Review and Outlook

The State Legislature has recessed after passing a "bare bones" budget but is expected to return in mid-September to address unmet budget and tax goals. Among these is the Bank Tax, which expired Dec. 31, 2000. NYBA is pleased with the progress on several other important items on its 2001 agenda. On June 29, Governor Pataki signed legislation to enact the revised Article 9 of the Uniform Commercial Code in New York as Chapter 84 of the Laws of 2001. This law, which was a top NYBA priority, became effective on July 1 and governs all loans secured by personal property. It has been called the most significant new commercial law in the United States since 1972. The Governor also signed NYBA-initiated legislation extending the commercial mortgage foreclosure law that was due to expire on July 1. This legislation permits nonjudicial foreclosure of commercial mortgages in uncontested situations and also clarifies provisions of the existing law permitting foreclosure on property containing up to 65% residential tenancies in New York City. The Legislature also passed a NYBA-negotiated reform of the State's Principal and Income Act, to be effective Jan. 1, 2002, which authorizes trustees to adjust funds from principal to income or vice versa in order to satisfy the needs of beneficiaries. The bill, which is awaiting signature by the Governor, also establishes an optional 4% unitrust into which trustees may choose to place both existing and newly established trusts.

To date, NYBA has been successful in its attempt to avert final passage of overly restrictive high-cost home lending legislation, most notably a bill strongly supported by the American Association of Retired Persons (AARP). The bill, which adopts the low threshold of five percentage points over the one-year Treasury rate as one of the definitions of a high-cost home loan, prohibits lenders from engaging in a range of practices with regard to high-cost home loans. While the Assembly did pass the AARP-sponsored bill on July 18, the Senate leadership has indicated that it plans to hold hearings on the legislation later this year or early next. Whether or not this bill becomes law, however, it is clear that predatory lending has become a predominant issue on the state and federal level. Several localities nationwide have already passed predatory lending bills, and several amendments to the regulations implementing the Home Owners Equity Protection Act (HOEPA) have been proposed by the Fed. These include a proposal to decrease the trigger interest rate from ten percentage points to eight percentage points over the comparable Treasury rate.

NYBA continued to state its strong opposition to predatory lending and its support for the Banking Department's Part 41 High-Cost Home Loan regulation, (which sets the threshold for high-cost home loans at 9% over comparable Treasury rates for first mortgage loans); however, the association remains concerned that overly restrictive legislation will have the unintended effect of limiting the availability of credit in low- and moderate-income neighborhoods.

As NYBA believes the best way to eradicate predatory lending is through consumer awareness and education, it has launched H.E.L.P (the House Equity Lending Project). The program was developed with a working group comprised of conventional mortgage lenders and faith-based community leaders in New York City and is designed to link potential borrowers with bank lenders in Southeast Queens and Central Brooklyn. This project was announced at a press conference on May 30th with H.E.L.P. advocates Senator Charles Schumer; Reverend David Cousins of Bridge Street AME Church, Brooklyn; Reverend Jesse Jackson; NYBA President Michael P. Smith and Fannie Mae Vice Chair Jamie S. Gorelick. NYBA also is working with a Federal Trade Commission (FTC)-sponsored task force to develop informational tools designed to educate consumers about the perils of predatory lending. The AARP, Better Business Bureau, the National Association for the Advancement of Colored People (NAACP) and the State Attorney General's office, are among the groups also represented on the FTC task force.

NYBA's most pressing regulatory issue was addressed at the Banking Department's June 2001 Board meeting. Superintendent of Banks Elizabeth McCaul presented a proposal to allow State-chartered banks to hold six board meetings a year (a minimum of one each quarter) instead of the ten mandated under current State law. The proposal imposes no requirement on executive committee meetings. This action was in direct response to NYBA's "wild card" petition filed with the Department last year. The proposal was published in the *State Register* on July 3 and public comments are due by August 17. If adopted, the proposed amendment should become effective this Fall.

While the industry was girded for what it thought would be a barrage of bills attempting to impose stricter

(Continued on page 3)

NYBA 2001 LEGISLATIVE AND REGULATORY PRIORITIES

Status Report - July 2001

	Issue	Bill Number	Committee	NYBA Position/Status
÷	Privacy	Numerous	Banks Consumer Protection	Oppose restrictive measures
÷	Predatory Lending	Numerous	Consumer Protection	Oppose restrictive measures
✔	Commercial Mortgage Reform	S.4784-A A.8554-A	Judiciary	Signed as Chapter 76
⇑	*Bank Tax Reform	Budget	Finance Ways & Means	Executive Budget extends Bank Tax moratorium provision for one year
÷	*Environmental Liability Relief for Trustees & Lenders	Budget	Finance Ways & Means	Support
÷	Fee Prohibitions	Numerous	Banks NY City Council	Oppose
✔	*UCC Article 9	S.5054-A A-8959-A	Judiciary	Signed as Chapter 84
⇑	*Trust Agenda			Support
	• Principal & Income Act Reform	S.5531-A/A.9050-B	Judiciary	Passed both Houses
	• Perpetual trusts	S.794/A.7317	Judiciary	
	• Tax relief	S.4781/A.8661	Finance/Ways & Means	
	FEDERAL ISSUES			
⇑	Deposit Insurance Reform		FDIC	FDIC reform recommendations released; NYBA policy filed with national trade groups
⇑	Bankruptcy Reform	H.R.333 S.420	Judiciary	Support - Passed both Houses
⇑	Regulatory Burden Relief *MMDA 24 transfers per month	S.229/S.601 H.R.974	Banking	NYBA petition to Fed for 24 MMDA transfers denied Bill passed House of Reps.
⇑	Real Estate Brokerage & Management		Federal Reserve Board/Treasury Dept.	Support - Comments filed

✔ action completed ⇑ action expected ÷ action stalled *NYBA initiative

If you have any questions on these or other legislative issues, please call Mike Smith at (212) 297-1699, Bill Bosies at (212) 297-1664, or Roberta Kotkin at (212) 297-1684. ▼

Review and Outlook, continued

privacy protections than those of the Gramm-Leach-Bliley Act (GLBA), the message that the current law should be given a chance to work before any new restrictions were added took hold. Consequently, as banks met their first deadline for the mailing of consumer privacy notices under the GLBA, none of the proposed privacy bills gathered much momentum at the State level. On the Federal level the issue continues to percolate and NYBA is closely monitoring the situation.

In Washington, the recent change in the Senate leadership from Republican to Democratic may permit legislation such as the bankruptcy reform bill to proceed. The previous 50-50 split made it impossible for the Senate to appoint conferees on contentious legislation. At this time, it is unclear when the Senate will take up legislation repealing the prohibition of interest on business checking and authorizing 24 transfers per month. NYBA has aggressively sought, over the past five years, a lengthy transition period for any elimination of the prohibition. ■

■ State Legislative Developments

■ SUB-PRIME LENDING

Predatory lending seized center stage this legislative session as the American Association of Retired Persons (AARP) mounted a nationwide campaign to pass legislation which, if enacted in New York, would severely restrict the legitimate sub-prime lending activities of NYBA's member banks. To date, NYBA has been successful in its attempt to avert passage of this legislation in both Houses. The bill was introduced in New York as S.5005(Farley)/A.7828(Greene) and adopts the low threshold of five percentage points over the one-year Treasury rate as one of the definitions of a high-cost home loan. NYBA believes that this legislation, which prohibits lenders from engaging in a range of practices with regard to high-cost home loans is overly restrictive and could therefore inadvertently result in a reduction of credit access in low- and moderate-income neighborhoods. In letters sent to Senate Majority Leader Joseph L. Bruno, Assembly Speaker Sheldon Silver, Senate Banks Committee Chairman Hugh T. Farley and Assembly Banks Committee Chairwoman Aurelia Greene, NYBA President Michael P. Smith explained that the rate threshold established in the AARP-sponsored bill was even more restrictive than those established in other jurisdictions throughout the country, including the threshold set in North Carolina's statute and Philadelphia's ordinance. Importantly, he noted that many lenders in Philadelphia have concluded that they will no longer be able to participate in the "high-cost" home loan market because the thresholds are so unreasonably restrictive. Thus, he reiterated NYBA's concern that passage of such legislation in New York could similarly reduce the availability of credit here. These concerns were further detailed in a Memorandum in Opposition submitted to both the New York Senate and Assembly. While the bill passed the Assembly on July 18, the Senate leadership has indicated that it plans to hold hearings on the legislation later this year or early next.

NYBA would welcome hearings on this matter, and continues to support Part 41 – the Banking Department's high-cost home loans regulation. NYBA also is engaging in several education and other initiatives designed to stamp out unscrupulous lending practices (see Federal Regulatory Developments, page 33).

■ PRIVACY

(For background, please see the February 5, 2001 *Banking Journal*.)

NYBA began the State legislative session anticipating that privacy would once again take center stage in Albany because of the July 1, 2001 implementation date of the privacy provisions (Title V) of the Gramm-Leach-Bliley Act (GLBA). While a number of bills were introduced in both Houses – several of which were passed in either the Senate or Assembly - no significant bills were ultimately enacted. Even NYBA-supported identity theft legislation, which was passed in the Senate (S.694, Goodman) and a companion bill which was passed in the Assembly (A.3648, Lentol), were never reconciled for final passage by both Houses. Thus, the groundwork laid by NYBA last year appears to have convinced legislators that the provisions of the GLBA should be allowed to take effect before creating any new and potentially conflicting State laws.

Only two privacy-related bills - both of which NYBA did not oppose - have, to date, passed both State legislative bodies. In 2000, the "Telemarketing Fraud Prevention Act" (Chapter Law 546) became law. The statute defines certain telemarketing practices as deceptive, and establishes certain licensing and registration

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requirements for telemarketers. Financial institutions and their affiliates are exempt from the licensing and registration requirements. The second law enacted in 2000 (Chapter Law 547) established a “do not call” statewide registry to be maintained by the Consumer Protection Board.

Effective April 1, 2001, The Consumer Protection Board published an Emergency Rulemaking in the *State Register* enacting the provisions of the “do not call” legislation. In a March 9, 2001 memo commenting on the proposed rulemaking, NYBA objected to the fact that the rulemaking was inconsistent with the legislative language in several key areas. Most notably, while the statute provided sharing of state registries between affiliates and included affiliates within the exception for established business relationships, the rule restricts the use of registries by affiliates and excludes affiliates’ relationships from the established business relationship exception. The emergency regulation as originally written became final on April 11, 2001.

■ ATM FEES

(For background, please see the February 5, 2001 *Banking Journal.*)

ATM fees continued to be of concern this year as a result of the introduction in January 2000 of ATM fee ban legislation by New York City Council Speaker Peter Vallone. The proposed legislation continued to be "live" throughout 2000. However, the issue did lose momentum for much of 2000, due, among other things, to an aggressive public relations campaign on the benefits of electronic banking and adequate consumer protections, and, importantly, to the number of positive court decisions throughout the nation affirming federal preemption. In December 2000, however, the issue resurfaced in New York City when, on December 6th, the New York City Council held a hearing on its proposed ATM fee ban legislation.

NYBA President Michael P. Smith testified at the hearing, urging that the proposed legislation not move forward, and emphasizing that a free-market system, devoid of price controls, provides the most conducive environment to the growth of cash machine availability and customer convenience. Mr. Smith also testified that New York State law, which the banking industry supports, mandates full disclosure of ATM fees and provides consumers with the opportunity to cancel any transaction that may incur a fee, and stated that the consumer has many alternatives to ATMs for accessing funds. Finally, Mr. Smith testified that the City ordinance would not apply to ATMs which are owned by non-banks, thus having the possible unintended consequence of limiting access to ATM machines owned by regulated banks, while leaving consumers vulnerable to potentially higher fees for access to a growing number of unregulated ATMs.

In addition to the arguments that Mr. Smith made in his testimony, outside counsel H. Rodgin Cohen of Sullivan & Cromwell testified that the bill violates both the U.S. and the New York Constitutions. It was evident throughout the session that there was no unanimity among the Council members on the legislation and several members were clearly concerned by the legal arguments and the fact that the legislation was directed solely at banking institutions. Since the hearing there has been no further action on this legislation. Moreover, the response following the hearing was generally encouraging with Mayor Giuliani voicing his opposition to the bill. NYBA will continue to work closely with its ATM Task Force and maintain communications with the City Council.

