FINANCIAL SERVICES REPORT

Quarterly News, Spring 2013

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MOFO METRICS

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MORRISON
FOERSTER

Editor's Note

This is a dignified law firm newsletter, not like the "Brand X" versions. You won't find pandering, attention-grabbing stories about Justin Bieber, Kim Kardashian, Ashton Kutcher, Prince William, or Charlie Sheen. Lady Gaga will not be mentioned. Sure, there are those who would resort to tricks to game the search engines, in order that their cartoonish scrawls clog the top of everyone's Google "hit list," but George Clooney is not someone we're going to talk about. Nothing here about Ben Affleck's Oscar or Oscar Pistorius's arraignment either. And forget about Adele's baby. Angelo. That's not to say that someone wouldn't sprinkle celebrity names throughout these pages (think "Where's Waldo" for bank lawyers), but that would simply ensure that you actually read these important articles because if you don't your institutions will fail. Consider this a public service. Kate Middleton's pregnancy? Not R Us! Try the other guys. You're welcome.

This quarter we had a lot of important stuff happen. A comet barely missed the planet, a bus-sized meteor exploded over Russia, and the President issued a cyber-security order. There were remittance transfer rules and then there weren't; lots of privacy, mortgage, and arbitration developments; and so much CFPB stuff that we almost had to ship by the pound.

Until next issue, don't litter, look both ways, and recycle this newsletter.

William Stern, Editor-in-chief

BELTWAY REPORT

Finally!

Despite numerous predictions of quick and easy passage, Congress finally passed and President Obama signed into law an amendment to the Federal Deposit Insurance Act (FDIA) specifying that submission of privileged information to the Consumer Financial Protection Bureau (CFPB) and any sharing of that information by the CFPB with other federal agencies does not waive the attorney-client privilege as to third parties. The legislation provides much-needed protection for entities under the CFPB's supervisory authority.

Tit for Tat

On February 12, 2013, the Federal Deposit Insurance Corporation (FDIC) proposed for public comment a rule that would exclude from federal deposit insurance coverage those deposits made at insured U.S. banks that are payable at a foreign branch of a U.S. bank. Dually payable deposits, which are payable at both domestic and overseas branches, would be subject to this rule, although they would be treated the same as purely domestic deposits in the event of a bank resolution. The FDIC's action responds to action taken by UK regulators last fall to prohibit UK branches of a non-EU bank from taking deposits if those deposits are not accorded depositor preference status under the laws of the bank's home country. Comments on the proposal are due by April 22, 2013. Read the details in our News Bulletin at http://www.mofo.com/files/Uploads/Images/130221-FDIC-Insurance-Deposits.pdf.

For more information, contact Charles Horn at chorn@mofo.com.

Layer Up

The Federal Reserve Board (FRB) has proposed rules to strengthen the oversight of U.S. operations of foreign banks, requiring foreign banks with a significant U.S. presence to create an intermediate holding company over their U.S. subsidiaries. The Board's proposal is intended to facilitate consistent and enhanced supervision and regulation of the U.S. operations of these foreign banks and resolution of failing U.S. operations of a foreign bank, if needed. Foreign banks also would be required to maintain stronger capital and liquidity positions in the U.S. to help increase the resiliency of their U.S. operations. The proposal implements provisions of the Dodd-Frank Act designed to address the risks associated with the increased complexity, interconnectedness, and concentration of the U.S. operations of foreign banks. Public comments will be accepted through March 31, 2013.

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

OPERATIONS REPORT

Check Yourself

The FRB issued a supplemental policy statement on the internal audit function and its outsourcing, supplementing 2003 interagency guidance. The statement applies to supervised financial institutions with greater than $10 billion in total consolidated assets. It identifies ways to strengthen internal audit practices, including by analyzing the effectiveness of all critical risk management functions, adoption of appropriate policies and procedures and effective controls, and active involvement of the board of directors and senior management in setting and monitoring compliance with the institution's risk tolerance limits. The policy statement reminds institutions that the responsibility for maintaining an effective system of internal controls cannot be delegated to a third party, and addresses various issues relating to outsourcing of internal audit functions.

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

Some Reprieve

On January 6, 2013, the Group of Governors and Heads of Supervision (GHOS), which oversees the Basel Committee on Banking Supervision (BCBS), approved a significantly revised version of the BCBS's liquidity coverage ratio (LCR). The LCR was designed to test a banking organization's ability to withstand a liquidity crisis over a 30-day period. The revised LCR modifies certain elements of the original LCR, published in December 2010 as part of the Basel III framework, and extends the deadline for full compliance with the LCR requirements. If all of these acronyms whet your appetite for more, read our News Bulletin at http://www.mofo.com/files/Uploads/Images/130110-Liquidity-Coverage-Ratio.pdf.

