Self-Reporting to Regulators: Responsible Conduct or Needless Risk?

American Bar Association Spring Meeting 2019
Vancouver, Canada

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So You’ve Found a Problem ...

- Financial institutions find problems in numerous ways, from monitoring their own operations to conducting compliance reviews, to analyzing complaints.
- When you find a problem, there is always a judgment call to be made about what to do about it.
- This judgment call depends on the facts and circumstances of each issue, as well as what will be done to resolve the issue.
Step 1: Fix the Problem

- When we find a problem, the first priority, and a step we will almost always take, is to fix the problem going forward.

- Failing to do this, after discovering the problem, puts the institution at maximum risk from a regulator, because the continuation of the problem can be fairly characterized as intentional if a decision is made not to resolve it.

- Consider how “noisy” the process of fixing the problem will be. Will it generate lots of documentation internally, or can it be resolved without that? (the answer will play into our self-reporting decision later on).

- Also consider whether additional monitoring should be put into place to make sure the “fix” is working.

- Guiding principle: the go-forward fix should be credible to a regulator examining it later.
Step 2: Consider Restitution

- After devising a plan to fix the problem going forward, we need to consider whether we should do anything to resolve the effects of the problem in the past
- Some problems, and even some clear violations of law, do not have any financial impact on consumers, and so restitution may not be necessary
- Others do have a financial impact, and if they do, restitution is likely needed
- Also consider non-financial remedial measures (e.g., correcting credit reporting)
- Our restitution decision should also be made in a way that will appear credible to a regulator later – *even if we don’t self-report*
- Whether restitution is required will also play a role in our self-reporting decision
Restitution Risk – Individual and Class Actions

- May preclude actions for actual damages for violations of federal law
  - Could leave open claims for statutory damages and punitive damages as well as costs and attorney fees
  - Ideal result would be if restitution could be structured to take advantage of available statutory defenses, such as correction of errors (full – TILA and EFTA; limited – ECOA and HMDA)

- Possible to foster actions for violations of related state laws
  - Could preclude UDAP actions where plaintiff must have suffered monetary damages or an ascertainable loss in order to sue
  - May or may not otherwise limit recoveries of actual damages but likely to leave open claims for statutory damages and punitive damages as well as costs and attorney fees
Step 3: Consider Self-Reporting

- Now that we’ve found and fixed the problem, do we tell our regulators?

- The answer depends on the circumstances of each issue, but the primary consideration is whether the regulator is likely to discover the issue absent self-reporting

- Several factors weigh into this analysis:
  - Regularity of examinations
  - Presence of consumer complaints
  - Public disclosure of problem through restitution efforts, or correction of credit reporting
  - Existence of private litigation on the issue
Why is Likelihood of Discovery Important?

• Self-reporting presents a very complex risk-benefit calculation
• The primary risk is reporting an issue the regulator did not know about, and would not discover otherwise: an institution could find itself with a consent order over an issue that the regulator would otherwise not have found
• A number of public consent orders have arisen from self-reported violations, so benefit of self-reporting may be limited (and uncertain)
• On the other hand, if the regulator is likely to discover the issue, failing to self-report it impacts the institution’s credibility with the regulator, and may trigger more vigorous punitive action
Self-reporting: The Complete Package

• Assuming self-reporting is made, how do we do it?

• Under any circumstances, self-reporting should be accompanied by a thorough and credible action/remediation plan (see steps 1 and 2 above)

• The self-report should be completely honest and should not hold back any key facts

• It should also be thorough, showing a consideration of all pertinent factors with respect to the cause of the problem and the solution adopted

• The institution’s credibility is at stake in this conversation – so act accordingly!

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Self-reporting: To How Many Regulators?

- If we self-report to one federal regulator, what about others federal or state agencies?
- Regulators may share information and coordinate
- Violation of state law versus federal law
- Likelihood of discovery may be very different as between different regulators
Other Regulators (continued)

- Notification or other reporting obligations impacted by self-reporting
  - State reporting obligations may be triggered
  - Nationwide Mortgage Licensing System disclosure requirements
  - Disclosure requirements from previous consent orders
- Federal or other approvals may be impacted
  - FHA-approved mortgagees - reporting and recertification requirements
  - Ineligibility Criteria: (i) subject to unresolved findings in a governmental investigation or review; (ii) engaged in business practices that do not conform to generally accepted practices of prudent mortgagees or that demonstrate irresponsibility
  - “Unresolved findings” - broadly defined; considered “unresolved” until an action is taken or the investigating entity formally determines that no action is warranted
Thank You

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