As NYBA monitored ATM fee ban developments in New York City, the association also paid close attention to developments in other jurisdictions where litigation has ensued regarding the rights of municipalities to impose ATM fee bans. In California, legislation arose out of the passage of ordinances in Santa Monica and San Francisco banning convenience fees on ATM use by non-customers. In response to those ordinances, Wells Fargo Bank and the Bank of America (i) filed a suit in Federal court claiming that local ordinances are preempted as to national banks by Federal regulations, and (ii) cut off access to ATM machines to non-custo-mers in Santa Monica. United States District Court Judge Vaughn Walker granted the banks a preliminary injunction in November 1999, which was upheld by the Ninth Circuit on March 31, 2000. In early July 2000, Judge Walker issued a ruling striking down the Santa Monica and San Francisco fee bans. Judge Walker ruled that only the Federal government could impose such restrictions on nationally-chartered banks and thrift institutions, citing the National Bank Act and the Home Owners Loan Act. Nevertheless, both Santa Monica and San Francisco filed notices of appeal on July 14, 2000 and filed their briefs on December 13, 2000. The outcome of these appeals is still pending. (Similar litigation arose in Woodbridge and Newark, NJ, but ended when both municipalities eliminated their ATM fee bans and acceded

to a permanent injunction by the United States District Court in the Fall of 2000.)

Significantly, on April 24, 2000, the U. S. Supreme Court denied *certiorari* in an Iowa case, letting stand a decision by the United States Court of Appeals for the Eighth Circuit allowing national banks to operate ATMs in states where they do not have branches. While the decision does not mirror exactly the ATM fee ban issue, it does reinforce and clarify the rights of national banks with respect to their ATM policies and practices. Thus, it adds strength to the Federal preemption arguments first raised in the New Jersey and California fee ban cases.

Most recently, litigation was filed on April 12, 2001 in Iowa by five national banks, challenging a state statute which was interpreted by the state banking department and the attorney general to ban ATM fees. (*Metrobank, N.A. v. Foster* (D. Ia. No. 4-01-CV-80226)). The state has filed a motion to dismiss the case as not ripe for adjudication, given that, to date, no bank is charging the ATM fees in question, and the state has therefore not threatened any enforcement action. This motion is still pending. (See Significant Legal Decisions, page 23.)

■ MARKETING OF CREDIT CARDS ON COLLEGE CAMPUSES

In January 2001, Senator George D. Maziarz (R-Niagara) introduced legislation that prohibits the direct merchandising of credit cards on the campuses of the State University of New York (SUNY) and the City University of New York (CUNY). Senator Maziarz held hearings on this matter in the Spring in Albany and in Brockport. The Senator, however, postponed at least until September, a New York City hearing originally scheduled for June 2001. This postponement is due at least in part to a letter written by NYBA President Michael P. Smith to Senator Maziarz on April 24, 2001, in which Mr. Smith announced the formation of a special Task Force of banking industry executives to help develop voluntary guidelines for the marketing of credit cards on college campuses. The Task Force is chaired by R. Carlos Carballada, Chancellor Emeritus of the New York State Board of Regents and a Director of M&T Bank. The Task Force is currently drafting these guidelines which are expected to include the principles set forth in the College Credit Card Marketing Industry's "Code of Conduct" for on-campus Credit Card Solicitation. It is expected that NYBA's guidelines will be finalized this Summer.

■ BANK TAX REFORM

The New York bank tax law expired on Dec. 31, 2000. At its December 1999 meetings, the Legislative and Regulatory Policy Committee recommended, and the Board of Directors endorsed, the establishment of a Bank Tax Task Force to study the possible benefits of reforming the bank tax in light of the changes made by the Gramm-Leach-Bliley Act (GLBA), including the possibility of merging the bank tax with the general corporation tax. The Task Force began meeting early in 2000 and identified as its first priority the enactment of "hold harmless" legislation that would permit banks to affiliate with non-banking corporations under the GLBA, without triggering adverse tax consequences under New York's Tax Law for either the bank or the nonbank. When the Budget was enacted in May 2000 it contained two NYBA initiatives:

The "hold harmless" language described above ensured that New York corporations would not be adversely affected by New York's Tax Law for affiliations authorized under the GLBA. In the absence of such a "hold harmless" provision, the Tax Law could impose significant adverse tax consequences on such affiliations by requiring general corporations to be taxed under the Bank Tax. A tax provision establishing such a moratorium was effective immediately. The moratorium applies to both State and New York City taxes.

Since 1998, NYBA has been seeking parity for banks with general corporations in the treatment of income received by mutual funds sponsored or advised by banks (the "Dreyfuss Rule"). Recommendations to both the State Tax Department and New York City Mayor Rudolph Giuliani's Tax Reform Task Force were endorsed by the State and City's Tax Departments. In last year's Budget, the "Dreyfuss Rule" was extended to banking corporations under both the State bank tax law and the New York City bank tax.

Turning to longer-range issues of reforming the bank tax, Task Force representatives participated in a number of meetings with other business interests as part of a Financial Services Modernization Working Group convened by Tax Commissioner Arthur Roth. NYBA's Task Force developed extensive materials for the Working Group describing the benefits and negative features of Articles 32 (the Bank Tax) and 9-A (the General Corporation Tax) and attempted to ensure that the banking industry spoke with one voice in its meetings with the Tax Department. For those purposes, the Task Force included representatives of the Indepen-

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dent Bankers Association of New York State, the Institute for International Bankers and the New York Clearing House Association.

The Task Force also established several subcommittees to analyze key differences between the two Articles of tax and submitted to the State a description of the banking industry's understanding of changes necessary for banks to pay taxes under Article 9-A. In response, the Tax Department decided to develop a discussion draft of concepts that would be included in the legislation to combine Articles 32 and 9-A of the Tax Law. (The Tax Department ran revenue projections with the apparent intent of ensuring that this draft does not increase the industry's overall level of taxation). In the Executive Budget released in January, the Governor proposed extending the Bank Tax, including the financial holding company moratorium provisions, for one year, consistent with NYBA's recommendation. The Task Force held several additional meetings, but has not yet finished its draft. In August, the State Legislature enacted a "bare bones" budget designed to draw Governor Pataki into negotiations on substantially increasing spending and tax cuts. No State tax items, specifically extension of the Bank Tax and financial holding company provisions, were included. The Legislature is expected to return in mid-September to continue working toward a supplemental budget package in which the Bank Tax and financial modernization provisions are expected to be included.

■ UCC AMENDMENTS

The Governor has signed legislation amending the Uniform Commercial Code's Article 9, which brings New York's Article 9 into conformity with the Act recently adopted by the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute. Article 9 governs secured transactions - the process by which lenders secure loans and other obligations with personal property. It also governs the sale of accounts (receivables arising from the sale of goods and services) and chattel paper. The new law expands the scope of the collateral transactions within its coverage, and provides various improvements to the system for the filing of financing statements, including a more centralized regime. Revised Article 9, took effect in 46 states (including New York) and the District of Columbia on July 1. Connecticut is delaying implementation until October 1, 2001 and Alaska, Florida and Mississippi until January 1, 2002. NYBA had made the passage of Revised Article 9 one of its foremost priorities.

In its Memorandum of Support NYBA noted that enactment of Revised Article 9 in New York will serve to avoid confusion and complexity in multi-state secured transactions involving New York parties. This is especially true as Revised Article 9 also changes the choice-of-law rule applicable to perfection and thus the filing location for financing statements, and further changes the rules for determining the debtor's location.

NYBA continues to support New York's adoption of Articles 3 and 4, although significant political problems remain preventing their passage, specifically the issue of check truncation. Although Senate Banks Committee Chairman Hugh T. Farley (R-Schenectady) has introduced legislation to adopt Articles 3 and 4 for several years, Senate Judiciary Committee Chairman James J. Lack (R-Suffolk) continues to express reservations about the information required to be sent to the customer under check truncation in the Uniform Commercial Code. The Assembly reviewed this issue, but no legislation was introduced last session. Most recently, the NCCUSL began a project to revise Articles 3 and 4 further, bringing them up to date with current practices in the payment system. NYBA is awaiting the revised NCCUSL draft of Articles 3 and 4 before continuing to pursue enactment of these Articles.

■ TRUST ISSUES

• **Principal and Income Act Reform** - NYBA aggresively pursued enactment of this legislation in the 2001 session. After extensive meetings and negotiations among the association, legislators, representatives of the Bar and the Surrogate's Association, both Houses passed S.5531-A(Lack)/A.9050-B (Rules, request of Weinstein). NYBA has written Governor Pataki urging that he approve the bill and is planning seminars in September on the issue.

The revised New York State Principal and Income Act:

• Adopts the Uniform Principal and Income Act as the default statute governing the payout of trust income in New York;

• Authorizes trustees to exercise an equitable power of adjustment to move funds from principal to income and from income to principal in order to accommodate the needs of trust beneficiaries;

• Creates an optional unitrust that trustees may elect to govern the payout of trust funds for both existing and newly created trusts; a trustee would have four

years to make an election with respect to existing trusts and two years with respect to newly-created trusts.

Background: In late May 2000, after three years of negotiations, NYBA reached agreement with the EPTL-SCPA Legislative Advisory Committee on a bill to reform the State's Principal and Income Act. The agreed upon draft was substantially revised and incorporated many of NYBA's suggestions. The revised draft was endorsed by the Trusts and Estates Section of the New York State Bar Association and forwarded to the Legislature.

Since beginning its review of the Principal and Income Act, the Legislative Advisory Committee had consistently favored a mandatory unitrust as the default statute to replace the Principal and Income Act. Late in 1999, Assembly Judiciary Committee Chair Weinstein introduced a study bill at the request of the Legislative Advisory Committee, containing the unitrust concept and the Committee asked the Internal Revenue Service to revise its regulations to ensure that a unitrust would not violate the requirements for the marital deduction.

NYBA strongly opposed the unitrust as a default statute (while not objecting to its enactment as a drafter's option) for several reasons: 1, in the absence of revised trust tax regulations on the marital deduction and other issues, a default unitrust could result in adverse tax consequences for grantors or beneficiaries; 2, price controls do not work, and the proposed 4% return standard of the unitrust could be inappropriate in a number of investment climates; 3, New York's becoming the only State to enact a default unitrust could place the State at a competitive disadvantage to those states that use a more flexible investment payout approach; 4, the mandatory unitrust is insufficiently flexible to accommodate the needs of all beneficiaries; and, 5, it is not clear that grantors presented with a choice would select a unitrust to govern payments from their trusts. Although the IRS agreed to consider amending its regulations, it became clear last year that the Legislature was not prepared to enact so important a reform of the State's Principal and Income Act unless there was agreement among the groups chiefly affected. As noted above, this agreement, reached in May 2000, ultimately resulted in the Act's passage in 2001.

• **Trust Income Tax Reform** - In the 2001 legislative session, NYBA-supported legislation to phase down the level of income taxation on resident trusts to the level of tax on non-resident trusts over five years was introduced in both houses of the Legislature with majority sponsorship. In the Senate, Judiciary Committee Chairman James J. Lack (R-Suffolk) introduced S.4781, while Assembly Ways and Means Committee Chairman Herman D. (Denny) Farrell, Jr. (D-Manhat-tan), joined by Judiciary Committee Chair Helene Weinstein (D-Brooklyn), introduced A.8661. Sponsor's memoranda that described the need for trust legislative relief in New York accompanied both bills.

The legislation was shared with the Trust and Estate Tax Committees of the New York City and State Bar Associations, the New York Surrogates' Association, the EPTL-SCPA Legislative Advisory Committee and other interested groups. The bill would result in New York resident trusts being taxed at the same level as non-resident trusts after a five-year phase-down period. Taxes would continue to be levied on New York source income, and the income taxation of New York estates would not be affected. The explicit purpose of the bill, as described in the Sponsor's Memorandum, was to encourage the creation and retention of trusts in New York and the subsequent strengthening of New York's trust industry.