For more information, contact Dwight Smith at dsmith@mofo.com.

Size Adjustments

The federal bank regulatory agencies announced the annual adjustment to the asset-size thresholds used to define small bank, small savings association, intermediate small bank, and intermediate small savings association under the Community Reinvestment Act (CRA) regulations. These thresholds impact applicable CRA examination procedures and reporting requirements. As of January 1, 2013, "small bank" or "small savings association" now means an institution that had assets of less than $1.186 billion as of December 31 of either of the prior two calendar years; and an "intermediate small bank" or "intermediate small savings association" is one with assets of at least $296 million and less than $1.186 billion as of December 31 of either of the prior two calendar years.

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

BUREAU REPORT

After several enforcement actions during the summer and early fall, the CFPB appears to have spent the past few months hitting the books and brushing up its understanding

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of several consumer financial services markets through requests for information, including those on products and credit cards offered to college students. Like college and university students, various divisions at the CFPB have found time for extracurricular activities, such as proposing new trial disclosure programs. There also has been a lot of time spent worrying about what President Obama and CFPB Director Richard Cordray have done during recess. Too busy with your own homework to keep up? Not to worry—we highlight all this, and more, below.

Who's in Charge?

Lending credence to those who argue recess is the most important school subject, the D.C. Circuit Court of Appeals issued a unanimous decision on the President's appointment power calling into question Richard Cordray's original 2012 recess appointment. *Noel Canning v. NLRB*, __ F.3d __, 2013 WL 276024 (D.C. Cir. Jan. 25, 2013). The court ruled that National Labor Relations Board appointments President Obama made on January 4, 2012, were not made in accordance with the Recess Appointments Clause of the U.S. Constitution because they were not made during a recess that occurred between sessions of Congress. President Obama appointed Richard Cordray at the same time as he made the appointments invalidated by this decision. If it stands, the decision has the potential to undermine several of the CFPB's authorities and decisions, including several final rules that the CFPB has issued and supervisory actions that the CFPB has taken.

For more information, contact Andrew Smith at andrewsmith@mofo.com, and see our Client Alert at http://www.mofo.com/files/Uploads/Images/130129-CFPB-Setback.pdf.

Exemption at Your Own Risk

On December 13, 2012, the CFPB proposed a new policy that, if implemented, would allow individual companies to apply to the CFPB for specific exemptions from federal disclosure laws to allow those companies to test the effectiveness of new disclosures. In proposing its policy, the CFPB exercised its authority pursuant to Section 1032(e) of the Dodd-Frank Act, which authorizes the CFPB to approve "trial disclosure programs." Participants would have to share the results of their disclosure testing with the CFPB and would have to self-identify any federal laws or regulations they believe they may have violated, essentially admitting fault. As a result, the program has the potential to expose those market participants who may already be using similar disclosure practices to litigation risk, especially if plaintiffs' attorneys begin using the CFPB's waivers as evidence of a violation of federal consumer financial law. Comments were due February 15, 2013.

For more information, contact Andrew Smith at andrewsmith@mofo.com.

How Has It Been for You?

On December 19, 2012, the CFPB requested public comment regarding the impact of the Credit Card Accountability, Responsibility, and Disclosure Act (CARD) Act, as required by Section 502(a) of that Act. In the announcement, CFPB Director Cordray explained that "the Bureau is seeking to understand how the credit card market is working in practice and how the CARD Act changes have affected consumers and credit card issuers." The information collected will form the basis of a CFPB report to Congress and will be used to "inform future policy decisions" by the CFPB.

Several industry participants, public interest groups, and research organizations responded with comments. Notably, the American Bankers Association provided aggregated industry data that indicated that the CARD Act has increased up-front transparency for consumers but at the price of higher interest rates and a severe reduction in available credit. These sentiments were echoed by several credit unions, which submitted their own letters, and MoFo's own Rick Fischer, who submitted a letter on behalf of several leading credit card issuers and retailers.

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

My, How You've Grown

The CFPB released its second annual report on its workforce development plans, as required by Section 1067 of the Dodd-Frank Act. The report details the CFPB's recruitment and retention plan, training and workforce development plan, and workforce flexibilities plan (e.g., health benefits and telework opportunities). Among the report's highlights was the CFPB's growth—as of November 3, 2012, the CFPB has 1,014 employees, up from 663 a year earlier. About a quarter of these employees transferred in from other banking or financial regulatory agencies.

For more information, contact Leonard Chanin at lchanin@mofo.com.

