Banking Update

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Court Overturns Regulation II Interchange & Routing Requirements

On July 31, 2013, the United States District Court for the District of Columbia issued an opinion granting summary judgment in a suit between various trade associations in the retail industry as well as some merchants (collectively referred to herein as "Plaintiffs") and the Board of Governors of the Federal Reserve System (the "Board").[1] The suit was brought by Plaintiffs to overturn the Board's Final Rule (designated as Regulation II) setting standards for debit card interchange and transaction fees ("Interchange Fees") and network exclusivity prohibitions pursuant to the "Durbin Amendment" to the Dodd–Frank Wall Street Reform and Consumer Protection Act. Plaintiffs and the Board made cross-motions for summary judgment and the court granted Plaintiffs' motion for the reasons set forth below.

II. Summary of Holding

A. Interchange Fees

Plaintiffs argued that the Board's Interchange Fee standard constituted an unreasonable interpretation of the Durbin Amendment because it ignored Congress' directives regarding Interchange Fees – namely, that only incremental cost for authorization, clearing and settlement ("ACS") of a transaction may be considered. Thus, according to Plaintiffs, the Board exceeded its authority and under the Administrative Procedure Act ("APA") the court must set aside the Board's rule. The court agreed, finding that the Board's Interchange Fee regulation was invalid under the APA.

The court's held that the Board's Interchange Fee rule violated the APA as the Durbin Amendment plainly limited the costs allowable in the Interchange Fee standard

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to incremental ACS costs. Specifically, the court reasoned that Congress' requirement that the Board distinguish between incremental ACS costs and "other costs" in setting its Interchange Fee standard showed a clear intent by Congress to separate fees that must be included in the Interchange Fee standard and those that must be excluded.

B. The Board's Network Non-Exclusivity Rule

According to the court, the key word in interpreting Congress' requirement as to network non-exclusivity is "transaction". Specifically, the court concluded that the plain language of the Durbin Amendment required merchants be given a choice between multiple unaffiliated networks not only for each card, but for each *transaction* on that card. Therefore, the Durbin Amendment requires two unaffiliated networks be available for each authentication method (e.g., signature and PIN) enabled on the card.

III. The Court's Remedy

Because the court found that the Board's rules on Interchange Fees and network non-exclusivity under the Durbin Amendment violated Congress' clear intent, it is required under the APA to set aside those rules. The court thus vacated the rules and remanded back to the Board for appropriate action. The vacatur is stayed, however, to limit any disruptive effect. The length of the stay and whether the Board's current standards will remain in place until valid regulations replace them will be determined after further briefing.

It is likely that the Board will appeal the court's ruling to the Court of Appeals. ■

Terrence P. Maher
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1 NACS v. Bd. Of Governors of the Fed. Reserve Sys., Civil Case No. 11-02075 (RJL) (D. D.C. July 31, 2013).

Amendments to UCC Article 9: FAQs on Filings Following the July 1, 2013 Transition

In 2010 the Nebraska legislature adopted amendments to Article 9 of the Uniform Commercial Code (the "Amendments"). To preserve the effectiveness of pre-Amendment records and to allow secured parties to bring affected records into compliance with the new requirements, the Amendments provide rules for an orderly transition. The transition rules are found in Part 8 of UCC Article 9. The transition period began on July 1, 2013. This article will discuss several questions that lenders frequently ask about the transition period.

Q: Do the Amendments impact all financing statements?

A: No. Only in limited cases will a secured creditor need to take action to remain perfected. For example, there are rare instances where the Amendments change the requirements for how a secured creditor must designate a debtor's name on a financing statement. Further, there are rare instances where the Amendments change the governing jurisdiction.

Q: In what instances will the Amendments change the requirements for a debtor's name on a financing statement?

