Buckley Sandler LLP

InfoBytes

FINANCIAL SERVICE HEADLINES & DEADLINES FOR OUR CLIENTS AND FRIENDS

October 5, 2012

TOPICS COVERED THIS WEEK (CLICK TO VIEW)

FEDERAL ISSUES

CFPB Continues Credit Card Enforcement Activity. On October 1, the CFPB announced a coordinated enforcement action taken by federal regulators against a major credit card company and several of its subsidiaries alleged to have violated multiple consumer financial protection laws. According to the CFPB, the investigations conducted by it and other federal regulators and a state regulator revealed that the companies (i) charged illegal late fees, (ii) discriminated on the basis of age in the offering of credit, (iii) engaged in deceptive marketing, and (iv) failed to properly report consumer credit disputes. To resolve the allegations, the companies agreed to enter into several different consent orders. Two orders obtained by the CFPB and a joint CFPB/FDIC order require three of the subsidiaries collectively to refund approximately $85 million to approximately 250,000 customers and pay a cumulative $18 million in civil money penalties. Likewise, the OCC issued a consent order that includes an additional $500,000 penalty, and provides for restitution that overlaps with the broader restitution ordered by the CFPB. Finally, an order obtained by the Federal Reserve Board, requires the company, and certain of its subsidiaries, to pay an additional $9 million penalty. Furthermore, pursuant to the various orders, the companies agreed to undergo an independent audit and implement enhanced compliance systems to address the alleged illegal practices. This is the third public CFPB-led enforcement action aimed at credit card companies, and the first to go beyond allegations regarding ancillary products and resolve alleged violations of the CARD Act, the Fair Credit Reporting Act, and the Equal Credit Opportunity Act.

CFPB Announces First Determination Of A Petition to Modify Or Set Aside A Civil Investigative Demand. On September 20, the CFPB issued its first Decision and Order on a petition to modify or set aside a civil investigative demand (CID). The petition challenged a CID issued to a non-bank mortgage seeking responses to twenty-one interrogatories and thirty-three document requests. CFPB Director Richard Cordray denied the petition in its entirety and ordered the Company to comply with the CID within twenty-one days. In addition to ruling on the substantive issues relevant to the petition, the Decision and Order demonstrates the importance of including detailed and specific objections in any petition to modify or set aside a CID and the crucial role of the meet-and-confer sessions. In a Special Alert BuckleySandler analyzes Director Cordray's decision and its implications for institutions

that are facing or could face a CFPB investigation.

CFPB to Host Remittance Rules Webinar, Announces Safe Harbor Countries. On October 16, the CFPB will host a webinar on the new requirements for remittance transfer providers. The CFPB issued a final remittance rule at the beginning of this year, and subsequently modified the rule to exempt certain institutions from its disclosure requirements. To further assist industry stakeholders with implementation of the remittance rule, the CFPB has also released a list of countries that qualify for the safe harbor exception to the rule's disclosure requirements. Under the exception, providers may disclose estimates of the amounts to be received in a foreign currency, fees, and taxes for transfers to Aruba, Brazil, China, Ethiopia, and Libya, in lieu of exact amounts. The remittance rule, and its safe harbor exception, becomes effective February 7, 2013.

Federal Reserve Board Reports on CFPB Consumer Protection Unit. This week, the Office of the Inspector General (OIG) for the Federal Reserve Board issued an evaluation of the CFPB's Consumer Response Unit, which is responsible for managing the CFPB's consumer complaint system. The report provides a concise overview of the CFPB's consumer complaint process and includes the OIG's evaluation of that process. Specifically, the OIG concludes that the CFPB's consumer complaint process is reasonable, generally compliant with the Dodd-Frank Act, and consistent with industry best practices. However, the report also indicates that the CFPB Consumer Response Unit could improve its process by further addressing (i) inaccurate manual data entry of consumer complaints, (ii) inconsistent complaint management system data, (iii) lack of a finalized agency-wide privacy policy, (iv) lack of a comprehensive quality assurance program, and (v) lack of a centralized tracking system for quality assurance reviews.