A recent NYBA survey of its member trust companies and bank trust departments found that corporate trustees paid in excess of $80 million per year in fiduciary income taxes. NYBA believes that this number represents the bulk of State revenue from the fiduciary income tax because smaller trusts that are less likely to have a corporate trustee are unlikely to pay any significant amount of fiduciary income tax. Because the fiduciary income tax is collected by New York State as part of the individual income tax, the State Department of Taxation and Finance does not currently have revenue estimates of the cost of reforming the fiduciary income tax, although the association would expect such estimates to be quickly developed if the Legislature were to consider reform. NYBA expects to meet with the Department in the near future to confirm the accuracy of the association's revenue estimates.

NYBA has reviewed the fiduciary income tax laws in a number of other states, particularly those most competitive with New York. The Trust and Investment Division recommends that the level of income tax on resident fiduciary trusts and estates be reduced over five years to the level of tax on non-resident trusts and estates. Essentially non-resident trusts and estates are taxed in New York solely on their New York sources of income (such as income-producing real or tangible personal property). This recommendation would reduce

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the revenue implications for New York State in three ways: 1, it would assure continued revenue from New York-source income; 2, by phasing down the tax over five years, it would reduce the revenue impact in any single year; and, 3, by eliminating incentives for trusts and estates to be moved out of New York, it would increase other sources of revenue, such as the personal income tax and sales and use taxes.

Senator Lack has indicated that he expects a thorough, non-partisan academic study of the revenue and job impact of trust tax reform before considering whether to move the bill. NYBA is evaluating outside consultants with the expertise to conduct such a study.

• **Perpetual Trust Legislation** - (See February 5, 2001 *Banking Journal* for background.) Recognizing the need to make New York's trust industry more competitive, in 2000 Assembly Speaker Sheldon Silver (D-Manhattan) and Judiciary Committee Chair Helene Weinstein (D-Brooklyn) created an unprecedented panel specifically to review all aspects of the Estates, Powers and Trusts Law (EPTL). The panel, a Subcommittee of the Judiciary Committee, is chaired by Assemblywoman Ann Margaret Carrozza (D-Queens), who spoke at NYBA's Annual Trust Conference in October 2000. In her remarks, she pledged that the repeal of the rule against perpetuities would be the first item reviewed by her Task Force. She also acknowledged the problems created by New York's discriminatory treatment of State residents under the trust income tax law.

This legislative session, Senate Judiciary Committee Chairman Lack introduced S.794, which authorizes the creation of perpetual trusts. Assemblywoman Carrozza introduced a similar bill, A.7317, that authorizes perpetual trusts and avoids certain adverse tax consequences that may result. The two bills are currently pending.

• **Environmental Liability Relief** - One disappointment of the 2000 legislative session was the continued failure of the Legislature to address environmental liability relief for lenders and trustees. NYBA has been part of a coalition of business and environmental groups that reached agreement in 1999 on a bill to provide such relief, patterned on the Federal environmental liability relief law adopted in 1996. The legislation also had the broader purpose to encourage the redevelopment of brownfields in New York. The legislation was included in Governor Pataki's 2000- 2001 Executive Budget, and again in the 2001-2002 Executive Budget, as part of a program to reauthorize the State's expiring mini-Superfund bill.

While the Senate has had a long history of supporting this legislation, Environmental Conservation Committee Chairman Richard Brodsky (D-Westchester) has never allowed the bill to come to a vote in the Assembly because of his desire for broader reform of the State's clean air and water laws. Last year, a strong coalition of environmental and business groups, including NYBA, urged consideration of the bill and it was placed on the Assembly Committee agenda. However, Chairman Brodsky again blocked the bill's consideration. NYBA is encouraged that the Governor and a broad legislative coalition have endorsed the bill, making passage at some point in the future more likely. ▼

■ State Legislative Activity

ELECTRONIC BANKING LEGISLATION

■ **Unsolicited E-mail -** S.1452(Rath)/A.7762 (Schimminger) Restricts unsolicited E-mail. **(POSITION UNDER REVIEW)** This bill passed the Senate and is pending in the Assembly Consumer Affairs and Protection Committee.

■ **Electronic Bill Paying** – S. 3479(Stafford)/A.9260 (Rules, Request of Abbate) Authorizes the payment of money owed by the State through electronic transfers **(SUPPORT)** This bill passed the Senate and is pending in the Assembly Ways and Means Committee.

■ **ATM Safety Act Jurisdiction** - S.3816(Goodman)/A.172(Markey) Grants New York City concurrent jurisdiction with the Banking Department over violations of the ATM Safety Act within the City. **(OPPOSE)** This bill is pending in the Senate Banks Committee and the Assembly Codes Committee.

■ **"Talking" ATM Machines** - S.4963(Maziarz)/S.5004(Farley)/A.5797-A(Weinberg) Requires "talking" ATM machines which may be accessed by blind consumers. **(OPPOSE)** NYBA filed a strong memorandum in opposition to the bill. This bill is pending in the Senate Banks Committee and was referred to the Assembly Rules Committee.

■ **911 Buttons and ATMs** - A.1615(Stringer) Requires ATM machines to be equipped with emergency (E-911) buttons to contact the police. **(OPPOSE)** This bill is pending in the Assembly Banks Committee.

PRIVACY LEGISLATION

■ **Identity Theft** - S.218-B(Nozzolio)/A.3198-B (Canestrari) Penalizes identity theft and prohibits the use of social security numbers without affirmative consent and provides customers rights for credit reports. **(Amendments being sought)** This bill was reported from the Senate Finance Committee to the Senate Rules Committee and is pending in the Assembly Consumer Affairs and Protection Committee.

■ **Identity Theft** - S.694-A(Goodman)A.3648(Lentol) Imposes strong criminal penalties for identity theft. **(SUPPORT)** This bill has passed the Senate and is pending in the Assembly Codes Committee.

■ **Opt Out** - S.1467(Velella)/ A.288(Kaufman) Permits consumers to opt out of the sharing of information and preclude entirely the sharing of credit card information and preclude the sharing of certain credit card data, such as account numbers. **(OPPOSE)** This bill is pending in the Senate Consumer Protection and Assembly Consumer Affairs and Protection Committees.

■ **Personal I.D. Information** - S.1468(Vellela)/ A.367(Kaufman) Prohibits any requirement that personal identification information be written on a credit card slip or any attachment thereto. **(OPPOSE)** This bill is pending in the Senate Codes and Assembly Governmental Operations Committees.

■ **Personal Privacy Act of 2002** - S.2330(Morahan)/ A.4230(Kaufman) A broad-based bill that, among other things, regulates unsolicited electronic and other advertisements. **(OPPOSE)** This bill is pending in the Senate Consumer Protection and Assembly Consumer Affairs and Protection Committees.

■ **Privacy** - S.4569(Saland)/A.7827(Tokasz) Prohibits the release of personal information for commercial purposes without customer consent. **(OPPOSE)** This bill is pending in the Senate Consumer Protection and Assembly Consumer Affairs & Protection Committees.

■ **Internet Privacy** - S.4624(Hannon)/A.2358 (Sweeney) Enacts the Internet Privacy Act, providing protection for customers of New York State agencies in dealing with those agencies over the Internet. **(DID NOT OPPOSE)** This bill PASSED BOTH Houses of the State Legislature, but has not yet been sent to the Governor.

■ **Privacy**- S.4631(Farley) Provides for the privacy of financial information in language parallel to that of Title V of the Gramm-Leach-Bliley Act. **(SUPPORT)** This bill passed the Senate.

■ **Information Privacy** - S.4971(Nozzolio)/A.8623 (Rules, Request of Grannis) Creates a new "information privacy" title of the general business law, requiring organizations to protect the privacy of their customers. **(UNDER STUDY)** This bill is pending in the Senate Consumer Protection and the Assembly Consumer Affairs and Protection Committees.

■ **Social Security Numbers** - S.4972(Nozzolio) Prohibits the sale, lease or trade of social security numbers without the informed written consent of individual account holders. **(OPPOSE)** This bill is pending in the Senate Consumer Protection Committee.

■ **Personal Financial Information** - S.5078(Hannon) Prohibits the disclosure of personal financial information by banking organizations without providing notice to the consumer. **(OPPOSE)** This bill is pending in the Senate Banks Committee.

■ **Opt-In** - A.18(Greene) Requires opt-in for banks, securities firms and insurance companies and provides expansive prohibitions on the release of account numbers and certain other customer information. **(OPPOSE)** This bill is pending in the Assembly Banks Committee.

■ **Identity Theft** - A.4939(Pheffer) Criminalizes identity theft and creates an identity theft prevention account and identity theft prevention unit. **(DO NOT SUPPORT)** This bill passed in the Assembly.

■ **Customer Opt-out** - A 7930(Greene) Requires a customer opt-in before financial institutions can disseminate confidential customer information. **(OPPOSE)** This bill is pending in the Assembly Banks Committee.

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■ **Attorney General Privacy Package** - A.8329-8333 (Rules, Request of Pheffer or Markey) Five bills that comprise the Attorney General's privacy package were introduced in the Assembly. The bills deal with internet privacy, unsolicited e-mail, consumers' rights under the Fair Credit Reporting Act, individual reference service providers and marketing list brokers, and telemarketing services. **(OPPOSE)** There are Senate companions to three of the bills. All remain pending in Committee.

RETAIL LEGISLATION

■ **Social Security Check Cashing** - S.91(Maltese)/A.202(Markey) Requires banks to cash properly endorsed Social Security checks for non-customers. **(OPPOSE)** This bill is pending in the Senate Banks Committee and has passed the Assembly.

■ **Dishonored Check Fees** - S.831(Monahan)/A.2561 (McLaughlin) Prohibits banks from charging a fee for the deposit of a check that is subsequently dishonored. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **Credit Card Fees** - S.1059(Santiago)/A.1870 (Lentol) Prohibits credit or debit card issuers from charging interest or fees from card holders who pay off their balances each month. **(OPPOSE)** This bill is pending in the Senate Consumer Protection Committee and passed the Assembly.

■ **Credit Cards at CUNY and SUNY** - S.1232 (Maziarz)/A.6706(Gromack) Prohibits credit cards from being marketed on campuses of the City and State University Systems. **(OPPOSE)** This bill is pending in the Senate Higher Education Committee. This bill was held in the Assembly Higher Education Committee at the sponsor's request. NYBA informed the sponsors in both Houses that it has created a Task Force under the chairmanship of former NYBA Chairman R. Carlos Carballada, Chairman Emeritus of the New York State Board of Regents, to develop "best practices" guidelines for on-campus credit card marketing.

■ **Totten Trusts for Securities** – S. 1389-A (Lack)/A. 7944 (Weinstein) Enacts the Transfer-on-Death Securities Registration Act, similar to Totten trusts for bank deposits, that permits securities to be registered in a form to take effect on the death of the owner. **(SUPPORT)** This bill passed the Assembly and is pending in the Senate Rules Committee.

■ **Banks' Right of Set-Off** - S.1676(Stachowski)/A.2746(Higgins) Limits banks' right of set-off against accounts into which social security or supplemental security income payments are deposited. **(OPPOSE)** This bill passed the Assembly Banks Committee and is pending on the Assembly Calendar and in the Senate Banks Committee.

■ **Day-of-deposit to Day-of-withdrawal Payment of Interest** - S.1817(Padavan)/A.829(Lafayette) Requires the payment of daily interest on certain savings accounts on a day-of-deposit to day-of-withdrawal basis. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **Passbook Savings Fees** - S.1819(Padovan)/A.2562(McLaughlin) Prohibits fees on passbook savings accounts. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **NSF Fees -** S.1847(Maltese)/A.884(Seminerio) Limits Non-Sufficient Funds (NSF) fees to $7.50. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **Leased Motor Vehicle Liability** – S. 3155 (Johnson)/ A.6089(Canestrari) – Transfers the liability for loss or damage to a motor vehicle leased for one year or more to the lessee from the lessor, if certain conditions are met. **(SUPPORT)** NYBA filed a strong memorandom in support of the bill. This bill is pending in the Senate Rules Committee and the Assembly Transportation Committee.