New Year, New Remittance Proposals

The CFPB published another proposal to amend its remittance transfer rule, required by the Dodd-Frank Act. With its December 2012 proposal, the CFPB sought to address industry criticism about three requirements within the final remittance transfer rule: 1) to provide additional flexibility and guidance on how foreign taxes and recipient institution fees may be disclosed; 2) to relieve providers from having to disclose foreign taxes at the regional, state, provincial, or local level; and 3) to provide that remittance providers would not be strictly liable to return a sender's funds in situations in which the sender provides the incorrect account number and the provider has given notice that the sender could lose the transfer amount due to such a mistake.

For more information, contact Ezra Levine at elevine@mofo.com.

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New Year, New Delays in Remittance Rule Effective Date

On January 22, 2013, the CFPB announced that it would delay yet again the effective date of its remittance transfer rule, which implements amendments made to the Electronic Fund Transfer Act (EFTA) by Section 1073 of the Dodd-Frank Act. The exact date has yet to be announced, but the CFPB has proposed an effective date that would be 90 days from the CFPB's finalizing of its December 31, 2012 proposed amendments to the remittance transfer rule.

For more information, contact Ezra Levine at elevine@mofo.com.

CFPB Finds Strength by Promoting from Within

The CFPB announced that Steven Antonakes was appointed as interim deputy director. Antonakes, who replaces Raj Date until a permanent deputy director is identified, currently serves as Associate Director for Supervision, Enforcement, and Fair Lending and before that as Assistant Director of Large Bank Supervision. He also was Massachusetts Commissioner of Banks from December 2003 until November 2010 and began his career as a bank examiner.

The promotion of Antonakes follows the CFPB's reorganization of its Headquarters supervision staff, which split the group into two sections: Policy and Examinations. The reorganization should provide a new channel for market participants to raise important policy issues within the Bureau. Peggy Twohig will be the Assistant Director of the new Policy Office, and Paul Sanford will be the Acting Assistant Director of the Examinations Office.

The Policy team will ensure that policy decisions for supervision are consistent with both the law and the CFPB's mission and that they are consistent across markets, charters, and regions. The CFPB is organizing this office by product or service market rather than by the type of financial institution. The Examinations team will oversee efforts to train and commission examiners, and ensure policies and procedures are followed. The four regional offices will report to Supervision Examinations.

For more information, contact Andrew Smith at andrewsmith@mofo.com.

College Financial Products 101

The CFPB announced it would request comment on financial services and products—including non-credit products such as bank accounts—offered to college and university students. Specifically, the CFPB has requested comment on how products are marketed through campus affinity relationships, including: what type of information is being provided to students in connection with these financial products; whether the use of products is mandatory to receive loans, scholarships, or other funds; what types of fees are associated with the products; and how often students file complaints about these products. In what may foreshadow a push for CARD Act–level public disclosures for student bank account and debit product agreements, the CFPB also is requesting information about the terms and conditions that colleges and universities agree to with financial institutions as well as information about how much revenue the institutions receive from such agreements. Comments are due March 18, 2013.

For more information, contact Rick Fischer at lfischer@mofo.com or Obrea Poindexter at opoindexter@mofo.com.

Cordray Comments

Richard Cordray took the opportunity of the CFPB's consumer advisory board's first meeting of 2013 to highlight four areas of focus for 2013. Speaking of the first area—combating deceptive and misleading consumer products—Cordray mentioned efforts both to improve consumer understanding, such as through the "Know Before You Owe" campaign, and to correct what he deemed as misleading and inaccurate information, such as the CFPB's recent enforcement actions against various credit card companies. The second area—reducing "debt traps"—brought references to consumers "in a financial jam" and those who believe that such products are their only option. (Cordray, however, failed to mention any other forms of short-term credit that may be available to consumers with less-than-perfect credit or the underbanked.) The third area concerns back-end credit functions, such as debt collection, credit reporting, and loan servicing. There, Cordray noted consumers were harmed by an inability to "vote with their feet," implying that this lack of free-market accountability allows servicers to deny loan modifications "even when a modification would make sense for all concerned." As a fourth area, Cordray noted that the CFPB would continue to work with other agencies such as the DOJ to halt discrimination.

For more information, contact Leonard Chanin at lchanin@mofo.com.

