate small bank" or "intermediate small savings association" means a small institution with assets of at least $277 million as of December 31 of both of the prior two calendar years, and less than $1.109 billion as of December 31 of either of the prior two calendar years.

For more information, contact Ollie Ireland at oireland@mofo.com.

MMIFF CHANGES

The Federal Reserve Board announced two changes to the Money Market Investor Funding Facility (MMIFF). First, the set of institutions eligible to participate in the MMIFF was expanded from U.S. money market mutual funds to also include a number of other money market investors. The newly eligible participants include U.S.-based securities-lending cash collateral reinvestment funds, portfolios, and accounts (securities lenders); and U.S.-based investment funds that operate in a manner similar to money market mutual funds, such as certain local government investment pools, common trust funds, and collective investment funds. Second, the Board authorized the adjustment of several of the economic parameters of the MMIFF, including the minimum yield on assets eligible to be sold to the MMIFF, to enable the program to remain a viable source of backup liquidity for money market investors even at very low levels of money market interest rates. ■

For more information, contact Barbara Mendelson at bmendelson@mofo.com.

Mortgage Report

Warning – Plot Spoiler. If you missed the movie, here's what happened: Populist anger at TARP shifts public opinion toward homeowner bailout; as credits roll, bailouts for everyone.

Note: We have issued detailed Client Alerts for many of these Mortgage Report items, which we update daily. For more information, go to http://www.mofo.com.

BAILOUTS "R" US

Last month, the White House added another acronym by releasing its much-anticipated Homeowner Affordability and Stability Plan (HASP), one component within the revamped TARP. HASP aims to help seven to nine million households avoid foreclosure via low mortgage rates, refinancing, and restructuring. It encourages the first by boosting Treasury's funding to Fannie Mae and Freddie Mac through purchases of GSE debt and mortgage-backed securities. It aims to help homeowners refinance into market-bearing fixed-rate loans for 30 or 15 years that they otherwise could not qualify for due to falling house values. Refinancing is only available for GSE-owned or securitized loans. At HASP's heart, and with a $75 billion sticker price, is the initiative to help at-risk homeowners modify their loans regardless of who owns or services the mortgage. While lender participation is voluntary, the Feds will provide cost-sharing incentives and make offers some cannot refuse. Going forward, lenders receiving TARP funds must participate. HASP's launch date is March 4, 2009.

For more information, contact Joe Gabai at jgabai@mofo.com.

CRAMDOWN

Loan servicers may soon join restaurants in needing to post signs demonstrating the Heimlich maneuver. Federal lawmakers introduced three bills that would give bankruptcy judges the power to rewrite the first mortgage on a homeowner's principal residence, including reductions in loan balance and interest rate, and an extension of loan duration. In a deal reached with Citigroup, Senator Durbin's bill (S.61) would only apply to mortgages originated before its enactment, and homeowners would have to certify that they attempted to contact their lender for a workout before filing for bankruptcy. On January 27, 2009, Representative Conyers's bill (H.R. 200) passed the House Judiciary Committee in a party-line vote and was modified to incorporate the Durbin-Citi deal. Senator Evan Bayh

Continued on Page 8

Mortgage Report

Continued from Page 7

(D-IN) has said that he hoped to draft a bipartisan compromise that would allow cramdowns only for the riskiest mortgages (read, existing subprime and Alt-A).

For more information, contact Adam Lewis at alewis@mofo.com.

MODS AND MORATORIUMS

The complications are getting hairier for mortgage modification programs. As part of President Obama's HASP (*see* "Bailouts 'R' Us," above), Treasury will roll out uniform guidance for loan workouts across the entire mortgage industry. These guidelines will be used in HASP restructurings by all lenders to receive TARP funds, by Fannie Mae and Freddie Mac for loans they own or guarantee, and by other federal agencies that own or guarantee loans. The Obama Administration plans to work with state regulators to implement Treasury's guidelines.

Meanwhile, in the name of economic stimulus, California Governor Schwarzenegger signed a bill in late February requiring lenders with borrowers in California to implement "comprehensive loan modification programs" or face a 90-day foreclosure moratorium. The effective date is May 21, 2009. If you want an exemption, you need to go to a state "commissioner." What this means for national banks, federal savings banks, and their operating subsidiaries remains to be seen. We have some ideas. California's mortgage modification bill was discussed in our Legal Update at: http://www.mofo.com/news/updates/files/14857.html.