■ **Short-Form Power of Attorney** – S.3193(Trunzo)/ A.5126(Levy) – Incorporates existing provisions of the General Obligations Law that require banks to accept properly executed short-form powers of attorney into the Banking Law, further protecting banks for liability for honoring the form. **(SUPPORT)** The bill has passed the Assembly and is pending in the Senate Rules Committee.

■ **Lienholder Rights** - S.3257-A(Johnson)/A.6491-A (Canestrari) – Protects the rights of lienholders in vessels, aircraft or vehicles seized for use in controlled substances crimes. **(SUPPORT)** This bill has passed both Houses but has not yet been sent to the Governor for his consideration.

■ **Excelsior Linked Deposit Program** - S.3398 (Saland)/A.6769(Schimminger) Makes permanent the provisions of the Program while updating the definition of 'highly distressed area' found in the law. **(Support)** The Governor signed this bill on March 30 as Chapter 14 of the Laws of 2001.

■ **Powers of Attorney** - S.4584(Saland)/A.226 (Kaufman) Imposes substantial penalties for the failure to honor short form powers of attorney. **(OPPOSE)** Click here to read NYBA's Memorandum in Opposition. The bill is pending in the Senate and Assembly Judiciary Committees.

■ **Credit Unions in Banking Development Districts** - S.4632(Farley)/A.966(Lafayette) Includes credit unions in banking development districts, providing them access to State and local deposits and permitting any residents of such districts to be members of credit unions in the districts. **(OPPOSE)** This bill passed the Assembly and is pending in the Senate Banks Committee.

■ **Credit Unions Tax Exempt Status**- S.4637 (Farley)/A.8539 (Rules, Request of Greene) Broadens the tax exempt status of State-chartered credit unions to parallel that of Federal credit unions. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **Community Bank Deposit Program** - S. 4639-A (Farley)/A.9215(Rules, Request of Farrell) – Would establish a community bank deposit program to encourage the State Comptroller and Commissioner of Taxation and Finance to deposit State funds in in-State banks. **(SUPPORT)** This bill has passed both houses of the Legislature, but not yet been sent to the Governor for his consideration.

■ **Credit Unions/Excelsior Linked Deposit Program** - S.4945(Marchi)/A.3550-B(Vann), Authorizes credit unions to participate in the Excelsior linked deposit program. **(OPPOSE)** NYBA filed a memorandum opposing this bill. The bill passed the Assembly and is pending in the Senate Finance Committee.

■ **Local Government Investments** - S.5243(Maziarz) A.5642(DiNapoli) Authorizes local governments to invest in money market mutual funds. **(OPPOSE)** NYBA has filed a memorandum strongly opposing this legislation, pointing out that money market mutual funds would not recycle the deposits in the form of local loans, have no Community Reinvestment Act obligations comparable to commercial banks, and do not provide additional services to local communities. This bill is pending in the Senate Local Government Committee and was reported from the Assembly Local Governments Committee to the Ways and Means Committee.

■ **Credit Card Rates and Fees** - S.1073-A(Fuschillo) Requires the Banking Department to publish on its web site information regarding credit card rates and fees provided by banks. Under the bill, banks will be required to provide a notice on their credit card statements of the availability of this information. **(AMENDMENTS BEING SOUGHT)** This bill is pending in the Senate Rules Committee.

■ **Banking Department Examinations** - S.2840 (Farley) Increases penalties for failure to permit Banking Department examinations. Increases daily fine levels for the first time since 1930. **(DO NOT OPPOSE)** This bill passed the Senate, but has no Assembly companion.

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■ **Fingerprinting Applicants for Bank Charters** - S.3788(Farley) Permits the Banking Department to submit routinely for processing the fingerprints of applicants for banking charters, licenses and changes in control; authorizes the Superintendent to waive the requirement for existing institutions. (**AMENDMENTS BEING SOUGHT)** This bill is pending in the Senate Finance Committee.

■ **UCC 3 & 4** - S.4437(Farley) Updates articles 3 and 4 of the Uniform Commercial Code dealing with negotiable instruments and bank deposits and collections. **(SUPPORT)** This bill is pending in the Senate Judiciary Committee.

■ **NSF Fees** - S.4440(Velella) Limits NSF fees to $15. **(OPPOSE)** This bill is pending in the Senate Banks Committee.

■ **Annual Reporting Requirements** - S.4634(Farley) Reduces annual reporting requirements. **(SUPPORT)** This bill passed the Senate.

■ **Expanding Credit Union's Common Bond** - S.4638(Farley) Permits State-chartered credit unions to add fields of members to their common bond without amending their bylaws or seeking the approval of the Banking Department. **(OPPOSE)** NYBA filed a memorandum strongly opposing this legislation that provides State credit unions with an advantage over Federal credit unions and enhances their competitive advantage over commercial banks. This bill is pending in the Senate Rules Committee.

■ **Unsolicited Checks** - S. 4661(Padavan) – Prohibits credit card issuers from sending blank, loan checks to card holders residing in the State. **(OPPOSE)** NYBA filed a memorandum opposing this legislation. This bill is pending in the Senate Consumer Protection Committee.

■ **Sale of Insurance** - S.5007(Farley) Imposes identical consumer protection requirements in the sale of insurance by licensed lenders, mortgage bankers and other types of lending institutions as currently apply to banks and thrifts. **(DO NOT OPPOSE)** This bill is pending in the Senate Rules Committee.

■ **Non-discrimination** - A.644(Brodsky) Requires that banks providing personal teller service at any of their branches not discriminate on the basis of size of account balance or other factors in providing such service. **(OPPOSE)** This bill was reported from the Assembly Banks Committee and is pending on the Assembly Calendar.

■ **Credit Card Fraud** - A.2093-B(Klein) Requires credit card issuers to implement certain fraud prevention measures. **(OPPOSE)** This bill was reported to the Assembly calendar, where it is pending.

■ **Basic Banking Account** - A.3173(Clark) Increases from eight to 12 the number of basic banking account withdrawals that would be required to be provided without additional charge. **(OPPOSE)** NYBA filed a memorandum strongly opposing this measure. This bill was reported from the Assembly Banks Committee to the Calendar.

■ **Consumer Bill of Rights** - A.5134(Ortiz) Creates a consumer bill of rights. **(OPPOSE)** This bill passed the Assembly Banks Committee and is pending on the Assembly Calendar.

■ **Public Deposits for Thrifts** - A.5639(DiNapoli) Authorizes thrift institutions to compete for public deposits. **(OPPOSE)** NYBA filed a memorandum strongly opposing this measure, which is pending in the Ways and Means Committee. There is no Senate companion.

TRUST LEGISLATION

■ **Fiduciaries' Commissions** - S.438(DeFrancisco) /A.212(Kaufman) Includes both real and personal property, other than specifically bequeathed or devised property, in the base on which all fiduciaries' commissions, other than trustees (such as executors), are computed. Currently, real property is not included in the commission base unless it is sold by the fiduciary. **(SUPPORT)** This bill is pending in the Senate Finance and Assembly Ways and Means Committees.

■ **Trustee Commissions** - S.795(Lack)/A.7792 (Weinstein) Revises trustee commissions under the wills of those dying before August 31, 1956. **(SUPPORT)** Click here to ready NYBA's memorandum in support. NYBA filed a memorandum in support of this bill. The bill has passed both Houses, but has not yet been sent to the Governor for his consideration.

■ **Probate Proceedings** – S.2936(Lack)/A.8357 (Rules, Request of Klein) – Clarifies that parties with no interest in a probate proceeding need not be served, in certain cases. **(SUPPORT)** This bill passed both Houses but has not yet been sent to the Governor.

■ **Trust Powers** - S.2964(Farley)/A.8632(Rules, request of Schimminger) Clarifies that branches of State-chartered banks headquartered outside of New York can exercise trust powers within the State. **(SUPPORT)** This bill passed the Senate and is pending in the Assembly Banks Committee.

■ **Powers of Appointment** – S.3751-A (Lack)/A.7699-A (Rivera) – Authorizes a trustee that possesses an unlimited power to invade principal to appoint assets in trust into further trust without the approval of interested parties. **(SUPPORT)** The bill passed the State Legislature, but has not yet been sent to the Governor. NYBA has written, urging that the bill be signed.

■ **Fiduciary Income Tax Reform** - S.4781(Lack)/A.8661(Rules, request of Farrell) Part of NYBA's trust agenda, this bill reforms the State's income tax on trusts and estates, eliminating the distinction between resident and non-resident trusts and estates over five years. **(SUPPORT)** This bill is pending in the Senate Investigations, Taxation and Government Finance and the Assembly Ways and Means Committees.

■ **Commissions on Charitable Trusts** - S.4782 (Lack)/A.4447(Weinstein) Provides paying a commission to a trustee for distributing the remaining funds in the corpus of a charitable trust to the charity at the termination of the trust and to allocate commissions on charitable trusts 1/3 against income and 2/3 against principal (as with other trusts). **(SUPPORT)** This bill passed the Assembly and is pending in the Senate Judiciary Committee.

■ **Environmental Liability Relief** - S.4788 (Marcellino)A.7498(Lopez) The "brownfields" coalition bill, which provides for environmental liability relief for lenders and trustees. **(SUPPORT)** This bill is pending in the Senate and Assembly Environmental Conservation Committees.

■ **Trial By Jury** – S. 5461 (Lack)/ A. 7791-A (Weinstein) – Provides for a right to a jury trial in cases of disputes over revocable trusts and incorporates by reference provisions regarding wills into revocable trusts. **(OPPOSE)** This bill passed the Assembly and is pending in the Senate Rules Committee.

■ **Debt and Claim Compromise** – S.5514(Lack)/A.7345(Rivera) – Permits an interested party, as well as a fiduciary, to make application to a court to settle a claim or debt against an estate. **(OPPOSE)** This bill passed the State Legislature, but has not yet been sent to the Governor for his consideration.

■ **Principal and Income Act Reform** – S.5531-A (Lack)/A.9050-B(Rules, Request of Weinstein) – A major element of NYBA's trust agenda, this bill reforms the State's 35-year old Principal and Income Act, providing trustees with the authority to equitably allocate funds between principal and income or to elect to place trust assets in a 4% unitrust. **(SUPPORT)** The association wrote strongly in support of this legislation. It has passed both houses but not yet been sent to the Governor for his consideration.

■ **Charitable Trust Disclosure** – S.5611-B(Stafford)/A.871-D(Morelle) – This legislation, which was amended at NYBA's request, provides for new disclosure and regulatory requirements for organizations engaged in fundraising on behalf of charities. It also clarifies reporting requirements for the trustees of charitable trusts. **(SUPPORT)** The bill passed the Assembly and is pending in the Senate Rules Committee.

■ **Perpetual Trusts** - S.794(Lack) Authorizes creation of perpetual trusts. **(SUPPORT)** This bill was reported from the Senate Judiciary Committee to the Rules Committee.

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■ **Fiduciary Liability** - S.4783(Lack) Relieves individual trustees of fiduciary liability for trust decisions delegated to corporate and other trustees. **(SUPPORT)** This bill is pending in the Senate Judiciary Committee.

■ **Perpetual Trusts -** A.7317(Carrozza) A bill authorizing perpetual trusts in New York. **(SUPPORT)** This bill is pending in the Assembly Judiciary Committee.

MORTGAGE LEGISLATION

■ **Mortgage Fees** - S.1816(Padavan)/A.2310 (McLaughlin) Prohibits mortgagees from charging fees for the issuance of a mortgage satisfaction. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **"Home Equity Fraud Act,"** - S.1818(Padavan) A.3717(Clark) Limits practices that could be characterized as predatory lending. **(OPPOSE)** This bill is pending in the Senate and Assembly Banks Committees.

■ **Real Estate Appraisers** - S.2838(Farley)/A.8608 (Rules, request of Schimminger) Permits real estate appraisers to be appointed according to policies adopted by bank boards of directors rather than by the boards themselves. **(SUPPORT)** This bill passed both Houses, but has not yet been sent to the Governor.

