Consumer Financial Services Committee Winter Meeting
January 12-13, 2009
Scottsdale, Arizona

CLE PROGRAM: Focus On Mortgage Lending - How Did We Get Here?
J. Douglas Cuthbertson, Miles & Stockbridge P.C.

Presented by: Subcommittee on Young Lawyers
Co-Chairs: Suzanne R. Haley, Franzén & Salzano, P.C.,
Norcross, GA and Emily G. Miller, Hudson Cook, LLP, Hanover,
MD
Speakers: Thomas M. Hanson, Dykema Gossett, PLLC, Ann
Arbor, MI; Lynette I. Hotchkiss, Hudson Cook, LLP, Hanover,
MD; Jed Mayk, Blank Rome LLP, Philadelphia, PA

Long-time committee members provided background information on topics that were covered in scheduled program meetings, including the history of mortgage lending and the new Reg Z/UDAP amendments, and participated in an informal Q&A.

History of Mortgage Lending

Mr. Hanson discussed the "History of the Mortgage, or, "How Did We Wind Up In This Mess?"

Beginning with the first "mortgages" in medieval England, Mr. Hanson traced the growth of mortgages in the United States. He described the first federal regulation of mortgages, the creation of the secondary mortgage market, the impact of the civil rights movement on the mortgage industry, and the recent mortgage boom and subprime meltdown.

Before 1932, homes generally were bought for cash in the United States, he said. Only limited short-term financing was available to a small segment of the market.

During the Great Depression, the federal government began regulating the industry with the creation of the Federal Home Loan Bank Board, the Home Owners Loan Act and the National Housing Act, which established the Federal Housing Administration ("FHA").

The secondary market was created in 1937, when Congress established Fannie Mae. Freddie Mac was created in 1970, and "mortgage-backed securities," collateralized mortgage obligations (CMOs) and other investment vehicles were developed in the early 1980s.

Salomon Brothers and First Boston created the first CMOs in 1983, he said. CMOs offered outstanding credit protection and risk management because of credit tranching and because the most senior bonds were the last to absorb losses.

Paraphrasing Lewis Ranieri of Salomon Brothers, inventor of the mortgage-backed securities market in the 1970s, Mr. Hanson said that "Mortgages are math. All you have to do is figure out how to crunch the numbers, and you can make money."

Throughout the 1960s and 1970s, the civil rights movement
affected the mortgage industry. Title VI of the Civil Rights Act, the Fair Housing Act, the Equal Credit Opportunity Act, the Home Mortgage Disclosure Act and the Community Reinvestment Act prohibited discrimination in mortgage lending practices.

The subprime boom of the 1990s was fed by the growth of the CMO market, Mr. Hanson said. Subprime origination grew by more than 3700%, from $35 billion in 1994 to $1.3 trillion by 2007, accounting for 1 in 3 mortgages.

This growth outstripped regulation and led to greater mortgage fraud and abuse, he said. From 2000 to 2003, Associates Finance/Citigroup, First Alliance Mortgage, Household and Fairbanks agreed to multimillion dollar settlements stemming from abusive lending practices. Many states reacted by passing predatory lending laws.

Mr. Hanson also gave a thumbnail sketch of the subprime mortgage meltdown.

"That's mortgages from the year 1190 to today in 35 minutes," he said.

**Nontraditional Mortgage Loans**

Lynette Hotchkiss discussed the advent of "higher-priced mortgages" and the market conditions that led to their creation.

She said that former Federal Reserve Board (FRB) Chairman Alan Greenspan expressed concern in September 2005 that exceptionally low mortgage interest rates were resulting in a froth of homebuilding and home turnover, causing home prices in some areas to rise to unsustainable levels.

Greenspan expressed concern about the dramatic increase in exotic mortgage products. He said these products "are seen as vehicles that enable marginally qualified, highly leveraged borrowers to purchase homes at inflated prices. In the event of widespread cooling in house prices, these borrowers, and the institutions that service them, could be exposed to significant losses."

According to a September 2006 report by the Government Accountability Office, from 2003 through 2005, alternative mortgage products grew from less than 10% to about 30% of residential mortgage originations.

