Buckley Sandler LLP

InfoBytes

FINANCIAL SERVICE HEADLINES & DEADLINES FOR OUR CLIENTS AND FRIENDS

December 3, 2010

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Federal Issues

HUD Issues Guidance on Completing FHA Annual Certification Process. On November 17, the Department of Housing and Urban Development (HUD) issued Mortgagee Letter 2010-38, which, among other things, provides new guidance on completing the electronic Federal Housing Administration (FHA) Annual Certification process. Under the new guidance, mortgagees must complete their online Annual Certification prior to submitting their annual renewal fee and audited financial statements. Additionally, mortgagees must certify the accuracy of each of the statements found in their certification, including that the officers, partners, directors, managers, principals, supervisors, loan processors, loan underwriters, and loan originators of their institutions participating in FHA programs (i) are not subject to any unresolved findings or federal lawsuits resulting from an investigation, audit, or review by HUD or other federal, state, or local governmental agencies, or any other regulatory/oversight entities, (ii) are not in violation of the provisions of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (S.A.F.E. Act) or any applicable provision of state law, and (iii) are in compliance with state licensing requirements as well as all federally-mandated licensing or registration requirements, such as Nationwide Mortgage Licensing System and Registry (NMLSR) licensing/registration. If a mortgagee is unsure of whether a statement in its certification is accurate, then it should check the "Unable to Certify" box and provide an explanation for its inability to certify. FHA will review the explanation within 15 days of submission and indicate whether the mortgagee may complete the Annual Recertification process or must provide additional information. Any mortgagee who submits a false certification for any reason will be referred to the Mortgagee Review Board. The requirements of the Mortgagee Letter are effective immediately. For a copy of Mortgagee Letter 2010-38, please see here.

HUD Issues Revised Certification Language for HECM Transactions. On November 19, the Department of Housing and Urban Development (HUD) issued Mortgagee Letter 2010-39 introducing revised language for the HUD-1 settlement statement closing certification in Home Equity Conversion

Mortgage (HECM) transactions. The revisions include (i) new statutory authority to impose penalties for false certifications or fraudulent activities, (ii) new certification language for sellers of a HECM for Purchase transaction, and (iii) replacing the language found in paragraph 6-9(g) of HUD Handbook 4235.1, REV-1, which is required for HECM traditional and refinance transactions. The new certification language must be used for all HECM case numbers assigned on or after December 1. For a copy of the letter, please see http://www.hud.gov/offices/adm/hudclips/letters/mortgagee/files/10-39ml.pdf.

FDIC Issues Supervisory Guidance on Automated Overdraft Payment Programs. On November 24, the Federal Deposit Insurance Corporation (FDIC) issued final guidance to assist institutions in identifying, managing, and mitigating risks associated with automated overdraft payment programs. After issuing proposed guidance on August 11, 2010 and considering comments received, the FDIC set forth a number of expectations in its final guidance, including that institutions (i) monitor overdraft programs for excessive customer use and undertake meaningful follow-up action if appropriate, such as contacting customers regarding less-costly alternatives, (ii) impose appropriate daily limits on customer costs, and (iii) ensure check-clearing procedures avoid maximizing overdraft fees. The FDIC also indicated that it will review overdraft programs at each examination. The FDIC expects any additional efforts to mitigate risk in accordance with the final guidance to be implemented by July 1, 2011. For a copy of the press release and final guidance, please see http://1.usa.gov/dPWQzC and http://1.usa.gov/oGj4W9.

Ginnie Mae Announces New Financial Requirements for Multifamily Program Participation. On November 29, Ginnie Mae announced changes to the net worth, a new liquid asset requirement and institution-wide capital requirements for Multifamily Program participants. Ginnie Mae announced that the net worth requirement for Multifamily Program participants is to increase from $500,000 to $1,000,000. Additionally, Ginnie Mae announced changes to the formula used for calculating the additional net worth required above the base net worth. Issuers eligible for the Multifamily Program must also have liquid assets of 20% of Ginnie Mae's net worth requirement in addition to heightened institution-wide capital requirements. According to Ginnie Mae, the increased net worth, liquid asset and capital requirements are intended to help ensure that funds are available when there is a need for cash to fund loan buyouts and/or to pay for potential indemnification requests from insuring agencies. In addition, the increased financial requirements are intended to provide better assurance that Issuers have sufficient capital to cover their financial risks. The amended net worth requirements are effective immediately for institutions currently seeking Issuer approval; existing Issuers will have until May 1, 2011 to meet the new net worth requirements. Further, the new liquid asset and institution-wide capital requirements become effective on October 1, 2011. For a copy of the press release, please see http://www.ginniemae.gov/apm/apm_pdf/10-22.pdf.

