

THE BANKERS' BULLETIN

Regulatory & Enforcement Insights on Recent Bank Industry Developments

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Supreme Court Rules CFPB's Funding Mechanism is Constitutional

- The decision will immediately clear a log jam at courts across the country that had paused CFPB investigations, enforcement actions, and rulemakings while the agency's constitutionality was litigated.
- With new momentum, expect the CFPB to push boundaries and target individual actors going forward.

2

Congress Acts to Limit SEC Encroachment into Bank Custody of Crypto Assets

- Attempts to unwind accounting guidance covering public banks signals censure of SEC overreach.
- Through Congressional Review Act disapproval or passage of a new law, legislative action will likely ensure that crypto custody supervision remains under the purview of the bank regulatory agencies.

3

OFAC Violation Exposure is Extended & Reporting Requirements Are Expanded

- New legislation has doubled the limitations period for OFAC sanctions, increasing civil and criminal exposure for violations. Lookback reviews and investigations will be broader and require more resources.
- Corresponding compliance system enhancements should be made to meet regulatory expectations.

4

CFPB Issues Interpretive Rule Subjecting BNPL Products to Reg. Z

- Avoiding notice-and-comment rulemaking, BNPL products will now be subject to a host of requirements.
- In advance of potential political changes, the CFPB continues to use available tools to force industry shifts.

5

FRB and FDIC Issue Reports on Key Risks and Supervisory Priorities

- Focus on risk management of liquidity and interest rate risks permeate both agencies' industry reports.
- In addition to financial risks, both reports continue to emphasize the need to address cybersecurity risks.

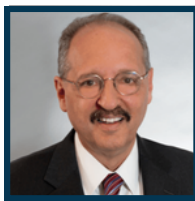
About The Firm

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.



Brendan Clegg

bclegg@luselaw.com



Marc Levy

mlevy@luselaw.com



Agata Troy

atroy@luselaw.com

Please reach out to any of our regulatory and enforcement attorneys above, or to your primary Luse Gorman contact, if you have any questions related to the topics covered in this edition of *The Bankers' Bulletin*.

Summary. On May 16, the Supreme Court upheld the funding mechanism for the CFPB in a 7-2 decision in *CFPB v. Community Financial Services Association of America*, overturning a Fifth Circuit decision that held the Bureau's funding was unconstitutional, and remanding the case.

Takeaways.

- The Fifth Circuit's 2022 decision had blocked implementation of the CFPB's 2017 Payday Lending Rule, and led courts across the country to invalidate or stay a variety of CFPB investigational, enforcement, and rulemaking actions while the case was up on appeal.
- Predictably, Director Chopra vowed to restart the actions stalled by the litigation. In public remarks, he noted the Bureau's push to expand its enforcement office, and highlighted that the agency will continue to focus on both repeat offenders and the individual executives behind alleged misconduct. Entities under investigation should prepare for individual action offshoots.

Bottom Line. With the major question of funding settled, banks and other financial services providers are likely out of Constitution-based arguments to stymie the Bureau's activities. The CFPB will push hard in the coming months to make up for lost time, and will seek quick wins in actions that would otherwise be abandoned by a new administration. But, recent court successes by the industry, and a general sense of overreach, have emboldened challengers to utilize new defenses to CFPB activities.

Supreme Court Rules CFPB's Funding Mechanism is Constitutional



Congress Acts to Limit SEC Oversight of Crypto Activities



Summary. On May 8 and May 16, the House and the Senate passed a bi-partisan resolution disapproving the SEC's Staff Accounting Bulletin (SAB) No. 121, but President Biden vetoed the resolution on May 31. On May 22, the House passed the Financial Innovation & Technology for the 21st Century Act (FIT21) to establish a regulatory framework for digital assets, and divide jurisdiction over those assets between the SEC and CFTC.

Takeaways.

- SAB 121, which requires SEC-regulated banks performing custodial duties for crypto assets to hold them on their balance sheets, engendered significant criticism from the banking industry and even other regulators, for both the effect, and the end-around of the rulemaking process.
- FIT21, if signed into law, would bar the SEC from requiring banks through regulation or supervisory action to alter their balance sheets related to crypto assets they hold in custody.
- Overturning SAB 121 under Congressional Review Act authority would prevent the SEC from trying to take a rulemaking action in "substantially the same form," effectively preventing the SEC from again encroaching on a traditional area of bank agency supervisory authority.

Bottom Line. While the SEC continues to aggressively pursue enforcement actions in the crypto space, Congress has now made clear that at least for crypto custody, the SEC should stay in its lane.

Summary. On Apr. 24, President Biden signed the 21st Century Peace through Strength Act extending the statute of limitations for certain sanctions violations from 5 to 10 years. On May 10, OFAC issued an interim final rule to create new reporting requirements, among other things.

Takeaways.