For more information, contact Joe Gabai at jgabai@mofo.com.

UNANIMOUS HIGH COURT DECISION RESTRICTS SUBPRIME FORECLOSURE

Not to be outdone by the other two branches of government, the judicial branch weighed in on subprime foreclosure last quarter. In December 2008, the highest court in Massachusetts unanimously upheld enjoining Fremont Investment & Loan from foreclosing on "presumptively unfair" subprime loans without court approval and notice to the state AG. *Commonwealth of Massachusetts v. Fremont Investment & Loan*, No. SJC-10258 (Mass.). These loans have four conditions: (1) an introductory adjustable rate for three years or less; (2) an introductory rate at least 3% lower than the fully indexed rate when the loan began plus the margin; (3) a debt-to-income ratio exceeding 50% when calculating debt using the fully indexed rate; and (4) a 100% LTV ratio, a significant prepayment penalty, or a penalty after the introductory period. From January 2004 to March 2007, Fremont initiated 14,578 loans in Massachusetts. Half to 60% were subprime.

For more information, contact Wendy Garbers at wgarbers@mofo.com.

FAIR LENDING AND OPTION ARM LITIGATION

The *NAACP* action has now moved beyond threshold challenges. In January 2009, the district court denied defendants' joint motion to dismiss, holding that the NAACP has standing; the complaint passes *Twombly* muster, plaintiff may simultaneously prosecute claims under the Equal Credit Opportunity Act and the Fair Housing Act, and disparate impact claims are available under ECOA, the FHA, and 42 U.S.C. § 1982 of the Civil Rights Act. The Section 1982 holding is contrary to Supreme Court precedent and other fair lending decisions.

Lenders scored a win when the first district court to rule on a class certification motion in these cases refused to certify a class. *Jordan v. Paul Financial, L.L.C., et al.*, No. 07-cv-04496-SI (N.D. Cal.). The court held that plaintiff lacked standing to represent the TILA class because his claim was time-barred and he failed to establish that equitable tolling applied. The court also held that plaintiff was not typical because he had extensive mortgage experience and dealings with his broker and because the lender had many different forms of loan documents that were different from plaintiff's documents. The court also denied plaintiff's preliminary injunction motion in light of its denial of the class certification motion. ■

For more information, contact Michael Agoglia at magoglia@mofo.com.

Preemption Report

HERE WE GO AGAIN

Remember when the Supreme Court decided to hear *Watters* even though there was no circuit split, and the banking world trembled? Well, the Supreme Court has again agreed to hear a preemption case that has many scratching their heads and biting their nails. The Court will review *Cuomo v. The Clearing House Assoc. LLC*, a Second Circuit decision holding that the NY AG cannot enforce New York fair lending laws against national banks because the National Bank Act gives the OCC sole authority to exercise "visitorial powers" over national banks, and an OCC regulation broadly defines "visitorial powers" to include state enforcement of state laws regulating national bank activities. The Supreme Court will consider whether the OCC regulation is entitled to *Chevron* deference and whether it is invalid as inconsistent with *First National Bank in St. Louis v. Missouri*, 263 U.S. 640 (1924). Given that the National Association of Attorneys General has made resisting federal preemption of enforcement of state banking and mortgage and foreclosure laws its top enforcement priority, we predict much hand-wringing ahead.

For further information, contact James McGuire at jmcguire@mofo.com.

The Court will review *Cuomo v. The Clearing House Assoc. LLC*, a Second Circuit decision holding that the NY AG cannot enforce New York fair lending laws against national banks because the National Bank Act gives the OCC sole authority to exercise "visitorial powers" over national banks, and an OCC regulation broadly defines "visitorial powers" to include state enforcement of state laws regulating national bank activities.

