State Bar of California
Business Law Section
Consumer Financial Services Committee

The Essentials Of The New Consumer Financial Protection Laws:
What They Mean For Your Law Practice

A Survey of 2010 Developments in Consumer Finance Regulation

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January 20, 2010

A number of significant legislative changes occurred in 2009 related to consumer finance regulation.

The most significant potential change—the Consumer Financial Protection Agency Act—is still in flux as it moves through the U.S. Senate. However, the version of the CFPA passed by the U.S. House contains several provisions of which every practitioner should be aware. New regulations governing credit card products and overdraft fees will also significantly impact consumer finance practice.

I. The Proposed Consumer Financial Protection Agency Legislation

On December 11, 2009, the U.S. House of Representatives passed the "Wall Street Reform and Consumer Protection Act of 2009," H.R. 4173. This sweeping legislation—a combination of several bills, including a modified version of the Consumer Financial Protection Agency Act, formerly HR 3126—includes broad new regulation of derivatives, executive compensation, systemic risk, investor rights, mortgages, credit-rating agencies, hedge funds and private equity, insurance, and consumer financial protection.

Title IV of the Act (sections 4001 – 4901) provides for the creation of a Consumer Financial Protection Agency (section 4101 – 4703), a new, independent federal agency called the Consumer Financial Protection Agency to oversee virtually every aspect of consumer financial services, including mortgages, credit cards, debit cards, car loans, gift cards, credit

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reporting agencies, debt collectors, and financial advisers. Certain merchants, such as auto dealers and pawnbrokers, would be exempted.

The CFPA as passed by the House is by no means final. The U.S. Senate version is likely to contain significant differences, including the possibility that the powers of the proposed CFPA would be folded into existing agencies, as opposed to being vested in a new agency. However, practitioners should be aware of the major changes called for by the House version.

A. The Consumer Financial Protection Agency

The Act provides for the transfer of broad areas of power to regulate consumer financial protection functions from a variety of federal agencies and the Federal Reserve to the proposed CFPA.

In general, the CFPA would have the authority and accountability to supervise, examine, and enforce consumer financial protection laws, including mortgages, credit cards, student loans, auto loans, payday loans, and more. The agency would be authorized to define and to ban deceptive practices, to regulate new consumer financial products and, to promote "transparency, simplicity, fairness, accountability, and access."

The Act would transfer functions and personnel to the new CFPA and provide for interim powers for the Secretary of Treasury pending the establishment of the CFPA and the completion of the transfer of powers and people.

B. Arbitration Provisions Under the CFPA

Section 4208 of the Act, entitled "Authority to Restrict Mandatory Predispute Arbitration," gives the Director of the proposed Consumer Financial Protection Agency the power to issue regulations to "prohibit or impose conditions or limitations on" a pre-dispute arbitration provision if the Director "finds that such a prohibition or imposition of conditions or limitations are in the public interest and for the protection of consumers."

This provision mirrors the arbitration limiting provisions of the erstwhile "Arbitration Fairness Act," and could effectively prohibit the enforcement of mandatory arbitration provisions in consumer finance agreements.

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C. Preemption Considerations under the CFPA

The Act calls for changes to current laws and regulations regarding preemption of state law (sections 4401 - 4410), providing that state law may be preempted as against National Banks if (a) application of a state law would have a discriminatory effect on national banks in comparison with the effect of the law on a bank chartered by that State; and (b) the Comptroller of the Currency determines by regulation or order on a case-by-case basis that a State law prevents or significantly interferes with the ability of an insured depository institution chartered as national bank to engage in the business of banking; or (c) the State law is preempted by Federal law other than this Act.

The Act does not preempt or alter the applicability of any State law to any national bank subsidiary, affiliate, or other entity that is not an insured depository institution chartered as a national bank. Moreover, the Act directs courts to review any claim that a State law is preempted by this Act as a matter of law and without deference to any agency claim that a state law is preempted under the Act.

II. Credit CARD Act of 2009

In May 2009, President Obama signed the "Credit Card Accountability, Responsibility, and Disclosure (CARD) Act" (the new law contains many provisions from the legislation previously known as the "Credit Cardholders' Bill of Rights.") The CARD Act includes significant amendments to Truth in Lending Act provisions related to interest rate increases, fees, and disclosures for credit card accounts.

A. Highlights of the Legislation

Highlights of specific provisions of the CARD Act include the following provisions:

- Bans rate increases on existing balances due to "any time, any reason" or "universal default" and severely restricts retroactive rate increases due to late payment.
- Revises disclosure and duration of contract terms for the entirety of the first year: issuers may continue to offer promotional rates with new accounts or during the life of an account, but these rates must be clearly disclosed and last at least 6 months.
- Requires issuers to give card holders at least 21 calendar days from time of mailing to pay a monthly bill.
- Requires issuers to apply excess payments to the highest interest balance first.
- Bans practice by which issuers use the balance in a previous month to calculate interest charges on the current month, so called "double-cycle" billing.
- Requires Opt-In to Over-Limit Fees: issuers will have to obtain a consumer's permission to process transactions that would place the account over the limit.