PRIVACY REPORT

President Issues Cybersecurity Order

President Obama issued his long-awaited cybersecurity Executive Order directing the federal government to take various steps to protect the nation's critical infrastructure. At the same time, the President also issued a related presidential policy directive establishing the nation's policy for the protection of critical infrastructure from all types of threats (not just cyberthreats). The Order includes several important principles that were widely supported by the private sector, as in provisions designed to improve the sharing of cyberthreat information between the federal government and the private sector and improvements to the private-sector security clearance

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process. But the Order also creates a regulatory-like process involving the development of cybersecurity standards, and a "voluntary" program to encourage companies to follow these standards.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

Privacy Policy Relief?

On December 12, 2012, the House of Representatives passed a bill (H.R. 5817) that is intended to limit the burden associated with providing annual Gramm-Leach-Bliley Act (GLBA) privacy policies for at least some financial institutions. Specifically, H.R. 5817 would provide that a financial institution is not required to provide its customers with an annual privacy policy if the institution: 1) only shares customer information with nonaffiliated third parties as permitted in the various GLBA exceptions; and 2) has not changed its practices relating to the sharing of customer information since the last time the institution provided its customers with an annual privacy policy. Importantly, the bill that passed the House did not include an earlier provision that would have also required that a financial institution not share information with its affiliates in order to be eligible for the exemption.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

New Telemarketing Rules

Key provisions of the Federal Communications Commission (FCC) telemarketing rule took effect in January, and others are to take effect in October. Effective January 14, 2013, the FCC's rule requires an automated, interactive opt-out mechanism for both prerecorded telemarketing messages and messages delivered to comply with the rule's call abandonment provisions. And, effective October 16, 2013, the FCC's rule will require prior express written consent to deliver: 1) an autodialed or prerecorded telemarketing call to a cell phone and 2) a prerecorded telemarketing message to a residential landline.

For more information, contact Julie O'Neill at joneill@mofo.com.

Who's Viewing Your Data?

In a Statement of Intent for sharing information with state banking and financial services regulators, the CFPB described how it intends to share information with regulators and laid out best practices for the coordination of supervision and information-sharing among the CFPB and state regulators. For example, the Statement indicates the CFPB's intention to provide state regulators with reports of non-bank examinations and consumer complaint information.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

FTC Credit Report Accuracy Study

In December 2012, the Federal Trade Commission (FTC) provided Congress with a report on the accuracy and completeness of consumer credit reports, as required by the Fair Credit Reporting Act (FCRA). The FTC engaged consumers, data furnishers, the nationwide credit reporting agencies, and the Fair Isaac Corporation (FICO), which develops the FICO credit scoring model. Ultimately, the FTC concluded that more than 20 percent of the study participants identified at least one error in their credit reports. Although more than 20 percent of the participants had a modification to their credit reports after the dispute process, only 13 percent experienced a change in their credit score as a result of these modifications.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

Spotlight on Credit Reporting

On December 13, 2012, the CFPB released a report on the credit reporting infrastructure at the largest nationwide consumer reporting agencies. The report describes and provides statistics relating to the processes by which information relating to consumers is furnished to consumer reporting agencies, how that information is matched to consumer files, and how the information is reviewed when consumers dispute its accuracy. Key findings include the fact that the largest consumer reporting agencies maintain credit files relating to over 200 million consumers, based on information received from over 10,000 furnishers who furnish information relating to over 1.3 billion consumer credit accounts each month. The CFPB indicated it prepared the report as a "public service," but note that the CFPB's larger participant rule permits it to supervise companies with annual receipts from "consumer reporting," as defined in the rule, of over $7 million.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

CFPB Warns Specialty CRAs

The CFPB sent letters to several nationwide specialty credit reporting agencies notifying them that the CFPB believes that they are not complying with the FCRA provisions designed to ensure easy consumer access to free annual credit reports and that require a response within 30 days. The CFPB also issued a Bulletin on the same topic. Nationwide specialty credit reporting agencies are defined by the FCRA to include those credit reporting agencies that maintain files relating to medical records or payments, tenant history, check writing history, employment history, and insurance claim history. Want to know more? Read our Client Alert available at http://www.mofo.com/files/Uploads/Images/121130-Nationwide-Specialty-CRAs.pdf.

For more information, contact Richard Fischer at lfischer@mofo.com.

