Davis Polk

Financial Services Regulatory Reform

FALL FOCUS EDITION

September 22, 2021

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These slides are designed to be a reference tool for the financial regulatory reform landscape. They gather in one place the state of play on a number of topics and set forth our views on the general outlook. They will be updated from time to time. To stay up to date on all topics related to financial regulatory reform, we invite you to visit our one-stop website at www.davispolk.com/capabilities/practice/financial-institutions/insights.

On the Agenda

Social and Antitrust Policy at the Forefront: The Biden Administration continues to be focused on activity at the intersection of financial regulation and social policy, including climate change and expanding financial inclusion and diversity. This intersection is also a key goal of House Financial Services Committee (**HFSC**) Chairwoman Waters and Senate Banking Committee (**SBC**) Chairman Brown. In addition, the White House is focused on antitrust policy in the banking sector as part of its larger policy goals to enhance antitrust regulation and enforcement across all sectors of the economy.

Congressional Legislative Priorities: Financial regulatory legislation remains a low priority for this Congress and significant legislative changes are unlikely. The Democratic majority in both houses nonetheless keeps open the possibility of incremental legislative action, but most likely only if attached to must-pass bills.

Oversight and Regulation: The primary means by which we expect Congress to act is through hearings with pointed questions to both regulators and private sector actors.

On the Agenda

Executive Orders: Given the sharply divided Congress, President Biden has relied heavily on Executive Orders which encourage the independent agencies to follow his policy goals, such as in climate change and antitrust, and which take a whole-of-the government approach. These Executive Orders will influence independent agency regulatory agendas and actions but will not dictate them.

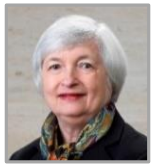
On Deck: In addition to the topics covered on the following slides, we expect to see Congressional and regulatory attention turn to areas including nonbanks and FSOC activities and entity designations, source of strength, overdraft fees, artificial intelligence, cross-border payments and executive accountability and compensation.

Regulatory Change and Leadership: A number of the financial regulatory leadership posts still do not have Senate-confirmed appointees, while the pace of nominations is slow. We expect the pace of regulatory change to accelerate late this year and into next year. For the current status of financial regulatory leadership, see the next slide.

The Evolving Landscape

Financial Regulatory Leadership as of September 22, 2021

Treasury


Secretary Yellen


Deputy Secretary Adeyemo


Under Secretary for Domestic Finance Liang

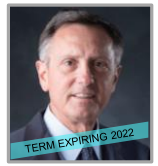
Under Secretary for International Affairs

Under Secretary for Terrorism and Financial Intelligence Brian Eddie Nelson

Assistant Secretary for Financial Institutions Graham Steele

Federal Reserve

Chair Powell



Vice Chair Clarida

Vice Chair for Supervision Quarles


Governor Brainard


Governor Waller


Governor Bowman

Governor

FDIC


Chairman McWilliams

Vice Chairman

Director Gruenberg

CFPB Director Nominee Rohit Chopra*

Acting CFPB Director Dave Uejio**

OCC Comptroller

Acting OCC Comptroller Michael Hsu***

SEC


Chairman Gensler


Commissioner Lee


Commissioner Roisman


Commissioner Crenshaw


Commissioner Peirce

CFPB

CFPB Director Nominee Rohit Chopra*

Acting CFPB Director Dave Uejio**

OCC

OCC Comptroller

Acting OCC Comptroller Michael Hsu***

* The nomination of Rohit Chopra has been discharged out of the SBC and is awaiting confirmation by the full Senate.

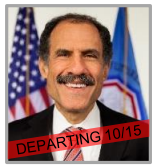
** President Biden has nominated Dave Uejio to serve as Assistant Secretary for Fair Housing and Equal Opportunity at the Department of Housing and Urban Development.

*** President Biden has not yet submitted a nominee for permanent Comptroller.

CFTC

Acting Chairman Behnam


Commissioner Stump



Commissioner Berkovitz

Christy Goldsmith Romero

Kristin Johnson

Climate Change

General Outlook: Addressing climate change is one of the highest priorities of the Biden Administration, and regulatory authorities in the United States and abroad continue to increase their attention on climate-related topics.

International and Domestic Agendas: Anticipated developments include:

- The FSOC is expected to publish a report on climate-related financial risk by November 16, 2021, pursuant to a Biden Executive Order. Please see this Davis Polk client memorandum for more information on the Executive Order.
- The pace of policy development on climate-related financial disclosures is expected to increase, following the communiqué released by the G7 Finance Ministers & Central Bank Governors in June 2021.

Climate Change

SEC: The SEC is expected to issue a proposed rulemaking on climate disclosures before year-end.

- The proposal will be informed by the numerous and varied comments the SEC received over the summer in response to its request for public input. Our summary of the comments is available here.
- Chair Gensler signaled publicly in June and July that the proposal will likely address, among other things:
  - Industry-specific metrics
  - The Task Force on Climate-related Financial Disclosures framework endorsed in the G7 communiqué, including climate governance and scenario analyses
  - Scope 1 and 2, and possibly 3, emissions
  - Requiring disclosures in Form 10-K
- Given the expected timing, it is unlikely these requirements would be in place for the next 10-K or proxy season.

The SEC's Divisions of Examinations and Enforcement continue to scrutinize climate disclosures, including of Environmental, Social and Governance (**ESG**) funds and how they are marketed.

Climate Change

Federal Reserve: The Federal Reserve's policy is not to mandate which businesses banks may lend to, as Chair Powell has emphasized and Treasury Secretary Yellen has echoed. We believe that the Federal Reserve's near-term bank regulatory agenda could include:

- Climate-related scenario analysis
- Supervisory focus on climate-related risk management practices
- Evaluation of concentration risk and underwriting standards in lending to non-green sectors (e.g., fossil fuels)
- Potential incentives to encourage environmental efforts such as classifying investments in local disaster recovery as Community Reinvestment Act-eligible activities (for further discussion on the Community Reinvestment Act, see slides 50 and 51)

Questions about the urgency of the Federal Reserve's climate agenda have become intertwined with Chair Powell's potential re-nomination.

- Some progressives in Congress have called for new leadership, arguing Chair Powell has not done enough.
- Conservatives, on the other hand, have expressed skepticism as to whether the Federal Reserve has the expertise or even the authority to regulate climate change at all, including Republican members of the Senate Banking Committee in a March 2021 letter to Chair Powell, available here.

Climate Change

OCC: As explained in Acting Comptroller Hsu's August 2021 SBC testimony, the OCC is pursuing a two-pronged approach: (1) coordinating with others, including joining the Network for Greening the Financial System, which the Federal Reserve joined in December 2020; and (2) supporting effective climate risk management practices at banks.

Other Regulatory Actions: Federal financial regulators are pursuing the development of climate risk-related policy through numerous committees, hubs, task forces, units and initiatives. Work is also being coordinated through the FSOC.

Legislative Initiatives: Various bills have been introduced in Congress, which would:

- Require climate-related disclosures by public companies
- Establish an FSOC committee dedicated to assessing and providing recommendations to Congress and federal and state financial regulatory agencies about climate risk and the financial system
- Require federal financial regulatory agencies and the FSOC to update applicable supervisory guidance and nonbank SIFI designation guidance, respectively, to include climate risk
- Require annual reports on climate risk from G-SIBs
- Require certain large banking organizations to discontinue new or expanded fossil fuel projects, thermal coal financing and fossil fuel financing by 2023, 2025 and 2030, respectively, among other actions, which would have the effect of changing the policy noted in the previous slide

Climate Change

President Biden's American Jobs Plan included a $27 billion "Clean Energy and Sustainability Accelerator," a public green bank intended to "mobilize private investment" for clean energy projects. Related legislation has been proposed that would promote the creation of "green banks" and establish a "National Climate Bank."

International Developments: The Basel Committee's Task Force on Climate-related Financial Risks is investigating how they might address climate-related financial risks, building off of two reports discussing transmission channels and measurement methodologies.

Capital-Related Initiatives: There are a number of ways that the Biden Administration's emphasis on climate change could make its way into capital requirements. Potential mechanisms that have been floated in the broader policy discussion, though without firm endorsement among policymakers in the United States, include:

- Incorporating a climate change scenario either into supervisory stress testing or otherwise
- Increasing risk weights for exposure to fossil fuel companies and decreasing risk weights for exposures to clean energy companies, bringing social goals into what has, until now, been largely a credit risk and market risk analysis
- We view it as unlikely that the Biden Administration would act unilaterally without Basel being the first mover.

Consumer Financial Protection

General Outlook: In the Spring 2021 Unified Regulatory Agenda, the CFPB identified a number of administrative actions that it intends to tackle and, notably, backed off from previous plans to potentially design new disclosures for payday loan borrowers.

- The Spring 2021 Unified Regulatory Agenda scrapped a project that began last fall under former Director Kathleen Kraninger to conduct consumer testing of payday loan disclosure options for a possible rulemaking on the subject.
  - The CFPB did note that Acting Director Uejio's decision to withdraw or table any given rulemaking project should not necessarily be read as a "substantive decision on the merits."
- The Spring 2021 Unified Regulatory Agenda further elaborated that the agency will prioritize issuing a final Libor transition rule for consumer products, completing its pandemic-related mortgage servicing rule proposed in April 2021, finalizing data-reporting requirements on small-business lending and finalizing consumer financial data-sharing rules. For more information on the data-sharing rules, see the Open Banking and Data Access section at slides 75 and 76.
- The agenda also emphasized that "[the CFPB's] new director, when confirmed, will assess further what regulatory actions the bureau should prioritize to best further our consumer protection mission and mandate, particularly in light of the ongoing pandemic and resulting economic crisis and the bureau's commitment to promoting racial equity."