Ms. Hotchkiss said that on October 4, 2006, the federal agencies—the FRB, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, Office of Thrift Administration, and National Credit Union Administration—issued a final *Interagency Guidance on Nontraditional Mortgage Products*. The Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators issued guidance to state regulators mirroring the agency's guidance.

The final guidance called for: (1) increased vigilance in underwriting standards; (2) appropriate portfolio and risk management practices; and (3) providing consumers with clear information about the risks and benefits of nontraditional mortgage products.

Ms. Hotchkiss also discussed the FRB's amendments to Regulation Z (Truth in Lending) and Regulation C (Home Mortgage Disclosure), proposed on July 8, 2008. The final amendments to Regulation Z prohibit certain acts and practices in connection with
closed-end mortgage loans, particularly higher-priced mortgage loans. They also revise the disclosure requirements for mortgage advertisements and revise the timing requirements for providing disclosures for closed-end mortgages. The proposed amendments to Regulation C would make rules for reporting higher-priced loans consistent with the Regulation Z amendments.

Regulation Z

Jed Mayk discussed some of the new amendments to Regulation Z and the changes imposed by the Housing and Economic Recovery Act of 2008 ("HERA").

Last summer, the FRB finalized significant amendments to Regulation Z, Mr. Mayk said. Most provisions of the amendments are effective on October 1, 2009. On the same day that the amendments to Regulation Z were published in the Federal Register, President Bush signed the HERA.

Mr. Mayk gave an overview of several of the significant Regulation Z amendments. He also discussed HERA’s amendments to the Truth in Lending Act ("TILA"), which caused the FRB to propose additional changes to Regulation Z.

Mr. Mayk discussed the new timing rules for the delivery of disclosures for closed-end mortgage loans and additional HERA-required disclosures; new requirements for "higher-priced" mortgage loans; rules relating to appraisal coercion and certain servicing practices; and amendments to Regulation Z's advertising rules for both closed-end and open-end mortgage loans.

CLE PROGRAM: Overview and Practical Considerations in Implementation of Final Regulation Z/UDAP Regulations

J. Douglas Cuthbertson, Miles & Stockbridge P.C.

Presented by: Subcommittee on Truth in Lending; Subcommittee on Internet Delivery/Electronic Banking and Subcommittee on Compliance Management

Chair: Jacqueline Parker, PayPal, San Jose, CA
Co-Vice Chairs: Catherine M. Brennan, Hudson Cook, LLP, Hanover, MD and Jeffrey P. Naimon, Buckley Kolar LLP, Washington, DC

Chair: Roberta G. Torian, Advanta Bank, Wilmington, DE
Vice Chair: Russell Schrader, Visa, Inc., San Francisco, CA
Chair: Joanne K. Sundheim, JP Morgan Chase & Co., Wilmington, DE

Co-Vice Chairs: Agnes Bundy Scanlan, Goodwin Procter LLP, Boston, MA and Ducie Le, Capital One, McLean, VA

Speakers: Karl Bergeson, Citigroup, New York, NY; Leonard Chanin, Federal Reserve Board, Washington, DC; Gail Hillebrand, Consumers Union of U.S., Inc., San Francisco, CA; Oliver I. Ireland, Morrison & Foerster, LLP, Washington, DC; Ducie Le, Capital One, McLean, VA

In May 2008, the Federal Reserve Board (FRB) proposed the most substantial overhaul of disclosure rules and restrictions on lender practices in decades. These rules amending the Board’s Regulations AA (Federal Trade Commission Act - Unfair or
Deceptive Acts or Practices) and Z (Truth in Lending) were both a response to Congressional action, public concern, and an effort to restrict certain lending and disclosure practices.

The panel discussed the final rules that were released at the end of 2008, examined the likely impact of the rules on consumers and financial institutions, and shared practical steps to implement operational changes necessary to comply with the new rules. Mandatory compliance with the rule is July 1, 2010.

Mr. Ireland summarized the proposed amendments to Regulation AA (UDAP Proposal).

**Reasonable Time to Make Payments**

Mr. Ireland and Mr. Chanin discussed the "reasonable amount of time requirement" in the UDAP Proposal.

They said the amendments would prohibit credit card issuers from treating payments as late for any purpose, eg., increasing the APR or imposing a fee, unless the consumer has been given a "reasonable amount of time" to make a payment. The amendments do not define what is a "reasonable amount of time" but provide a safe harbor for credit card issuers that mail or deliver statements at least 21 days before the payment due date.