FTC Settles Social Networking Case and Issues Mobile Privacy Recommendations

On February 1, 2013, the FTC announced a potentially groundbreaking settlement with the social networking

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app Path and released an important new staff report on Mobile Privacy Disclosures. The FTC has long encouraged heightened notice and consent prior to the collection and use of sensitive data, such as health and financial information. The settlement, however, requires such notice and consent for the collection and use of information that is not inherently sensitive, but that, from the FTC's perspective at least, might surprise consumers based on the context of the collection. The FTC's staff report reinforces this sentiment by encouraging all the major players in the mobile ecosystem—including app developers, ad networks, and trade associations—to increase the transparency of the mobile ecosystem through clear, accessible disclosures about information collection and sharing at appropriate times.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

Not-So-Friendly Skies: At Least in California

On December 6, 2012, the California Attorney General (AG) announced the first California legal action to enforce the state's Online Privacy Protection Act (OPPA). The complaint alleges that Delta Airlines has maintained a mobile app since 2010 and that the mobile app does not have a privacy policy, which the complaint alleges is a violation of the OPPA. The suit seeks to enjoin Delta from distributing its app without a privacy policy and seeks penalties of up to $2,500 for each violation.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

California AG Mobile App Recommendations

On January 10, 2013, the California AG issued a report providing recommendations for mobile app developers and the mobile industry to safeguard consumer privacy. The AG's report provides guidance on developing strong privacy practices, translating these practices into mobile-friendly policies, and coordinating with mobile industry actors to promote comprehensive transparency. For example, to accommodate the smaller screens of mobile devices, the report recommends the use of special notifications, such as icons or pop-up notifications, to inform consumers about how personally identifiable information is being collected and shared. The recommendations go beyond the presentation and content of privacy policies, including recommendations on limiting data collection and retention.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

China Cares About Data Privacy

Yes, you are reading that correctly. The Standing Committee of the National People's Congress, China's legislature, weighed in on data privacy by issuing the Decision on Reinforcing the Protection of Network Information. For the most part, the decision merely affirms legal obligations already put in place by prior legislation. The most significant aspect of the decision may be that it was issued by China's legislature, signaling the importance being placed on data privacy at the highest level of China's lawmaking system. Also notable, however, are provisions unrelated to data privacy that seek to enhance government control of freedom of communications over the Internet.

For more information, contact Paul McKenzie at pmckenzie@mofo.com.

Watch What You Tweet!

On January 23, 2013, the Federal Financial Institutions Examination Council (FFIEC) requested public comment on proposed guidance for financial institutions relating to their use of social media. The proposed guidance is intended to help financial institutions understand potential risks associated with the use of social media and to communicate the expectations of the agencies that make up the FFIEC for how financial institutions should manage these risks. The proposed guidance largely would focus on identifying potential risks related to a financial institution's use of social media, including a lengthy identification of more than 15 federal laws under which a financial institution may be exposed to compliance and legal risks. Comments on the proposed guidance are due by March 25, 2013.

For more information, contact Nathan Taylor at ndtaylor@mofo.com.

ARBITRATION REPORT

The Supremes Revisit Arbitration

The Supreme Court has agreed to hear Oxford Health Plans' appeal over whether class arbitration is permissible when an underlying contract does not explicitly authorize it. *Oxford Health Plans LLC v. Sutter*, No. 12-135. The Court could resolve an issue left open by its prior decision in *Stolt-Nielsen S.A. v. Animalfeeds Int'l Corp.*, 130 S. Ct. 1758 (2010), in which the majority held that class arbitration was not permitted unless the parties expressed a clear intent to engage in such arbitration. But what happens when a contract contains a broad clause under which "any dispute" between the parties shall be arbitrated, without expressly providing for class arbitration? In *Oxford Health Plans*, the Third Circuit found a contractual basis for class arbitration where the contract contained such a broad arbitration clause without expressly addressing class arbitration. 675 F.3d 215, 217 (3d Cir. 2012). The Third Circuit distinguished *Stolt-Nielsen*, noting that the arbitration clause in *Oxford* was not "silent" regarding class arbitration. *Id.* at 221.

For more information, contact Rebekah Kaufman at rkaufman@mofo.com.

Delegate That!

The named plaintiff in a putative class action against Citibank and Discover that challenges student loan interest disclosures must arbitrate his claims pursuant to the terms of his loan

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agreement. *Kuehn v. Citibank, N.A.*, No. 12 Civ. 3287 (DLC), 2012 U.S. Dist. LEXIS 173346 (S.D.N.Y. Dec. 6, 2012). The agreement contained an arbitration provision that delegated to the arbitrator the threshold question of whether the arbitration agreement itself was enforceable. Though the plaintiff argued that the arbitration agreement was unconscionable, a New York federal judge found that the plaintiff failed to demonstrate that this delegation provision was unenforceable.

For more information, contact Rebekah Kaufman at rkaufman@mofo.com.