Fannie Mae Announces Servicing Policy Changes. On November 29, Fannie Mae announced updates and clarifications to several servicing policies. The first is an update to the unique hardships policy for problem drywall. Fannie Mae will now consider extensions beyond the previously announced six months of forbearance for borrowers with financial hardships due to problem drywall. The second change is termination of the option to submit manually prepared reports. Beginning with the 2010 tax year, servicers must electronically file all Forms 1099-A filed on Fannie Mae's behalf,

even if the servicer has already submitted manual Forms 1099-A to Fannie Mae for 2010. The third clarification addresses delivery of repurchased loans, clarifying that a loan that was required to be repurchased by a secondary market investor, government sponsored enterprise (GSE), or private institutional investor other than Fannie Mae is not eligible for delivery to Fannie Mae even if the identified defect has been cured by the lender and may otherwise meet Fannie Mae requirements. The policy changes in the announcement are effective immediately. For a copy of the announcement, please see here.

Senate Passes Amendment to FCRA Clarifying Red Flags Rule. On November 30, the Senate passed the Red Flag Program Clarification Act of 2010, S. 3987, an amendment to the Fair Credit Reporting Act (FCRA), that clarifies the definition of "creditor" under its so-called Red Flag Rules. Those rules require a "creditor" to protect the credit card and debit card information of their customers by developing identity theft and protection programs. As originally drafted, certain professions (*e.g.*, healthcare, accounting, and legal practices) arguably fall within the rules' definition "creditor," which would require implementation of such programs despite not engaging in the traditional creditor relationship. The amendment would address this issue by narrowing the definition of "creditor" to expressly exclude individuals that "advance funds on behalf of a person for expenses incidental to a service provided by the creditor to that person." A companion bill, H.R. 6420, was referred to the House Committee on Financial Services on November 17. For a copy of S. 3987, please see here.

Informational Meetings on the OTS' Integration Into the OCC Scheduled. The Office of the Comptroller of the Currency (OCC) and the Office of Thrift Supervision (OTS) have scheduled meetings to inform regulated institutions about the changes associated with the OTS' integration into the OCC. The OCC and OTS are sponsoring these informational meetings in various cities nationwide to take place from mid-January through late March. For a copy of the meeting schedule and agenda, please see here.

FTC Issues Privacy Report with Framework for Protecting Privacy Interests from Online Tracking. On December 1, the Federal Trade Commission (FTC) issued a preliminary staff report, entitled "Protecting Consumer Privacy in an Era of Rapid Change: A Proposed Framework for Businesses and Policymakers," that recommending a framework for better regulating use of online tracking, which would attempt to balance the privacy interests of consumers against industry's use of consumer information to develop beneficial new products and services. The report's intended purpose, among other things, is to educate policymakers, including Congress, as they develop policies to regulate advances in technology that allow for rapid data collection and sharing that is often invisible to consumers as they browse and use the Internet. The report reasons that the current privacy policies governing online tracking - primarily long, legalistic disclosures that consumers usually do not read or do not understand - force consumers to bear the burden of protecting their privacy. To alleviate this burden, the report suggests that companies adopt a "privacy by design" approach, meaning that privacy protections should be built into companies' everyday business practices. These privacy protections should include: (i) reasonable security for consumer data, (ii) limited collection and retention of such data, and (iii) reasonable procedures to promote data accuracy. In addition, the report advises companies to implement and enforce procedurally sound privacy practices throughout their organizations. The proposed framework also recommends

presenting consumers with a simplified choice about the collection and sharing of data detailing their online browsing activities. For example, offering a "Do Not Track" mechanism, which would allow consumers to opt out of the collection of information for targeted ads. Finally, the report also suggests other measures to improve the transparency of information practices, including (i) standardized notices, (ii) "reasonable access" for consumers to the data that companies maintain about them, and (iii) education efforts to explain commercial data practices and available choices. The public comment period on the report runs until January 31, 2011. For a copy of the press release and the preliminary report, please see http://1.usa.gov/oGj4W9 and http://1.usa.gov/hUv6qF.