**Payment Allocation**

Mr. Ireland also discussed the amendments regarding allocation of payments.

He said the UDAP Proposal would require credit card issuers to allocate payments in excess of the minimum payment among different balances in one of the following ways: (1) apply the excess payment to the balances in descending order of the balances' APRs first; (2) apply equal portions of the excess payment to each balance; and (3) apply the excess payment pro rata on the amounts of the balances.

A credit card issuer may use another payment allocation method as long as it results in the assessment of the same or a lesser amount of interest charges as would be assessed under one of these three methods, he said.

The minimum payment could be allocated at the discretion of the credit card issuer, subject to appropriate disclosure, he said.

For discounted promotional rate balances, i.e., balance transfers, payments could be allocated to any promotional rate balance or deferred interest balance only after other non-promotional balances have been fully paid, except that the entire amount of excess payments may be allocated to deferred interest balances in the last two billing cycles before the expiration of the deferred interest period, he said.

Mr. Ireland also said that the UDAP Proposal would prohibit credit card issuers from requiring consumers to repay any promotional rate balances or deferred interest balances in order to take full advantage of any grace period offered on other balances that would otherwise apply.

**Increased Interest Rates on Outstanding Balances**

The UDAP Proposal would prohibit credit card issuers from increasing the APR on an outstanding balance, subject to limited exceptions. "Outstanding balance" means the amount owed at the
end of the 14th day after the credit card issuer provides notice of the change. The exceptions include:

1. increases due to variable rates which are the operation of an index that is publicly available and not under the credit card issuer's control;
2. increases due to the expiration of a promotional rate;
3. increases due to the consumer's failure to make the minimum payment within 30 days after the due date; and
4. increases due to a default by the consumer under a workout plan.

Mr. Chanin said these provisions are the most controversial, and present the most complicated issues for both consumers and financial institutions.

**Double-Cycle Billing**

To address complaints about double-cycle billing, the UDAP Proposal would prohibit credit card issuers from imposing finance charges for balances on days in prior billing cycles, Mr. Ireland said.

He said this prohibition would be subject to two exceptions: (1) assessment of deferred interest; and (2) adjusting finance charges after resolving a billing error dispute, under sections 226.12(b) or 226.12(13) of Regulation Z.

**Deposits for Account Opening**

The UDAP Proposal also would prohibit credit card issuers from financing security deposits or fees for issuance or availability of credit if those deposits or fees, in the aggregate, constitute the majority of the available credit on the account during the first year, Mr. Ireland said.

The panel also discussed the highlights of the proposed amendments to Regulation Z.

Ms. Hillebrand said the features of the UDAP Proposal are transparency in pricing and product design. No one benefits from increased costs of completed transactions, she said.

However, she said there is unfinished business with respect to the effective date of the amendments. She believed that 18 months is a long time for consumers to wait for the Rule's mandatory effective date.

Ms. Le discussed compliance with the amendments. She said Capital One engages in consumer testing and tries to be transparent. She said Capital One's letter of August 4, 2008 to the agencies about the UDAP Proposal addresses Ms. Hillebrand's concerns.

Ms. Bergeson discussed implementation of operational changes necessary to comply with the UDAP Proposal. She mentioned that the FRB has said that financial institutions will be required to change their business models. She said every consumer communication will change. Financial institutions will need to have senior management review all business models and will need as much guidance as they can get to comply with the new rules, she said.
CLE PROGRAM: Implementation of Affiliate Sharing Rule and Red Flag Rule

J. Douglas Cuthbertson, Miles & Stockbridge P.C.

Presented by: Subcommittee on Privacy
Chair: Patricia E.M. Covington, Hudson Cook, LLP, Hanover, MD
Vice Chair: Obrea Poindexter, Morrison & Foerster LLP; Washington, DC
Speakers: Anne Fortney, Hudson Cook, LLP, Washington, DC; Peter Gilbert, Capital One, McLean, VA; David Stein, Federal Reserve Board, Washington, DC; Rebecca Kuehn, Federal Trade Commission, Washington, DC

Though the compliance deadlines for complying with the Affiliate Marketing Rule and Red Flag Rules have come and gone, there continue to be questions surrounding what is required to comply. The panel discussed issues and questions that have arisen in connection with compliance with these new rules, and the federal agencies’ interpretations of the requirements.

