VOLUME No. 2

FEBRUARY 2024

LUSE GORMAN

THE BANKERS' BULLETIN

Regulatory & Enforcement Insights on Recent Bank Industry Developments

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About The Firm

Luse Gorman, PC is a Washington, D.C.-based law firm specializing in mergers, capital raising transactions, regulatory, enforcement, corporate, securities, employee benefits, executive compensation, and tax law for regional and community banks across the United States. Our attorneys have served with the major federal banking and securities agencies, and regularly engage with regulators on a range of novel and complex legal issues.

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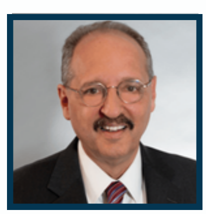

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CFPB Proposes Multiple Rules Aimed at Overdraft and Other Fees

Summary. On Jan. 17, the CFPB proposed a rule to subject overdraft lending services to Regs E and Z and limit financial institutions from charging "excessive" overdraft fees. On Jan. 24, the CFPB proposed a rule to prohibit institutions from charging NSF fees on instantly declined transactions.

Takeaways.

- Labeling overdrafts "loans," the Overdraft Rule proposes to set regulatory limits on the amount of overdraft fees that can be charged. Exceeding the cap would force banks to comply with various regulatory obligations related to periodic statements, disclosures, underwriting, and advertising.
- The Overdraft Rule would initially apply to banks with $10B+ in assets, but the Bureau stated it plans to "monitor" the market response and determine whether banks with less assets should later be covered.
- The NSF Rule is unusual in that its a preemptive effort to ban transaction fees the CFPB believes *may* become more prevalent with technological advancements. The regulation deems NSF fees on covered transactions as "abusive" and bars them for all institutions, regardless of asset size.

Bottom Line. The twin proposals reflect Director Chopra's most direct *regulatory* efforts to wage the Biden Admin.'s battle against so-called "junk fees." By using rules rather than supervisory pressure or one-off enforcement actions, more institutions will be exposed to potential violations if they maintain current fee practices. This may portend a more aggressive push on the "abusive" standard.

The FRB and NYDFS Penalize Unauthorized Disclosures of CSI

Summary. On Jan. 11, the FRB permanently barred from banking a state member bank employee for misappropriating confidential supervisory information (CSI). On Jan. 19, the FRB issued a CSI-based consent order (CO) and a $2.4MM civil money penalty against ICBC and its New York branch. NYDFS issued its own order and a $30MM civil money penalty, based partly on a CSI disclosure violation.

Takeaways.

- The FRB demonstrated its view that unauthorized disclosure of CSI warrants the most severe personal enforcement action, a prohibition. The action highlighted that the individual defendant, a former CFO, was aware of the FRB's regulations restricting the availability of CSI.
- The CO against ICBC noted aggravating factors, including a lack of formal policies, procedures, training, or controls regarding proper handling of CSI, and highlighted that disclosure occurred *after* the FRB instructed a prior waiver was necessary. These factors prompted the severe action.
- The CO requires building out a CSI framework and designating a CSI officer with expertise.

Bottom Line. Regulators can and will impose severe penalties for unauthorized CSI disclosures. Policies and procedures around handling CSI are a necessity. Banks and individuals with CSI access should adopt a very conservative approach to disclosure and seek prior approval from the agencies.

The Bank Agencies Update Rules Governing Their Administrative Hearings

Summary. On Dec. 28, the OCC, FRB, FDIC, and NCUA (FBAs) issued a final rule updating the regulations governing their administrative enforcement processes. The changes modernize a framework that has largely been static since the late 1990s. The rule becomes effective on April 1, 2024, but the old regulations will still apply to proceedings initiated before that date.

Takeaways.

- The rule both standardizes certain processes across FBAs and updates each FBA's own "local" regs. The FRB added regulations governing its pre-hearing, formal investigations for the first time, and the OCC's will now more completely shield its investigational materials from access.
- The rule prohibits respondents from obtaining documents covered by the bank examination or deliberative process privileges during administrative discovery. By codifying these privileges, respondents will have less flexibility to uncover details behind FBA decision making.
- Recognizing changes to modern practice, the new rules permit depositions to be taken by remote means, which will significantly reduce costs and burden for respondents defending actions.