A: The Amendments clarify how secured creditors should designate the debtor's name when the debtor is an individual, a registered organization, a personal representative, or a trust. If the debtor is an individual with an unexpired Nebraska driver's license, then the financing statement must provide the individual's name as it appears on the driver's license. If the debtor is a registered organization, the financing statement must list the debtor's name as it appears on the registered organization's "public organic record." When collateral is administered by a personal representative, the financing statement must provide the decedent's name as the debtor's name. Finally, when collateral is held in a trust that is not a registered organization, the financing statement must provide the trust's name as it appears on the trust's organizing document. Only when a secured creditor's already-filed financing statement does not

conform to the Amended rules will a secured creditor need to take action. For a full discussion of the Amendments' substantive changes please reference our earlier article, which can be found by clicking here.

Q: If the Amendments do impact how a secured creditor should designate a debtor's name, does a secured creditor need to immediately amend the financing statement to reflect the Amendment's changes?

A: No. So long as the financing statement satisfies the requirements for perfection under Nebraska law as it existed before July 1, 2013, the Amendments do not immediately impact filed financing statements. However, if the Amendments impact an already-filed financing statement, the secured creditor only has until the financing statement lapses (or until the secured creditor files its continuation statement) to make necessary changes.

Q: Do the Amendments change the jurisdiction in which a secured creditor must file its financing statement?

A: Only in rare circumstances. The Amendments expand the types of entities that fall within the definition of "registered organization" to include business trusts, entities created by legislation, and entities created by the issuance of a charter by a division of government. Prior to the Amendments, these types of entities generally did not qualify as registered organizations. Under the pre-Amendment location rules, these entities were located at their principal place of business or chief executive office. After the Amendments take effect, however, these registered organizations are located where they were organized. Thus, if the debtor's principal place of business or chief executive office is in a different state than where it was organized, there will be a change in governing law.

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Q: What should a secured creditor do if the governing law does change?

A: First, it is important to note that the pre-Amendment financing statement does not cease to be effective on July 1, 2013, simply because the Amendments change the governing law. The pre-amendment financing statement remains effective until it would naturally lapse (i.e. five years after filing). After the Amendments take effect, however, the secured creditor should discontinue filing any UCC record in the former jurisdiction. Any further UCC record filed in the former jurisdiction, including a continuation statement, has no effect. If the secured creditor needs to amend or continue a financing statement filed in the debtor's former jurisdiction, then it will need to "move" the financing statement to the new jurisdiction. The transition rules allow the secured party to do this by filing an "In Lieu" in the new state. An In Lieu is simply a financing statement with some additional information. In addition to the financing statement requirements listed in 9-502(a), an In Lieu must identify the office in which the original financing statement was filed, identify the file number and file date of that financing statement and, if applicable, the most recent continuation. Finally, the In Lieu must indicate that the original financing statement remains effective.

Q: How should a secured creditor prepare for the Amendment's transition period?

A: Secured parties should modify procedures to include a review of potentially impacted records when making continuation decisions. To be most effective, that process should begin early. The secured creditor should allow sufficient time for the due diligence necessary to prepare any amendments it must file. Then, the secured creditor must be sure to file those records prior to the scheduled lapse date. ■

Eric J. Adams
Emily Z. McElravy

CFPB Issues New Guidance On Debt Collection Practices

The Consumer Financial Protection Bureau ("CFPB") has issued two new bulletins designed to provide guidance on what conduct by creditors and debt buyers (collectively, "debt owners") and debt collectors may be deemed unfair, deceptive, or abusive acts or practices, and what representations regarding a consumer's credit score, credit report or creditworthiness may be deceptive in violation of the Dodd-Frank Act and the Fair Debt Collection Practices Act ("FDCPA").

Bulletin 2013-17

Bulletin 2013-17 discusses what conduct may be considered "unfair, deceptive, or abusive acts or practices" (collectively, "UDAAPs") in violation of both the Dodd-Frank Act and the FDCPA. The FDCPA makes it illegal for debt collectors to engage in conduct "the natural consequence of which is to harass, oppress, or abuse any person in connection with the collection of a debt," to "use any false, deceptive, or misleading representation or means in connection with the collection of any debt," or to "use any unfair or unconscionable means to collect or attempt to collect any debt."