Red Flag Rules

Mr. Stein discussed coverage under the Red Flag Rules. The questions that need to be asked to determine whether an entity is covered by the rules are: (1) is the entity a "financial institution" or a "creditor" and (2) does the entity offer a "covered account," as those terms are defined in the rules, he said. Not every financial institution has to have a program.

Ms. Fortney mentioned that hospitals, universities and utilities, as well as traditional creditors, may be included within the definition of "creditor." Essentially, any entity that provides a product or service for which the consumer pays after delivery is covered. These are issues that have surprised everyone, she said.

If an account is a "covered account," the creditor has to develop a written red flag program, she said.

Ms. Covington asked whether retailers, as agents for creditors (eg., private label credit cards), are covered by the rules. Ms. Fortney said this issue is unresolved.

Third-party debt collectors may also be covered, depending on what they do, Ms. Kuehn said. If they renegotiate debt and set terms of credit, then they are covered. If they just send out notices and accept payment, they are not, she said.

Ms. Kuehn said that the Red Flag Rules also apply to municipalities, and the FTC has jurisdiction to enforce compliance.

Mr. Gilbert discussed the establishment of identity theft prevention programs. He said the definition of identity theft is broad, and some types of fraud are not identity theft. Capital One has reviewed every type of its accounts to see if there is a reasonable possibility of identity theft, he said. In developing the program, a creditor’s actual experience is important.

The most difficult area in developing a program is business purpose loans, Mr. Gilbert said. Small business loans and accounts are covered, and large business accounts probably are
not, but there is a lot of gray area in the middle, he said.

There is an ongoing requirement to update the program periodically, and Capital One does an annual assessment of its program, he said.

Mr. Stein said that when determining whether prepaid products are covered accounts, a creditor must go through the analysis to see whether the accounts fall within the definition in the rules. Gift cards are not covered, but payroll card accounts are covered, he said. Between these two types of accounts, there is a broad spectrum of prepaid products. Issuers will have to do an analysis on a case-by-case basis, and many products will be covered accounts, he said.

Ms. Kuehn said that there is overlap between data security laws, eg., Gramm-Leach-Bliley, and the Red Flag Rules. Creditors don't have to start from scratch but can look at existing data security programs and see which parts apply to reducing identity theft, she said.

Financial institutions and creditors may use automated systems, but the rules do not require any specific technology, Mr. Stein said. And an automated solution may only satisfy some obligations of the rule, he said. If all consumer contact is online, then an automated solution may be adequate. But if a creditor has walk-in consumers, its program will require "low tech" solutions, such as checking IDs.

The requirements for administration of the program are flexible, but there are particular requirements, Mr. Gilbert said. Oversight by the board of directors is required, as is oversight of service providers, he said.

The rules require a risk-based approach to vendor oversight, because the definition of "service provider" in the rules is broad, said Ms. Fortney. A creditor must exercise effective control over its service providers, and this is an ongoing process which requires assessment of whether the service providers have access to customers' account records. The rules do not provide much guidance as to what constitutes effective oversight, she said.

The relevant service providers are those that are doing what a financial institution would do that would be covered by the rules, eg., application intake, Mr. Stein said. In that instance, only the service provider could do an ID check.

The address discrepancy rule applies to the three national credit reporting agencies, Ms. Fortney said. It requires certain address verification and confirmation by users of consumer reports that receive a "notice of address discrepancy" from a credit reporting agency.

The receipt of such a notice requires action by the user of the consumer report, she said. Mr. Gilbert added that the costs of verification and confirmation are borne by the user.

**Affiliate Marketing Rule**

The panel also discussed the Affiliate Marketing Rule.

The rule specifically defines "eligibility information," said Mr. Gilbert. But practically, any information that an affiliate would want to share will be considered "eligibility information," he said.
The rule defines "solicitation" as "the marketing of a product or service initiated by an affiliate to a consumer that is based on eligibility information from its affiliate and intended to encourage the consumer to purchase or attain a product or service."