Bottom Line. The updates to incorporate new technology are long overdue. But the investigational and administrative processes still occur on the FBAs home turf, and defendants play by their rules.

OCC Acting Comptroller Outlines Thoughts on Managing Liquidity Risk

Summary. On Jan. 18, the acting Comptroller of the Currency, Michael J. Hsu, delivered remarks on bank liquidity risk at Columbia Law School, providing a window into his thinking for how future risks in this area should be addressed in the wake of the regional bank failures in the spring of 2023.

Takeaways.

- Hsu emphasized the preemptive categorization of deposits, and utilizing outflow stress tests, as a way to identify which groups of deposits may leave a bank en masse and the resulting effects. Key to the categorization is correctly identifying which deposits should be considered high risk.
- Hsu also advised banks to keep their operational procedures primed for emergency borrowing, especially from the Fed, so that they aren't exercising these muscles for the first time in a crisis. He floated the concept of regulatory backing to remove Fed discount window borrowing stigma.
- Hsu also expressed support for new regulations governing liquidity, which would add to the avalanche of proposed regulations that will impact banks in all areas of operation by next year.

Bottom Line. In both public statements and in the examination process, liquidity has emerged as a hot area of examiner focus. Banks are seeing the agencies more quickly address deficient liquidity practices through MRAs, informal, and formal actions, reinforcing the agencies' renewed focus.

Senators Introduce the FAIR Exams Act to Create Independent Appeals Process

Summary. On Dec. 14, Senators Moran (R-Kan.) and Manchin (D-WV) introduced the bipartisan Fair Audits and Inspections for Regulators' (FAIR) Exams Act in the Senate Banking Committee. If passed, the bill would make several important changes to the supervisory process at the federal banking agencies (FBAs) and introduce a new mechanism to appeal within each agency.

Takeaways.

- The bill would address a longstanding complaint regarding the timing of when banks receive final exam reports by requiring the FBAs to provide them no later than 60 days after an exit interview, unless the bank sent the FBAs new information. Exit interview timing is prescribed to occur 9 months after an exam starts, unless the FBAs extend the period in writing.
- The bill would establish an Office of Independent Examination Review within the FFIEC to hear appeals of FBA "material supervisory determinations." Banks would be able to request information the FBAs relied on. The FFIEC could hear appeals or refer matters to an ALJ.
- In all likelihood, this process would practically supplant the Ombudsman appeals process found within each agency, which banks traditionally have been hesitant to utilize for various reasons.

Bottom Line. Elements could be tacked onto larger bipartisan bills, like appropriations. But, Congressional interest could spur FBA action even without passage, building on post-SVB changes.

Other Developments That You May Have Missed . . .

- **FTC Issues Combatting Auto Retail Scams (CARS) Rule.** On Dec. 12, the FTC issued the CARS Rule governing the sale, financing, and leasing of motor vehicles by covered dealers. The FTC rejected inclusion of a safe harbor for contract assignees—*i.e.*, third-party finance companies, such as banks—that could have limited downstream liability for Rule violations to those apparent on the face of contracts. This exposure reinforces the need for indirect auto lenders to monitor dealer conduct and comply with TPRM principles.

- **CSBS Files Brief in Preemption Case.** On Dec. 15, the Conference of State Bank Supervisors (CSBS) filed an amicus brief in the pending Supreme Court case on the legal standard for preemption, *Cantero v. Bank of America.* CSBS argued that state laws should not be preempted for national banks, and asserted that national banks should not escape the reach of state consumer protection laws. A narrowing of the existing standard could significantly affect national bank powers, and the brief may influence the Court's decision.

- **Fiserv Applies for Limited Purpose Bank Charter.** On Jan. 12, it was reported that Fiserv had applied for a Merchant Acquirer Limited Purpose Bank charter in Georgia. A successful application by such a dominant player in the payments space could encourage others to apply, and reignite the debate over special purpose charters and BHCA loopholes that have subsided in recent months.

- **NYDFS Issues Guidance on D&O Selections.** On Jan. 22, the NYDFS issued guidance to state-chartered banks setting expectations for rigorous vetting of directors and senior officers at onboarding and on an ongoing basis. NYDFS also expects a robust framework be erected around the vetting process. The framework should designate red flags requiring enhanced vetting and be consistently updated. NYDFS will review these policies and procedures as part of its safety and soundness exams to ensure consistency with the guidance.