Bank Regulatory News and Trends

Executive order on promoting competition includes banking and consumer finance provisions

BANK REGULATORY NEWS AND TRENDS

23 July 2021

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This regular publication from DLA Piper focuses on helping banking and financial services clients navigate the ever-changing federal regulatory landscape.

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Executive order on promoting competition includes banking and consumer finance provisions. President Biden on July 9 signed a sweeping Executive Order on Promoting Competition in the American Economy. The presidential action – which aims to promote competition and limit corporate consolidation to protect consumers, workers and smaller companies – includes proposals relating to the banking and consumer finance sector. While the executive order does not necessarily constitute a strict mandate, it provides a sense of direction for agencies to adopt policies to achieve the president's stated goals.

- The Biden Administration said it wants to make it easier and cheaper for people to switch banks. An accompanying fact sheet from the White House states that the president "encourages the Consumer Financial Protection Bureau (CFPB) to issue rules allowing customers to download their banking data and take it with them" from bank to bank.
- The executive order also encourages the Justice Department and the federal bank regulatory agencies "to update guidelines on banking mergers to provide more robust scrutiny of mergers." According to the White House fact sheet: "Over the past two decades, the United States has lost 70% of the banks it once had, with around 10,000 bank closures." Banks considering seeking approval of transactions under the Bank Merger Act or the Change in Bank Control Act should expect stricter scrutiny of reduced competition or other community impacts that may result from the transaction.

Federal legislation repeals OCC "true lender" rule. President Biden on June 30 signed into law legislation to overturn a rule governing partnerships between banks and third-party lenders commonly known as the "true lender rule." As we advised in the May 13, 2021 edition of *Bank Regulatory News and Trends*, the rule, enacted by the Office of the Comptroller of the Currency (OCC) last October, confirmed when a national bank or federal savings association makes a loan and is considered the true lender in the context of a partnership between a bank and a third party, such as a marketplace lender. Congressional Democrats spearheaded the repeal with a resolution under the Congressional Review Act, arguing that the rule helped payday lenders issue predatory loans. The legislation passed in the Senate in May and the House last month on largely party-line votes.

OCC wins appeal against NYDFS on national fintech charters. A federal appeals court ruling could give the go-ahead for the Office of the Comptroller of the Currency to issue federal bank charters to financial institutions that do not take deposits. In a June 3 decision, the Court of Appeals for the Second Circuit overturned the 2019 judgment of the US District Court for the Southern District of New York in *Lacewell v. Office of the Comptroller of the Currency*. Ruling on procedural grounds, the Second Circuit reversed the District Court's decision enjoining the OCC from issuing special purpose national bank charters to non-depository firms. The appeals court did not rule on the merits of the challenge to OCC's fintech charter brought by the New York State Department of Financial Services and its superintendent Linda Lacewell. Rather than taking a position on whether the "business of banking" under the National Bank Act requires the acceptance of deposits as a condition of eligibility for an OCC charter, the Second Circuit dismissed the case without prejudice after deciding that the NYDFS lacked standing and its claims were not constitutionally ripe. Because no fintech has yet applied for a special purpose national bank charter, no state law or regulation has been pre-empted, and the Second Circuit determined NYDFS's claims were not ripe. "At least until a non-depository fintech that DFS currently regulates—or would otherwise regulate—decides to apply for an [special purpose national bank] charter, this alleged assessment loss will remain purely 'conjectural or hypothetical,' rather than 'imminent' as the Constitution requires," the June 3 decision states.

- As we have been regularly advising in *Bank Regulatory News and Trends*, since the OCC's 2018 announcement that it would begin accepting applications from fintechs for the special charters, state banking regulators – including the Conference of State Bank Supervisors as well as NYDFS – have been challenging the OCC on jurisdictional grounds in federal courts. On June 15, Judge Dabney L. Friedrich of the US District Court for the District of Columbia approved a motion by the CSBS describing its agreement with the OCC to pause for 90 days litigation over a special purpose charter application.
- We expect the legal controversies between state regulators and the OCC over the fintech charters to continue, pending either Congressional action or ultimate resolution by the US Supreme Court.