FCRA YOU TOO

Listen up, you FCRA preemption geeks who fear suit in California. The FCRA expressly exempts from preemption California Civil Code § 1725(a), which pertains to liability of furnishers of information. In December, a California Court of Appeal agreed with the district courts that have considered this provision, and held that this exemption does not allow litigants to pursue a claim against information furnishers under California law because the private right of action created by this statute is not included in § 1725(a). *Liceaga v. Debt Recovery Solutions, LLC*, 169 Cal. App. 4th 901 (2008). But wait a few weeks later, the Ninth Circuit and another division of the California Court of Appeal ruled otherwise. *Gorman v. Wolpoff & Abramson, LLP*, 552 F.3d 1008 (9th Cir. 2009); *Sanai v. Saltz*, 170 Cal. App. 4th 746 (2009). Looks like FCRA preemption will be a lot more complicated going forward.

For further information, contact Nancy Thomas at nthomas@mofo.com.

NEVER ON SUNDAY

A California Court of Appeal held that OCC regulations preempt state "holiday statutes" providing that whenever a payment is due on a weekend or holiday, the creditor must accept the payment on the next business day without any adverse consequence. *Miller v. Bank of America, N.A.*, 170 Cal. App. 4th 980 (2009). The court found that by changing when a payment is due, these state statutes were expressly preempted by 12 C.F.R. § 7.4008(d)(2)(iv) because they affected the "schedule for repayment of principal and interest" and the "payments due" set by a national bank. ■

For further information, contact Nancy Thomas at nthomas@mofo.com.

Privacy Report

DUCK AND COVER IN MASSACHUSETTS

Last September, the Massachusetts Office of Consumer Affairs and Business Regulation (OCABR) adopted sweeping data security rules that require every person that owns, licenses, stores, or maintains "personal information" about a resident to implement a written information security program for any records containing such information, and the particular standards ranging from due diligence and contract requirements for vendors to detailed computer security requirements posed significant compliance issues. After a public hearing on the compliance deadline, among other issues, the OCABR extended the deadline to January 1, 2010. Significantly, the OCABR streamlined the requirements for overseeing service providers: covered organizations must take all reasonable steps to (1) verify that any provider with access to such information has the "capacity to protect such personal information in the manner provided for in the [rules]" and (2) ensure that the provider's safeguards are "at least as stringent" as those required under the rules.

For more information, contact Miriam Wugmeister at mwugmeister@mofo.com.

HIPAA STIMULUS

Like a hippo emerging from the wild, the privacy and data security regulations adopted under HIPAA are again looming large – now with new security breach notification requirements enacted in the American Recovery and Reinvestment Act (ARRA). The new Health Insurance Portability and Accountability Act (HIPAA) notification requirements will apply to "covered entities," "business associates," and a catch-all category of "vendors" of "personal health records." The HIPAA notification requirements become effective 30 days after rules are adopted by HHS (for covered entities and business associates) or the FTC (for vendors). Congress culled the state notification laws for several response measures, including: a 60-day timetable for notification (subject to a law enforcement exception); detailed standards on notification methods; notice to HHS (which must identify the covered entity on the agency's web site if that entity notifies more than 500 individuals) or notice to the FTC; and notice-content requirements.

For more information, contact Tom Scanlon at tscanlon@mofo.com.

HIPAA ENFORCEMENT MEASURES STRENGTHENED

Effective immediately, a state attorney general may bring a private cause of action for non-compliance with HIPAA privacy requirements on behalf of affected residents; available damages for this action include costs and attorneys' fees. Also, the ARRA creates a tiered system with varying increased civil monetary penalties, based on whether the violation was made without knowledge ($100 per violation), due to reasonable cause ($1,000 per violation), or due to willful neglect ($10,000 per violation). Furthermore, the ARRA requires that, in two years, HHS must formally investigate all complaints of non-compliance and mandates civil penalties for privacy and security violations that HHS determines were due to "willful neglect."

For more information, contact Tom Scanlon at tscanlon@mofo.com.