Consumer Financial Protection

We expect the CFPB to focus, once the new director is confirmed, on topics beyond what was identified in the Spring 2021 Unified Regulatory Agenda, including:

- Increased enforcement efforts, which would build on the recent upward trend, with a reinvigorated Office of Fair Lending and Equal Opportunity empowered to target lenders found to engage in discriminatory practices
- Use of the disparate impact standard to hold “major financial institutions accountable for discriminatory lending practices,” discussed on slides 16 - 18 in the Disparate Impact section
- Enhanced scrutiny of higher education lenders, servicers and debt collectors and forbearance of federal student loans. The consent order against Better Future Forward is part of this trend.
- Small dollar lending practices and underwriting standards, and the establishment of a federal usury limit, though this would require Congress to act
- Bolstering protections against abusive debt collection practices, with a particular focus on overdraft fees

Consumer Financial Protection

Competition and UDAAP: The Competition Order provides the CFPB a stronger role at the White House Council than the prudential banking agencies and encourages the CFPB to broadly read its unfair, deceptive, or abusive acts or practices (**UDAAP**) authority so as to ensure competitive markets for consumer financial products and services.

Enforcement:

- On March 11, 2021, the CFPB rescinded self-imposed restrictions on its ability to collect civil penalties and disgorgement from banks and financial companies for abusive acts and practices.
- Additionally, in the Spring 2021 Unified Regulatory Agenda, the CFPB downgraded a project exploring how to use its rulemaking authority to set more boundaries on what it considers abusive conduct from a longer-term initiative to inactive status.

Consumer Financial Protection

Small-Business Loan Data: On September 1, 2021 the CFPB released its long-awaited notice of proposed rulemaking that would require banks and other lenders to collect and report data meant to identify discrimination and barriers to credit in small-business lending.

- Section 1071 of the Dodd-Frank Act directed the CFPB to adopt regulations governing the collection of small business lending data.
- The proposal backtracks on a September 2020 suggestion made by the agency during the Trump Administration that it would exempt a significant portion of community banks from the reporting requirements, sparking concern among smaller banks and fintechs that the rule will be too broad. The CFPB also expanded the scope of the proposal to cover merchant cash advances.
- The lack of data on loans made to small businesses has been notable during the pandemic, particularly as the forgivable loans provided to small businesses under the Paycheck Protection Program have been beset by accusations of fraud and concerns that small businesses in underserved communities did not get enough loans.
- We expect the proposal to receive significant attention and comments, with small banks and fintechs seeking to limit the scope of the new reporting obligations.

For more on the topic, please refer to Ballard Spahr's post, CFPB issues Section 1071 proposed rule on small business lending data collection (Sept. 1, 2021) and Kate Berry, *CFPB small-business data plan scares banks. Activists say it should*, American Bank (Sept. 12, 2021).

Consumer Financial Protection

Fintech: Some in Congress have also called on the CFPB to take measures to address the risks that nonbank fintech companies pose to consumers. In a letter to the CFPB, Chairman Brown wrote to the Acting Director Uejio, stating that "Chime's abrupt, involuntary closures of its customers' accounts" call for further "insight into the risks posed by nonbanks to consumers as well as the measures the Bureau is taking to address the risks by nonbank fintech companies and their affiliated banks."

Strengthen Fair Lending and Fair Housing: The Biden Administration has started to roll back regulatory measures undertaken during the Trump Administration that are viewed as reducing the efficacy of fair housing protections, such as reinstating the federal risk-sharing program to incentivize private sector funding of affordable housing, and has signaled that strengthening fair lending and fair housing will be a CFPB priority. For a deeper dive on the CFPB's actions to strengthen fair lending and fair housing, see slides 16 - 18 in the Disparate Impact section. Additional actions include:

- Reinstating the federal risk-sharing program to incentivize private sector funding of affordable housing
- On March 9, 2021, the CFPB issued an interpretive rule clarifying that the prohibition against sex discrimination under the Equal Credit Opportunity Act and implementing Regulation B extends to discrimination involving sexual orientation and gender identity

Disparate Impact

Fair Lending: We expect an increase in fair lending enforcement actions by the CFPB and HUD, including based on disparate impact.

- Acting CFPB Director Uejio said that fair lending enforcement will be a top priority for the CFPB, with a focus on racial equity, but that the CFPB will also “look more broadly, beyond fair lending, to identify and root out unlawful conduct that disproportionately impacts communities of color and other vulnerable populations.”
- Rohit Chopra, President Biden’s nominee for CFPB Director, affirmed his commitment to fair lending enforcement in his confirmation hearing before the SBC.
- The CFPB’s fair lending enforcement focus will not be limited to racial discrimination. The CFPB stated in a March 2021 interpretive rule that the Equal Credit Opportunity Act (**ECOA**) and Regulation B prohibit discrimination by lenders based on sexual orientation and gender identity.
- The CFPB may issue a rule or guidance clarifying its approach to disparate impact analysis under the ECOA and/or Regulation B, as the CFPB suggested in a July 2020 request for information.

Disparate Impact

Fair Housing: HUD issued two rules in June 2021 following an Executive Order from President Biden directing HUD to examine the effects of two Trump Administration rules.

- An interim final rule repeals the Trump Administration's 2020 Affirmatively Furthering Fair Housing (**AFFH**) rule and restores certain definitions and certifications from the Obama Administration's 2015 AFFH rule. The interim final rule does not reinstate the standardized assessment that was required under the 2015 AFFH rule. HUD will issue a separate proposal on a new fair housing planning process and framework.
- A proposed rule would repeal the Trump Administration's 2020 rule on disparate impact standard under the FHA and recodify the discriminatory effects standard from the Obama Administration's 2013 rule.
  - The Trump Administration's 2020 rule, which would have introduced more stringent pleading requirements for plaintiffs making disparate impact claims, was due to go into effect in October 2020 but was stayed by a Massachusetts federal district court ruling.
- Like the CFPB, HUD announced in February 2021 that it will administer and enforce the FHA to prohibit discrimination based on sexual orientation and gender identity.

Disparate Impact

HUD and FHFA Memorandum of Understanding: In August 2021, HUD and the FHFA announced a memorandum of understanding (**MOU**) aimed at enhancing their collaborative oversight and enforcement efforts with respect to both fair lending and fair housing. The MOU contemplates information sharing and increased coordination between the agencies. The MOU will remain in effect through December 31, 2025.

- In September 2021, making reference to “insight and expertise” provided by HUD under the MOU, the FHFA announced that it would require Fannie Mae and Freddie Mac to develop plans to reduce the nation’s racial homeownership gap and remediate underinvestment in areas previously subject to discriminatory lending practices. The two government-sponsored enterprises will each be required to submit a three-year plan by the end of December 2021 and thereafter provide annual progress reports.

AI and Alternative Data

AI and Alternative Data: The major financial regulators have issued a request for information on the use of AI and alternative data. The request includes multiple questions on AI and fair lending, including on the risks that AI can be biased and/or result in discrimination on prohibited bases. The comment period closed, after extension, on July 31, 2021. No related announcements have been made since by the major financial regulators.

- The National Community Reinvestment Coalition and six fintech companies submitted a letter to the CFPB requesting guidance on how the CFPB will apply ECOA and Regulation B to systems that use AI or alternative data to make lending decisions. Among other things, the letter recommends that the CFPB align Regulation B's "legitimate business need" standard to HUD's 2013 discriminatory effects rule.
- For more detailed discussion and analysis of the major financial regulators' focus on AI and machine learning, our client memorandum is available here.

Federal Reserve Racial and Economic Equity Act: In April 2021, the HFSC passed a bill introduced by Chairwoman Waters that would require the Federal Reserve to exercise all its duties and functions in a manner that fosters the elimination of disparities across racial and ethnic groups with respect to employment income, wealth, and access to affordable credit. Senators Warren and Gillibrand introduced a Senate version.

Home Appraisals

Home Appraisals: The Biden Administration and various agencies have indicated that addressing racial disparities in home appraisals is a key goal. We expect to see rulemaking and potential executive action in this area.

- In June 2021, the Biden Administration announced, as part of its strategy to address the racial wealth gap, "a first-of-its-kind interagency effort to address inequity in home appraisals, and conduc[t] rulemaking to aggressively combat housing discrimination."
- The first meeting of the Interagency Task Force on Property Appraisal and Valuation Equity (**PAVE**), chaired by HUD Secretary Marcia Fudge and Domestic Policy Council Director Susan Rice, took place in August 2021. The PAVE members agreed that the body will focus on four principal goals:
  - Ensuring that government oversight and industry practice further valuation equity
  - Combatting valuation bias through educating the consumer and training the practitioner
  - Ensuring equity in valuation by making available high-quality data
  - Creating a comprehensive approach to combating valuation bias through enforcement and other efforts
- PAVE is expected to deliver a final action report by the end of January 2022.
- Acting Comptroller Hsu has separately emphasized that under his leadership, addressing inequality will be a top OCC priority. He has also emphasized the need to eliminate racial bias in home value appraisals and indicated support for enforcement actions against banks that use discriminatory appraisals.

Underbanked and Basic Access

Banking Access: The following are some of the most prominent proposals to increase banking and financial services access.

Banking for All Act: Chairman Brown continues to voice his support for the Banking for All Act, which would require Federal Reserve member banks to offer direct digital U.S. dollar accounts to all U.S. individuals and businesses.

- Banks would be required to offer certain minimum banking services on terms no less favorable than those that the bank offers for existing transaction accounts, provide a minimum interest rate and not charge account fees or have minimum or maximum balance requirements.
- In areas with limited access to Federal Reserve member banks, such banks would be required to partner with U.S. Postal Service retail facilities to provide access to accounts.
- As discussed on slides 65 - 69 in the Central Bank Digital Currency section, the Banking for All Act and two other pending bills would also provide for direct digital dollar accounts for individual and businesses at Federal Reserve Banks.