FHFA Proposes New Secondary Market Infrastructure. On October 4, the FHFA released a white paper describing the framework for a new mortgage securitization platform and a model Pooling and Servicing Agreement. The proposed changes are part of a larger program to align and improve Fannie Mae's and Freddie Mac's (the Enterprises) business practices. Consistent with that program, the new platform would replace the proprietary structures used by the Enterprises with a more efficient common platform. Additionally, it would include certain enhancements and new capabilities. The proposed securitization platform would (i) facilitate broader sharing of credit risk, (ii) perform services related to the issuance and administration of mortgage-backed securities, (iii) be adaptable to policy changes and emerging technologies, and (iv) have an open architecture to drive interoperability. The model Pooling and Servicing Agreement would leverage the existing structures used by the Enterprises and, in doing so, would establish basic contractual requirements for pooling and selling and for the MBS/PC Trust. The FHFA seeks industry comment on the proposed framework, including responses to specific questions posed in the white paper. Comments must be submitted by December 3, 2012 and will be posted for public review.

Fannie Mae and Freddie Mac Align Certain Servicing Policies. On October 3, Fannie Mae and Freddie Mac (the Enterprises) issued announcements reflecting their recent effort to comply with an FHFA directive that the Enterprises work together to harmonize certain of their servicing policies and develop a consistent framework for assessing servicer performance. For example, Fannie Mae's Servicing Guide Announcement SVC-2012-21 and Freddie Mac's Bulletin 2012-20 include revisions

to the Enterprises' policies and practices regarding performance metrics for assessing servicers' fulfillment of their duties. The Enterprises also updated servicing policies to harmonize (i) compensatory fee structures, (ii) servicer violations and remedies, and (iii) servicing terminations and transfer of servicing. The effective date of most changes discussed in the announcements is January 1, 2013. However, Fannie Mae announced miscellaneous contractual changes that are effective immediately, including its adoption of New York law as its choice of law provision, and its clarification of certain Servicing Guide sections related to indemnification and electronic records.

Fannie Mae Announces Numerous Selling Guide Updates. On October 2, Fannie Mae issued Selling Guide Announcement SEL-2012-10, which updates and clarifies certain Selling Guide policies and procedures. First, the Announcement explains that the Selling Guide has been updated to incorporate prior changes announced in SEL-2012-09 (Updates to Refi Plus and DU Refi Plus) and SEL 2012-03 (Changes to Pricing Terms). Second, effective immediately, lenders must use the higher of the outstanding unpaid principle balance or the modified credit limit when calculating the HCLTV ratio for permanently modified home equity lines of credit. Third, Fannie Mae has removed the limit on the weighted-average coupon of fixed rate mortgage loans in MBS pools that involve a guaranty fee buyup, also effective immediately. Fourth, Fannie Mae has (i) clarified clarify distinctions between inactive and deactivated lenders, (ii) revised document custodian and custodial depository requirements, and (iii) updated the Eligibility Matrix.

OCC Refines Consideration of BSA/AML Examination Findings. On September 28, the OCC issued Bulletin 2012-30 to refine how examiners consider Bank Secrecy Act/Anti-Money Laundering (BSA/AML) examination findings in the FFIEC Uniform Ratings System and the OCC's risk assessment system for national banks and federal savings associations, and in the Risk Management, Operational Controls, Compliance, and Asset Quality ratings and risk assessment system for federal branches and agencies of foreign banking organizations. To align OCC practices with those of other federal regulators, OCC examiners no longer consider BSA/AML findings when assigning consumer compliance ratings. However, the findings still are considered when assessing overall compliance risk. Additionally, the current practice of considering such findings in the safety and soundness context will continue, and serious compliance deficiencies create a presumption that a bank's management component rating will be hurt. Similarly, current practices regarding consideration of findings with regard to foreign banks remain applicable.

STATE ISSUES

NY AG Files First RMBS Working Group Action, Expects More to Follow. On October 2, the Residential Mortgage-Backed Securities (RMBS) Working Group announced its first legal action. The civil complaint, filed against a major bank by New York Attorney General Eric Schneiderman on behalf of the people of that state, alleges that an underwriter acquired by the bank made fraudulent misrepresentations and omissions in the sale of RMBS to investors. The suit claims that losses resulting from the allegedly fraudulent sales total approximately $22.5 billion to date, but the complaint does not specify the damages sought. In announcing the suit, Attorney General Schneiderman, as well as Acting U.S. Associate Attorney General Tony West and other federal Working Group members, described the coordinated efforts that culminated in this filing. Specifically,

Working Group members stressed the assistance provided by the SEC and the FHFA. Indeed, the allegations in the New York Attorney General's complaint are similar to allegations previously made by the FHFA on behalf of Fannie Mae and Freddie Mac against numerous financial institutions. The allegations also parallel those made by private plaintiffs. On behalf of the RMBS Working Group, which was first announced by President Obama during his 2012 State of the Union address, Mr. Schneiderman has promised more civil, and potentially criminal, enforcement activity against other financial institutions.