PREVIEW OF JOINT HHS/FTC ENFORCEMENT OF HIPAA RULES

Right on cue, the HHS and the FTC illustrated the shape of the regulatory regime that might emerge to enforce the new HIPAA privacy and data security regulations. The agencies announced settlements with CVS Caremark Corp. (CVS), which had allegedly disposed improperly of protected health information (PHI) by throwing it in a dumpster. CVS agreed to pay HHS a $2.25 million "resolution amount" and implement a "corrective action plan," including the development of HIPAA-compliant policies and procedures, and new training, auditing, and employee disciplinary procedures. To settle FTC charges that it violated the FTC Act by falsely promising in its privacy policy to safeguard PHI, CVS agreed to establish a comprehensive information security program and obtain an independent professional audit of the program every two years for the next two decades, requirements that closely track other recent FTC consent decrees in this area. ■

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Arbitration Report

SECOND CIRCUIT SAYS NO TO CLASS WAIVER

The Second Circuit became the first circuit court to invalidate a class action waiver based on the Federal Arbitration Act rather than state unconscionability law principles. That could matter. *See In re American Express Merchants' Litigation*, No. 06-871 (2d Cir. Jan. 30, 2009). In the face of evidence showing that the likely costs of litigating an antitrust claim brought by American Express merchants were prohibitively high, the Second Circuit held that the class action waiver was unenforceable as a matter of federal law because it would effectively preclude any action seeking to vindicate the claims asserted by the plaintiffs. This ruling is especially troubling for companies hoping that choice-of-law clauses from class-waiver-friendly forums would protect their ability to compel arbitration on an individual basis. If courts in other circuits follow the Second Circuit's analysis, they will have a basis to invalidate class waivers without ever reaching state law or state choice-of-law analysis.

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VISIONS OF CIRCUIT SPLIT

Class waiver enthusiasts thought they'd discovered the Holy Grail for Supreme Court review when the Third Circuit issued *Gay v. CreditInform*, 511 F.3d 369 (3d Cir. 2007), a murky decision that seemed to stand for the proposition that state law class waiver analysis was preempted by the FAA. The Ninth Circuit cooperated by quickly rejecting the Third Circuit's approach. Unfortunately, in February the Third Circuit dashed those hopes, issuing a decision backing away from the broadest interpretation of *Gay* by holding that state law class waiver unconscionability analysis is not always preempted by the FAA and by coming close to invalidating a class waiver under New Jersey law. *Homa v. American Express Co., et al.*, No. 07-2921 (3d Cir. Feb. 24, 2009). So now it's back to the drawing board.

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ONCE MORE UNTO THE BREACH

The House has again introduced a bill, H.R. 1020, which would amend the Federal Arbitration Act to make unenforceable any pre-dispute arbitration agreement if it would require arbitration of any consumer, franchise, or employment dispute. Whether the Arbitration Fairness Act of 2009 will fare better than its predecessors remains to be seen, but the change in Administration and makeup of Congress may give the effort more traction this time around. Especially since this is one of the trial lawyers' top agenda items.

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What if an arbitration clause fell in the woods and no one heard it?

FEAR OF ENFORCEMENT

What if an arbitration clause fell in the woods and no one heard it? Leave it to the California courts to worry about such things. The California Supreme Court held that the mere presence of an allegedly unconscionable arbitration provision that was never actually invoked does not create the sort of injury necessary to state a claim under California's Consumer Legal Remedies Act. *Meyer v. Sprint Spectrum LP*, No. S153846 (Jan. 29, 2009). The CLRA is one of the broad consumer-protection statutes that gives California its much-deserved pro-consumer reputation, and many thought the statute could accommodate vaporous claims like this. Although the court was construing the "damages" provision of the CLRA, it also held that a no-injury claim cannot be brought as an injunction-only claim either. ■

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Beltway Report

Continued from Page 3

ond rule provides a temporary limited exception from sections 23A and 23B of the Federal Reserve Act, which establish certain restrictions on and requirements for transactions between a bank and its affiliates.

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POSSIBLE REGULATION D AMENDMENTS

The Federal Reserve Board has requested public comment on proposed changes to Regulation D (Reserve Requirements of Depository Institutions) to authorize the establishment of limited purpose accounts, called "excess balance accounts" (EBAs), at Federal Reserve Banks. The authorization of EBAs for the excess balances of institutions eligible to receive earnings on their balances maintained at Federal Reserve Banks is intended to address pressures on correspondent-respondent business relationships in the current market environment. The establishment of EBAs would allow EBA participants to earn interest at the excess balance rate in a Federal Reserve Bank account managed by a correspondent or other agent without EBA participants having to open a separate individual account at the Federal Reserve Bank. The public comment period ended March 2, 2009. ■

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