Federal Agencies Issue Final Interagency Appraisal and Evaluation Guidelines. On December 2, the Federal Reserve Board, the Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, the Office of Thrift Supervision, and National Credit Union Administration (Agencies) issued final supervisory guidelines on sound practices by financial institutions for real estate appraisals and evaluations. Specifically, the *Interagency Appraisal and Evaluation Guidelines*, which replace the 1994 guidelines, explain the Agencies' minimum regulatory standards for appraisals. Among other things, the guidelines emphasize that financial institutions (i) are responsible for selecting appropriate appraisers and people performing evaluations, and (ii) must maintain strong internal controls to ensure reliable appraisals and evaluations. The Agencies noted that further revisions to these guidelines may be necessary after regulations are adopted to implement the Dodd-Frank Wall Street Financial Reform and Consumer Protection Action of 2010. For a copy of the press release and guidelines, please see here.

State Issues

District of Columbia Issues Guidance on Foreclosure Law Compliance. On November 29, the District of Columbia Department of Insurance, Securities and Banking (DISB) announced it had issued a November 24 bulletin informing licensed residential mortgage lenders and mortgage borrowers of the enactment of a new emergency law requiring mortgage lenders to go through six months of mediation with a homeowner before proceeding with a foreclosure. The law, titled the Saving D.C. Homes from Foreclosure Emergency Amendment Act of 2010, requires lenders to send homeowners a form to opt in or out of mediation when the homeowners receive foreclosure notices from the lenders. Borrowers who opt in will enter mediation with their lender and have 90 days, in addition to the 30 days they had to decide whether to opt in or out, to reach a settlement. Mediation will be guided by foreclosure mediators, and the program will be administered by DISB. The law became effective immediately upon the signature of Mayor Adrian Fenty on November 17 and will expire on February 15, 2011. For a copy of the press release, including a link to the bulletin, please see here.

CSBS Announces Renewal of Idaho Regulator's Certificate of Accreditation. On November 30, the Conference of State Bank Supervisors (CSBS) announced that the Idaho Department of Finance (Department) successfully renewed its Certificate of Accreditation. CSBS accreditation certifies that an external review of the Department has concluded that it meets threshold supervision standards and practices as established by CSBS's Accreditation Program. For a copy of the press release, please see here.

Courts

Eleventh Circuit Dismisses RESPA Case Alleging That Discount Points Are Settlement Services. The U.S. Court of Appeals for the Eleventh Circuit has affirmed the dismissal of a case alleging that the charging of "exorbitant" discount points amounted to "disguised unearned fees" in violation of the Real Estate Settlement Procedures Act (RESPA). *Wooten v. Quicken Loans, Inc.*, No 08-11245, 2010 WL 4723054 (11th Cir. Nov. 23, 2010). In this case, the plaintiffs obtained residential mortgage loans from the defendant lender. In each transaction, the lender charged discount points to the plaintiffs, and the discount points were disclosed on the HUD-1 settlement statements. The discount points were ostensibly paid by the plaintiffs to obtain a lower interest rate. The plaintiffs filed suit, alleging that, despite their paying discount points, the plaintiffs did not obtain any reduction in interest rate. The district court dismissed the case, finding that discount points are not "settlement services," as that term is defined under RESPA and are therefore not subject to the prohibition under section 8(b) of RESPA on the charging of fees for which no services are performed. The Eleventh Circuit, in affirming the district court, emphasized that discount points are not any type of "service," and that, even if the discount points were services, the plaintiffs failed to identify any services that were not provided. For a copy of the opinion, please see here.