Underbanked and Basic Access

Postal Banking: Although we believe that postal banking is unlikely to gain traction, several Democrats in both the Senate and the House are vocal proponents, including Senators Sanders and Warren. Short of full postal banking, the U.S. Postal Service could be leveraged to facilitate access to other programs, as proposed in the Banking for All Act. 33 House members voiced support for including postal non-bank financial services pilot programs in the fiscal year 2022 Appropriations Bill.

Public Banking: Today, only one state-owned bank exists, in North Dakota, but there has been a movement by some on the progressive left to expand state and locally owned and operated public banks.

- In 2019, California passed legislation that allows California counties and cities to create public banks, and in late March 2021, introduced a bill for the California Public Banking Option Act, with the goal of providing a "zero-fee, zero-penalty public option for basic financial services." Several California counties are exploring a partnership to jointly open a "Central Coast" public bank.

Underbanked and Basic Access

- Several other states have also introduced bills to permit chartering of public banks. At the federal level, Representatives Tlaib and Ocasio-Cortez introduced a bill for the Public Banking Act, which would promote the chartering of state and local public banks.

Green Banks: Among other proposed legislation concerning green banks, as part of the American Jobs Plan, the Biden Administration has proposed the establishment of a $27 billion Clean Energy and Sustainability Accelerator to mobilize private investment into distributed energy resources; retrofits of residential, commercial and municipal buildings; and clean transportation. The Biden Administration explained that "[t]hese investments have a particular focus on disadvantaged communities that have not yet benefited from clean energy investments."

- Funds for the Accelerator were not included in the Infrastructure Investment and Jobs Act but are included in the $3.5 trillion budget resolution passed by the Senate in August 2021, which currently awaits a vote in the House.

Private Sector Response: Although federal legislative proposals to improve banking access are unlikely to be passed in the current environment, the private sector is starting to voluntarily embrace some of these ideas. For example, banks representing 52% of U.S. deposits offer accounts certified by the Cities for Financial Empowerment Fund's Bank On program, and which charge low or no fees and do not charge overdraft fees.

Underbanked and Basic Access

Fintech and Innovation: The Chief Innovation Officers at both the OCC and CFTC have stated that their agencies will be thinking about how technological innovations can help the underbanked and unbanked, as well as address other structural issues that present barriers to expanded financial inclusion.

The FDIC is similarly focused, announcing in June 2021 a technology-focused challenge that encourages banks, nonprofits, academic institutions and others to identify better resources to help underbanked Americans. Eight teams of banks, non-profits and fintechs are participating and preparing presentations in advance of a September 2021 demo day in front of FDIC judges.

Government-Owned Credit Reporting Bureau: The Biden Administration may seek to create a government-owned credit reporting bureau to compete with, or eventually replace, the three major private-sector credit reporting bureaus, Equifax, TransUnion and Experian. The current credit reporting framework has been identified as a barrier to financial inclusion, including with respect to access to financial services such as mortgages.

- In June 2021, House Democrats introduced the National Credit Reporting Agency Act, which would establish the Public Credit Registry within the CFPB, creating a public option for consumers who choose to utilize it.

Underbanked and Basic Access

FDIC #GetBanked Campaign: The FDIC has launched a public awareness campaign about the benefits of opening a traditional bank account. Focusing on U.S. households without a bank account, the campaign is initially focusing on the Houston and Atlanta areas, but will likely be extended nation-wide if successful.

- The FDIC campaign should be seen a sister campaign to the national Bank On program.

Cannabis-Related Banking and Marijuana Legalization

General Outlook

- The direction of the federal regulatory and enforcement framework for financial institutions providing services to U.S. cannabis-related businesses has been unclear, with most banking organizations finding the provision of banking services to such businesses too perilous. FinCEN reported that as of June 30, 2021, there were only 706 financial institutions providing banking services to cannabis-related businesses.
- The **Cannabis Administration and Opportunity Act** (**CAOA**) represents the most prominent legislative proposal on cannabis reform and was released by Senate Majority Leader Schumer and Senators Booker and Wyden as a discussion draft on July 14, 2021. As proposed, this bill would, among other things:
  - Deschedule cannabis from the Controlled Substances Act (**CSA**) and transfer primary agency jurisdiction over cannabis from the Drug Enforcement Agency (**DEA**) to the Food and Drug Administration (**FDA**), the Treasury Department's Alcohol and Tobacco Tax and Trade Bureau (**TTB**) and the Justice Department's Bureau of Alcohol Tobacco Firearms and Explosives (**ATF**)
  - Recognize state law as controlling the possession, production, or distribution of cannabis
  - Require expungement of arrests and convictions for non-violent federal cannabis offenses
  - Establish 21 years of age as the minimum age required to purchase cannabis
  - Impose taxation of cannabis and establish social equity programs

Cannabis-Related Banking and Marijuana Legalization

- The Sponsoring Offices of the CAOA requested public comment on the bill by September 1 before its formal introduction into Congress. Among other topics, stakeholders have expressed interest in which federal agency or agencies should take the lead on cannabis regulation:
  - "The FDA's role should be precisely defined and narrow in scope. The track record of the FDA suggests it having a significant role would lead to a very restrictive market, with rapid consolidation into a handful of large players and the resurgence of the underground market."
    - *Marijuana Policy Project, Comments on the CAOA*
  - "A program that relies heavily on the FDA will be prohibitively expensive for small business operators, and the FDA is unlikely to support state medical cannabis programs or access for patients…. We propose a program that is led primarily by TTB, but with an important role for FDA on an ongoing basis."
    - *US Cannabis Council*

Cannabis-Related Banking and Marijuana Legalization

- Until a legislative fix is reached, contradictions of the Federal government's cannabis policy continue to persist.
  - "Once comprehensive, the Federal Government's current approach is a half-in, half-out regime that simultaneously tolerates and forbids local use of marijuana. This contradictory and unstable state of affairs strains basic principles of federalism and conceals traps for the unwary."
    - *Justice Thomas, in a statement respecting petition for writ of certiorari for Standing Akimbo, LLC v. U.S.*
- Contrary to statements during the campaign for the 2020 election, the Biden Administration has not prioritized federal cannabis decriminalization or legalization.

Cannabis-Related Banking and Marijuana Legalization

- Although Democrats control the White House and both chambers of Congress, competing legislative priorities leave a narrow path for legalization before the 2022 midterm elections.
  - "At the highest level, we believe Senate Democrats will prioritize a comprehensive reform package that will burn a fair amount of Congressional clock without attracting sufficient GOP support in the Senate. We could envision a narrower legislative package covering banking and certain restorative justice issues passing in 2022, but we believe the next year in cannabis policy on Capitol Hill will be defined by an unsuccessful attempt at comprehensive reform."
    - *Isaac Boltansky, CompassPoint Research & Trading, LLC*
  - "Senators on the more cautious end of the cannabis spectrum argue that the Senate should vote on a narrower bill first, in the hopes of getting something passed, and avoiding the legislative quagmire that may come with a more broad-sweeping bill. Opponents of this incremental approach argue that a narrow bill won't get the job done, and that the industry, the victims of the War on Drugs, and the public at large want (and deserve) something bolder.... For now, both sides are locked in an attritive war of strategic ideas, while the industry and its millions of enthusiastic supporters wait to see who blinks first."
    - *Feuerstein Kulick LLP*

Cannabis-Related Banking and Marijuana Legalization

Legislative Alternatives

- Although increasingly overshadowed, other legislative alternatives to cannabis reform include the following:
  - The **Secure and Fair Enforcement Banking Act** (**SAFE Banking Act**) would create protections for financial institutions to provide financial services to cannabis-related businesses that comply with state laws.
    - After introducing the CAOA, Senator Booker declared his intent to block any legislation focused solely on cannabis-related banking. He later moderated his comments, stating, “I support the SAFE Banking Act. I think it’s a phenomenal bill . . . For me, a good bipartisan bill like the banking bill is a necessary sweetener to get people to move along on the equitable justice elements that are really critical.”
  - The **Marijuana Opportunity Reinvestment and Expungement Act** (**MORE Act**) would deschedule cannabis on a nationwide basis while accomplishing social justice goals, some shared with the CAOA.
  - The **Strengthening the Tenth Amendment Through Entrusting States Act** (**STATES Act**) would amend the CSA to render inapplicable its prohibitions on cannabis-related conduct that complies with state law.

Cannabis-Related Banking and Marijuana Legalization

- The growth of the cannabis sector has been accompanied with the emergence of new stakeholders, both in the sector and in regional and state markets. The unfolding of those stakeholder dynamics could influence the shape of cannabis legislation, its implementation and the implications for the financial sector.

Our visual memorandum analyzing the SAFE Banking Act, MORE Act, and STATES Act is available here.

Capital and Stress Testing

Federal Reserve Developments on Pandemic Changes: The Federal Reserve continues to give attention to bank capital requirements, including capital actions taken in response to the pandemic.

Developments include:

- Termination of exclusion of reserves held at the Federal Reserve and U.S. Treasury securities from total leverage exposure of the supplementary leverage ratio (**SLR**)
  - On March 30, 2021, the SLR relief expired. The Federal Reserve also announced on March 19, 2021 that it would "soon" seek comment on measures to adjust the SLR, which would "not erode the overall strength of bank capital requirements."
    - At a Federal Open Market Committee meeting on June 16, 2021, Federal Reserve Chair Powell stated, "Because of the substantial increase in reserves, treasuries, and other safe assets in the banking system, the SLR is rapidly ceasing to be the intended backstop for big firms that we want it to be. So we do think it's appropriate to consider ways to adapt it to this new high reserves environment, and we're looking hard at the issue."

Capital and Stress Testing

- One option that the Federal Reserve could consider is a permanent exclusion from the SLR denominator for reserves and potentially U.S. Treasury securities, along with adjusting the SLR minimum and buffer requirements.
  - A similar proposal has been floated by some, including Nellie Liang, now the Under Secretary for Domestic Finance at the Treasury Department.*

- Termination of supervisory limitations on dividends and share repurchases for banking organizations subject to the stress capital buffer
  - On June 30, 2021, the Federal Reserve's temporary supervisory limitations on dividends and share repurchases for banking organizations subject to the stress capital buffer, which were put in place during the pandemic, expired.
    - Large firms will remain subject to the normal restrictions imposed by the capital regulatory framework, including the stress capital buffer.