State Regulators Oppose Basel III Capital Requirements. On October 3, the Conference of State Bank Supervisors (CSBS) announced its opposition to the "highly reactionary" approach federal regulators have proposed to implement the Basel III capital accord. Although they support higher levels and improved quality of capital, the state regulators argue that the transaction-level approach proposed by federal regulators is too complex and leaves the financial system susceptible to more volatility. Instead, the state regulators favor an approach based on risk management and the supervisory process. Further, the state regulators charge that the federal proposal, including the proposed specific risk-weighted asset requirements, lack empirical support. The CSBS argues that the proposed standardized risk-weighted assets present a specific challenge to mortgage lending, and in other areas would replace supervisory judgment and institution-specific analysis. The state regulators believe that implementing Basel III as currently proposed will only increase industry costs, limit credit availability, and force industry consolidation.

California Governor Signs Two "Buy Here Pay Here" Auto Dealer Bills, Vetoes a Third. On September 29, California Governor Jerry Brown signed AB 1447 and AB 1534, imposing new requirements on Buy-Here-Pay-Here automobile dealers (BHPH Dealers), defined as those dealers who assign less than 90% of their sale and lease contracts to an unaffiliated third party within 45 days of entering the contract unless they meet certain other criteria. The enacted bills require BHPH dealers to, among other things, (i) provide buyers and lessees with a 30-day/1,000 mile warranty covering certain components of the vehicle, (ii) make repairs at no cost to the consumer or refund the full amount of the purchase or lease, minus a reasonable amount for any damage to the vehicle after the lease or sale, when a covered warranty claim is made, and (iii) disclose the reasonable market value of a used vehicle by posting it on the vehicle, including what information was used to determine that value, and a copy of any information obtained from a nationally recognized pricing guide must be provided to potential purchasers of the vehicle. At the same time, the Governor vetoed a third bill, SB 956, which could have had far reaching implications for BHPH Dealers and auto finance companies who purchase loan contracts from BHPH Dealers, including (i) ensuring those dealers were properly licensed before making a purchase, (ii) limiting the interest rate that can be charged on those loans, and (iii) requiring those loans provide consumers with a longer grace period before repossession than is otherwise available under California law. Additional details about all three bills are available in a recent BuckleySandler blog post.

California Enacts Additional Mortgage-Related Bills. Last week, California enacted several additional mortgage-related bills. First, AB 1599 requires that a mortgagee, trustee, beneficiary, or authorized agent attach to the already required recorded notice of default and notice of sale, a summary of the information required to be contained in those notices. The notices must include a

statement referencing the attached summary, but the summary need not be recorded or published. Second, SB 980 extends until January 1, 2017 the existing prohibition against persons facilitating loan modifications from requiring or accepting pre-performance compensation, requiring collateral to secure payment, or taking power of attorney from the borrower. Finally, AB 2010 requires that reverse mortgage counseling be conducted in person, unless the borrower elected to receive counseling in another manner.

California Mortgage Settlement Monitor Reports on Dual Tracking. On October 2, California's Monitor of the commitments made by the nation's five mortgage companies pursuant to the national mortgage servicer settlement issued her first report. The report focuses on the progress the mortgage companies have made in complying with settlement restrictions on the use of dual tracking. The report's primary finding is that the servicers used the full 180-day implementation period allowed by the national settlement to end dual tracking, the practice whereby mortgage companies, seeking to protect their interests, allow a foreclosure to proceed even though the borrower has applied for a mortgage modification. The report does not allege any noncompliance with the settlement and acknowledges that complaints about dual tracking by the settling companies declined as the October 3, 2012 compliance deadline approached.

Oklahoma Transitions Money Transmitter Licensing to NMLS. On October 1, Oklahoma began transitioning state-licensed money transmitters to the NMLS. Existing and new licensees must create a company record in the NMLS and begin using the system for new licenses and renewals. The NMLS has issued instructions for new applications as well as company transition requests. Because the Oklahoma State Banking Department cannot receive electronic payments, licensees still must mail fee payments to the Department with a copy of the new or renewal application.