Federal Court Holds That Online Brokerage Agreement Allowing Unilateral Changes to Fee Schedules Without Notice to the Customer is Unenforceable. On November 22, the U.S. District for the Northern District of California held that E*Trade customers properly stated a claim for unjust enrichment under either California or New York law based on allegations that E*Trade's online brokerage agreement allowed the Company to "unilaterally, and without notice, change the operative fee schedule." *Roling v. E*Trade Securities, LLC*, No. C 10-0488 (N.D. Cal. Nov. 22, 2010). The brokerage agreement that the Plaintiffs agreed to allowed E*Trade to charge fees according to its "then-current" fee schedule, which was to be posted on the E*Trade website. E*Trade charged the Plaintiffs a $40 per quarter "inactivity fee" when no trades were made during a quarter. When the fees owed exceeded the balance in the Plaintiffs' accounts, E*Trade liquidated the accounts and kept the proceeds in satisfaction of the fees. The Plaintiffs claimed that E*Trade's ability to change the operative schedule unilaterally and without notice to customers was unconscionable, thus rendering that provision of the brokerage agreement unenforceable. This meant that E*Trade was unjustly enriched when it collected fees based on that provision. The Court agreed that Plaintiffs stated a claim and rejected E*Trade's motion to dismiss, noting that "[n]one of E*Trade's authorities addresses whether a contract is unenforceable as a matter of law where it allows a contracting party to change the provisions of the contract without notice." The Court also denied E*Trade's motion to dismiss with respect to the Plaintiffs' alternative breach of express contract claim, which was premised on the allegation that the language of the fee schedule that Plaintiffs believed to be applicable did not permit inactivity fees. The Court held that both sides offered reasonable interpretations of the fee schedule and, because it could not resort to extrinsic evidence on a motion to dismiss, it could not resolve the ambiguity. Next, the Court dismissed the Plaintiffs' claim that the inactivity fee constituted a liquidated damages clause in violation of California law because it did not depend on the Plaintiffs having breached their contracts. Finally, the Court held that the Plaintiffs did state a claim for violation of California's unfair competition law, but the claim was duplicative of the other claims and therefore no independent damages would be permitted. For a copy of the opinion, please see here.

New Jersey Courts Deny Enforcement of Mortgage Notes. In two notable cases decided in the past several months, New Jersey courts have rejected creditors' attempts to enforce the promissory notes entered into in connection with home mortgages. In both cases, the courts denied the creditors' claims on the basis that the creditors were not in possession of the notes, as required under the New Jersey Uniform Commercial Code (New Jersey UCC), at the time the claims were filed. In a case decided on November 16, the U.S. Bankruptcy Court for the District of New Jersey sustained the debtor's challenge to the creditor's proof of claim filed in connection with the debtor's Chapter 13 bankruptcy proceeding. *Kemp v. Countrywide Home Loans, Inc.*, Case No. 08-18700-JHW, Adversary No. 08-2448, 2010 WL 4777625 (Bankr. D.N.J. November 16, 2010). Some time prior to this case, the defendant, Countrywide Home Loans, Inc. (Countrywide), made a home mortgage loan to plaintiff. After making the loan, Countrywide pooled it with other loans and sold the loan pool to the Bank of New York, as Trustee (BNY). Under the Pooling and Servicing Agreement, Countrywide was required to transfer title to the loans, together with the original note, endorsed in blank, and deliver the original loan documents to BNY. The court found that at the time Countrywide (acting as servicer for BNY) filed the proof of claim on Mr. Kemp's mortgage loan, Countrywide had assigned the mortgage, but had not transferred possession of the note, to BNY. The court stated that under New Jersey's UCC, the note was unenforceable, because the owner of the note, BNY never had possession of the note, and the note was not properly endorsed to BNY. Thus, although BNY had a valid claim of ownership of the loan, it could not enforce the note. As servicer of the loan, Countrywide could properly file a proof of claim on behalf of BNY, but only if BNY itself had the right to enforce the note. The court stated that "[b]ecause the Bank of New York has no right to enforce the note, Countrywide as its agent and servicer cannot enforce the note." Therefore, the court disallowed the claim. For a copy of the opinion, please see here. In a case decided on June 29, the Superior Court of New Jersey, Chancery Division, Atlantic County, dismissed the creditor's complaint in foreclosure without prejudice, because the creditor was not in possession of the note at the time the complaint was filed. *Bank of New York v. Raftogianis*, No. F-7356-09 (N.J. Super. June 29, 2010). In this case, BNY was the trustee of a pool of mortgage loans containing the debtors' loan. In deciding this case, the court considered whether BNY was the holder of the mortgage note, as required by the New Jersey UCC in order to enforce the note. To enforce a note, the plaintiff holder must be in possession of the note, and the note must be endorsed prior to or at the time of delivery, to the plaintiff or in blank. The court concluded that BNY failed to establish that the note was in its possession at the time it filed the foreclosure complaint and dismissed the complaint without prejudice. The dismissal permits the plaintiff to file a new complaint in foreclosure but requires the plaintiff to accompany the new complaint with "appropriate certification, executed by one with personal knowledge of the circumstances, confirming the plaintiff is in possession of the original note as of the date any new action is filed." The court further required that the certification "must indicate the physical location of the note and the name of the individual or entity in possession." For a copy of the opinion, please see here.