* Nellie Liang & Patrick Parkinson, *Enhancing the Liquidity of U.S. Treasury Markets Under Stress*, Brookings Institute (Dec. 16, 2020)

Capital and Stress Testing

Tailoring: Both Chairwoman Waters and Chairman Brown have expressed support for changes to the application of the SLR, LCR and NSFR requirements and reinstating the CCAR qualitative objection, all of which would require amendments to the relevant final rules.

- While legislative change is unlikely, Chairwoman Waters and Chairman Brown may pressure the U.S. banking agencies to amend the regulatory thresholds and criteria for application of certain prudential requirements above the statutory thresholds.

Stress Testing and Capital Planning: Changes to stress testing and capital planning requirements might include:

- More severe stress scenarios, which could have the effect of increasing firms' stress capital buffers
- Possible return of the formal qualitative objection to capital plans

Capital and Stress Testing

G-SIB Requirements: Changes to the regulations applicable to G-SIBs could include:

- Adjustments to the factors underlying G-SIB surcharge scores, including further emphasis on the short-term wholesale funding factor and the possibility of a more graduated surcharge structure (i.e., reducing cliff effects)
- Increased external TLAC requirements
- New internal TLAC requirements

Other Initiatives: There are a number of pending rulemaking initiatives on the banking agencies' agenda, including:

- Finalization of the implementation of Basel III, including significant amendments to the market risk capital rule (Fundamental Review of the Trading Book)
  - On May 25, 2021, Federal Reserve Vice Chair for Supervision Quarles said that "tailoring the regulatory framework will remain a principle that we have in mind as we come out with proposals to implement the final pieces of Basel III."

Capital and Stress Testing

- Potential deployment of the countercyclical capital buffer (**CCyB**) in BAU as a means of stimulating lending in stress
  - On June 3, 2021, Federal Reserve Vice Chair for Supervision Quarles stated, "The Federal Reserve should only turn on the CCyB in times of significant irrational exuberance; for example, in the face of a self-reinforcing cycle of borrowing and asset prices of the kind we saw in 2004–06. Yet, in my view, our through-the-cycle capital levels...in the United States have been set so high, that our CCyB is effectively already 'on.'"
  - On March 1, 2021, Federal Reserve Governor Brainard stated a different view: "Over a longer horizon, changes in the economic environment associated with low equilibrium interest rates, persistently below-target trend inflation, and low sensitivity of inflation to resource utilization could be expected to contribute to a low-for-long interest rate environment and reach-for-yield behavior. In these kinds of environments, it is valuable to deploy macroprudential tools, such as the countercyclical capital buffer, to mitigate potential increases in financial imbalances."
- Potential changes to capital requirements related to climate change initiatives
  - Refer to slides 6 - 10 for more information on climate change initiatives, including potential changes related to prudential capital requirements.

Capital and Stress Testing

- Refinement, finalization and implementation prudential capital and liquidity treatment of cryptoasset exposures
  - The Basel Committee published a preliminary proposal for the prudential treatment of cryptoasset exposures of banks and other institutions subject to the Basel capital framework in June 2021.
  - The consultation:
    - Set out guiding principles for the prudential treatment of cryptoasset exposures
    - Proposed a classification system for categories of cryptoassets for purposes of the prudential framework
    - Proposed capital and liquidity requirements and supervisory expectations for banks that engage in cryptoasset activities
  - As proposed, the consultation would impose significant responsibilities on banks for assessing and monitoring the appropriate classification of cryptoasset exposures and, while generally applying elements of the existing Basel capital framework, would adopt a conservative approach to the proposed capital and liquidity requirements applicable to these exposures.
  - **Our visual memorandum analyzing the Basel Committee's consultation is available here.**

Securities Market Structure

General Outlook: Regulatory change to securities market structure and practices is a high priority for the SEC under Chair Gensler and the Treasury under Secretary Yellen, especially for retail public equity trading and U.S. Treasury markets. In August 2021, the SEC issued a request for comment on "digital engagement practices" by broker-dealers and investment advisers, such as so-called "gamification" of trading, and the use of technology such as artificial intelligence and machine learning.

Our client update, "*It's all fun and games: SEC requests information on digital engagement practices*," is available here.

Equity Market Reforms: In light of the significant uptick in stock trading by retail investors in 2020 and 2021, particularly in "meme" stocks, SEC Chair Gensler has expressed concerns over broker-dealers' compliance with their best execution obligations and concentration of order flow within a small number of market makers, particularly given current payment for order flow practices and off-exchange equity trading.

- Chair Gensler has stated that he has asked SEC staff to consider whether the current equity market structure best promotes efficiency and competition and has indicated that rulemaking in this area would be on the horizon.
- Potential rulemaking could involve further SEC rules or guidance on payment for order flow, best execution, and how the national best bid and offer is calculated.

Securities Market Structure

Treasury Market Reforms: In March 2020, the onset of the COVID-19 pandemic triggered a significant pricing disruption in the U.S. Treasury market as many investors sought to liquidate holdings of Treasuries faster than Treasury dealers were willing and able to accommodate.

- Several potential Treasury market reforms have been suggested by market participants, including the G30 (our public memo on the relevant July 2021 G30 report is available here). These include:
  - A standing repo facility that could provide backstop repurchases during periods of stress
  - Increased central clearing in Treasury cash and repo markets
  - Modifications to the supplementary leverage ratio calculation to avoid discouraging banks from providing liquidity in Treasury markets
  - SEC review of prudential safeguards at broker-dealers in U.S. Treasury securities and Treasury repos that are not affiliated with banks
  - Expansion of the TRACE reporting system to capture all transactions in U.S. Treasury securities and Treasury repos
- Reform of the Treasury markets is also an area of focus in the academy, including this article forthcoming in the Columbia Law Review and this Vanderbilt Law Research Paper.

Securities Market Structure

- Application of SEC Regulations ATS and SCI to all significant trading platforms for Treasury securities
- An interagency study and reconsideration of all exemptions of Treasury securities from U.S. securities laws

– In September 2021, Chair Gensler announced that the SEC is actively considering recommendations to expand central clearing in cash and repo Treasury market, including those from the July 2021 G30 report. He also stated that he has asked SEC staff to reconsider some initiatives on Treasury trading platforms and to consider whether firms that are significant players in Treasury markets should be required to register as dealers with the SEC.

Securities Market Structure

Federal Reserve Repo Facilities: In July 2021, the Federal Reserve announced the establishment of a permanent domestic Standing Repo Facility (**SRF**), under which the Federal Reserve will conduct daily overnight repo operations against Treasury securities, agency debt securities and agency mortgage-backed securities with a minimum bid rate of 25 basis points, which is higher than the general level of overnight interest rates. The SRF will initially be open only to primary dealers, but on October 1, 2021, certain depository institutions will be permitted to express interest in becoming SRF counterparties.

- The Federal Reserve also announced a permanent foreign and international monetary authorities repo facility, under which the Federal Reserve will enter into overnight repurchase agreements with foreign official institutions against their holdings of Treasury securities.
- Bill Nelson of the Bank Policy Institute noted that the facilities could be a useful tool to lend to banks in a manner that looks and feels different from the discount window, thereby potentially reducing the stigma associated with utilization of such loans, which has impaired the discount window's effectiveness in serving as a source of liquidity in times of stress.

Reforms to Short-Term Funding Markets

More Work to be Done: In the aftermath of the Financial Crisis, regulators sought to decrease reliance on the use of short-term wholesale funding (including money market funds (**MMFs**), repo and commercial paper), and to enhance the stability of short-term funding markets. The COVID-19 shock in the spring of 2020 again revealed vulnerabilities in short-term funding markets, making clear that the post-2008 reforms had not fully achieved their aims and that more needs to be done. There has been bipartisan focus on further reforms, particularly as they relate to MMFs, but no consensus on what reforms in this area of interconnectedness between the banking and nonbanking sectors might look like.

Reform Ideas: In December 2020, the President's Working Group on Financial Markets released a report (**PWG Report**) offering several MMF reform ideas:

- Removing the tie between MMF liquidity and fee and gate thresholds
- Reforming conditions for imposing redemption gates
- Minimum balance at risk (**MBR**) rules, meaning that a portion of a shareholder's recent balances in an MMF would be available for redemption only on a delayed basis
- New or modified liquidity management requirements, including new categories of liquidity requirements or additional Weekly Liquid Assets (**WLAs**) thresholds to augment current liquidity buffers

Reforms to Short-Term Funding Markets

- Countercyclical WLA requirements, under which minimum WLA requirements could be calibrated such that they would automatically decline in certain circumstances, including when net redemptions are large
- Floating net asset value (**NAV**) requirements for all prime and tax-exempt MMFs
- Capital buffer requirements
- Requiring prime and tax-exempt MMFs to be members of a private liquidity exchange bank
- Swing pricing rules, meaning that when a fund's NAV "swings" down, redeeming investors would receive less for their shares, thus imposing costs stemming from redemptions directly on redeeming investors, rather than on other investors in the fund
- New requirements governing sponsor support that would clarify who bears MMF risks by establishing clear rules for when a sponsor would be required to provide support

Reforms to Short-Term Funding Markets

In the months since publication of the PWG Report, other influential persons and groups have endorsed ideas similar to those in the PWG Report. For example:

- In a March 2021 speech, Federal Reserve Governor Brainard signaled support for three MMF reform ideas: swing pricing, MBR rules and capital buffers.
- In June 2021, the FSB released a consultation report on policy proposals to enhance MMF resilience. As discussed in our update, many of these proposals are consistent with those in the PWG Report.
- In a September 2021 Senate Banking Committee hearing with SEC Chair Gensler, Ranking Member Toomey stated his belief that there is "widespread support" for removing the link between MMF liquidity and fee and gate thresholds.
  - Senator Toomey also noted, however, that he did not see a need for "regulatory reforms that would eliminate or reduce the viability of [MMFs] as an investment."