■ **Private Mortgage Insurance** - S.4277(Velella)/ A.4716(Grannis), Eliminates payments for private mortgage insurance, under certain circumstances, when the loan to value ratio falls below 75%. **(OPPOSE)** This bill passed the Assembly and is pending in the Senate Insurance Committee.

■ **Commercial Mortgage Foreclosure** - S.4784(Lack) /A.8554(Tokasz) A NYBA initiative, the bill makes permanent the commercial mortgage foreclosure reform law that was scheduled to expire in July and clarifies that the exemption from the law for buildings with more than 65% residential tenancies in New York City is determined with reference to the number of units in the building. **(SUPPORT)** Governor Pataki signed this bill on June 29 as Chapter 76 of the Laws of 2001.

■ **Environmental Liability Relief** - S.4788 (Marcellino)A.7498(Lopez) The "brownfields" coalition bill, which provides for environmental liability relief for lenders and trustees. **(SUPPORT)** This bill is pending in the Senate and Assembly Environmental Conservation Committees.

■ **Title Insurance Agency** - S.4974(Nozzolio)/ A.1832(Lopez) Prohibits mortgage lenders from using the services of a particular title insurance agency. At NYBA's request, the bill was amended to parallel the language in the "wild card" statute. **(SUPPORT)** This bill passed both Houses, but has not yet been sent to the Governor.

■ **High Cost Home Loans** - S.5005(Farley)/A.7828 (Greene) This is AARP-backed legislation that restricts high cost home loans in New York. NYBA filed a strong memorandum in opposition to the bill and has had numerous meetings with legislative leaders on its provisions. **(OPPOSE)** This bill passed the Assembly and is pending in the Senate Banks Committee.

■ **Mortgagee Penalty** - S.582(DeFrancisco) Imposes penalties on mortgagees for failing to provide a mortgage discharge in a timely fashion. **(OPPOSE)** This bill is pending in the Senate Judiciary Committee.

■ **Referral Fees** - S.4431-A (Farley) Prohibits payment of referral fees or other compensation by banks and other lenders to a home improvement contractor unless the contractor is employed by the lender and certain other conditions are met. **(SUPPORT)** This bill is pending in the Senate Banks Committee.

■ **Mortgage Fraud**- S.4640(Farley) Penalizes mortgage fraud; includes overly broad language penalizing lenders if their agents or employees participate in committing fraud. **(OPPOSE)** This bill was referred to the Senate Codes Committee.

■ **Mortgage Loan Payoffs** - S.4659(Padavan) Requires banks to accept payoffs of mortgage loans at any branch. **(OPPOSE)** This bill is pending in the Senate Banks Committee.

■ **Mortgage Broker Regulation** – S. 5598 (Farley) – Expands the authority of the Banking Department over mortgage banking and brokerage practices, including policing for mortgage fraud. **(NO POSITION)** This bill is pending in the Senate Banks Committee.

■ **Third-Party Predatory Lending Practices** – S. 5635 (Smith) – Prohibits the State, public authorities and political subdivisions and districts from engaging in business with financial institutions that engage in predatory lending. **(OPPOSE)** The bill is pending in the Senate Rules Committee.

■ **Debt Collecting Practices -** A.3781(Pheffer) Regulates debt collecting practices and requires additional notices to consumers by debt collectors and restrictions on the actions of "principal creditors." **(OPPOSE)** This bill is pending on the Assembly Calendar.

■ **Discriminitory Practices** - A.4003(Lafayette) Prohibits banking organizations making loans secured by real estate from engaging in underwriting, appraisal or other practices that could have a "discriminatory effect" on any protected borrower class unless the practice is necessary for a legitimate banking purpose. This bill is very troubling because it could force banks to defend underwriting practices. **(OPPOSE)** This bill is pending in the Assembly Banks Committee.

MISCELLANEOUS LEGISLATION

■ **Foreign Bank Bonding Obligations** - S.849 (Balboni)/ A.8991(Rules, Request of Greene) Expands foreign bank bonding obligations to include Sallie Mae and Freddie Mac obligations. **(SUPPORT)** This bill passed the Senate and is pending in the Assembly Banks Committee.

■ **UCC Article 9** - S.1147 (Budget)/ A.1899 (Budget); S. 5404-A (Lack)/ A. 8959-A (Weinstein) – Part of NYBA's 2001 Legislative Agenda, the bill repeals New York's Uniform Commercial Code Article 9, governing secured transactions, and replaces it with the revised and updated Article 9. **(SUPPORT)** Governor Pataki signed S. 5404-A/A. 8959- on June 29 as Chapter Law 84 of the Laws of 2001. The uniform revisions had a nationwide effective date of July 1 and the law has been called the most significant commercial statute since 1972.

■ **Environmental Liability** - S.1148(Budget)/A.2000 (Budget) - Provides protection from liability for lenders and trustees for pollution they did not cause or contribute to. **(SUPPORT)** This bill is pending in the Senate Finance and Assembly Ways & Means Committees.

■ **Taxes** - S.1149(Budget)/A.2001(Budget) - Extends the Bank Tax and Financial Holding Company Moratorium provisions for one year. **(SUPPORT)** This bill is pending in the Senate Finance and Assembly Ways & Means Committees.

■ **Bankruptcy and Mutual Fund Shares** - S.1470 (Velella)/A.382 (Kaufman) - Expands the cash exemption to the State's bankruptcy law to include shares in a mutual fund. **(OPPOSE)** This bill passed the Assembly and is pending in the Senate Judiciary Committee.

■ **Bankruptcy and Credit Reports** - S.1530(Volker)/ A.2390(Eve) - Limits the time period for reporting organizations in bankruptcy on credit reports and prohibits credit reports of bankruptcies that do not identify the Chapter of bankruptcy under which the proceeding was brought. **(OPPOSE)** This bill is pending in the Senate Consumer Protection and Assembly Consumer Affairs and Protection Committees.

■ **Foreign Banks' Personal Loan Limitations -** S.2839(Farley)/A.8609(Rules, request of Schimminger) Conforms foreign banks' personal loan limitations to those of domestic banks. **(SUPPORT)** This bill has passed the Senate and is pending in the Assembly Banks Committee.

■ **Light Pollution** – S. 3368-B (Balboni)/A.5352-B (Grannis) – This bill, principally designed to regulate lighting by State agencies, would create the new offense of "light trespass." It prohibits any person from lighting their property in such a way as to cause glare or hazardous conditions for others. NYBA is working with the Banking Department to use the bill to resolve some of the problems with the lighting provisions of the ATM Safety Act. **(POSITION UNDER REVIEW)** The bill has passed both Houses of the Legislature, but not yet been sent to the Governor for his consideration.

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■ **Subordinate Liens -** S.3401(Johnson)/A.7052 (Schimminger) A bill to subordinate liens for the storage of motor vehicles, boats and aircraft to pre-existing liens unless there is a contract for storage of the items was introduced. **(SUPPORT)** This bill protects the rights of pre-existing lien-holders when vehicles are towed, impounded or otherwise put in involuntary storage. This bill is pending in the Senate and Assembly Judiciary Committees.

■ **Monthly Board Reports** - S.3790(Farley)/A.9147 (Rules, Request of Greene) A Banking Department bill that repeals the requirement that banks must report financial transactions each month to their boards and reduces the number of directors of a banking institution who must be U.S. citizens. **(SUPPORT)** This bill is pending in the Senate Banks and Assembly Rules Committees.

■ **Banking Department Supervisory Powers** – S.3791-A(Farley)/A.9146-A(Rules, Request of Greene) – clarifies the supervisory authority of the Banking Department; NYBA sought amendments which have now been included to protect bank due process rights. **(SUPPORT)** This bill is pending in the Assembly Rules and Senate Banks Committees.

■ **New York City Mutual Fund Investments -** S.3814(Goodman)/A.172(Markey) Permits New York City to invest in certain mutual funds. **(OPPOSE)** This bill is pending in the Senate Cities Committee and in the Assembly Local Governments Committee.

■ **Check Cashing Facilities** - S.5006-B (Farley)/ A.8806-A (Rules, Request of Greene) Originally a bill to subject banks that operate separate check cashing facilities to the geographic restrictions, rate limitations and other restrictions of the check cashers law, it has been materially amended to grandfather all existing bank check cashing operations and to eliminate provisions that would have subjected bank check cashing operations to any provisions of the check cashers law other than geographic restrictions. **(OPPOSE)** This bill passed both Houses and has not yet been sent to the Governor. NYBA expects to write the Governor, respectfully requesting a veto of the bill.

■ **Payday Loans** - S.5008-B (Farley)/A.3645-C(Klein) Authorizes check cashers to make “payday loans” or deferred deposit agreements at annual percentage rates up to 180%. (**NO POSITION)** This bill is pending in the Senate Banks and Assembly Codes Committees.

■ **Credit Union Membership** – S. 5549 (Farley)/ A. 8538-A (Rules, Request of Greene) – Authorizes the addition of new groups to existing credit unions without an amendment to the credit union’s bylaws so long as the group contains fewer than 500 members. **(OPPOSE)** This bill has passed both Houses, but not yet been sent to the Governor for his consideration.

■ **Thrift Holding Company Powers** – S. 5592 (Farley)/ A. 9145-A (Rules, Request of Greene) – This bill provides State-chartered mutual holding companies the same powers as Federal thrifts and holding companies. NYBA submitted an opinion by Nixon Peabody which raises concerns that the bill may authorize evasion of the home office protection statute and may provide mutual holding companies with substantially more expansive powers than financial holding companies. The bill has now been amended to address those concerns. **(NO POSITION)** The bill has passed the Senate and is pending in the Assembly Codes Committee.

■ **Background Checks and Fingerprint Requirements** - S.3788(Farley) A Banking Department bill that provides the Department expanded flexibility with regard to background checks and fingerprint requirements for banking applicants. (**NYBA SOUGHT AMENDMENTS TO RESOLVE DUE PROCESS CONCERNS)** The bill is pending on the Senate Calendar.

■ State Regulatory Developments

■ BANKING BOARD ACTIONS

(For background on the ATM lighting issue, please see the February 5, 2001 *Banking Journal*.)

1. ATM Lighting Standards -- NYBA continues to engage in a dialogue with the New York Banking Department regarding its enforcement of the ATM Safety Act. Numerous NYBA members have expressed concern that they are often cited for violations of the lighting standards, despite their best efforts at compliance and their belief that some of the requirements are disturbing to neighbors and, in fact, may violate local codes. Superintendent of Banks Elizabeth McCaul has repeatedly stated that she has no discretion under the statute to provide flexibility in its administration or enforcement. Progress was made in this regard at the end of the 2000 legislative session, with both the Banking Department and NYBA supporting a technical correction to the ATM Safety Act designed to allow the Banking Department greater flexibility in its enforcement. Although this corrective legislation was debated in the final week of the session, an agreement could not be reached. No such legislation was introduced in the 2001 legislative session.

In the meantime, however, NYBA and its member banks are working with a doctoral student from the Lighting Research Center at Renssalear Polytechnic Institute to try and find a lighting solution that is acceptable both to the banks and the Banking Department. This mission is the subject of the student's doctoral thesis, which NYBA hopes will provide a practical solution to this problem. NYBA expects to have the preliminary conclusions from the Lighting Research Center this Summer. NYBA is coordinating these research efforts with the Banking Department.

A potential new “wrinkle” in this issue may be added as a result of the passage in June 2001 of legislation designed to control light pollution. (A.5352-B(Grannis)/ S.3386-B(Balboni).)

Among other provisions, this legislation prohibits any person from committing “light trespass” defined as operating any light fixture in a way that casts glare on any other property so as to reduce privacy, hinder sleep or detract from the appearance of an area in violation of rules and regulations to be adopted by the Commissioner of the Department of Environmental Conservation. NYBA believes that this bill will conflict with the ATM Safety Act. The sponsors have said they intend to write the Governor to suggest that it was not their intent to interfere with the ATM Safety Act. Nevertheless, if this bill is signed by the Governor its provisions may create tension between the strict standards for lighting set forth in the ATM Safety Act. NYBA is working with the Banking Department to resolve conflicts between the ATM Safety Act standards and the light pollution regulation.