Washington State Supreme Court Holds Federal Privacy Laws Apply to Disclosure of Borrower Information Obtained by State Attorney General. The Supreme Court of the State of Washington recently held in *Ameriquest Mortgage Co. v. Washington State Office of the Attorney General*, No. 82690-1, 2010 WL 4351968 (Wash. Nov. 4, 2010) that federal privacy laws apply to a consumer lawyer's request to the state attorney general (AG) for borrower information obtained in the

course of an investigation. Citing Washington's Public Records Act (PRA), the lawyer had requested, and the AG had agreed to provide, borrower names, addresses, and loan terms and costs. The court held the federal Gramm-Leach-Bliley Act (GLBA) and relevant Federal Trade Commission rules preempt the PRA and prohibit the AG from disclosing non-public information, since the AG was a nonaffiliated third party under GLBA and the lawyer was not an affiliate of the AG. The court further held that only aggregate information or blind data that does not contain personal identifiers is exempt from the federal privacy rules. For a copy of the opinion, please see here.

Firm News

Bob Serino received the Richard Peterson Award at the Federal Bar Association's Banking Law Committee Annual General Counsel dinner which was held on November 18. The Executive Council of the Federal Bar Association's Banking Law Committee presented the award to Bob Serino for his outstanding contribution to Federal Banking Regulation and Policy throughout his career with the Federal Government and in private practice.

David Krakoff, James Parkinson and Lauren Randell will be speaking in the "FCPA Enforcement Update: Individuals in the Line of Fire,"web conference on December 6. This 60-minute CLE webinar will provide an update on recent FCPA enforcement activities related to individuals.

Andrew Sandler will be a speaking at PLI's Banking Law Institute 2010: The Future is Here, on December 8. Mr. Sandler's session is: Consumer Financial Protection & Enforcement Proceedings under the New Legislation.

Noel Gruber and David Baris will present a webinar on the Small Business Lending Fund, "Small Business Lending Fund - TARP Warmed Over or Something New?" for the Western Independent Bankers/American Association of Bank Directors on December 9.

James Parkinson will speak in the Strafford web conference, "The FCPA's Exception and Affirmative Defenses: Complying with the Requirements for Gifts, Hospitality, and Facilitation Payments" at 1pm EST on December 21. This 75-minute CLE webinar will provide guidance to counsel for U.S. Companies conducting business internationally on navigating the facilitation-payment exception and affirmative defenses under the FCPA in order to avoid violations and penalties.

James Parkinson will be speaking at the web conference "FCPA Compliance: Best Practices for Your Anti-Corruption Compliance Program," hosted by National Constitution Center Conferences on January 19, 2011.

Donna Wilson will be speaking at the ACI Privacy & Security of Consumer & Employee Information Conference on January 25-26, 2011 in Washington, DC. The topic will be "Responding to the Latest Cyber Threats: Mobile Workforces, Technology, Data Thefts, and Cloud Computing."

Andrew Sandler will be speaking at the American Conference Institute's 10th Annual Advanced Forum on Consumer Finance Class Actions & Litigation on January 27, 2011 at 11am. The

conference is taking place at The Helmsley Park Lane Hotel, 36 Central Park South, NYC. The topic will be Emerging Federal and State Regulatory and Enforcement Initiatives: FTC, DOJ, SEC, FRB, and State AGs Perspectives. Also on the panel with Andy will be Attorney General William Sorrell, AG, State of Vermont and Attorney General Greg Zoeller, AG, State of Indiana.

Miscellany

Wisconsin Federal Court Sentences Bank Fraud Defendant to Three Months in Prison. On November 23, Amy Strait was sentenced to three months in prison, followed by two years of supervised release, after pleading guilty to conspiracy to obstruct a bank fraud investigation related to the submission of forged tax returns to the bank at which Strait worked as a loan officer. Strait admitted that after her bank discovered that income on tax returns submitted in support of loans did not match income reported to the Internal Revenue Service (IRS), she alerted her co-conspirators to the investigation, leading them to destroy evidence of the fraud. Four other defendants have pleaded guilty in the bank fraud scheme or a related tax fraud scheme, and three have been sentenced, with sentences ranging from a year and a day, to a year and a half in prison. The investigation was a joint effort of the Federal Bureau of Investigation and IRS Criminal Investigation. For a copy of the press release, please see here.