Agencies commit to joint action on CRA overhaul. The Office of the Comptroller of the Currency, the Federal Reserve and the Federal Deposit Insurance Corporation signaled their intention to pursue a unified approach to update regulations governing the 1977 Community Reinvestment Act designed to encourage commercial banks and savings associations to help meet the needs of borrowers in all segments of their communities, including low- and moderate-income neighborhoods. In a July 20 interagency statement, the agencies said they "are committed to working together to jointly strengthen and modernize regulations implementing the Community Reinvestment Act (CRA)." As we advised in the January 14, 2020 edition of *Bank Regulatory News and Trends*, the OCC and the FDIC announced a proposal to revamp the regulatory framework governing implementation of the anti-redlining statute. But the Fed, which shares jurisdiction over CRA enforcement with the OCC and the FDIC, did not join the other two agencies. Instead, as noted in the October 2, 2020 edition, the Fed issued a request for comment seeking a "consistent approach" for the agencies to modernize the CRA regs. Under former Director Joseph Otting, the OCC published its final CRA rule last year without the participation of the FDIC and in the face of opposition from Congressional Democrats, community organizations and many banks. A coalition of major banking organizations in May of this year issued a Request to Formally Withdraw or Delay the June 2020 CRA Rule. Acting Comptroller of the Currency Michael Hsu indicated that he would issue a proposal formally rescinding OCC's CRA rule, having previously advised banks they did not need to prepare for it to take effect.

Regulators propose guidelines for partnerships between banks and fintechs or other third-party relationships. Three federal bank regulatory agencies have proposed guidance that would clarify how banks can partner with fintechs and other financial services providers. The proposed guidance would replace each agency's existing, separate guidance and create a uniform approach. The Proposed Interagency Guidance on Third-Party Relationships: Risk Management was jointly announced on July 13 by the Fed, the FDIC and the OCC. According to a June 25 memo prepared by Fed staff, the proposed guidance is based on the OCC's existing third-party risk management guidance from 2013. "The proposed guidance recognizes differences in the nature, level of risk, and complexity of banking organizations and their third-party relationships," the memo states. The new proposal provides a framework based on sound risk management and describes third-party relationships as business arrangements between a banking organization and another entity, by contract or otherwise. Banks would be required to develop plans outlining their strategies for partnering and working with third parties, identifying risk, negotiating contracts, conducting ongoing monitoring and due diligence, and developing contingency plans for terminating relationships. Comments must be received no later than September 17, 2021.

Mark Calabria out as FHFA director after Supreme Court ruling on agency structure. Hours after the US Supreme Court ruled that the Federal Housing Finance Agency was structured unconstitutionally and that the president has the right to remove its director, the Biden Administration replaced FHFA Director Mark Calabria with Acting Director Sandra Thompson. In a unanimous June 23 decision, the high court ruled that the structure of the mortgage agency that oversees Fannie Mae, Freddie Mac and the Federal Home Loan Bank system violated separation of powers principles. Writing for the court, Justice Samuel Alito said that, as the justices found in a similar case last year regarding the Consumer Financial Protection Bureau, "the Constitution prohibits even 'modest restrictions' on the President's power to remove the head of an agency with a single top officer." "There is a widespread lack of affordable housing and access to credit, especially in communities of color," Thompson said in the June 23 announcement of her appointment. "It is FHFA's duty through our regulated entities to ensure that all Americans have equal access to safe, decent, and affordable housing." In a separate statement issued the same day, Calabria said he respected the Supreme Court decision and wished his successor well.

- In a key early policy action under its new leadership, FHFA announced on July 16 that, effective August 1, Fannie and Freddie will no longer impose a 50 basis point fee on lenders when they deliver refinanced mortgages. The decision marks a reversal from Calabria's decision last September to require Fannie and Freddie to start charging the temporary fee as a way to cover projected losses arising from the COVID-19 pandemic. "Eliminating the Adverse Market Refinance Fee will help families take advantage of the low-rate environment to save more money," Thompson said.