2. **Wild Card Petition - Number of Required Board Meetings --** On June 15, 2001 the Banking Board approved to issue for public comment a proposed amendment to Part 6 of the General Regulations of the Banking Board, which would permit the boards of directors of State-chartered banks and trust companies that are well-capitalized, well-managed, and have been in existence for more than five years to meet a minimum of six times per year – as opposed to the ten times per year currently mandated by Section 7010 of the Banking Law. Moreover, the current requirement in Section 7010 that the executive committee meet at least once in each thirty day period during which the board does not meet, has been eliminated for qualifying institutions. This action was in direct response to NYBA’s “wild card” petition which was filed with the Banking Department last year, in order to gain parity for state-chartered institutions. (National banks are not subject to a legally mandated schedule of meetings.) The proposed amendment to Part 6 was published in the July 3, 2001 edition of the *State Register*. Public comments will be received until 45 days after such publication (August 17). NYBA expects that this proposed amendment will become effective sometime this Fall.

3. Mobile Homes -- On July 30, 1999, NYBA asked the Banking Department to issue an interpretive letter, designed to expand the permissible terms of loans on mobile homes. Currently, mobile home loans are statutorily limited (under Section 105(5-a) of the Banking Law) to 240 months. NYBA asked that, notwithstanding this term limitation, Section 108(4)(b), which sets no term limits on personal loans in excess of $1,200 with interest rates below 16%, now be construed to include mobile home loans in its purview. NYBA continues to await a response from the Banking Department.

4. Wild Card Petition - Appraisal Requirements -- In late March 1999, NYBA received a response from the Banking Department to its July 28, 1998 "wild card" pe-

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FOCUS

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Outsourcing of Banking Functions: The Virtual Bank

Introduction

The bottom line risk to banks, if problems develop with respect to their outsourcing arrangements, is enormous. Virtual banking has increased that risk many times over, as banks have lost more and more control over the access points to their systems and, thus, are more vulnerable to loss of information, fraudulent transactions and service interruptions that may damage their business. The new emphasis on technology also has spawned numerous intellectual property suits involving in many instances, what banks thought were ordinary business processes. For example, a company that had developed a method of awarding bonus points to salespeople sued a number of credit card issuers participating in awards card programs, claiming that they were violating the company's patent.[1]

Part I below highlights a few, of many, issues that arise in outsourcing, including partnering arrangements that have become common on the Web. A number of comprehensive supervisory guidelines have been issued on outsourcing that will be referenced and briefly discussed in Part II.

I. Outsourcing Issues

A. Customer Confusion

Providing customer information in conjunction with third parties may lead to customer confusion with respect to which products and services are offered by the bank and which are offered by a third party. The common use of "framing" third party content on bank Web sites adds to the confusion and possible bank liability. Adding hyperlinks to third party Web sites, without disclosing to the consumer that he or she is leaving the bank site and entering a site with different terms of use and privacy standards raises similar issues. Yet adding disclosures disrupts the consumer's ease of navigating the Web and may be annoying. However, without disclaimers, the bank could have liability for the third party's practices. At the outset, a financial institution needs to consider whether a company with which it does business is acting in a service capacity or an independent agent capacity. The characterization often will have impact on whether both parties must give disclosures to the consumer under privacy laws.

B. Liability for Processing Errors In contract negotiations, service providers often take the position (and often prevail) that they cannot take responsibility for unlimited liability in a high volume environment where the amount of their fees does not appropriately compensate them for such level of risk. Unless adequate insurance is required, the bank could have enormous exposure, particularly in the consumer area, where a minor error may affect millions of accounts and require restitution, as well as damages. While the automatic processing of accounts using standard software promotes uniformity and avoids individual errors, changes to software can result in a chain reaction of errors. For example, a minor change that cause finance charges to be out of legally mandated tolerances may be difficult to cure because of problems in recreating daily balances. Yet adequate insurance may be very costly.[2]

C. Privacy and Security Concerns

Increased access points to customer information increase the possibility of customer information being improperly appropriated. Understanding and auditing the flow of data in virtual banking is not easy and makes safeguarding customer information much more difficult. Many banks are using independent auditors with special technological training (yet more outsourcing!). Privacy and security concerns are increased by the proliferation of subcontracting and use of multiple service providers. Moreover, as will be discussed Part II, privacy laws may permit the sharing of some data and not others. Thus, the need exists to be able to tag individual datum, often by source, in order for an institution to determine subsequent permissible use. Evolving privacy laws make construction of flexible consumer data bases very difficult.

D. Ownership and License

In addition to risk of intellectual property suits, insuring access to licensed software and providing for updated documentation of programming is critical. Many institutions now require that licensed software code and documentation be placed in escrow and reviewed periodically by independent auditors, with provisions in the escrow agreement permitting the licensee to access the software under certain circumstances, for example, insolvency of the vendor.

E. Linking Siloed Legacy Systems

Banks remain challenged by their existing legacy systems. Ensuring that data transmitted between bank legacy systems both internally and to other parties are integrated properly is difficult. Compounding the difficulty are privacy laws that often interfere with the updating of information through subsequent customer contacts with affiliates or third parties. The increasing pace of bank mergers and the growth of diverse financial companies in recent years in the United States only has increased the complexity of linking operating systems both internally and externally. For example,one large U.S. finanicial institution, in its credit card area alone, has purchased four substantial card portfolios in the last three years, resulting in numerous operation centers and different operating systems.

F. Contingency Planning

Customers now expect "24/7" access to their accounts and legal liabilities many flow from any downtime, which is why many institutions disclose to their customers when they regularly schedule downtime for systems adjustments and updates. "Act of God" exceptions for liability may not apply to computer problems, as some courts take the view that they are foreseeable,[3] unless such problems are triggered by natural disasters such as hurricanes. Thus, contingency planning is more important than ever; files must be appropriately backed up and procedures must be in place to transfer processing in the event of service interruption at any point in the flow of information.

II. Supervisory Law Aspects

United States bank regulatory agencies have been quite proactive in addressing outsourcing risks and attempting to deal with new e-commerce developments thoughtfully, so as to appropriately assess and address risk, without inhibiting new developments. Much of the regulators' control is found in the Bank Services Company Act. The regulators also have issued numerous guidances in recent years on outsourcing and related issues, a few of which will be highlighted below. Guidances, while not subject to legal enforcement, are an important signal of what safeguards regulatory agencies believe financial institutions should take and often are indicative of newly evolving standards that may be strongly encouraged by regulatory examiners. Such guidances thus play an important quasi-legal function. For example, while the banking regulators have not formally regulated account aggregation, the Office of the Comptroller of the Currency ("OCC") recently issued a guidance on bank provided aggregation services, addressing the risks and suggesting controls.

The privacy provisions in the GLBA require that financial institutions take steps to safeguard customer information. The newly promulgated implementing regulations for the GLBA strongly emphasize the need to oversee service provider arrangements and are causing banks to reexamine all of their service relationships, and in many cases, to add new contractual provisions to such arrangements regarding security and audits.

Finally, electronic banking risk management issues also are being addressed at the international level. As discussed below, the Basel Committee on Banking Supervision has issued a report on the supervisory challenges of electronic banking, including the impact of outsourcing.

The sources cited below are a small subset of materials produced by regulators addressing electronic banking and outsourcing. In addition to the materials discussed, a large body of manuals, handbooks and examination guidelines also address the issues.

A. Bank Services Company Act

The Bank Services Company Act[4] provides Federal banking agencies with the authority to examine third party service providers in the United States that provide significant banking services to financial institutions. Banks must notify the appropriate Federal banking agency of the existence of a service relationship within thirty days after entering into a service agreement or the start of performance of service, whichever comes first.[5]

B. The Federal Financial Institutions Examination Council, Uniform Rating System for Information Technology

The Federal Financial institutions Examination Council ("FFIEC") revised its rating system for information systems in 1999[6] which rates both institutions and service providers on a 1 to 5 scale from strongest performance and management practices and the least degree of supervisory concern, to weakest performance and management practices and highest degree of supervisory concern.

C. Office of the Comptroller of the Currency Bulletin 99-9, Infrastructure Threats from Cyber-Terrorists

This bulletin discusses types of cyber-terrorist attacks and suggests additional procedures that banks should implement to avoid becoming cyber-attack victims.[7]

D. Federal Reserve Bank of New York, Outsourcing Financial Services Activities: Industry Practices to Mitigate Risks

The Federal Reserve Bank of New York interviewed a cross section of financial services institutions, service providers, management and process consultants, lawyers and academics to produce a paper on best practices for mitigation outsourcing risk. The paper discusses four primary concerns: selecting a vendor and structuring the agreement, managing and monitoring the agreement, ensuring effective controls and developing adequate contingency planning.[8]

E. Federal Financial Institutions Examination Council Guidance, Risk Management of Outsourced Technology Services

This FFIEC guidance on technology outsourcing discusses risk assessment for outsourcing, due diligence in selecting a service provider, contract issues to be addressed and service provider oversight.[9]

F. Office of the Comptroller of the Currency Bulletin 2001-12, Bank-Provided Account Aggregation Services

This bulletin discusses the risks of bank-provided account aggregation services and suggests control

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mechanisms for banks to consider.[10] "Key controls involve security, compliance, vendor management, data gathering and use, contracting, and customer education, disclosures, and services."[11]

The bulletin suggests that "an automatic log-in feature to conduct electronic fund transfers on other entities' Web sites could trigger the application of Regulation E. The automatic log-in feature allows customers to click a hyperlink and thereby cause the user names and passwords stored at the aggregator to be used to log into other Web sites. Banks that provide this feature might be considered to offer, in essence, an access device for electronic fund transfer services."[12] The bulletin also suggests facilitating securities transactions could trigger application of the federal securities laws and regulations.

The bulletin encourages the use of data feed arrangements where practical, on the basis that they reduce transaction risk because they are more reliable and traceable that screen-scraping. The OCC emphasizes that agreements with vendors should include the OCC's authority to examine the service provider's operation and enumerates other issues that should be contractually addressed, such as submission of financial statement, indemnification, performance reporting, data use restrictions, and security.

Finally, the bulletin discusses the need for consumer education and appropriate disclosures with respect to the aggregation service. In essence, the bulletin begins to provide a roadmap with respect to what aspects of account aggregation eventually may be regulated and what practices will protect financial institutions from challenge on privacy grounds, unfair and deceptive claims and under existing regulations.

G. GLBA and the Interagency Guidelines Establishing Standards for Safeguarding Customer Information and Rescission of Year 2000 Standards for Safety and Soundness; Final Rule

The interagency guidelines ("Security Guidelines") issued by the OCC, Office of Thrift Supervision ("OTS"), Federal Reserve System and Federal Deposit Insurance Corporation establish standards for safeguarding customer information under Sections 501 and 505(b) of the GLBA and contain provisions regarding overseeing service provider arrangements. The Security Guidelines affect all service provider arrangements, not merely major outsourcing agreements.[13] The Security Guidelines require the board of the bank holding company or an appropriate committee of the board to approve the bank's written information security program and receive reports at least annually on material matters such as "risk assessment; risk management and control decisions; service provider arrangements; results of testing; security breaches or violations and management's responses; and recommendations for changes in the information security program.

In addition to security provisions, GLBA also contains limitations on reuse and re-disclosure of non-public personal information received by a nonaffiliated third party from a financial institution. So many companies touch non-public personal information from financial institutions, such as mail houses, Web hosting companies, storage companies and traditional service companies, that a huge number of companies will be swept under the GLBA umbrella.

Furthermore, the definition of "financial institution" in GLBA is extremely broad; "financial institution means any institution the business of which is engaging in financial activities as described in section 4(k) of the Bank Holding Company Act of 1956."[14] Such financial activities include servicing loans, asset management, furnishing general economic information and advice, and tax planning. The Federal Trade Commission ("FTC"), which has regulatory oversight with respect to any financial institutions not regulated by the banking regulators, Securities and Exchange Commission or state insurance regulators, has given examples of financial institutions in its implementing regulation to GLBA including, but not limited to automobile dealerships offering long term leases, check printers, money wirers, accountants and credit counseling service. Thus, many service providers to banks, securities firms and insurance companies could find themselves independently subject to GLBA.