The rule does not prohibit "constructive sharing" of eligibility information between a person and its affiliate for use in marketing consumers when the affiliate has a pre-existing business relationship with the consumer, as long as the rule's restrictions on the use of eligibility information are met.

**PROGRAM: What Can We Learn, What Should We Learn, and What Have We Learned From the Seismic Shift in the Financial Market?**

*J. Douglas Cuthbertson, Miles & Stockbridge P.C.*

**Moderator:** Therese G. Franzén, Franzén & Salzano, P.C., Norcross, GA  
**Speakers:** Kathleen Keest, Center for Responsible Lending, Durham, NC; Eldon Spencer, Leonard O'Brien Spencer Gale and Sayre, Ltd., Minneapolis, MN; Oliver I. Ireland, Morrison & Foerster, LLP, Washington, DC

Many factors have contributed to the financial meltdown. Has a lack of accountability (at least until now) been compounded by inadequate legal accountability? Did our concept of the role of lawyers shape our contribution to the crisis? In this program, the panel engaged in a lively discussion of these issues.

Most people trace the beginning of the current financial meltdown to October 2007. But it is probably traceable to the Gramm-Leach-Bliley Act in 1999, which repealed portions of the Glass-Steagall Act separating investment and commercial banking, Mr. Ireland said. As a result, portions of the consumer financial services industry were placed outside of the federal regulatory safety net, he said.

The panel did not focus on lawyers' roles in shaping policy issues. Rather, it focused on the lawyer's role in advising clients on a transactional compliance basis at the retail level.

Mr. Ireland said that clients need advice on legal compliance, but they also need practical advice. Lawyers could have advised their clients on underwriting issues, such as no documentation loans, stated income loans and loan-to-value issues, he said. One of the ways lawyers could have helped more was to help clients focus on the risks associated with these underwriting issues, not just whether they were in compliance with the law, he said.

Mr. Spencer commented that lawyers sometimes view their representation from the perspective of whether a particular transaction was successful or not. But he said that there is also the larger perspective that short-term gains sometimes outweigh long-term gains. That perspective may have been missing from mortgage brokers up to investors, he said.

He also said that some of the rush to action on the part of Congress will undermine lawyers, eg., by promulgating vague or inappropriate standards regarding the suitability of a particular loan for a particular consumer.
On a practical level, Mr. Spencer said that when serving as local counsel to a national bank, attorneys need to exercise discretion when counseling their clients. The bank may have a checklist of 40 things that it would like to see in its loan documentation, eg, a waiver of jury trial. But if there are too many anti-consumer provisions in the documentation, the judge likely will get irritated when the bank moves for summary judgment, he said.

Attorneys also need to counsel their clients to have their standards (eg, loan closing disclosures) written down and systematically enforced, he said.

Ms. Keest said the overall trend over the past couple of years of deregulation has negatively impacted the ability of lawyers to challenge certain practices. The asymmetric allocation of legal resources to consumer financial services entities, as opposed to consumers, also has been a problem, she said.

Fee-shifting provisions, class actions and public enforcement were intended to level the playing field by making attorneys available to consumers, she said. But over the past 30 years, these mechanisms have been made less effective by the courts and by political rhetoric, she said.

Ms. Keest also discussed the role of a lawyer as a counselor/adjutor. Quoting Elihu Root, she said "About half the practice of a decent lawyer consists in telling would-be clients that they are damned fools and should stop."

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**PROGRAM: Deposit Products and Payment Systems Subcommittee Presentation**

*Lauren Campisi, McGlinchey Stafford PLLC*

**Speakers:** Ryan S. Stinneford, Pierce Atwood LLP and Laura H. Brown, McGlinchey Stafford PLLC

At the Winter Meeting, Ryan S. Stinneford and Laura H. Brown, co-chairs of the Deposit Products and Payment Systems Subcommittee, provided a "hot topics" presentation that focused on three legislative and regulatory reactions to the recent events in the banking and financial world: (1) new insurance coverage issues for deposit and stored value products; (2) new rules to restrict internet gambling; and (3) new requirements and restrictions for overdraft protection products.