COURTS

Federal District Court Holds Foreclosures Negate Trust's Ability to Enforce Representations and Warranties. On October 1, the U.S. District Court for the District of Minnesota granted a lender's motion for partial summary judgment finding that a trustee's foreclosure on properties securing mortgage loans extinguished the loans and rendered them unavailable for repurchase by a lender. *MASTR Asset Backed Securities Trust 2006-HE3 v. WMC Mortgage Corporation*, No. 11-2542, 2012 WL 4511065 (D. Minn. Oct. 1, 2012). The trustee filed the action to compel the lender to repurchase certain loans the lender sold to the trust, alleging that the lender breached representations and warranties made in connection with the sale. The lender moved for partial summary judgment on the grounds that (i) the loans at issue no longer existed to be repurchased after the trust foreclosed on the properties securing the mortgages, and (ii) the trust failed to provide the lender with "prompt notice" of the alleged breaches on which it's repurchase demands were based as was required by the relevant agreement between the parties. In opposition to the lender's motion, the trustee argued that, notwithstanding its foreclosure on the properties securing the loans, the loans remained available for repurchase given that the relevant agreement between the parties defined "mortgage loans" to include proceeds from any foreclosure sale. The court rejected the trustee's argument and granted the lender's motion for partial summary judgment, concluding that the loans no longer existed for repurchase. With respect to the lender's "prompt notice," that court said that while it found notice was

not "prompt" under the circumstances presented, it could not grant summary judgment on that basis prior to discovery.

Nevada Supreme Court Validates MERS' Role as Beneficiary and Its Relationship to Note-Holder. On September 27, the Nevada Supreme Court held that when Mortgage Electronic Registration Systems, Inc. (MERS) is named as the beneficiary of a deed of trust but a different party holds the promissory note, such a split does not invalidate the instrument if the promissory note and deed of trust are later reunified. *Edelstein v. Bank of New York Mellon*, No. 57430, 2012 WL 4461716 (Nev. Sep. 27, 2012). In *Edelstein*, a borrower challenged a bank's standing to foreclose on his property arguing that the initial designation of MERS as the beneficiary on the deed of trust and another entity as the beneficiary of the promissory note irreparably split the documents such that the bank's foreclosure was precluded. The borrower argued that state law requires a party seeking to foreclose to demonstrate that it holds both the deed of trust and the promissory note. While acknowledging this requirement, the court rejected the borrower's argument that the bank lacked standing to foreclose. The court held that while the designation of MERS' as the initial beneficiary of the deed of trust effectively "split" the note and the deed, that split was not fatal and MERS could and did properly assign its interest in the deed of trust to the bank that had been assigned the promissory note at some point after the inception of the loan. Because the bank held both the deed of trust and the note, the court concluded that the bank had standing to foreclose on the borrower's property.

Nevada's Federal District Court Declines to Enforce Browsewrap Arbitration Agreement. On September 27, the U.S. District Court for the District of Nevada followed other federal courts and held that an arbitration clause within the Terms of Use agreement on Zappos.com was unenforceable given that users were neither provided with notice of the agreement nor an opportunity to affirmatively assent to the agreement. *In re Zappos.com, Inc. Customer Data Sec. Breach Litig.*, No. 12-325, 2012 WL 4466660 (D. Nev. Sep. 27, 2012). Customers sued Zappos in several federal district courts for damages resulting from a security breach of the company's website. After those actions were consolidated, Zappos filed a motion to compel arbitration based on the argument that by using the website the customers accepted and agreed to its Terms of Use, which included an agreement to arbitrate all claims arising from use of the website, and which were available through a hyperlink on each page of Zappos.com. Such hyperlinked Terms of Use are known as "browsewrap" agreements. The court held that despite the broad federal policy in favor of arbitration, the company had provided no evidence that the customers clicked on, viewed, or expressly manifested assent to the Terms of Use agreement, there was no acceptance of the Terms of Use provisions by customers, and thus those provisions, including the arbitration clause, were unenforceable. Moreover, the court held that because Zappos retained the unilateral right to revise the Terms of Use, the contract was illusory and therefore unenforceable. Accordingly, the court denied Zappos motion to compel arbitration.