The FDCPA generally applies to third-party debt collectors, such as collection agencies, debt purchasers, and attorneys who are regularly engaged in debt collection. However, the bulletin's main focus is the Dodd-Frank Act which prohibits any covered person, including creditors who collect their own debts, debt buyers, as well as debt collectors from engaging in UDAAPs in violation of the Act. Therefore, any party covered by the FDCPA must comply with any obligations they have under the FDCPA, in addition to any obligations to refrain from UDAAPs in violation of the Dodd-Frank Act.

The CFPB notes that while a practice may be unfair, deceptive and abusive, each of the prohibitions are "separate and distinct" and governed by separate legal standards. For example, the guidance states an act or practice is unfair when (1) it causes or is likely to cause substantial injury to consumers; (2) the injury is not reasonably avoidable by consumers; and (3) the injury is not outweighed by countervailing benefits to consumers or to competition. By contrast, the guidance defines an act or practice as deceptive when (1) the act or practice misleads or is likely to mislead the consumer; (2) the consumer's interpretation is reasonable under the circumstances; and (3) the misleading act or practice is material. Therefore, an act or practice must be evaluated under the standards of each of the prohibitions.

Examples of Unfair, Deceptive and/or Abusive Acts or Practices

The CFPB also provided a non-exhaustive list of examples of conduct that could constitute UDAAPs and indicated its intent to watch the listed practices closely:

- Collecting or assessing a debt and/or any additional amounts in connection with a debt (including interest, fees, and charges) not expressly authorized by the agreement creating the debt or permitted by law.
- Failing to post payments timely or properly or to credit a consumer's account with payments that the consumer submitted on time and then charging late fees to that consumer.
- Taking possession of property without the legal right to do so.
- Revealing the consumer's debt, without the consumer's consent, to the consumer's employer and/or co-workers.
- Falsely representing the character, amount, or legal status of the debt.
- Misrepresenting that a debt collection communication is from an attorney.
- Misrepresenting that a communication is from a government source or that the source of the communication is affiliated with the government.
- Misrepresenting whether information about a payment or nonpayment would be furnished to a credit reporting agency.

- Misrepresenting to consumers that their debts would be waived or forgiven if they accepted a settlement offer, when the company does not, in fact, forgive or waive the debt.

- Threatening any action that is not intended or the covered person or service provider does not have the authorization to pursue, including false threats of lawsuits, arrest, prosecution, or imprisonment for non-payment of a debt.

A creditor who collects its own debts, and any other covered person, should be aware of the prohibitions imposed by the Dodd-Frank Act and review its debt collection practices to ensure it is not engaging in practices that may be deemed unfair, deceptive or abusive.

Bulletin 2013-08

Bulletin 2013-08 provides guidance to covered persons under the Dodd-Frank Act, and debt collectors under the FDCPA, of what representations in regard to credit scores, credit reports, and creditworthiness in the debt collection process may be considered deceptive. The CFPB warns that certain material representations intended to influence consumers to pay their debts in collection may be deceptive, including but not limited to, statements regarding the relationship between:

- Paying debts in collection and improvements in a consumer's credit report

- Paying debts in collection and improvements in a consumer's credit score;

- Paying debts in collection and improvements in a consumer's creditworthiness; or

- Paying debts in collection and the increased likelihood of a consumer receiving credit or more favorable credit terms from a lender.

The CFPB states its concerns with the prevalence of such representations in the event that it is influencing consumers and the representations are not true or accurate. The CFPB also informs debt owners and debt collectors that "in the course of supervision activities or enforcement investigations," it "may review communication materials, scripts, and training manuals and related documentation to assess whether owners of debts and third-party debt collectors are making these types of claims and the factual basis for them." Therefore, debt owners and debt collectors should take steps to ensure that any claims they make about the payment of debts in collection with a consumer's credit report, credit score, or creditworthiness are not "deceptive under the FDCPA, the Dodd-Frank Act, or both." ■

Terrence P. Maher
Samantha Ritter, Summer Associate

CFPB Exercises Authority to Censure "Abusive" Practices; More Enforcement Actions Pending

The Consumer Federal Protection Bureau (CFPB) recently settled an abusive practices enforcement action with American Debt Settlement Solutions, Inc. (ADSS), a Florida for-profit corporation. The settlement marks the first time the CFPB has exercised its new authority to censure "abusive" practices in addition to those that are deemed unfair or deceptive. Under the terms of the settlement, ADSS agreed to pay nearly $500,000 in damages and fees. In addition, ADSS no longer is permitted to advertise, market, or sell debt-relief products or services to consumers.