**FDIC Coverage Changes**

Mr. Stinneford highlighted the recent changes to federal deposit insurance coverage amounts and requirements. The first change involves a temporary increase in the Standard Maximum Deposit Insurance Amount ("SMDIA") from $100,000 to $250,000. The change became effective on October 3, 2008 and sunsets on December 31, 2009. In connection with this change, the FDIC issued the following language for customer-facing communications:

On October 3, 2008, FDIC deposit insurance temporarily increased from $100,000 to $250,000 per depositor through
On October 14, 2008, the SMDIA on non-interest bearing accounts was also temporarily increased through the Temporary Liquidity Guarantee Program ("Liquidity Program"). As of that date, all balances on non-interest bearing transaction accounts are fully insured, without regard to the SMDIA cap and without charge to the depository institution until November 12, 2008. Non-interest bearing accounts include Interest on Lawyers Trust Accounts ("IOLTAs") and Negotiable Order of Withdrawal ("NOW") accounts with interest rates less than or equal to 0.50%.

Unless a depository institution opted-out of the Liquidity Program by December 5, 2008, the institution will remain enrolled until December 31, 2009 and will be charged a special assessment equal to 10-basis points on deposit amounts over $250,000 in non-interest bearing accounts, including IOLTA and NOW accounts. The special assessment is retroactive to November 13, 2008.

The Liquidity Program also affects the treatment of sweep programs and retail repurchase agreements. The Liquidity Program relies on FDIC rules regarding failed institutions to determine whether funds are in a non-interest bearing account. Generally, the FDIC will treat the funds as being in the account to which they are swept or transferred. However, funds transferred from a non-interest bearing transaction account to a non-interest bearing savings product will be treated as being in the non-interest bearing transaction account and will be eligible for full coverage under the Liquidity Program.

Effective December 19, 2008, two types of disclosures are required: (1) lobby notices regarding participation in the Liquidity Program if the institution offers non-interest bearing transaction accounts; and (2) notices to sweep and reclassification customers. The FDIC has provided model language only for the first type of notice. In November 2008, the FDIC provided supplemental information regarding disclosures of non-conventional situations. The only example given was official checks dawn on another depository institution.

On September 30, 2008, the FDIC issued an Interim Final Rule, which simplifies the coverage requirements for revocable trust accounts. The new rule removes the prior requirement that the beneficiary of the trust be the spouse, child, grandchild, parent or sibling of the account owner. Now, the beneficiary may be any natural person, charity or non-profit. The new rule also simplifies the coverage calculation if the beneficial interests are unequal. If the account is less than or equal to $500,000, coverage is determined by multiplying the number of beneficiaries by the SMDIA. Otherwise, coverage is the greater of $500,000 or the sum of all beneficial interests in the account (capped at the SMDIA per beneficiary). The new rule also provides coverage for each life estate interest in a revocable trust up to the SMDIA. Finally, the new rule keeps the coverage calculation for a revocable living trust even if the account becomes irrevocable due to the death of the account owner.

On October 10, 2008, deposit insurance coverage on mortgage servicer accounts was also simplified. Under the new rule, which is permanent and became effective immediately, coverage is provided to lenders and investors as a collective group based on the cumulative amount of principal and interest payments in the account by each borrower, up to the SMDIA. Insurance coverage is not aggregated with other accounts held by the borrowers(s) at
the institution holding the mortgage servicer accounts. The new rule only affects the coverage calculation for principal and interest payments held by mortgage servicers. It does not change the rules for tax and insurance amounts held by a servicer in escrow, which are insured on a pass-through basis as the funds of the borrower.

In July 2008, the FDIC adopted an Interim Rule for determining deposit balances at failed institutions, which became effective on August 18, 2008. The Interim Rule establishes the following practices: (1) the FDIC will treat deposits in accordance with their underlying obligations based on the end-of-day ledger balance for the account, taking into account the bank's normal posting and cutoff procedures; (2) as a receiver, the FDIC will attempt to stop inbound and outbound transfers or new liabilities or the extinguishing of existing liabilities for the institution; and (3) the FDIC will establish a cutoff point as to which time these transfers will be stopped, irrespective of the bank's normal cutoff point.

Calculation of account balances is also subject to the following provisions: (1) adjustment to account balances for uncollectible items; (2) sweeps of funds to internal non-deposit investment accounts that are scheduled to take place for the end-of-day balance calculation will be processed only if they occur before the FDIC cutoff point.