Regulators push banks to transition away from LIBOR by year's end. At its June 11 meeting, the Financial Stability Oversight Council urged banks to stop using the London Interbank Offered Rate (LIBOR) on new transactions by the end of 2021 – and warned that many firms are not moving in a timely manner to transition to the new benchmark, the Secured Overnight Financing Rate. According to a Treasury Department readout, the FSOC "also received an update from the Federal Reserve Board on the importance of accelerating the financial sector's transition from LIBOR and using reference rates for derivatives and capital markets products that have sufficient underlying volumes compared to contracts referencing the rate." Fed Vice Chair for Supervision Randal Quarles emphasized there is "no path forward" for LIBOR, which is being phased out after banks were fined for manipulating it, and that firms have no reason to delay moving derivatives and other market contracts to the Fed's preferred replacement, the SOFR. Quarles also warned banks that the use of USD LIBOR quotes available after December 2021 is appropriate only for legacy contracts, and using them for new products would create safety and soundness risks.

- The message was echoed by other senior officials, including Treasury Secretary Janet Yellen, Fed Chair Jerome Powell and Securities and Exchange Commissioner Gary Gensler.
  - Yellen said SOFR would "provide a robust rate suitable for use in most products and with underlying transaction volumes that are unmatched by other LIBOR alternatives." Yellen also questioned the use of alternative rates where the volume of derivatives contracts could outnumber the transaction volume underlying the reference rate.
  - Gensler expressed concern that a number of commercial banks have shown interest in the use of the Bloomberg Short-Term Bank Yield Index (BSBY) as a potential replacement for LIBOR, warning that BSBY could be vulnerable to the same type of manipulative conduct LIBOR fell victim to.

- The FSOC was created under Dodd-Frank to identify risks to US financial stability, promote market discipline and respond to emerging risks. The council is chaired by the Treasury Secretary and includes the major federal financial regulatory agencies, such as the Fed, FDIC, OCC and SEC.

Fed to end temporary COVID-19-era restrictions on dividends and share repurchases following latest stress tests. The Federal Reserve on June 24 released the results of its annual bank stress tests, which showed that large banks continue to have strong capital levels and could continue lending to households and businesses during a severe recession. As a result, temporary restrictions on dividends and share repurchases for firms with over $100 billion in total assets imposed during the height of the COVID-19 pandemic will end. The Fed determined that banks subjected to the Fed's economic crisis simulation exercise remained well above their risk-based minimum capital requirements. With this, going forward, the banks will be subject to the normal restrictions of the Fed's stress capital buffer framework, which was finalized last year. The Fed explained that this year's hypothetical scenario included a severe global recession with substantial stress in commercial real estate and corporate debt markets, unemployment rising to over 10 percent, GDP falling 4 percent from the fourth quarter of 2020 through the third quarter of 2022 and asset prices declining sharply, with a 55 percent drop in equity prices. "Over the past year, the Federal Reserve has run three stress tests with several different hypothetical recessions and all have confirmed that the banking system is strongly positioned to support the ongoing recovery," said Quarles.

BPI calls for fintechs processing payments to undergo examinations like those faced by traditional banks. The Bank Policy Institute is making the case that fintech firms that gain access to the Federal Reserve's payment rails should undergo supervision in a "substantially equivalent way as the federal banking agencies examine insured banks" by the chartering agency or the Federal Reserve. The BPI on June 14 issued a report titled *Fed Account Access for Nonbanks: An Analysis of the Policy Implications and Potential Risks to the U.S. Financial System*. In it, the influential financial services advocacy organization says that, as the Fed considers providing accounts to companies that do not take government-insured deposits but obtain nontraditional bank charters, many of the top priorities for bank examiners remain relevant. The report draws a distinction between regulation, focused primarily on limiting risk-taking and imposing capital and liquidity requirements, and examination, with its particular emphasis on anti-money laundering and terrorist financing, adherence to US sanctions and cybersecurity and other operational risks. BPI states that, "For an uninsured bank (particularly one that takes no deposits), where taxpayers are not at risk and there is no moral hazard, there clearly is diminished need for such regulation." But, with the threat that bad actors could finance illegal activity or otherwise disrupt the payments system through banks with nontraditional charters, "there appears no case to be made for examining an uninsured bank or FinTech processing payments any differently from an insured bank processing payments."