Next on the Agenda:

The SEC's Spring 2021 Regulatory Agenda lists MMF reform as being in the proposed rule stage, with a notice of proposed rulemaking expected by April 2022.

Reforms to Short-Term Funding Markets

Elsewhere in the United States:

- In June 2021 FSOC stated that it intends to "continue to monitor [the SEC's MMF reform] initiative in the broader context of efforts by financial regulators to strengthen short-term funding markets and support orderly market functioning, including during periods of heightened market stress."
- According to FOMC meeting minutes from the July 27-28, 2021 meeting, Federal Reserve staff observed during that meeting that, although U.S. banks hold significant quantities of HQLAs and rely only to a limited extent on STWF, "significant structural vulnerabilities remained at entities such as prime money funds, and new financial arrangements such as stablecoins appeared to have the same structural maturity and liquidity transformation vulnerabilities but with less transparency and an underdeveloped regulatory framework."
- On a global level, the FSB is due to produce a final report on MMF reform policy proposals by October 2021.

BSA / AML

General Outlook: Regulatory change to the Bank Secrecy Act (**BSA**)/anti-money laundering (**AML**) regime remains a high priority. Himamauli "Him" Das became Acting Director of FinCEN on August 3, 2021.

Legislative and Regulatory Changes: The Anti-Money Laundering Act of 2020 (**AMLA**) is the most important BSA/AML legislation in years and could have a significant impact on AML compliance and supervision once it is fully implemented.

- The legislation's ultimate impact will be determined by implementing regulations to be issued by the Treasury Department and other government stakeholders and which are not expected in the near term.
- Once implemented, AMLA will affect banks' and other financial institutions' AML compliance obligations and the way they are evaluated through:
  - Issuance of national AML and countering the financing of terrorism (**CFT**) priorities
  - The creation of a national beneficial ownership registry maintained by FinCEN
  - Pared back beneficial ownership requirements applicable to banks and other covered institutions
  - Streamlined Suspicious Activity Reports
  - Codification of the BSA's applicability to virtual currency

Our visual memorandum on AMLA is available here.

BSA / AML

Continuation of Ongoing AML/CFT Reform Efforts: Initiatives begun in 2020, such as FinCEN's ANPR on Program Effectiveness and significant changes to the Travel and Recordkeeping Rules, are continuing despite new Treasury leadership. FinCEN, pursuant to AMLA, released the first national priorities for AML/CFT policy (the Priorities) on June 30, 2021. FinCEN must issue implementing regulations by December 27, 2021, and to remain on schedule for this deadline should issue a proposed rule early this fall.

Even though banks are not required to incorporate the Priorities into their risk-based BSA compliance programs until the effective date of the final implementing regulations, financial institutions should start considering how they will incorporate the Priorities into their risk-based BSA compliance programs, per guidance in the interagency statement released with the announcement of the Priorities. The Priorities include:

- Corruption
- Cybercrime, including relevant cybersecurity and virtual currency considerations
- Terrorist financing
- Fraud
- Transnational criminal organization activity
- Drug trafficking organization activity
- Human trafficking and human smuggling
- Proliferation financing

BSA / AML

No-Action Letter Process: On June 30, 2021, FinCEN also issued a report (the **No-Action Report**) on its assessment of whether it should establish a no-action letter process to respond to inquiries concerning the application of the BSA and other AML laws and regulations to specific conduct. While FinCEN concluded that a no-action letter process would complement its current forms of regulatory guidance and relief, the independent authority of other Federal functional regulators to enforce the BSA may limit the usefulness of no-action letters issued by FinCEN.

Our client update on the Priorities and the No-Action Report is available here.

Beneficial Ownership Registry: On April 5, 2021 FinCEN published an ANPR to begin the rulemaking process to implement the beneficial ownership reporting provisions of the Corporate Transparency Act (**CTA**) , with the comment period closing on May 5, 2021. The CTA discourages the use of shell corporations to disguise and move illicit funds, therefore it requires legal entities to report beneficial ownership information at the time of formation or registration. FinCEN will maintain this information in the Beneficial Ownership Registry (the **Registry**). FinCEN must finalize the rule by January 2022.

BSA / AML

AML Supervision and Enforcement: AML is likely to continue to be a high priority for the financial regulators and, while overall enforcement numbers have been down in recent years, regulators, especially the New York State Department of Financial Services, will not hesitate to use their enforcement powers in cases involving serious AML program breakdowns.

Greater scrutiny of Fintechs/Crypto: Greater regulatory scrutiny for AML compliance is expected for Fintechs (especially payments-related) and crypto firms as they assume an increasingly important role in financial services.

- For example, on August 10, 2021, FinCEN and the CFTC announced that the agencies has assessed a $100 million civil money penalty against BitMEX for, among other things, a failure to establish a BSA/AML compliance program. Our memo on the BitMEX enforcement action is available here.

Community Reinvestment Act

Another Shot at Harmonizing:

- There is renewed hope of a harmonized interagency approach under the Biden Administration—the Federal Reserve, FDIC and OCC issued an interagency statement stating that they are committed to working together to jointly strengthen and modernize regulations implementing the CRA.

Building on Federal Reserve Proposal:

- Acting Comptroller Hsu stated that any joint rulemaking should build on the Federal Reserve's September 2020 proposal, which addresses some of the main criticisms of the OCC rule related to CRA scoring, data collection and assessment areas.
  - *CRA Scoring*: The Federal Reserve proposal would score retail lending and community development performance separately, while the OCC's rule uses a single metric.
  - *Data Collection*: The Federal Reserve's proposed metrics would rely on existing data while the OCC's rule requires banks to submit new compliance data.
  - *Assessment Areas*: The Federal Reserve proposal requested feedback on a number of different assessment area options, but is skeptical that the OCC's deposit-based assessment areas for certain institutions would adequately address the reinvestment needs of affected communities.

Community Reinvestment Act

Climate Resiliency:

- In February 2021, the NYDFS issued guidance that allows banks to earn credit under New York's CRA by financing activities that bolster climate resiliency in low- to moderate-income communities. Based on the Biden Administration's current priorities, a similar expansion of qualifying activities may occur on the national level.
- Furthermore, there has been discussion of legislative expansion of the CRA to include investments promoting climate resiliency (see, e.g., Marilyn Waite's March 2021 testimony to the Senate Banking, Housing and Urban Affairs Committee). For further discussion of climate initiatives, see the Climate Change section at slides 6 - 10.

Timing:

- In the Spring 2021 Unified Regulatory Agenda, both the Federal Reserve and the OCC included the CRA in their lists of Long-Term Actions, which indicates that revisions to the CRA are under development.
- On September 9, the OCC issued a proposal to rescind its 2020 CRA rule—a necessary step toward building an interagency approach—with the aim of having it fully repealed by January 2022. Comments to the proposal are due by October 29.

Antitrust

President Biden has announced that his Administration will prioritize steps to "address overconcentration, monopolization, and unfair competition in the American economy" and has issued an executive order on Competition (the **Competition Order**) on July 9, 2021. With respect to banking and consumer finance, the Competition Order:

- Encourages the Attorney General, in consultation with the Chairman of the Federal Reserve, the Chairperson of the FDIC, and the Comptroller of the Currency to adopt a plan for the revitalization of merger oversight under the Bank Merger Act and BHC Act. Action is required by January 5, 2022.
- Directs the Secretary of the Treasury to submit a report assessing the effects on competition of large technology firms' and other non-bank companies' entry into consumer finance markets. Action is required by April 5, 2022.
- Encourages the CFPB to consider:
  - Commencing or continuing a rulemaking under section 1033 of the Dodd-Frank Act to facilitate the portability of consumer financial transaction data so consumers can more easily switch financial institutions and use new, innovative financial products
  - Using its UDAAP authority to ensure that actors engaged in unlawful activities do not distort the proper functioning of the competitive process or obtain an unfair advantage over competitors who follow the law
- References the "pro-competition" jurisdiction and objectives of the CFPB and directs the Chair of the newly-formed White House Competition Council to invite the Director of the CFPB to participate in the Council to the extent consistent with the CFPB's statutory authorities and obligations.
  - This invitation is not extended to the prudential banking regulators.

Our client update on the Competition Order is available here.

FDIC Remote Exams

Overview: The digital era practice of partly remote examinations was accelerated by the COVID-19 pandemic, which required regulators to adjust to an entirely remote environment. Regulators are looking to the lessons of the past 18 months to help shape their future approach. The FDIC has begun its retrospection with a Notice and Request for Information (**RFI**) this summer and we can expect other regulators to either follow or track closely the answer to the FDIC RFI.

FDIC: The FDIC's RFI asks state non-member banks to respond to questions about the FDIC's supervisory approach to examinations during the pandemic, including on-site and off-site activities, use of technology, and communication methods.

- Some of the considerations between on-site and remote examinations include the examiners' ability to access real-time information off-site, reductions in the travel commitments and time that examination teams spend on-site, the bank's ability to develop relationships and communicate with examiners without face-to-face interactions, and technological difficulties in sharing data and exam files digitally.
- We believe that some type of hybrid model, with tailoring depending upon the size and complexity of the bank is a likely path forward.
- Comments are due by October 12, 2021.