Compliance with GLBA is complicated by the need to characterize the relationship. Servicers may be exempt from making independent privacy disclosures to consumers, when they are acting only in a servicing capacity, and consumers may not opt out of sharing of information with servicers. However, if a company is an independent agent, for example, an insurance agent, such agent may have an independent duty to provide a privacy disclosure. GLBA also has a joint marketing servicing exception that permits financial institutions to market financial products together and allows financial institutions to outsource their marketing. GLBA does not provide customers with an opt out for information shared under such joint marketing and servicing arrangements; however, initial disclosures must be made by financial institutions to their customers regarding such arrangements. No such opt-out exception exists for joint marketing arrangements with non-financial companies. Therefore, consent must be built into agreements with customers if sharing of information will occur in such non-financial "partnerships." Assessing how to characterize companies in partnerships, wheth-

er a party is a financial or non-financial institution, whether a party is a servicer, joint marketer or independent agent may be difficult and fact sensitive.

H. Basel Committee for Banking Supervision, Electronic Banking Group Initiatives and White Papers

The Electronic Banking Group ("EBG") intends to develop guiding principles for the prudent risk management of e-banking activities, including sound risk management for technology outsourcing and network and data security. The October 2000 paper includes a specific discussion of electronic banking risk management issues.[15]

The paper notes the large task faced by banks to integrate their existing legacy systems with the systems of multiple service providers and partners and the risks faced from errors in transaction processing, if the systems for e-banking are not properly integrated. The paper suggests that "[to limit operational risk, banking organizations may want to consider implementing an integrated enterprise-side architecture and technology infrastructure that can facilitate inter-operability, ensure the security, integrity and availability of data and support the management of relationships with third party service providers." (p. 16).[16]

Unfortunately, enormous operational, contractual and possibly legal barriers to the implementation of such an integrated enterprise-wide architecture and technology infrastructure exist. System conversions in one line of business, for example, a credit card business seeking to integrate a newly purchased portfolio, may take up to six months and errors often occur in the mapping from one system to another. Such system conversions often require amendments to customer agreements to reflect system differences that impact legally required disclosures. Many financial institutions are reluctant to move from siloed systems to enterprise-wide systems because of concerns over lack of control. Privacy concerns are another inhibitor; tagging data for an individual customer by company within the holding company would need to be done and appropriate restrictions on access would need to be put in place to ensure that each company would only have access to information it is permitted by law to use in the applicable jurisdiction. Under the Fair Credit Reporting Act in the United States, customers have the right to opt out of allowing affiliates to share credit report information (which also includes application information).

Conclusion

Outsourcing of banking functions in the brave new world of virtual banking raises difficult risk management and regulatory issues. Supervisory law is rapidly evolving to meet the new challenges. Yet supervisors also hesitate to move too quickly to address new developments, such as account aggregation, in which consumers have shown an interest and that have the promise of consumer benefits. Therefore, regulators often move by "signaling" — holding workshops, soliciting discussion and suggesting sources of supervisory authority. For example, the FRB has requested comments on the possible application of Regulation E on Electronic Funds Transfers to account aggregation, while the OCC has suggested that automatic log in features to facilitate fund transfers on other entities' Web sites could trigger application of Regulation E. In essence, the banking regulators are searching for a new paradigm to enable the application of existing regulation to a new product. For counsel advising clients on such new products, "reading the tea leaves" is important. Careful review of agency comments can help structure businesses today in a manner that will facilitate meeting future compliance requirements.

Finally, no discussion of regulation would be complete without mention of new sources of supervisory authority that have been developing, particularly in the United States, to deal with privacy issues and other related virtual bank issues. These new "supervisors" are private industry organizations dedicated to "self-regulation." Examples include privacy seal organizations, such as TRUSTe and BBBOnline, the Network Alliance Initiative, which is setting standards for on line profiling on the Web, and the Information Reference Service Group, which has negotiated standards for information gathering relating to individuals with the FTC. The Safe Harbor negotiations between the U.S. Department of Commerce and the EU are an interesting example of private and quasi governmental action.

The benefits of self-regulation are debatable. On the one hand, it provides guidance in the absence of government regulation, yet does not provide the same level of comfort to consumers as government regulation. The differences in self-regulatory schemes may be difficult for consumers to understand easily, for example what a privacy seal from BBBOnline means in comparison to one from TRUSTe. Companies that participate in self-regulatory activities may find that such self regulation will have the effect of law, as customers begin to claim that self regulation protections constitute a part of their agreements with such companies. In the United States, we already have seen lawsuits under state Unfair and Deceptive Trade Practices Acts, claiming that companies have violated their privacy policies.

That self-regulation may be dangerous is highlighted by a bill introduced in Congress recently that would restrict unsolicited e-mails and permit lawsuits, including damages based in individual Internet Service Provider internal rules on what constitutes unsolicited e-

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■ NYBA in Court

■ VISA CHECK/MASTERMONEY ANTITRUST LITIGATION

Recent Developments: On Feb. 22, 2000, United States District Court Judge John Gleeson for the Eastern District of New York issued an order in this antitrust litigation. The order granted class status to "all persons and business entities who have accepted Visa and/or MasterCard credit cards and therefore have been required to accept VisaCheck and/or MasterMoney debit cards under the challenged tying arrangements." The bank card associations appealed this decision to the Second Circuit Court of Appeals and NYBA filed a motion along with the American Bankers Association (ABA), the Consumer Bankers Association and the Financial Services Roundtable, seeking leave to file an *amicus curiae* brief with respect to the issue of class certification. While plaintiffs filed a motion in opposition to this filing, NYBA's motion was granted on Aug. 24, 2000. Oral arguments took place on Feb. 5, 2001, but there has been no decision on the appeal of the class certification.

KEY POINT: In time, the issue of whether the card associations' pricing of their debit card products violated Federal antitrust laws will become the focus of this legislation. The current issue, however, is the appropriateness and legality of certifying a class of virtually every retailer in the nation. The class action suit would potentially seek a multi-billion dollar damage award against two bank card associations that play key roles in administering payment systems through which approximately $1 trillion in transactions are conducted annually. Given the interrelation of the components of the payment system, should this class certification be upheld, the impact to the banking industry and the overall economy could be significant. It is possible, too, that if this class certification is upheld, the defendants, who will be faced with potentially enormous damages, will be "coerced" into a settlement long before the merits of the case are tested. The effect of this decision as a precedent could also make it easier for other plaintiff classes to win certification against financial institutions that are often targets of class action litigation.

Background: In this case, several of the nation's largest retailers, including Wal-Mart Stores, Sears Roebuck, Safeway and Circuit City, along with a number of smaller merchants and three retail associations, have challenged rules issued by Visa and MasterCard that require stores accepting their credit cards to also accept their debit cards. The plaintiffs allege that this is a tying arrangement and that the defendants have attempted and conspired to monopolize the debit card market, all in violation of the Sherman Antitrust Act.

Plaintiffs moved for certification of their case as a class action pursuant to Rule 23 of the Federal Rules of Civil Procedure, with the proposed class being comprised of all individuals and businesses that have accepted Visa and/or MasterCard credit cards, and have therefore been required to accept the debit cards, within the statute of limitations period. The class includes in total approximately four million merchants. The district court granted class certification, rejecting the defendants' argument that plaintiffs' expert testimony regarding the appropriateness of class certification was inadmissible. He also rejected defendants' claim that class certification was inappropriate because members of the proposed class would not be able to show injury and because the injuries of others would vary in ways not "susceptible to resolution by a class-wide formula."

In its *amicus curiae* brief, NYBA challenged whether the court engaged in the "rigorous analysis" necessary to ensure that the requirements of Rule 23 allowing class certification were met. NYBA stated that the court wrongly failed to address any conflicts posed by the opposing parties' experts and also failed to consider the issue of manageability, noting that the court wrongly put off for another day the question of whether the damages issues in this case could end up requiring four million individual trials to resolve the question of damages.

Outlook: As oral arguments were only recently heard with respect to the class certification appeal, it is not yet possible to predict whether this decision will be overturned. If the class certification is upheld, it is possible that the threat of the enormous potential damage award will force an early settlement. While this could result in many negative ramifications for the banking industry, it would very possibly also prevent the underlying antitrust allegations brought in this suit from being litigated. ▼

■ Significant Legal Decisions

■ NATIONAL BANK ACT & ATM SURCHARGE FEES

Metrobank, N.A. v. Foster (D. Ia. 4-01-CV-80226)

Recent Developments: On May 31, 2001 the defendant, Iowa's Superintendent of Banks, filed a motion to dismiss this case, which seeks a declaratory judgment finding that the National Bank Act preempts Iowa Code Chapter 527. Chapter 527 has been interpreted by the Superintendent of Banks and Iowa's Attorney General to ban ATM surcharges. In his motion, the defendant claims that the case is not yet ripe for adjudication because no bank has yet to charge the ATM fees in question and thus the state has not threatened any enforcement action. The defendant also claims that the court should refrain from exercising jurisdiction in this case under the principle of abstention - that is, due to the possibility that defendant's interpretation of Chapter 527 could be challenged in state court, and thus eliminate the need for Federal involvement. As yet, there has been no ruling on this motion.

KEY POINT: As in the California ATM surcharge case, this case may ultimately provide determinative law with respect to the question of whether state and municipal laws and regulations regarding the imposition of ATM surcharges may be preempted by the National Bank Act with respect to national banks.

Background: On April 12, 2001 five national banks filed suit in the United States District Court for the Southern District of Iowa Central Division, seeking a declaratory judgment finding that the National Bank Act preempts Iowa Code Chapter 527, as well as injunctive relief. The complaint alleges that the interpretation and effect of Chapter 527 is to ban ATM surcharges, although the statute does not explicitly say so. Rather, the statute requires that ATMs be available to other financial institutions and to all customers "on a nondiscriminatory basis" – a requirement that Iowa's Superintendent of Banks and Attorney General have both apparently interpreted to create a fee ban.

On May 31, 2001, the defendant filed a motion to dismiss the case on two main grounds: (i) that the case is not ripe for adjudication insofar, as to date, no bank is charging ATM surcharges, and the state has not threatened enforcement against any bank; and (ii) under the principle of abstention, because of the "realistic possibility that Defendant's interpretation of chapter 527 could be challenged in another case by Plaintiffs or some other bank" presumably in state court. To date, there has been no decision on the motion to dismiss.

Outlook: Because this case is in its most preliminary stages, and the issues before the court in defendant's current motion to dismiss are more technical than substantive, it is far too early to predict what impact this case will ultimately have on the final resolution of the ATM surcharge issue.

■ ATM SURCHARGE FEES

Bank of America, et al. v. City and County of San Francisco, et al. (No. C-99-4817-VRW)

Recent Developments: In July 2000, the United States District Court for the Northern District of California issued a ruling that struck down ATM surcharge bans in Santa Monica and San Francisco. U.S. District Court Judge Vaughn Walker ruled that only the Federal government could impose such restrictions on nationally-chartered banks and thrift institutions, citing the National Bank Act and Home Owners Loan Act. Both Santa Monica and San Francisco filed notices of appeal on July 14, 2000. The banks filed their briefs in this matter on Dec. 13, 2000.

KEY POINT: This case is providing red letter law with respect to the question of whether and to what extent a state regulatory body has enforcement powers over a national bank - at least with respect to the bank's ability to set fees. As more and more municipalities and state governments question the appropriateness of banks' array of fees, and the amount of those fees, the decision, finding that Federal law preempts state governmental regulation with respect to national banks, if upheld, may be pivotal in maintaining a deregulated competitive pricing environment.

Background: On Oct. 12, 1999 the citizenry of the City of Santa Monica voted to adopt section 4.32.040 of the Municipal Code, thereby banning (effective Nov. 11, 1999), the imposition by banks of ATM convenience fees by use of ATM machines by non-customers. The voters of the City and County of San Francisco, California, on Nov. 2, 1999 approved Proposition F, an ordinance also banning ATM convenience fees. (The San Francisco ordinance was scheduled to become effec-

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tive on or about Dec. 1, 1999.) On Nov. 3, 1999 the plaintiffs in this matter filed suit in the United States District Court for the Northern District of California, seeking declaratory and injunctive relief, preventing implementation of the fee bans. The banks claimed that the San Francisco and Santa Monica ordinances are preempted by the National Bank Act, 12 U.S.C. Section 21 *et seq.*, as well as regulations adopted by the Office of the Comptroller of the Currency.