Historically, the prudential banking regulators had a UDAP mandate, which prohibited only unfair and deceptive acts and practices. However, *abusive* acts or practices also were made unlawful under Sections 1031 and 1036 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, thus resulting in the new "UDAAP" acronym. Section 1031 now grants the CFPB the authority to "prevent a covered person or service provider from committing or engaging in an unfair, deceptive, or *abusive* act or practice." In addition, Section 1036 says that is it unlawful for any covered person "to engage in an unfair, deceptive, or *abusive* act or practice."

Section 1031(d) defines the term "abusive," stating that an act or practice is abusive if it:

> "1) materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
>
> (2) takes unreasonable advantage of—
>
> > (A) a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
> >
> > (B) the inability of the consumer to protect the interests of the consumer in selecting or using a consumer
> >
> > (C) the reasonable reliance by the consumer on a covered person to act in the interests of the consumer."

The "abusive" standard is found in the Telemarketing Sales Act and serves as a basis for the Federal Trade Commission's Telemarketing Sales Rule (TSR), which also played a role in the ADSS settlement.

Because the ADSS settlement marks the first time the CFPB has used its new, broad authority, it provides a window into how the Bureau may exercise its authority in the future.

In the recent settlement between the CFPB and ADSS, the Bureau charged the company with multiple violations of the TSR and the Dodd-Frank Act. The Bureau alleged that the company charged consumers fees for debt-relief services before the company had actually settled the consumers' debts. In addition, the company also allegedly made multiple misrepresentations about its debt relief services. Among the misrepresentations listed in the settlement are: failure to disclose that it was almost impossible for ADSS to assist consumers with debts under $700; misrepresentation of the time required to assist consumers with debts; and the general misrepresentation that ADSS would be able to assist consumers with debts at all. The Bureau also charged the company with knowingly enrolling consumers whose financial situations made it highly unlikely they would be able to complete the ADSS program.

To date, the CFPB has provided little guidance on how it will exercise the new authority and on which products it will focus its attention. Because the ADSS settlement marks the first time the CFPB has used its new, broad authority, it provides a window into how the Bureau may exercise its authority in the future. More actions are widely anticipated, which will provide more guidance as to what the new UDAAP standard means for banks, but unfortunately, will come at a steep cost. ■

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Upcoming Speaking Engagements

On Friday, September 20, 2013, Thomas O. Ashby will present "Actual and Constructive Fraudulent Transfers: Considerations for Transactional Counsel, Litigators, Lenders and Insurers," at the Iowa State Bar Association's Commercial Law and Bankruptcy Section in Des Moines, Iowa.

Terrence P. Maher will be presenting around the country this fall at various conferences, forums and seminars:

On August 28, 2013, he will present at the International Association of Financial Crime Investigators' 45th Annual Training Conference in Denver, CO. The panels are titled "Fundamentals of Prepaid" and "Scenarios to Success…..Prepaid in the Field for Law Enforcement."

On September 9th and 10th, he will present at the Law Seminars International Mobile Payments Conference to be held in Washington, DC. His presentation is titled "Individual Security: Dealing with Lost Phones and Fraudulently Duplicated SIMM Cards."

Terry will participate in a panel on September 18, 2013, in Washington, DC, at the American Conference Institute's 6th National Forum on Balancing Innovation with Consumer Protections in Emerging Payments Systems. The panel is titled "UDAP/UDAAP, Disclosures and Marketing: Regulatory and Compliance Considerations for New Payment Models."

He is co-chairing the American Conference Institute's 8th National Forum on Prepaid Card Compliance to be held in San Francisco, CA on October 3-4, 2013, where he is also participating in a panel titled: "The Latest on CFPB and Prepaid Cards: Money Transmitters, the Extension of Reg E to Prepaid, Proposed GPR Rulemaking, Comments on ANPR, and More." ■

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