Pew Reports

The Pew Charitable Trusts recently released a report on the use of arbitration clauses by banks in checking account agreements. Pew studied the account agreements of the 100 largest retail banks and credit unions by deposit volume and surveyed 603 consumers. The Pew study determined that more than half of the largest institutions have mandatory arbitration clauses in their account agreements, 75 percent of which contain a class action waiver. The study also reports that more than two-thirds of consumers believe they should have a choice between taking their dispute to arbitration and taking it to court. Critics have attacked the survey design as misleading. It presumably is not a coincidence that Pew released its study while the CFPB is conducting its own study of the use of arbitration agreements by banks and other providers of consumer financial products.

For more information, contact Rebekah Kaufman at rkaufman@mofo.com.

PREEMPTION REPORT

Ticket to Federal Court

A Hawaii federal court held that the Hawaii Attorney General's state law challenge to national and state-chartered banks' payment protection programs was completely preempted by the National Bank Act and the Depository Institutions Deregulation and Monetary Control Act of 1980. *Hawaii ex rel. Louie v. JP Morgan Chase & Co.*, No. 12-00263, 2012 U.S. Dist. LEXIS 170440 (D. Haw. Nov. 30, 2012). The court concluded that at least part of the AG's suit focused on the amount of the fees charged for these programs and that these fees constituted interest under the federal statutes. Under established case law, the court reasoned, these theories can only be pursued under federal law, and the court had supplemental jurisdiction over the remaining theories and claims. The court granted the AG's request to file an interlocutory appeal, so stay tuned for further developments.

For more information, contact Jim McCabe at jmccabe@mofo.com or James McGuire at jmcguire@mofo.com.

Debt Cancellation and Collection Duo

The Fourth Circuit rejected Capital One's preemption defense in a case alleging a violation of a state debt cancellation statute requiring that any debt cancellation agreement had to provide for cancellation of the remaining loan balance upon occurrence of a triggering event. *DeCohen v. Capital One, N.A.*, 703 F.3d 216 (4th Cir. 2012). The court found the National Bank Act (NBA) and Office of the Comptroller of the Currency (OCC) regulations providing debt cancellation contracts entered into by national banks were governed by federal law did not apply in this case because Capital One had purchased the underlying loan from a local lender. The court further found conflict preemption did not apply because state law did not treat national banks differently than other lenders and because it was not "physically impossible to comply with both laws." *Id.* at 225.

A North Carolina district court held a state debt collection statute was not preempted by the NBA and OCC regulations. *Sacco v. Bank of America, N.A.*, No. 5:12-cv-00006, 2012 U.S. Dist. LEXIS 178030 (W.D.N.C. Dec. 17, 2012). The court started by joining the small number of courts that have ignored the Dodd-Frank Act provision indicating it applies only to contracts entered into after the effective date and instead found the preemption provisions in the Act apply retroactively. The court concluded that state laws prohibiting abusive debt collection practices did not prohibit or significantly impair the national bank from collecting debts.

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

Payment Posting Preemption

The Ninth Circuit reversed a $203 million judgment against Wells Fargo based on its high-to-low payment posting practices, finding plaintiff's claims based on violation of state law are preempted by the NBA and OCC regulations. *Gutierrez v. Wells Fargo Bank, N.A.*, 704 F.3d 712 (9th Cir. 2012). The court reasoned that state law, in this case the "good faith" requirement in the California Commercial Code, cannot dictate a national bank's payment posting practices, which constitute pricing decisions authorized by federal law. The court deferred to an OCC interpretive letter finding payment posting practices are pricing decisions authorized by OCC regulations. However, the court further found that claims based on alleged misleading statements were not preempted, and remanded the case for a determination of what relief, if any, is appropriate as to those claims.

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

MORTGAGE REPORT

Magner Redux

Hot on the heels of the last-minute settlement of *Magner v. Gallagher*, which was engineered to avoid Supreme Court review, the Supreme Court appears poised to take up another case testing

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whether the Fair Housing Act (FHA) allows disparate impact claims. In *Mount Holly Gardens Citizens in Action, Inc. v. Township of Mt. Holly*, 658 F.3d 375 (3d Cir. 2011), plaintiffs contended a redevelopment plan violates the FHA because it has a disparate impact on minority residents. The district court granted summary judgment in favor of the defendant, the Township of Mount Holly, but the Third Circuit reversed and remanded. The Township petitioned the Supreme Court for review. The Township correctly points out that the Supreme Court recently held that provisions of the Age Discrimination Employment Act (ADEA) and Title VII, which contain language nearly identical to the FHA, address *intentional* discrimination only, not disparate impacts. In October, the Supreme Court asked the Solicitor General to express its views on whether the Court should take up *Mount Holly*.