FFIEC Authentication and Access Guidance

Guidance: In August 2021, the FFIEC issued guidance providing financial institutions with examples of effective authentication and access risk management principles and practices for accessing digital banking services and information systems. The guidance:

- Describes expanded threats to digital access points, including due to increased remote access by customers and users, and the use of third-party data aggregators and cloud services, and emphasizes that previously effective authentication controls may no longer be effective
- Provides numerous examples of risk management practices related to access management, authentication and supporting controls
- Recommends the use of (1) layered security that incorporates multiple preventative, detective and corrective controls, (2) multi-factor authentication, and (3) monitoring, activity logging and reporting processes and controls to identify attempts at, or actual, unauthorized access
- Discusses the use and development of user and customer awareness and education programs about digital authentication and access risks

Regulation Best Interest and its Variants

Regulation Best Interest: The SEC adopted Reg BI in June 2019, requiring broker-dealers and their associated persons, when making a recommendation to a retail customer, to act in the best interest of the retail customer at the time the recommendation is made.

- Compliance was required by June 2020 and included additional obligations relating to disclosure, a standard of care, conflicts of interest, policies and procedures.
- The SEC has so far adopted a measured approach to implementation and enforcement of Reg BI. Initial examinations have focused on "assessing whether firms have made a good faith effort to implement policies and procedures reasonably designed to comply" with Reg BI.
- SEC Chair Gensler intends to take a stronger approach, stating in May 2021 that "We're going to vigorously get the most out of Reg BI, but we're also going to evaluate . . . If it's not serving the purpose of investors, then we will update and freshen that rule as well as other rules." Chair Gensler also appointed Barbara Roper, an investor advocate at the Consumer Federation of America that has criticized Reg BI as "too weak and undefined," as a Senior Advisor.

Regulation Best Interest and its Variants

State Law Analogues. 23 states, by one count, as of July 2021 have proposed or adopted best interest requirements or standards of fiduciary conduct that are similar to Reg BI, and potentially more stringent.

- After Massachusetts filed an administrative complaint in December 2020 alleging that Robinhood had violated its state law fiduciary duty rule, Robinhood responded in April 2021 by filing suit in MA state court, asserting, among other arguments, that the MA fiduciary duty rule is preempted by Reg BI and thus invalid. The court's decision is likely to serve as a bellwether for similar rules in other states.

DOL fiduciary rule. The Biden Administration will begin a new chapter in the long and tortuous history of the DOL fiduciary rule. After the Fifth Circuit had vacated an earlier, Obama-era version of the fiduciary rule in 2018, the Trump-era DOL in June 2020 proposed and in December 2020 finalized a more industry-friendly version of the rule, which took effect in February 2021.

- The now-effective DOL fiduciary rule reinstates the five-part test for defining an investment advice fiduciary that had previously been in effect since 1975, which many regard as impeding DOL enforcement due to its complexity.
- The DOL concurrently adopted a new exemption for certain categories of conflicted investment advice while also clarifying that fiduciary requirements may apply to recommendations to roll assets out of an ERISA-protected plan into an IRA.
- Though some were surprised that the incoming Biden Administration did not prevent the 2020 rule from taking effect, the DOL under new leadership in April 2021 announced its intent to amend or revoke many of the Trump-era changes through notice-and-comment rulemaking.

Digital Assets

Bank Regulation. Traditional financial services firms continue to seek onramps to the sector as digital assets move into the mainstream. A lack of regulatory clarity risks limiting the ability of these legacy financial institutions to engage in the same types of activities. Regulators and Congress are focused on all aspects of digital assets, with a fair amount of activity expected in the fourth quarter of 2021:

- The Federal Reserve is expected to publish a long-awaited paper in September on the risks and benefits associated with cryptocurrencies, stablecoins and central bank digital currencies (**CBDCs**). The Federal Reserve Bank of Boston in collaboration with MIT is also expected to release a paper on a hypothetical CBDC in the coming weeks.
- The President's Working Group on Financial Markets (**PWG**) is expected to release a report on a comprehensive framework for stablecoins, also in the coming weeks. The FSOC also may be reviewing whether stablecoins are systemic activities**,** as described by anonymous government sources to Bloomberg. See following slides for more details on stablecoin developments.
- In a speech on September 21, Acting Comptroller Hsu signaled both skepticism and openness to digital assets. He labeled some innovation as "fool's gold" and suggested that claims of financial inclusion had been overstated. He also noted, "If you apply the lessons from the 2008 crisis—anchor innovation in clear purpose, foster an environment for skeptics to speak up, and follow the money—the risks of fool's gold can be mitigated and the real promise of blockchain innovation can be achieved."

Digital Assets

Bank Regulation.

- The FDIC has issued a request for information about current and potential digital asset activities at insured depository institutions. In addition to questions regarding potential use cases, the FDIC is seeking to understand whether traditional bank supervision and existing compliance frameworks are sufficient to address the risks posed by digital asset products and services, signaling a potential future area of regulatory focus.
- The Basel Committee on Banking Supervision (**BCBS**) in June 2021 published a proposal for the prudential treatment of cryptoassets. The BCBS consultation is based on three general principles:
  - **Same risk, same activity, same treatment**. Prudential regulation of cryptoassets should be technologically neutral and based upon the risks and functions of cryptoassets.
  - **Simplicity**. Given the newness of cryptoassets, the prudential frameworks focuses on simplicity and the "cautious" treatment of cryptoasset exposures.
  - **Minimum standards**. The BCBS recommendations are meant to provide minimum standards, with national jurisdictions being free to adopt more stringent requirements in implementing the standards.

Digital Assets

Taxes.

- **Tax Rules:** On September 13, the House Ways & Means Committee released legislative language and summaries of tax provisions as a way of paying for its $3.5 trillion budget proposal. The first proposal would expand the scope of the "wash sale" rules, which currently apply only to stock, securities and certain related derivatives, to digital assets. The wash sale rules generally prevent a taxpayer from recognizing a loss on the sale of an asset if the taxpayer acquires a substantially identical asset within a period beginning 30 days before and ending 30 days after the sale. The second proposal would expand the scope of the "constructive sale" rules, which currently apply only to stock, securities and certain partnership and trust interests, to digital assets. The constructive sale rules cause a taxpayer to have a deemed disposition of an appreciated financial position if the taxpayer enters into certain hedging transactions (e.g., a short sale against the box) with respect to the appreciated financial position.
- **Tax Reporting:** On August 10, the Senate passed its infrastructure bill containing provisions that would require cryptocurrency trading platforms and other firms to report digital asset transactions to the IRS, similar to the rules in place for stock brokers. The bill is now pending in the House, where a bipartisan group of House lawmakers, with the support of cryptocurrency lobbyists, are rallying to scale back the cryptocurrency tax rules in the infrastructure bill. If the bill is amended in the House, it will then be sent back to the Senate.

Digital Assets

Legislation.

- **Republican Minority Ideas and Proposals:** U.S. Senate Banking Committee Ranking Member Pat Toomey (R-Pa.) announced on August 26, that he was soliciting ideas and legislative proposals to ensure federal law supports the development of emerging cryptocurrency and open blockchain network technologies while continuing to protect crypto investors. Potential topics that proposals should address include stablecoins, custody regulation, decentralized finance (**DeFi**), and removing existing regulatory ambiguities related to cryptocurrency.

Digital Assets

Application of Securities Laws to Digital Assets. Gensler likened the cryptocurrency market to the "Wild West," stating that "we just don't have enough investor protection in crypto." Much of the early action by the SEC under Chair Gensler seem to be focused on enforcement rather than regulation.

- The SEC and various state regulators are investigating cryptocurrency "yield" products, which offer customers interest on cryptocurrencies they deposit with or lend to cryptocurrency platforms.
- Chair Gensler announced that the Commission may consider granting approval for a 1940 Act ETF that provides exposure to bitcoin. It is not clear whether this signals broader movement to approve ETFs and ETPs that provide digital asset exposure.
- The SEC has also begun investigations in to decentralized finance (**DeFI**) platforms. SEC Chair Gensler in a July 21 speech stated that platforms, "whether in the decentralized or centralized finance space," that offer stock tokens, stablecoins or any other virtual product that provides synthetic exposure to underlying securities "are implicated by the securities laws and must work within our securities regime." The SEC announced its first ever action involving securities on August 6, 2021 when it charged the operators of a DeFi Money Market with misleading investors and selling unregistered securities.

Digital Assets

Application of Securities Laws to Digital Assets.

- Senator Warren and Chair Gensler have been exchanging letters regarding how the SEC expects to regulate digital assets. On July 7, 2021, Senator Warren requested information on the SEC's existing authority to protect consumer investors who participate in cryptocurrency exchanges, and whether additional action was needed from Congress, stating that "the harm to consumers as a result of this under-regulated market are real and continue to proliferate in the absence of effective SEC regulations." Chair Gensler's response on August 5, 2021, described the SEC's existing authority, and the actions it has taken in the area of token-related cases involving fraud or other significant harm to investors, and stated that the SEC "will continue to take our authorities as far as they go," but that help from Congress was needed to address regulatory gaps. According to Chair Gensler, "the legislative priority should center on crypto trading, lending, and DeFi platforms," and that "[r]egulators would benefit from additional plenary authority to write rules for and attach guardrails to crypto trading and lending."
- The SEC's complaint against Ripple Labs and two of its executives, alleging they raised over $1.3 billion through an unregistered, ongoing digital asset securities offering of its XRP token since 2013, may establish an important precedent for the Howey test and the application of securities laws to the sale of digital assets.

Digital Assets

CFTC.

- CFTC Commissioner Berkovitz has criticized DeFi for lacking intermediaries to "monitor markets for fraud and manipulation, prevent money laundering, safeguard deposit funds, ensure counterparty performance or make customers whole when processes fail. He stated that "we should not permit DeFi to become an unregulated shadow financial market in direct competition with regulated markets" and that the CFTC and other regulators need to "focus more attention to this growing area of concern and address regulatory violations appropriately."
- Cryptocurrency platforms are starting to move into regulated cryptocurrency derivatives markets. FTX.US announced a proposed acquisition of LedgerX, a CFTC-registered futures exchange and clearinghouse. Coinbase announced its application to establish a registered futures commission merchant with the NFA and CFTC.

Digital Assets

Stablecoins. In a meeting of the PWG on July 19, 2021, Secretary Yellen stated the "need to act quickly to ensure there is an appropriate U.S. regulatory framework in place."