On July 17, 2008, the FDIC adopted a Final Rule that provides new requirements for certain large depository institutions to modernize the insurance claims process and make it easier for the FDIC to calculate deposit insurance coverage quickly, and provide depositors faster access to their funds after a large bank failure.

**Stored Value Cards**

On November 13, 2008, the FDIC issued a new version of General Counsel Opinion No. 8, which replaces the prior version issues in 1996. Effective immediately, the new General Counsel Opinion No. 8 declares all funds underlying stored-value products, including gift cards, payroll cards, prepaid cards and governmental benefit cards, and other non-traditional access mechanisms to be "deposits" under the FDIA if the funds are placed with an insured depository institution. Accordingly, depository institutions will be assessed insurance premiums on such fund balances. As Mr. Stinneford noted, however, General Counsel Opinion No. 8 raises new issues regarding the application of Regulations D, E, CC and DD, for example.

**Internet Gambling**

The second "hot topic" involved the Unlawful Internet Gambling Enforcement Act of 2006 (the "Act"). Ms. Brown explained that the Federal Reserve Board ("FRB") and Department of Treasury (collectively "Agencies") jointly adopted identical regulations implementing the Act. Compliance with the new regulations becomes mandatory on December 1, 2009. Ms. Brown explained that the scope and effect of the new regulations are minimal. State and federal law continue to determine what is illegal, the new regulations simply place new "policing" duties on banks and financial institutions.

Specifically, the Act prohibits banks from knowingly processing "restricted transactions," meaning payments related to another person's participation in unlawful internet gambling. "Restricted transactions" may include: (1) credit extended to person engaged in unlawful internet gambling (including credit card transactions);
(2) an EFT transmitted by/through money transmitting business; and (3) a check drawn by/on behalf of person engaged in unlawful internet gambling. However, "restricted transactions" only involve funds going to commercial customers. Pursuant to the Act, the Agencies identified the following Designated Payment Systems ("DPS"): (1) ACH systems; (2) card systems (credit, debit, prepaid cards or stored value products); (3) check collection systems; (4) money transmitting businesses that permit customers to remotely initiate money transmission transactions; and (5) wire transfer systems. The new regulations exempt all participants in DPS except for those with a customer relationship with a commercial customer.

The new regulations require non-exempt DPS participants to create policies and procedures that are reasonably designed to identify and block restricted transactions. Non-exempt participants also must notify all commercial customers that restricted transactions are prohibited from being processed. The new regulations also require due diligence procedures that vary depending on the risk level of the customer.

**Overdraft Protection**

The last "hot topic" involved new requirements and restrictions for overdraft protection products. In May 2008, the FRB proposed to amend Regulations AA and DD to condition a bank's ability to charge a fee for overdraft services on providing the consumer with notice and right to opt-out of overdraft service. On December 18, 2008, the Fed issued final changes to Regulation DD, including periodic and year-to-date aggregate fee disclosure requirements and balance disclosure rules. However, after considering comments and results of consumer testing, the FRB concluded that overdraft service opt-out rules should be located in Regulation E. Accordingly, the FRB published another proposed rule under Regulation E.

Under the proposed rule, the FRB proposed two alternatives regarding overdraft services. The first alternative involves an "opt-out" process through which the consumer must receive notice of right to opt-out of overdraft service for ATM withdrawals and one-time debit card transactions before a bank charges an overdraft fee. This opt-out notice would be required at account opening and for each periodic statement cycle in which the consumer pays an overdraft fee. The opt-out process would not apply to: (1) checks; (2) preauthorized EFTs; or (3) ACH transactions. Under the opt-out alternative, the bank must provide notice and wait 30 days before assessing an overdraft fee when paying an ATM withdrawal or one-time debit card transaction and provide notice before or at account opening and require consumer to make an opt-out decision as a necessary step to opening an account. The opt-out notices would not be required if: (1) the institution has a policy of declining to pay ATM/debit card transactions if its believes the consumer has insufficient funds; or (2) the institution requires the consumer to opt-in before assessing any fees for paying ATM/debit card overdrafts. The second alternative involves an "opt-in" process by which the consumer must opt-in to an overdraft service for ATM withdrawals and one-time debit card transactions before a bank can charge an overdraft fee. The opt-in must be written, and the institution could send the consumer written confirmation of the opt-in.