- As noted in the May 13, 2021 edition of *Bank Regulatory News and Trends*, the Fed has issued and requested comment on *Proposed Guidelines for Evaluating Account and Services Requests* within the digital money transfer infrastructure. While the proposed guidelines do not use the term "fintech" per se, the Fed references the recent "introduction of new financial products and delivery mechanisms for traditional banking services, notably leveraging emerging technologies, including from institutions with novel types of banking charters designed to support such innovation." BPI praised the Fed for taking "an important first step in proposing a set of the standards that must be met before an institution is permitted to open a master account or access Reserve Bank services," but warns that "the Reserve Banks should not compromise on those standards."

CFPB announces transition from foreclosure moratoriums, adopts temporary safeguards for borrowers. The

Consumer Financial Protection Bureau announced that it will not extend the current emergency foreclosure moratoriums that various federal agencies established beyond the current July 31 expiration date. Instead, the CFPB on June 28 finalized a new rule, Protections for Borrowers Affected by the COVID-19 Emergency Under the Real Estate Settlement Procedures Act (RESPA), Regulation X. The rule amends federal mortgage servicing regulations and goes into effect on August 31 to “help protect mortgage borrowers from unwelcome surprises as they exit forbearance,” the CFPB said. According to an executive summary, the new rule addresses the servicing of mortgage loans set forth in both Regulation X and Regulation Z (the Truth in Lending Act). The rule provides for early intervention with delinquent borrowers and imposes certain loss mitigation requirements, including setting procedures for reviewing loss mitigation applications and providing borrower protections during those reviews. It also includes temporary provisions to ensure that a borrower has a meaningful opportunity to apply for loss mitigation before the mortgage account is referred to foreclosure after the current moratoriums have ended and provide servicers the ability to offer borrowers certain COVID-19-related streamlined loan modifications without a complete loss mitigation application. Additional information must be provided promptly after early intervention live contacts are established with delinquent borrowers, and new requirements for when servicers must renew reasonable diligence efforts to obtain complete loss mitigation applications from certain borrowers would be established. There will be a temporary period through the end of the year when a loan servicer must make sure that at least one of the three procedural safeguards is met before referring certain 120-day delinquent accounts for foreclosure:

- The borrower was evaluated based on a complete loss mitigation application and existing foreclosure protection conditions are met
- The property is abandoned
- The borrower is unresponsive to servicer outreach

Many of the current forbearance programs were set up by the Coronavirus Aid, Relief, and Economic Security Act last year and apply to federally backed loans. Some private lenders and servicers also set up their own forbearance programs. The CFPB’s proposed rule would cover all homeowners’ primary residences, including those with mortgages through private lenders.

- Approximately 2 million homeowners are still in some type of mortgage forbearance amid the health and financial fallout brought on by the pandemic, according to the latest survey by the Mortgage Bankers Association (MBA), published June 22.

New digital assets working group at House Financial Services. Representative Maxine Waters (D-CA), chair of the House Financial Services Committee, has announced that she has organized a Digital Assets Working Group of Democratic committee members. Waters made the announcement at the June 15 hearing of the committee’s Task Force on Financial Technology titled “Digitizing the Dollar: Investigating the Technological Infrastructure, Privacy, and Financial Inclusion Implications of Central Bank Digital Currencies.” The working group will meet with experts and government officials with the goal of developing legislation and policy solutions on cryptocurrency regulation, the use of blockchain and distributed ledger technology, and the possible development of a US Central Bank Digital Currency. “As cryptocurrencies, central bank digital currencies and other digital assets enter the mainstream, the Committee will look at how digital assets have begun to enter many aspects of our lives – from payments to investments to remittances – and consider how to devise legislation to support responsible innovation that protects consumers and investors while promoting greater financial inclusion,” Waters said.

- In a related development, the FDIC recently issued a Request for Information and Comment on Digital Assets to receive stakeholder “input on current and potential digital asset use cases involving IDIs [insured depository institutions] and their affiliates.”