Mortgages

HUD Issues Guidance on Completing FHA Annual Certification Process. On November 17, the Department of Housing and Urban Development (HUD) issued Mortgagee Letter 2010-38, which, among other things, provides new guidance on completing the electronic Federal Housing Administration (FHA) Annual Certification process. Under the new guidance, mortgagees must complete their online Annual Certification prior to submitting their annual renewal fee and audited financial statements. Additionally, mortgagees must certify the accuracy of each of the statements found in their certification, including that the officers, partners, directors, managers, principals, supervisors, loan processors, loan underwriters, and loan originators of their institutions participating in FHA programs (i) are not subject to any unresolved findings or federal lawsuits resulting from an investigation, audit, or review by HUD or other federal, state, or local governmental agencies, or any other regulatory/oversight entities, (ii) are not in violation of the provisions of the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (S.A.F.E. Act) or any applicable provision of state law, and (iii) are in compliance with state licensing requirements as well as all federally-mandated licensing or registration requirements, such as Nationwide Mortgage Licensing System and Registry (NMLSR) licensing/registration. If a mortgagee is unsure of whether a statement in its certification is accurate, then it should check the "Unable to Certify" box and provide an explanation for its inability to certify. FHA will review the explanation within 15 days of submission and indicate whether the mortgagee may complete the Annual Recertification process or must provide additional information. Any mortgagee who submits a false certification for any reason will be referred to the Mortgagee Review Board. The requirements of the Mortgagee Letter are effective immediately. For a copy of Mortgagee Letter 2010-38, please see here.

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Eleventh Circuit Dismisses RESPA Case Alleging That Discount Points Are Settlement Services. The U.S. Court of Appeals for the Eleventh Circuit has affirmed the dismissal of a case alleging that the charging of "exorbitant" discount points amounted to "disguised unearned fees" in violation of the Real Estate Settlement Procedures Act (RESPA). *Wooten v. Quicken Loans, Inc.*, No 08-11245, 2010 WL 4723054 (11th Cir. Nov. 23, 2010). In this case, the plaintiffs obtained residential mortgage loans from the defendant lender. In each transaction, the lender charged discount points to the plaintiffs, and the discount points were disclosed on the HUD-1 settlement statements. The discount points were ostensibly paid by the plaintiffs to obtain a lower interest rate. The plaintiffs filed suit, alleging that, despite their paying discount points, the plaintiffs did not obtain any reduction in interest rate. The district court dismissed the case, finding that discount points are not "settlement services," as that term is defined under RESPA and are therefore not subject to the prohibition under section 8(b) of RESPA on the charging of fees for which no services are performed. The Eleventh Circuit, in affirming the district court, emphasized that discount points are not any type of "service," and that, even if the discount points were services, the plaintiffs failed to identify any services that were not provided. For a copy of the opinion, please see here.

Federal Court Holds That Online Brokerage Agreement Allowing Unilateral Changes to Fee Schedules Without Notice to the Customer is Unenforceable. On November 22, the U.S. District for the Northern District of California held that E*Trade customers properly stated a claim for unjust enrichment under either California or New York law based on allegations that E*Trade's online brokerage agreement allowed the Company to "unilaterally, and without notice, change the operative

fee schedule." *Roling v. E*Trade Securities, LLC*, No. C 10-0488 (N.D. Cal. Nov. 22, 2010). The brokerage agreement that the Plaintiffs agreed to allowed E*Trade to charge fees according to its "then-current" fee schedule, which was to be posted on the E*Trade website. E*Trade charged the Plaintiffs a $40 per quarter "inactivity fee" when no trades were made during a quarter. When the fees owed exceeded the balance in the Plaintiffs' accounts, E*Trade liquidated the accounts and kept the proceeds in satisfaction of the fees. The Plaintiffs claimed that E*Trade's ability to change the operative schedule unilaterally and without notice to customers was unconscionable, thus rendering that provision of the brokerage agreement unenforceable. This meant that E*Trade was unjustly enriched when it collected fees based on that provision. The Court agreed that Plaintiffs stated a claim and rejected E*Trade's motion to dismiss, noting that "[n]one of E*Trade's authorities addresses whether a contract is unenforceable as a matter of law where it allows a contracting party to change the provisions of the contract without notice." The Court also denied E*Trade's motion to dismiss with respect to the Plaintiffs' alternative breach of express contract claim, which was premised on the allegation that the language of the fee schedule that Plaintiffs believed to be applicable did not permit inactivity fees. The Court held that both sides offered reasonable interpretations of the fee schedule and, because it could not resort to extrinsic evidence on a motion to dismiss, it could not resolve the ambiguity. Next, the Court dismissed the Plaintiffs' claim that the inactivity fee constituted a liquidated damages clause in violation of California law because it did not depend on the Plaintiffs having breached their contracts. Finally, the Court held that the Plaintiffs did state a claim for violation of California's unfair competition law, but the claim was duplicative of the other claims and therefore no independent damages would be permitted. For a copy of the opinion, please see here.