- Practically, if a sanctions-related lookback review or investigation is required, the time horizon covered will also double. This will result in an investment of substantially more resources and human capital, and could reveal data and document retention gaps or systems conversion issues.
- Be prepared to revise retention procedures for OFAC-related records. DOJ, OFAC, and the banking agencies will expect banks to root out potential violations from the entire limitations period.
- On the corporate side, banks should review relevant contractual reps and expand due diligence.
- OFAC's new rule will require banks to file reports within 10 business days of when blocked property is unblocked or transferred. Procedures, training, and internal reporting structures will need to incorporate this additional feature of the OFAC reporting regime.

Bottom Line. By doubling the limitations period for nearly all OFAC sanctions programs, banks' exposure to civil and criminal actions has been significantly expanded at a time when sanctions compliance is a top federal priority. Expect agency actions to quickly implement the new time period.

OFAC Violation Exposure is Extended & Reporting Requirements Are Expanded



CFPB Issues Interpretive Rule Subjecting BNPL Products to Reg. Z



Summary. On May 22, the CFPB issued an interpretive rule concluding that lenders that offer Buy Now, Pay Later (BNPL) products are “card issuers” under the Truth-in-Lending Act’s Regulation Z, and that BNPL loans are subject to some, although not all, of Reg. Z’s credit card regulations.

Takeaways.

- Among other things, this designation triggers compliance with provisions covering cost of credit disclosures, billing dispute resolution, periodic statements, and refunds back to consumers.
- The CFPB has opened the rule up to comments, but even with strong pushback from the industry, it will very likely not be deterred by an expected negative response, absent litigation.
- The interpretive rule continues the CFPB’s approach under Director Chopra to use means other than notice-and-comment rulemakings to try to shape industry practice and behavior.
- In 2023 guidance, the OCC stated it expects national banks and FSAs to offer BNPL products in a manner that “complies with applicable laws and regulations.” Commentary from the banking agencies should be monitored to see how they view the status of the interpretive rule.

Bottom Line. The CFPB expects compliance in a very tight window: 60 days from publication in the FR. Banks should ensure their third-party lending partners have addressed applicable requirements.

Summary. On May 14, the FRB published its Supervision and Regulation Report, providing details on its supervisory and regulatory policies and actions. On May 22, the FDIC published its Risk Report.

Takeaways.

- Not surprisingly, the FRB’s Report confirms the agency continues to try to improve the “speed, force, and agility” of its supervision, echoing other post-SVB pronouncements. Confirming experience on the ground, the FRB remains primarily focused on credit, interest rate, and liquidity risks, and the quality of banks’ risk management frameworks aimed at those specific risks.
- The FRB expects its banks to “regularly test” their ability to access multiple sources of contingent funding. CRE concentrations are and will be the subject of “in-depth” examinations by the FRB.
- Outstanding supervisory findings in these areas increased in 2023, confirming the agency’s increased focus. The FRB noted remediation of prior findings as a standalone supervisory priority.
- The FDIC’s Report on key risks from 2023 echoed many of these same themes and points of emphasis, focusing on liquidity and interest rate risks, deposit and funding sources, and CRE.

Bottom Line. Although not styled as industry guidance, banks should review their supervisors’ industry summary reports to extract, and get ahead of, the agencies’ key risks, priorities, and expectations.

FRB and FDIC Issue Reports on Key Risks and Supervisory Priorities



Other Developments That You May Have Missed . . .

Tennessee Legislature Bars Credit Union Acquisitions of State Banks. In Apr. 2024, in response to a previous appellate court ruling, the Governor of TN signed legislation to permit banks to sell or transfer all of their assets *only* to FDIC-insured institutions, effectively excluding credit unions from making such purchases. TN is the most recent battleground in the push-pull between courts, legislatures, and regulators within states over the future of bank-CU M&A activity, with a patchwork approach now materializing across the U.S.

Maryland Authorizes OFR to Examine Third-Party Providers. On May 9, Gov. Moore signed legislation allowing the Office of Financial Regulation to directly examine third-party service providers performing services for regulated institutions. Direct supervision could blow back on bank partners, if the exams reveal critical compliance or governance weaknesses that should have been caught in diligence.

Federal Judge in TX Stays CFPB’s Credit Card late Fee Rule. On May 10, a federal district court judge in Texas granted a preliminary injunction staying the CFPB’s credit card late fee rule from taking effect. He later tried to transfer the case to D.C., but the Fifth Circuit stayed his attempted transfer to D.C. for a second time on May 29. The rollercoaster procedural nature of the case gives little comfort or clarity to covered parties about their compliance obligations going forward.

CFPB Extends Compliance Dates for Small Business Lending Rule. On May 17, following the Supreme Court’s decision in the *CFS* case, the CFPB announced its intent to issue an interim final rule to extend the compliance deadlines for its Dodd-Frank Section 1071 rule out until 2025 and 2026, depending on the lenders’ loan volumes. Other grounds for legal challenge may still impact those deadlines.

FRB-NY Conditionally Approves Master Account. On May 23, a CT de novo bank, Numisma Bank, confirmed receipt of conditional approval for a master account as a Tier 3 uninsured bank. The approval order should finally shed light on the FRB’s key considerations.