Federal District Court Holds Federal Law Pre-empts Massachusetts' Statutory Limits On Mortgage Insurance. On September 21, the U.S. District Court for the District of Massachusetts held that the Federal Homeowners Loan Act pre-empted a Massachusetts law that forbids lenders from requiring borrowers to purchase insurance greater than the replacement cost of the building on the mortgaged property. *Silverstein v. ING Bank, fsb*, No. 12-10015, 2012 WL 4340587 (D. Mass. Sep. 21, 2012). A borrower brought a putative class action in state court alleging that the bank's

requirement that borrowers purchase insurance equal to the outstanding principal balance on the mortgage violated the state's limit on mortgage insurance. The bank removed the case to federal court and subsequently moved to dismiss while the borrower moved to remand the case. In denying the motion to remand and granting the bank's motion to dismiss, the court held that the Massachusetts statute limiting mortgage insurance to the replacement cost of the building falls plainly within the illustrative list of pre-empted state laws provided by the Homeowners Loan Act's implementing regulations. The court conceded that the borrower could bring common law claims against the bank, but held that the borrower's attempt to label his clear statutory claims as common law claims failed.

FIRM NEWS

James Parkinson will speak at the American Bar Association's International White Collar Crime Conference in London on October 8, 2012. Mr. Parkinson's panel is entitled "What Every General Counsel Needs to Know Regarding Compliance and Internal Investigations."

Jonice Gray Tucker, Valerie Hletko, and Amanda Raines will present a webinar sponsored by the California Mortgage Bankers Association on October 9, 2012. Their remarks will focus on fair lending enforcement trends and related risk assessments.

Jeff Naimon will be an instructor at the American Bar Association Consumer Financial Services Committee's Third Annual National Institute on Consumer Financial Services Basics on October 9, 2012. Mr. Naimon will be co-presenting on the topic of fair lending with Patrice Ficklin, CFPB Assistant Director, Office of Fair Lending and Equal Enforcement.

John Stoner will speak on a panel addressing "The Uniform Commercial Code and the Mortgage Crisis" at the State Bar of California Annual Meeting on October 12, 2012. Mr. Stoner recently was appointed to the Commercial Transactions Committee of the State Bar of California.

David Krakoff will participate on a panel at The American Bar Association's Fifth Annual National Institute on the Foreign Corrupt Practices Act, being held October 17 - 19, 2012 at The Westin Georgetown. Mr. Krakoff's session on October 18, 2012 is titled "The Trial of an FCPA Case: Pitfalls and Pratfalls."

Thomas Sporkin will speak at the Securities Enforcement Forum 2012 on October 18, 2012, in Washington, DC. The Securities Enforcement Forum 2012 brings together securities enforcement and white-collar attorneys, current and former senior SEC and DOJ officials, in-house counsel and compliance executives, and other top professionals in the field.

Margo Tank will speak at the ACORD Implementation Forum in Ft. Lauderdale, FL on October 24, 2012. Ms. Tank's panel is titled "Guidelines for e-Signatures and e-Delivery in the Insurance - Cutting through the Legalese."

David Krakoff, James Parkinson, Andrew Schilling, and Thomas Sporkin will speak at the Commerce and Industry Group's seminar, "Anti-Bribery: The Changing Anti-Corruption Environment in Key Jurisdictions" on October 24, 2012, in London. The panel will examine recent developments in anti-corruption enforcement in the UK, US, and Continental Europe; it will also consider best practices to identify and mitigate exposure to corruption risk.

James Parkinson will speak at the ACI's 28th National Conference on Foreign Corrupt Practices Act in Washington, D.C. Mr. Parkinson's panel, entitled "Data and Document Management Strategies for FCPA Investigations: Practical Tools for Effectively Accessing, Obtaining and Controlling Data and Documents during an FCPA Investigation," will be held November 14.

Margo Tank will speak at The Electronic Signature and Records Association's Annual Conference, November 14-15, 2012, in Washington, DC. Ms. Tank's panel will discuss electronic signatures and mobile technology.

David Krakoff will speak at ACI's Inaugural Summit on White Collar Litigation being held January 23-24, 2013, in New York, NY. Mr. Krakoff will participate in the session entitled "FCPA Case Review: A Hands-On Look at the Year in the FCPA and What Litigators Need to Take Away."

FIRM PUBLICATIONS

David Krakoff and Lauren Randall contributed "FCPA: Were the Sting Trials Doomed from the Start?" for the September 2012 Business Crimes Bulletin.

Matthew Previn, Andrew Pennacchia, and Jonathan Cannon published "Rising Tide of Operational Risk Demands Due Diligence in Vendor Selection" on September 20, 2012 in National Mortgage News.

Jonice Gray Tucker and Jeff Naimon wrote "Liability for Servicers: Localities Jump in the Game," which appears in *Mortgage Servicing News*' October 2012 issue.