New Jersey Courts Deny Enforcement of Mortgage Notes. In two notable cases decided in the past several months, New Jersey courts have rejected creditors' attempts to enforce the promissory notes entered into in connection with home mortgages. In both cases, the courts denied the creditors' claims on the basis that the creditors were not in possession of the notes, as required under the New Jersey Uniform Commercial Code (New Jersey UCC), at the time the claims were filed. In a case decided on November 16, the U.S. Bankruptcy Court for the District of New Jersey sustained the debtor's challenge to the creditor's proof of claim filed in connection with the debtor's Chapter 13 bankruptcy proceeding. *Kemp v. Countrywide Home Loans, Inc.*, Case No. 08-18700-JHW, Adversary No. 08-2448, 2010 WL 4777625 (Bankr. D.N.J. November 16, 2010). Some time prior to this case, the defendant, Countrywide Home Loans, Inc. (Countrywide), made a home mortgage loan to plaintiff. After making the loan, Countrywide pooled it with other loans and sold the loan pool to the Bank of New York, as Trustee (BNY). Under the Pooling and Servicing Agreement, Countrywide was required to transfer title to the loans, together with the original note, endorsed in blank, and deliver the original loan documents to BNY. The court found that at the time Countrywide (acting as servicer for BNY) filed the proof of claim on Mr. Kemp's mortgage loan, Countrywide had assigned the mortgage, but had not transferred possession of the note, to BNY. The court stated that under New Jersey's UCC, the note was unenforceable, because the owner of the note, BNY never had possession of the note, and the note was not properly endorsed to BNY. Thus, although BNY had a valid claim of ownership of the loan, it could not enforce the note. As servicer of the loan, Countrywide could properly file a proof of claim on behalf of BNY, but only if BNY itself had the right to enforce the note. The court stated that "[b]ecause the Bank of New York has no right to enforce the note, Countrywide as its agent and servicer cannot enforce the note." Therefore, the court disallowed the claim. For a

copy of the opinion, please see here. In a case decided on June 29, the Superior Court of New Jersey, Chancery Division, Atlantic County, dismissed the creditor's complaint in foreclosure without prejudice, because the creditor was not in possession of the note at the time the complaint was filed. *Bank of New York v. Raftogianis*, No. F-7356-09 (N.J. Super. June 29, 2010). In this case, BNY was the trustee of a pool of mortgage loans containing the debtors' loan. In deciding this case, the court considered whether BNY was the holder of the mortgage note, as required by the New Jersey UCC in order to enforce the note. To enforce a note, the plaintiff holder must be in possession of the note, and the note must be endorsed prior to or at the time of delivery, to the plaintiff or in blank. The court concluded that BNY failed to establish that the note was in its possession at the time it filed the foreclosure complaint and dismissed the complaint without prejudice. The dismissal permits the plaintiff to file a new complaint in foreclosure but requires the plaintiff to accompany the new complaint with "appropriate certification, executed by one with personal knowledge of the circumstances, confirming the plaintiff is in possession of the original note as of the date any new action is filed." The court further required that the certification "must indicate the physical location of the note and the name of the individual or entity in possession." For a copy of the opinion, please see here.