- A PWG task force led by Treasury Under Secretary for Domestic Finance Nellie Liang is expected to issue a report in October that will contain an outline or at least a direction of travel on a U.S. framework for regulating stablecoins.
- FSOC is increasingly understood to be about to take a deep look at stablecoins and anonymous government sources spoke to Bloomberg about an FSOC examination of stablecoins.
- Senator Warren sent Secretary Yellen, in the latter's capacity as FSOC Chair, a letter urging the federal agencies to develop a "coordinated and cohesive regulatory strategy on cryptocurrencies" with FSOC taking a leading role. Senator Warren warned of the "extent to which cryptocurrencies currently touch or can ripple through nearly every corner of the financial system."
- Vice Chair for Supervision Quarles on June 28, 2021 expressed an optimistic view of stablecoins, stating that "we do not need to fear stablecoins," and that "we must take strong account of the potential benefits of stablecoins, including the possibility that a U.S. dollar stablecoin might support the role of the dollar in the global economy."

Central Bank Digital Currency

Overview: The Federal Reserve and other central banks around the world are actively engaging in work on CBDCs. The Federal Reserve is expected to publish a long-awaited discussion paper in the coming weeks, addressing key policy issues raised by a potential retail U.S. CBDC, as well as digital payments and cryptocurrencies more broadly.

Background:

- CBDC is an electronic form of money that, like paper currency, is a direct liability of the central bank itself, not of an intermediary such as a commercial bank.
- Electronic central bank money already exists in the United States today, in the form of Federal Reserve Bank account balances held by member banks. The key difference is a retail CBDC would be available to the general public.
- CBDCs raise a host of legal and regulatory issues that are the subject of vibrant debate and a growing body of scholarship, including issues of data privacy, combating financial crimes, monetary policy and impact on the commercial banking sector.
- Relatively few central banks, and none in major jurisdictions, have yet decided whether to issue a retail CBDC, but most are conducting research and developing proofs-of-concept while continuing to consider the policy issues.
- Developing a retail CBDC is a “very high priority project” for the Federal Reserve, Chair Powell has stated, though he remains “legitimately undecided” about whether the benefits of a retail CBDC outweigh the risks.

Central Bank Digital Currency

Congressional action: The Federal Reserve's authority to issue a retail CBDC is unclear under existing law, and legislation is likely necessary to authorize and implement it.

- In his testimony before the HSFC on March 22, 2021, Chair Powell has suggested that the Federal Reserve would not act without authorizing legislation: "we would need a buy-in from Congress" before there is a retail CBDC, and he reiterated "you can expect us to move with great care and transparency."
- Three bills to implement a U.S. digital dollar were introduced in Congress in 2020, sponsored by Chairman Brown, Chairwoman Waters and Representative Tlaib, but none have progressed to committee or the floor.
  - The bills have been influenced by the work of a few key legal scholars in this area. We expect that legal and other scholarship, as well as lessons learned from other countries, will continue to shape legislative proposals in the future.
- Both the SBC and the HFSC held hearings in June 2021 to discuss policy issues raised by a U.S. CBDC.
  - For legislators on both sides of the aisle, maintaining the U.S. dollar as the global reserve currency is an important reason to consider a U.S. CBDC, and many cited China's digital yuan project as a concern.
  - The 21st Century Dollar Act, a bipartisan bill introduced in the House in April 2021, would require Treasury to establish a strategy to facilitate the U.S. dollar's continued primacy and submit a report to Congress to that end. The report must address, among other topics, the status of efforts to develop a U.S. CBDC.

Central Bank Digital Currency

Differences of opinion: Public statements by members of the Federal Reserve Board have expressed differing views on the potential benefits of a U.S. CBDC:

- Chair Powell, in a May 2021 video message, outlined the Federal Reserve's official stance:
  - "Our key focus is on whether and how a CBDC could improve on an already safe, effective, dynamic, and efficient U.S. domestic payments system."
  - A potential U.S. CBDC would complement, not replace, cash and current private-sector forms of money.
  - The design of CBDC raises "important monetary policy, financial stability, consumer protection, legal, and privacy considerations" requiring careful analysis, as well as input from the public and elected officials.
- Governor Lael Brainard, in a May 2021 speech, described the potential benefits of a U.S. CBDC, such as financial inclusion and a more efficient payments system, and potential costs and risks, as important reasons why the Federal Reserve is stepping up its research and public engagement on CBDC.
- Vice Chair for Supervision Quarles, in a June 2021 speech, expressed a more skeptical view: "public interest in a 'digital dollar' has reached a fever pitch… I am puzzled, however, as to how a Federal Reserve CBDC could promote innovation in a way that a private-sector stablecoin or other new payment mechanism could not."

Central Bank Digital Currency

CBDC vs stablecoins: A key question in the debate among policymakers, legislators and academics relates to the respective roles of the public and private sector in creating money, and whether private-sector stablecoins may obviate the benefits of a retail U.S. CBDC in addressing shortcomings of the U.S. payments system.

- "In my judgment, we do not need to fear stablecoins," Vice Chair Quarles stated in a June 2021 speech, arguing that "a global U.S. dollar stablecoin network could encourage use of the dollar by making cross-border payments faster and cheaper, and it potentially could be deployed much faster and with fewer downsides than a CBDC."
- In *What is Money?* (July 2021), Jess Cheng and Joseph Torregrossa take a more nuanced view, exploring the U.S. payments system through the lens of "network effects" and "interoperability." They argue that the current U.S. dollar payment system functions well largely because of the Federal Reserve's role as a "network hub," and while innovation has benefited consumers and businesses in the past, there are emerging risks from users' "lack of understanding" of their rights, "lack of clarity" as to regulatory protections, and the resulting "system inefficiencies."
- In *Taming Wildcat Stablecoins* (July 2021), Gary Gorton and Jeffrey Zhang argue that privately issued stablecoins fail to satisfy the "no-questions-asked (**NQA**) principle, which requires that money be accepted in a transaction without due diligence on its value," and CBDCs could effectively substitute as a medium of exchange.

Central Bank Digital Currency

- In *Stablecoins and the Future of Money* (August 2021), Christian Catalini and our own Jai Massari argue that CBDCs are one of three ways that technology can be safely harnessed to create sound money that satisfies the NQA principle, together with “true” stablecoins that are 100% backed by high-quality, liquid assets and “deposit” stablecoins that are demand deposit claims, on blockchain rails, against insured commercial banks.

FedNow

General Outlook: The Federal Reserve intends to build a new round-the-clock real-time payment and settlement service called the FedNow Service to support faster payments in the United States. The 24x7x365 real-time gross settlement (**RTGS**) service for retail payments, which the Federal Reserve expects to be available in 2023, may be accompanied by a separate expansion of hours for the Fedwire Funds Service and the National Settlement Service (**NSS**), which are designed for large-value wholesale payments.

Next Steps

- The Federal Reserve announced in January 2021 that more than 110 financial institutions and processors were participating in the FedNow Service pilot program to test the system's functionality. The same release provided that an "ecosystem participant" pilot program would be launched later in 2021 to solicit feedback from organizations that provide payment systems and services for financial institutions and end users.
- On June 1, 2021, the Federal Reserve released a proposed rule establishing the legal framework for the FedNow Service, modeled on the existing Regulation J provisions that govern transfers through the Fedwire Funds Service.

Bank Charters

General Outlook: The digital transformation and fintech competition can be expected to intensify, which will lead to a continued focus on obtaining both traditional and innovative bank charters through M&A activity or de novo charter applications.

- Fintechs seeking to obtain a bank charter are pursuing various approaches, influenced by their business priorities.
  - The benefits of a bank charter include direct access to the payment system, the ability to use deposits as a low-cost source of funds, the ability to export interest rates, exemption from or preemption of state licensing requirements and, for national banks, federal preemption of state lending laws.
  - Certain bank charter options avoid causing the bank's parent company and the parent company's controlling shareholders to be subject to the Bank Holding Company Act, but these options have their own drawbacks.
  - The broader trend of fintechs expanding into traditional banking services is expected to increase competitive pressures on traditional banks over time.

Bank Charters

- Receptiveness to non-traditional bank charter applications under the Biden Administration has decreased.
- Acting Comptroller Hsu has said he is reviewing all pending chartering decisions and interpretative letters, while deliberately staking out a neutral position on issuing charters to fintechs, stating in his August 3, 2021 testimony before the Senate Committee on Banking, Housing, and Urban Affairs:
  - "[S]ome are concerned that providing charters to fintechs will convey the benefits of banking without its responsibilities. Others are concerned that refusing to charter fintechs will encourage growth of another shadow banking system outside the reach of regulators. I share both of those concerns. Denying a charter will not make the problem go away, just as granting a charter will not automatically make a fintech safe, sound, and fair. I will expect any fintechs that the OCC charters to address the financial needs of consumers and businesses in a fair and equitable manner and support the important goal of promoting the availability of credit."
- Despite the OCC's recent court victory against the NYDFS on procedural grounds, the fintech charter is likely to stay bogged down in court cases for a long time. At stake is whether the emerging fast and real-time payments systems will be subject to 50 different state regulators or a national regulator at the federal level.

Bank Charters

ILCs and Other State Charters

- The FDIC's approval of applications for federal deposit insurance by two de novo ILCs in 2020 suggested that an ILC charter could be one option for fintechs. That said, there have been no new approvals since the Biden Administration's appointees have resulted in a new Democratic majority on the FDIC Board.
  - In January, Japanese e-commerce and financial technology company Rakuten filed its third application for FDIC deposit insurance for a de novo ILC.
  - Political risk is an issue for ILC charters, as reflected by bills that propose to (1) impose a new 3-year moratorium on regulatory approval of deposit insurance for de novo ILCs and certain changes of control of existing ILCs and (2) remove the ILC exemption from the definition of "bank" in the BHC Act.
- We expect novel digital currency-oriented state bank charters such as the Wyoming special purpose depository institution (**SPDI**) charter, the Nebraska digital asset depository institution charter and the proposed Illinois special purpose trust charter to continue to grow in number, but such charters may come under pressure from the SEC or prudential banking agencies.