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• Restricts fees on subprime, low-limit credit cards.
• Revises disclosure on fees for gift and stored value cards and restricts inactivity fees unless the card has been inactive for at least 12 months.
• Revises required disclosures of account terms to consumers before consumers open an account, and on statements of the activity on consumers' accounts afterwards.
• Requires issuers to show "the consequences to consumers of their credit decisions."
• Requires issuers to post contracts available on the Internet in a usable format.
• Requires regulators to report annually to the Congress on their enforcement of credit card protections.
• Increases penalties on card issuers that violate these new restrictions.
• Requires card issuers and universities to disclose agreements with respect to the marketing or distribution of credit cards to students.

B. Federal Reserve Rules

Although most provisions of the Credit CARD Act of 2009 become effective in February and July 2010, certain provisions of the Act became effective in August 2009, including:

• Creditors must provide written notice to consumers 45 days before the creditor increases an annual percentage rate on a credit card account or makes a significant change to the terms of a credit card account;
• Creditors must inform consumers in the same notice of their right to cancel the credit card account before the increase or change goes into effect. If a consumer does so, the creditor is generally prohibited from applying the increase or change to the account; and
• Creditors generally must mail or deliver periodic statements for credit cards and other open-end consumer credit accounts at least 21 days before payment is due.

Last week, the Federal Reserve issued its final rules amending Regulation Z pursuant to the Credit CARD Act. (Previous legislative efforts to expedite the effective date of the CARD Act resulted in no changes.) Among other things, provisions of the final rule effective February 22, 2010 will:

• limit the application of increased rates to existing credit card balances;
• require credit card issuers to consider a consumer's ability to make the required payments;
• establish special requirements for extensions of credit to consumers who are under the age of 21; and
• limit the assessment of fees for exceeding the credit limit on a credit card account.

The Fed has posted a summary of the rule changes for consumers.

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III. Federal Reserve Overdraft Rules

The Federal Reserve issued a final rule governing overdraft fees and charges, effective in July 2010. Highlights of the overdraft rule:

• Opt-In. The final rule requires consumers to opt in, or affirmatively consent, to the institution's overdraft service for ATM and one-time debit card transactions, before overdraft fees may be assessed on the account.

• The rule also provides consumers an ongoing right to revoke consent.

• Consumers Covered. The opt-in right applies to all consumers, including existing account holders.

• Conditioning the Opt-In. The final rule prohibits financial institutions from tying the payment of overdrafts for checks and other transactions to the consumer opting into the overdraft service for ATM and one-time debit card transactions.

• Same Account Terms, Conditions and Features. The final rule requires institutions to provide consumers who do not opt in with the same account terms, conditions and features, including price, as provided to consumers who do opt in.

• Mandatory Compliance Date. The mandatory compliance date is July 1, 2010.

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Mr. O'Rielly is a partner in the San Francisco law firm O'Rielly & Roche LLP, a business litigation law firm founded by litigators with extensive experience representing corporate clients throughout California. Mr. O'Rielly focuses his practice on consumer financial services litigation and commercial litigation. He specializes in the defense of financial institutions, including banks, credit card issuers, mortgage lenders, and consumer lenders in litigation involving state and federal consumer finance laws. Mr. O'Rielly has extensive experience defending financial institutions in class actions.

Mr. O'Rielly publishes a blog entitled ***California Consumer Finance Litigation***, (www.consumerfinancelitigation.com) reporting on recent developments and providing analysis of important finance topics related to banking, credit cards, mortgages, and consumer finance statutes and regulations.

Mr. O'Rielly also represents businesses in commercial litigation, including contract disputes, employment litigation, and related issues. He is a certified mediator, focusing on mediating disputes involving consumer finance claims, contract disputes, and unfair business practices.

Education

Cornell University J.D., 1998.
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Bar Admissions

Illinois, 1998; U.S. District Court for the Northern District of Illinois; U.S. Court of Appeals for the Seventh Circuit; California, 2001; U.S. District Courts for the Northern, Eastern, Central, and Southern Districts of California; U.S. Court of Appeals for the Ninth Circuit.

Special Training

Mediation and Conflict Resolution (Certified Mediator). University of California at Berkeley, Extension. Berkeley, California, 2008.

National Institute for Trial Advocacy. Southwest Regional Trial Skills Program. Los Angeles, California, 2003.