Banking Committee Republicans oppose Biden CFPB nominee. All 12 of the Republican members of the Senate Banking Committee have all but declared their intention to oppose the nomination of Rohit Chopra as director of the Consumer Financial Protection Bureau. In a July 13 letter to Chopra, currently a commissioner at the Federal Trade Commission, the committee Republicans faulted the nominee for failing to respond to a series of questions based on reports claiming that the Biden Administration is removing senior career officials at the CFPB in an effort to replace Trump Administration appointees with its own preferred appointees, potentially violating civil service protections. “Your refusal to answer basic questions about whether you were privy to the troubling and possibly unlawful actions described in the press is unacceptable from a federal nominee and in our view should disqualify you from consideration as CFPB Director,” the senators wrote.

Delaware adds cryptocurrency to law on unclaimed property. Governor John Carney of Delaware on June 30 signed into law Senate Bill 103 that adds "virtual currency" to the definition of "property" subject to the reporting and remitting requirements of Delaware's 2016 Revised Uniform Unclaimed Property Act. Effective August 1, virtual currency is presumed abandoned five years after the owner's last indication of interest in property. At that point, the holder of the abandoned virtual currency must report it to Delaware as unclaimed property. Within 90 days prior to filing the report, the holder of the virtual currency must liquidate the virtual currency and remit the proceeds. The owner of the virtual currency has no recourse against the Delaware Escheator to recover gains in value that would have been realized had the virtual currency not been liquidated.

- "Virtual currency" is defined as "an electronic medium of exchange that, unlike real money, is not controlled or backed by a central government or central bank" and includes crypto-currencies such as Bitcoin, Ripple, Litecoin, Peercoin and Dogecoin, according to an advisory from the Delaware Attorney General's Investor Protection Unit. Under Delaware law, the definition of virtual currency explicitly excludes "game-related digital content," which is defined as "digital content that exists only in an electronic game or electronic-game platform." It includes game-play currency, such as a virtual wallet, but "does not include an item that the issuer permits to be redeemed for use outside a game or platform for money or goods or services that have more than minimal value or otherwise monetizes for use outside of a game or platform."

NYDFS issues ransomware guidance for its regulated entities. The New York State Department of Financial Services on June 30 announced new guidance addressing ransomware attacks and highlighting cybersecurity measures to significantly reduce the risk of an attack. The guidance comes amid increasing ransomware attacks and builds on NYDFS's April guidance on cybersecurity and supply chain risks. NYDFS urged its regulated entities to prepare for a ransomware attack by implementing measures such as:

- Training employees in cybersecurity awareness and anti-phishing
- Implementing a vulnerability and patch management program
- Using multi-factor authentication and strong passwords
- Employing privileged access management to safeguard credentials for privileged accounts
- Using monitoring and response to detect and contain intruders
- Segregating and testing backups to ensure that critical systems can be restored in the face of an attack and
- Having a ransomware-specific incident response plan that is tested by senior leadership.

For a more detailed discussion of the NYDFS guidance, please see this July 7 DLA Piper publication, *Ransomware preparedness: NYDFS announces additional expectations of regulated entities' cybersecurity programs*.

California DFPI opens transition period for companies holding California Financing Law license not currently licensed through NMLS; transition requests should be submitted by December 31, 2021. The California Department of Financial Protection and Innovation (DFPI) has opened the period for companies currently holding a California Financing Law (CFL) license not currently licensed through the Nationwide Multistate Licensing System (NMLS) to submit a license transition request through NMLS. While regulations requiring all CFL licensees to be on NMLS by December 31, 2021 are not yet effective and transitioning at this time is voluntary, regulations are expected to be final later in 2021. All existing CFL licensees should submit their transition requests by filing a Company Form (MU1) and an Individual Form (MU2) for each control person by December 31, 2021. The DFPI recently posted its CFL Transition Checklist and CFL Transition FAQs, as well as the NMLS' own instructions for transitioning an existing state license over to the NMLS platform, to assist existing licensees in the process. All new applicants for a California Financing Law license are now expected to use NMLS to submit applications.

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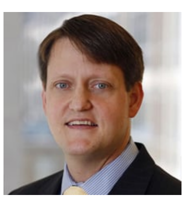

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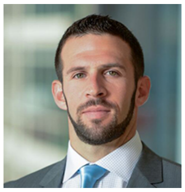

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