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

Aggressive New Fair Housing Rule

Meanwhile, the U.S. Department of Housing and Urban Development (HUD) is charging ahead with disparate impact cases and recently issued its much-debated disparate impact rule. Under the rule, defendants may be held liable under the FHA for practices that have a "discriminatory effect" unless the defendant can provide a legally sufficient justification for the practice. HUD says that the rule—which it plans to apply retroactively—is simply a codification of its existing positions. But, as we recently reported, the new rule goes well beyond that. For example, it requires defendants to "prove" that a challenged practice is "necessary" to achieve a "substantial, legitimate nondiscriminatory interest"—a standard the courts have affirmatively rejected. It is unclear why HUD waited so long to issue the new rule, when it issued the proposed rule in November of 2011, and the CFPB announced plans in April 2012 to apply disparate impact under ECOA and Regulation B, but the timing in relation to the Mount Holly cert. petition, discussed above, seems awfully coincidental.

For more information, contact Michael Agoglia at magoglia@mofo.com or Thomas Noto at tnoto@mofo.com.

CFPB Sets Its Sights on Fair Lending

The CFPB also is ramping up its fair lending enforcement. It followed its bullish 2012 year-end report, discussed in our Winter Newsletter, with an announcement that it is joining forces with the Department of Justice (DOJ) to share information and prosecute fair lending actions. The CFPB and DOJ memorandum of understanding (MOU) supplements the existing agreement between the DOJ, HUD, and FTC, focusing on information-sharing and the possibility of "joint investigations." The MOU is part of a broader set of recent DOJ and CFPB initiatives and announcements that warn of increasingly aggressive fair lending enforcement, including a recent settlement press release that touted plans for more "aggressive, coordinated and proactive" prosecutions in 2013.

For more information, contact Michael Agoglia at magoglia@mofo.com or Thomas Noto at tnoto@mofo.com.

CFPB: It's Raining Rules

In January, the CFPB issued a deluge of new mortgage rules implementing Dodd-Frank. Here's a summary of three of the rules with the most immediate impact on the financial services industry.

1. **Ability to Repay (ATR):** At first blush, the ATR Rules may seem straightforward—mortgage lenders must assess borrowers' ability to repay the loans they apply for, using a list of traditional factors like income, assets, and credit history. And there is a compliance safe harbor for Qualified Mortgages (QMs). QMs are regularly amortizing loans, underwritten to standard rules and assumptions that carry no more than a prescribed number of points and fees. Certain QMs may not exceed a 43 percent debt-to-income ratio. But, as we reported here in January, the devil is in the details, and there are a *lot* of details in the 800-plus-page ATR Rules. They include the new Regulation Z Appendix Q, which may set a record for complexity, regulatory pitfalls, and real-world impracticality.

2. **Mortgage Servicing:** CFPB says these rules will "put the service back in mortgage servicing." We don't know about that premise, but we do know that the new 1,800-page rules will require careful work to implement this year. The rules amend Regulations Z (TILA) and X (RESPA) to cover nine major topics: (1-3) enhanced borrower notices; (4) limitations on force placed insurance; (5) resolving errors and responding to borrower requests; (6) early intervention with delinquent borrowers; (7) "continuity" of personnel working with delinquent borrowers; (8) loss mitigation, including a prohibition on the initiation of the foreclosure process until a loan has been more than 120 days delinquent; and (9) creating internal policies and procedures to implement the rules. The complete rules are available here.

3. **Higher-Cost Loans:** Dodd-Frank extended the Home Ownership and Equity Protection Act (HOEPA) to cover higher-cost home purchase loans and home equity lines of credit, in addition to the home equity lending and refinances it currently covers. The new rule implements those changes. It generally bans (1) balloon payments, (2) monthly late fees that exceed 4 percent of the borrower's regular payment, (3) pre-payment penalties, and (4) charging fees for loan modifications, and (5) limits fees related to payoff statement requests.

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4. **And plenty more...** Other new CFPB rules address appraisals, escrow accounts, and compensation and qualifications for loan originators. They're all announced here.

Implementation: In February, perhaps realizing the enormity of what it had done in January, the CFPB pledged to undertake a number of efforts to "support rule implementation." It says it will publish "plain-language" and "readiness" guides and "official interpretations" of its rules, coordinate with other agencies that examine lenders, and, of course, undertake a "broad-reaching consumer education campaign." The vast majority of the new rules are scheduled to take effect in January 2014, though certain rules become effective in June 2013. We'll continue to monitor, but for now it's safe to say that the rules present a number of compliance challenges and could strongly influence what types of mortgage products will be offered in the future.