Bank Charters

OCC Charters

- An alternative to pursuing the special purpose nondepository national bank charter for fintechs is chartering a full purpose national bank that limits its deposit-taking to uninsured long-term certificates of deposit from accredited investors in minimum denominations of $250,000. The CSBS added this alternative charter in its most recent court challenge to the OCC's authority to grant special purpose fintech charters.

Open Banking and Data Access

Potential Expansion of Open Banking

- In October 2020, the CFPB issued an ANPR soliciting public comments on how to implement Section 1033 of the Dodd-Frank Act, which provides for consumer rights to access financial records. This ANPR appears on the CFPB's rule list for the Spring 2021 Unified Regulatory Agenda, which states that the CFPB is reviewing comments and assessing next steps.
- The CFPB ANPR recognizes the following:
  - The providers of consumer financial products and services generally accumulate data about consumers and their use of those products and services.
  - Consumer access to these data allow consumers to manage their financial accounts and can enhance consumers' control of their financial matters.
  - While consumer access to financial records can enable the development of innovative and beneficial consumer financial products, it can also present consumer risks.
- The Competition Order states that the Director of the CFPB is encouraged to consider commencing or continuing a rulemaking under Section 1033 to facilitate the portability of consumer financial transaction data so consumers can more easily switch financial institutions and use new, innovative financial products.

Open Banking and Data Access

- Both banks and the fintechs they compete with are unhappy with the status quo.
  - Banks have long objected to screen scraping, and in response to consumer demand, many have entered into agreements with fintechs such as Plaid to share data through APIs. Such partnerships, nonetheless, can be burdensome from a third-party risk management perspective.
  - Plaid and other fintechs engaged in data aggregation are in favor of becoming regulated and supervised by the CFPB, arguing the benefits of stronger access rights for consumers and better oversight and assurances for the authorized data ecosystem.
  - For Plaid's perspective on why additional CFPB regulation is needed, see Plaid's February 5, 2021 comment letter on the CFPB's ANPR, available here.

Bank Partnerships with FinTechs

Risk Management of Third-Party Relationships

- There is an increasing supervisory focus on bank/fintech partnerships, a trend we expect to continue.
- Only July 12, the Federal Reserve, FDIC, and OCC proposed interagency guidance on how banking organizations should manage the risk associated with their third-party relationships. **Our client update analyzing the proposal is available here.** Comments are due by September 17, 2021.
  - Practically speaking, banking organizations with mature compliance and third-party risk management processes and policies would likely need make relatively minimal updates to their third-party risk management frameworks.
  - The proposal may represent a more meaningful change for smaller institutions currently subject to existing Federal Reserve or FDIC guidance, which is generally less prescriptive and detailed than the proposal and the existing OCC guidance on which it is based.

Focus on Community Banks

- On August 27, the Federal Reserve, FDIC and OCC issued a guide for community banks in conducting due diligence on fintechs.
- On September 9, the Federal Reserve published a paper focused on the strategic and tactical decisions that support effective partnerships between community banks and fintechs.

Federal Reserve Master Accounts

Overview: The Federal Reserve's May 5 proposed guidelines for allowing access to accounts and payments services at Federal Reserve Banks signals a push to provide clarity on when firms with non-traditional bank charters may access the Federal Reserve's master accounts and other associated services, though the guidelines reiterate the legal barriers preventing non-depository institutions, including many fintech payments companies, from opening master accounts.

- The proposed guidelines are built around six principles, founded on an approach of risk management and mitigation.
- The first principle of the proposed guidelines reiterates section 19(b) of the Federal Reserve Act, which provides that only member banks or insured or uninsured depository institutions are eligible to open master accounts, as well as requiring Reserve Banks to consider a depository institution's compliance with the Bank Secrecy Act, AML and sanctions restrictions and other laws – effectively reiterating the bar on non-depository institution payments companies from gaining direct access to the Federal Reserve's payment systems.
- The remaining principles relate to:
  - Safety and soundness of the banking system – i.e., credit, operational, settlement, cyber or other risks to the Reserve Bank
  - Potential risks to the payment system
  - U.S. financial stability
  - Prevention of financial crimes
  - Potential adverse effects on the Federal Reserve's ability to implement monetary policy.

Our May 2021 client update on Federal Reserve master accounts is available here.

Valid-When-Made

General Outlook: In mid-2020, the OCC and the FDIC issued final rules affirming a longstanding "valid-when-made" doctrine, which the 2nd Circuit's 2015 Madden decision did not address, thereby creating uncertainty about the enforceability of a loan's interest rate following the assignment of that loan to a non-bank. The ultimate fate of these rules now rest with the courts.

OCC and FDIC Valid-When-Made Final Rules

- **OCC rule** (June 2, 2020)—A loan that is legally originated by national banks and savings associations continues to be valid upon its transfer, sale, or other assignment, so that interest permissible under 12 U.S.C. § 85 or § 1468(g) before the transfer continues to be permissible after the transfer.
  - This rule is different from the OCC's true lender rule, which was invalidated under the Congressional Review Act, as discussed below on slides 81 - 83.
- **FDIC rule** (June 25, 2020)—Whether interest on a loan is permissible under § 27 of the FDIA is determined as of the date the loan was made and shall not be affected by the sale, assignment, or other transfer of the loan, in whole or in part.

For more on the topic, please refer to our white paper, *Federal Banking Regulators Can and Should Resolve* Madden *and True Lender Developments* (Aug. 14, 2018) and our follow-up client updates: "*The OCC Reaffirms the Valid-When-Made Doctrine*" (June 1, 2020).

Valid-When-Made

Reactions and Further Developments

- In July 2020, state AGs from CA, IL, and NY filed a complaint challenging the final rules on the grounds, among others, that the procedures for preemption were not followed and that the rules were arbitrary, capricious, and an abuse of discretion, creating a regulatory vacuum effectively exempting some market participants from state and federal oversight, and that the OCC rule, in particular, impermissibly seeks to expand National Bank Act preemption beyond national banks.
- In March 2021, the OCC filed a reply in support of its motion for summary judgment in the lawsuit filed by the state AGs.
  - The OCC argues that the challenged final rule is a reasonable interpretation of § 85 of the National Bank Act and should be upheld and that the AGs' opposition is "premised on the erroneous assumption that the [final rule] preempts state law and inappropriately extends § 85 to non-banks."
- Similarly, in May 2021, the FDIC filed a motion for summary judgment in the lawsuit filed by certain state AGs to rescind the rule, arguing the challenged final rule is a reasonable interpretation of § 27 of the FDIA.
- In the midst these ongoing legal battles brought by the state AGs, in April 2021, the MA District Court upheld the validity of the "valid when made" doctrine acknowledging its historical pedigree from the 19th century. *Robinson v. Nat'l Collegiate Student Loan Trust* 2006-2 (1:20-cv-10203).
- Acting Comptroller Hsu indicated that the OCC under his direction will not look to rescind the rule (June 2021).

True Lender

OCC True Lender Rule: In October 2020, the OCC issued a rule that the true lender in a partnership between a federally chartered bank and a fintech firm or other nonbank would be considered the bank if it funds the loans or is named as the lender in the loan documents at the date of origination. 12 C.F.R. § 7.

- The OCC held that its true lender rule should not be subject to the limitations on its authority to preempt state consumer finance laws imposed by the Dodd-Frank Act. OCC Interpretive Letter (Dec. 2020).
- Some welcomed the True Lender Rule, including Republicans and certain financial industry groups, claiming that the bright-line rule would give underserved consumers better access to favorable loan rates. Others, such as Democrats and consumer advocacy groups, strongly opposed it, arguing that the rule would allow predatory lenders to skirt state interest rate limits on loans and prey on vulnerable consumers.

Repeal of OCC True Lender Rule

- On June 30, 2021, President Biden signed a joint resolution of disapproval passed by the House (by a vote of 218-208) and the Senate (by a vote of 52-47) under the Congressional Review Act to repeal.
- The True Lender Rule was nullified and is treated as though if it had never taken effect. The OCC is prohibited from issuing any replacement rule unless it obtains statutory authorization.

For more on the topic, please refer to our white paper, *Federal Banking Regulators Can and Should Resolve* Madden *and True Lender Developments* (Aug. 14, 2018) and our follow-up client updates: The OCC's true lender rule has been repealed (July 1, 2021).

True Lender

Impact of the Repeal of the True Lender Rule

- Marks a return to a world in which true lender issues will be determined on a case-by-case basis, informed by differing state laws and the facts in each particular instance.
  - Certain states (e.g., Illinois and Maine) codified modified versions of the "predominant economic interest" test to determine the true lender subject to state licensing and usury requirements. See here for details.
- Creates uncertainty for investors, banks and marketplace lenders about the ability of loan purchasers to collect, as assignee of loans, the interest rates that had originally been agreed to.
  - In one pre-True Lender Rule instance, that uncertainty led to a state regulator filing a lawsuit against a marketplace lender that was resolved, after several years of litigation, by a settlement in which an out-of-state bank agreed (among other things) to cap the interest rates on all loans it made in the state.
- The practical impact may be limited in today's low interest rate environment but may become more important as interest rates rise. The prospect of federal legislation is unclear, but there have been various proposed bills that would create a federal usury limit while they still have a long way ahead in the legislation process. *See e.g.*, H.R.5050; S.2833; S.1659.

True Lender

FDIC's Position: It seems unlikely that the FDIC would issue a comparable rule for state-chartered banks. FDIC Deputy to the Chairman for Consumer Protection & Innovation Chanin stated in a PLI conference that the FDIA does not grant the same authority to the FDIC as the National Bank Act does to the OCC.