Washington State Supreme Court Holds Federal Privacy Laws Apply to Disclosure of Borrower Information Obtained by State Attorney General. The Supreme Court of the State of Washington recently held in *Ameriquest Mortgage Co. v. Washington State Office of the Attorney General*, No. 82690-1, 2010 WL 4351968 (Wash. Nov. 4, 2010) that federal privacy laws apply to a consumer lawyer's request to the state attorney general (AG) for borrower information obtained in the course of an investigation. Citing Washington's Public Records Act (PRA), the lawyer had requested, and the AG had agreed to provide, borrower names, addresses, and loan terms and costs. The court held the federal Gramm-Leach-Bliley Act (GLBA) and relevant Federal Trade Commission rules preempt the PRA and prohibit the AG from disclosing non-public information, since the AG was a nonaffiliated third party under GLBA and the lawyer was not an affiliate of the AG. The court further held that only aggregate information or blind data that does not contain personal identifiers is exempt from the federal privacy rules. For a copy of the opinion, please see here.

E-Financial Services

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that provision of the brokerage agreement unenforceable. This meant that E*Trade was unjustly enriched when it collected fees based on that provision. The Court agreed that Plaintiffs stated a claim and rejected E*Trade's motion to dismiss, noting that "[n]one of E*Trade's authorities addresses whether a contract is unenforceable as a matter of law where it allows a contracting party to change the provisions of the contract without notice." The Court also denied E*Trade's motion to dismiss with respect to the Plaintiffs' alternative breach of express contract claim, which was premised on the allegation that the language of the fee schedule that Plaintiffs believed to be applicable did not permit inactivity fees. The Court held that both sides offered reasonable interpretations of the fee schedule and, because it could not resort to extrinsic evidence on a motion to dismiss, it could not resolve the ambiguity. Next, the Court dismissed the Plaintiffs' claim that the inactivity fee constituted a liquidated damages clause in violation of California law because it did not depend on the Plaintiffs having breached their contracts. Finally, the Court held that the Plaintiffs did state a claim for violation of California's unfair competition law, but the claim was duplicative of the other claims and therefore no independent damages would be permitted. For a copy of the opinion, please see here.

Privacy/Data Security

FTC Issues Privacy Report with Framework for Protecting Privacy Interests from Online Tracking. On December 1, the Federal Trade Commission (FTC) issued a preliminary staff report, entitled "Protecting Consumer Privacy in an Era of Rapid Change: A Proposed Framework for Businesses and Policymakers," that recommending a framework for better regulating use of online tracking, which would attempt to balance the privacy interests of consumers against industry's use of consumer information to develop beneficial new products and services. The report's intended purpose, among other things, is to educate policymakers, including Congress, as they develop policies to regulate advances in technology that allow for rapid data collection and sharing that is often invisible to consumers as they browse and use the Internet. The report reasons that the current privacy policies governing online tracking - primarily long, legalistic disclosures that consumers usually do not read or do not understand - force consumers to bear the burden of protecting their privacy. To alleviate this burden, the report suggests that companies adopt a "privacy by design" approach, meaning that privacy protections should be built into companies' everyday business practices. These privacy protections should include: (i) reasonable security for consumer data, (ii) limited collection and retention of such data, and (iii) reasonable procedures to promote data accuracy. In addition, the report advises companies to implement and enforce procedurally sound privacy practices throughout their organizations. The proposed framework also recommends presenting consumers with a simplified choice about the collection and sharing of data detailing their online browsing activities. For example, offering a "Do Not Track" mechanism, which would allow consumers to opt out of the collection of information for targeted ads. Finally, the report also suggests other measures to improve the transparency of information practices, including (i) standardized notices, (ii) "reasonable access" for consumers to the data that companies maintain about them, and (iii) education efforts to explain commercial data practices and available choices. The public comment period on the report runs until January 31, 2011. For a copy of the press release and the preliminary report, please see http://1.usa.gov/oGj4W9 and http://1.usa.gov/hUv6qF.

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Criminal Enforcement Action

Wisconsin Federal Court Sentences Bank Fraud Defendant to Three Months in Prison. On November 23, Amy Strait was sentenced to three months in prison, followed by two years of supervised release, after pleading guilty to conspiracy to obstruct a bank fraud investigation related to the submission of forged tax returns to the bank at which Strait worked as a loan officer. Strait admitted that after her bank discovered that income on tax returns submitted in support of loans did not match income reported to the Internal Revenue Service (IRS), she alerted her co-conspirators to the investigation, leading them to destroy evidence of the fraud. Four other defendants have pleaded guilty in the bank fraud scheme or a related tax fraud scheme, and three have been sentenced, with sentences ranging from a year and a day, to a year and a half in prison. The investigation was a joint effort of the Federal Bureau of Investigation and IRS Criminal Investigation. For a copy of the press release, please see here.

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