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Final Rule on Appraisals for Higher-Priced Mortgage Loans

The federal financial regulatory agencies issued a final rule establishing new appraisal requirements for "higher-priced mortgage loans," which implements amendments to TILA made by Dodd-Frank. The rule also requires a second appraisal for homes acquired by the seller for a lower price during the prior six months. If the price difference is above certain thresholds, creditors will have to obtain a second appraisal at no cost to the consumer. The rule exempts certain types of loans, including qualified mortgages, temporary bridge loans, and construction loans. The rule becomes effective on January 18, 2014. Still to come—a supplemental proposal to request additional comment on possible exemptions for "streamlined" refinance programs and small dollar loans.

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National Foreclosure Settlement Scrapped; Banks to Pay $9 Billion Instead

The OCC and Fed gave up on implementing their April 2011 consent decree with thirteen of the country's largest lenders over alleged loan servicing errors. The original consent orders required independent foreclosure reviews, involving file-by-file review of millions of individual borrower files. Of no surprise to those who work in the industry, the government was forced to conclude that individual file review and remediation simply isn't feasible for most of these lenders. Under the newly modified consent orders, banks will instead pay $3.6 billion directly to borrowers and devote $5.7 billion to other borrower assistance. For their part, three servicers are sticking with their original consent orders.

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Rubber About to Meet the Road in HAMP Class Actions

The Fifth, Sixth, and Eighth Circuits, and numerous district courts, have rejected loan modification claims based on oral promises and other alleged misrepresentations. And as we've reported, the Fourth, Fifth, and Eleventh Circuits have already held that Home Affordable Modification Program (HAMP) Trial Payment Plans (TPP) themselves do not promise permanent modifications. A similar appeal is pending in the Ninth Circuit. The Seventh Circuit bucked the trend, allowing claims based on a TPP to proceed because the servicer, by countersigning and returning the TPP, certified that the borrower was qualified for a permanent modification. Meanwhile, the HAMP cases that have survived dismissal are working their way through the district courts. Class certification briefing in the consolidated loan modification MDLs pending in the Central District of California and the District of Massachusetts is scheduled to be filed this spring.

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

Debt Collection FDCPA Circuit Split Widens

The Sixth Circuit weighed in on a circuit split over whether foreclosures are "debt collection" under the Fair Debt Collection Practices Act (FDCPA). It held that mortgage foreclosure actions *do* constitute debt collection under the FDCPA. *Glazer v. Chase Home Fin. LLC*, 704 F.3d 453 (6th Cir. 2013). The Sixth Circuit expanded on Third and Fourth Circuit authority and rejected contrary authority from the Ninth and Eleventh Circuits and a majority of district courts. The practical effect of the ruling on lenders and servicers is limited, though. It applies only to those who acquired the loan or servicing rights *after* the loan was in default in accordance with the plain language of the FDCPA.

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Dukes Continues to Doom Class Certification in Discriminatory Lending Suits

District courts across the country are applying *Dukes* to reject motions to certify classes of borrowers who claim that mortgage lenders disproportionately denied loan applications or provided less advantageous terms. The Sixth Circuit considered one of these cases, affirming the district court's denial of class certification. *In re: Countrywide Fin. Corp. Mortg. Lending Practices Litig.*, ___ F.3d ___, No. 12-5250, 2013 WL 149853 (6th Cir. Jan. 15, 2013). Plaintiffs attempted to rely on a law professor's regression analysis of nearly 3 million borrowers' data to conclude that, on average, "minorities paid more for Countrywide mortgage

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loans than whites with similar risk-characteristics." *Id.* at *__. The Sixth Circuit rejected this approach, finding plaintiffs had failed to establish either a uniform policy or practice, or a common mode as required by *Dukes*.

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Quieting Querulous QWRs

The Ninth Circuit joined the Seventh Circuit in limiting the definition of "qualified written requests" (QWRs) under RESPA. In *Medrano v. Flagstar Bank*, No. 11-55412, 2012 U.S. App. LEXIS 25274 (9th Cir. Dec. 11, 2012), the court held that borrower letters challenging monthly mortgage payments were not QWRs and therefore did not trigger the servicer's duty to respond. Following the Seventh Circuit's decision in *Catalan v. GMAC Mortgage Corp.*, 629 F.3d 676 (7th Cir. 2011), the Ninth Circuit held that RESPA limits QWRs to requests that: 1) reasonably identify the borrower's name and account; 2) state the borrower's reasons for believing that the account is in error or provide adequate detail about other information sought; and 3) seek information about the servicing of the loan. Because the plaintiffs' letters did not seek information about the servicing of the loan, but rather challenged the loan's terms, the Ninth Circuit concluded their letters were not QWRs.

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This newsletter addresses recent financial services developments. Because of its generality, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations.

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