In its Nov. 15, 1999 ruling, (which was reaffirmed and clarified on Nov. 24, 1999), the court granted the preliminary injunction based on its assessment that the ordinances were likely preempted by federal law as to the national bank plaintiffs and the provisions applicable to state-chartered banks non-severable and thus also invalid. While enjoining the defendants from enforcing the disputed ordinance, the court also required plaintiffs to escrow any fees whose collection would otherwise violate the ordinances pending the outcome of the litigation, and to post $50,000 bond. In its Nov. 24, 1999 ruling the Court further prohibited the City of San Francisco from certifying its referendum results and barred residents in Santa Monica - which had already enacted its ordinance - from suing banks over the issue.

On March 31,2000, the Ninth Circuit upheld the granting of the preliminary injunction by the United States District Court enjoining the defendants from enforcing these disputed city ordinances.

Outlook: This decision may have far reaching effects with respect to the ongoing initiatives in many localities to impose ATM fee restrictions and limitations. Indeed, this decision - which has clearly ruled that national banks cannot be subjected to ATM fee bans imposed on them by local governments - coupled with similarly favorable recent decisions in other cases addressing this issue nationwide, will hopefully quell the interest of local governments in pursuing this kind of fee ban. Clearly, this decision strengthens NYBA's arguments against any New York City initiative. However, as both local governments are appealing, the final resolution of this issue may still be far off.

■ CONSUMER PROTECTION LAW

Jules Polonetsky, etc., et al. v. Better Homes Depot, Inc. and Eric Fessler (279 A.D.2d 418, 720 N.Y.S.2d 59, 2001 N.Y. App. Div. LEXIS 651

Recent Developments: On January 25, 2001, the Appellate Division First Department, unanimously modified an order of the New York County Supreme Court, thereby granting defendant's motion to dismiss the complaint as against Better Homes Depot. The lower court had denied defendant's pre-answer motion to dismiss pursuant to C.P.L.R. 3211(a)(3), (7), which motion argued that the real estate transactions in this case did not constitute consumer transactions within New York City's Consumer Protection Law, and thus, that the complaint failed to state a cause of action.

KEY POINT: While there are a number of laws which already exist to protect consumers against predatory lending, as well as Part 41, the New York State Banking Department's "high-cost" home loan regulation, it is clear from this decision that, at least at this time, New York City's Consumer Protection Law, cannot be used as a vehicle for addressing real estate-related transactions. As the predatory lending debate gains public attention and therefore may attract unwarranted (as well as warranted) litigation, this may be a significant factor for defendants and plaintiffs alike.

Background: The plaintiffs sued to enjoin defendants from "committing deceptive trade practices in the marketing and sale of residential homes," and to recover fines pursuant to New York City's Consumer Protection Law (the "Law"). The plaintiffs alleged that defendant Better Homes Depots, Inc. violated the Law by, among other things: (i) inducing consumers to purchase a home with promises of making needed repairs and renovations, and then failing to make such proposed repairs and renovations; (ii) causing electrical, plumbing and other repairs and renovations to be made without the required permits and without informing consumers of this failure; and (iii) discouraging home buyers from exercising their right to retain an attorney of their choosing and instead steering consumers to lawyers pre-selected by the defendant. Better Homes Depot filed a motion to dismiss on the grounds that these real estate transactions did not constitute consumer transactions within the meaning of the Law, and thus, the complaint failed to state a cause of action. The Supreme Court disagreed with defendant's position, stating instead the real estate transactions in the case, were "within the scope of the Consumer Protection Law, and state a cause of action against Better Homes Depot."

On appeal, the Appellate Division, First Department

unanimously modified the lower court's decision, granting the motion to dismiss the complaint as to defendant Better Homes Depot. The Appellate Division stated that the lower court had erred in failing to dismiss the complaint as against this defendant "because real estate sales do not fall within the plain and unambiguous definition of consumer goods or services contained" in the Law.

Outlook: Because the Appellate Division decision was unanimous, the plaintiff was required to seek leave to appeal, which motion was granted. While plaintiff intends to file a further appeal, it has not as yet done so; thus it is not possible to predict at this time the likelihood of such an appeal's success.

■ CORPORATE FIDUCIARY LIABILITY

New Developments: On Aug. 10, 2000, the Third Department, Appellate Division, upheld the March 1999 order of the Otsego County Surrogate Court in the *Matter of the Will of Rowe*, which found that the bank trustee had acted imprudently in failing to diversify the assets of the trust which consisted largely of IBM stock. The Appellate Division also rejected the bank's contention that the Surrogate Court had erroneously computed damages by "front-loading interest" - that is, adding compound interest to the value of the stock at the time it should have been sold and then subtracting the value of the stock at the time it was sold or, if unsold, the time of the accounting, rather than computing interest on the difference between the two values. (Wilber National Bank filed an appeal to the Appellate Division challenging the order signed on March 19, 1999 (and entered on March 23, 1999), by the Otsego County Surrogate Court. That order reaffirmed the Court's prior decisions in the case by ordering that the Letters of Trusteeship issued to Wilber National Bank be revoked; that Wilber refund to the Trust all commissions received by it from September l989 through Dec. 31, 1994; and that Wilber pay damages in excess of $630,000. In a Dec. 7, 1998 decision, the Court reaffirmed its earlier damage calculation.)

Wilber filed a motion with the Appelate Division for leave to appeal this decision, which motion was denied. Wilber subsequently filed a similar motion with the Court of Appeals in January 2001, which motion also was denied on March 27, 2001.

KEY POINT: The *Rowe* decision is troublesome for several reasons. First, the Surrogate's assessment of damages (plus interest) in a case in which the assets of the trust - although admittedly significantly diminished for a period of time - ultimately were replenished, may indicate a willingness on the part of triers of fact to infer the negligence of any fiduciary who fails to diversify. Second, the Surrogate's compounding of interest from the date on which the diversification should have occurred, may indicate a willingness to infer the negligence of any fiduciary who fails to achieve a 9% compound annual rate of return on trust assets. In any event, the affirmation of damage methodology which front-loads interest can have serious economic ramifications to those trustees against whom damages are assessed for failure to diversity.

Background: In the *Rowe* case, Wilber National Bank was trustee of a testamentary charitable lead trust that was funded in September 1989 with 30,000 shares of IBM stock. At the date of an intermediate accounting in December 1994, the trust still held over 19,000 shares of IBM stock, despite the stock's price decline and the Bank's written policy encouraging diversification of trust assets.

In an initial ruling in August 1997, the Surrogate stated that while it was critical of the trustee's failure to diversify the assets, it could not surcharge the trustee if such an action would result in "unjust enrichment to the objectants." However, in a February 1998 opinion, dealing in large part with the issue of damages, the Surrogate found the bank to be "grossly negligent" for maintaining the majority of the trust's assets in IBM stock through an intermediate accounting which took place approximately five years after the trust was funded. During that time IBM's share value diminished significantly. The Court also assessed a $496,259 surcharge, plus interest from the date of the accounting, denied Wilber its commission and removed it as trustee. In this opinion, the Court rejected the increase in IBM's stock value as a reason not to assess damages, crediting the increase "to good fortune" rather than to the fiduciary's investment strategy.

In calculating the damages, the Surrogate cited the decision in the *Matter of Lincoln First Bank, N.A.,* which states that damages should be ascertained by determining the value of the stock on the date it should have been sold and subtracting from that figure the proceeds

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from the sale of the stock, or if the stock is still retained by the estate, the value of the stock at the time of the accounting. In calculating the interest on this figure, however, the Surrogate began by compounding interest of 9% on the value of the stock on the date it should have been sold, and subtracting the value of the stock on the date of the intermediate accounting from that total figure. Wilber contends that according to the *Lincoln First Bank* case, interest, if any, should be assessed only after the stock's value on the date of the accounting is deducted from the stock's value on the date it should have been divested.

Outlook: Because Wilber's motions for leave to appeal were denied, the practice of front-loading of interest will undoubtedly increase the total damage awards assessed against fiduciaries in the future. ▼

■ Federal Legislative Developments

■ PRIVACY

While over 50 bills were introduced at the federal level this year, to date no legislation placing further restrictions on banks' use of consumer and customer information has passed. The focus of federal legislative interest, however, has been on measures designed to address identity theft – with particular interest in limiting the use of social security numbers.

In this regard, The Social Security Number Privacy and Identity Theft Prevention Act of 2001 (H.R.2036) introduced by Congressman E. Clay Shaw, Jr. (R-FL) and a companion bill, the Social Security Number Misuse Prevention Act of 2001 (S.848), introduced by Senators Dianne Feinstein (D-CA) and Judd Gregg (R-NH) – neither of which have yet been scheduled for a hearing or markup - may have some traction. Among other things, these bills prohibit the sale or purchase of an individual's Social Security number without the consent of the individual. Congressman Shaw, who is Chairman of the Ways and Means Committee, took testimony on this issue even before introducing the bill, at which, among others, New York City police officers, FBI agents and victims of identity theft testified.

Additionally, two anti-spam bills recently introduced in the House of Representatives are attracting attention. In particular Congresswoman Heather Wilson (R-NM) has introduced H.R.718 entitled the Unsolicited Commercial Electronic Mail Act. This is a fairly broad bill which includes, among other things, a private right of action. A narrower bill (H.R.1017), which is generally less objectionable to the banking industry, was introduced by Congressman Bob Goodlatte (R-VA). The House Commerce Committee has already marked-up Congresswoman Wilson's bill and the House Judiciary Committee has done a markup of Congressman Goodlatte's bill.

Among the other privacy initiatives that NYBA is monitoring is an opt-in bill, "The Financial Information Privacy Protection Act of 2001," (S.30) which was introduced in January 2001 by Senator Paul S. Sarbanes (D-MD). This bill calls for an opt-out for the sharing of information among affiliates and an opt-in for some types of information sharing outside of the corporate "family." To date, this bill has not progressed beyond the Senate Banking Commitee; however, as Senator Sarbanes has assumed Chairmanship of the Banking Committee, this bill could take on new significance, particularly if opt-in bills (such as one with a considerable chance of passage in California) begin to become law in states around the country.

On the regulatory side, Regulation P, which implements the privacy provisions (Title V) of the Gramm-Leach-Bliley Act (GLBA), went into effect on July 1, 2001. Among other things, the regulation (i) requires financial institutions to establish privacy policies and disclose them annually to all customers, setting forth how the bank will share non-public personal financial information with affiliates and third parties; (ii) permits customers to prohibit (opt-out of) institutions from disclosing personal financial information to nonaffiliated third parties; (iii) prohibits the transfer of credit card or other account number to third-party marketers; and (iv) prohibits pretext calls (that is, makes it illegal for information brokers to call banks to obtain customer information with the intent to defraud the bank or the customer). Additionally, Regulation P directs regulators to establish regulatory standards that ensure the security and confidentiality of customer's information. These guidelines, which were announced on Feb.1, 2001, require institutions to have written information security programs approved by their boards of directors.

■ PREDATORY LENDING

While the 2000 Congressional session saw the introduction of a number of predatory lending bills, including Senator Charles E. Schumer's (D-NY) Predatory Lending Deterrence Act, (which required impartial credit counseling for borrowers and redefined high-cost loans as those with an interest rate 8 points above the Treasury rate or with points and fees exceeding 4% of the total loan), none were passed.

To date this year, only a few bills have been introduced in the House, the most significant of which is Rep. John J. LaFalce's (D-NY) "The Predatory Lending Consumer Protection Act of 2001." This bill would amend the Truth in Lending Act guidelines for high-cost home mortgages, and among other things, requires additional disclosures; specifies additional prohibitions against prepayment penalties; prohibits all balloon payments; and prohibits the terms of a high-cost mortgage from including advance collection of some single premium credit insurance products. Additionally the bill would amend the Fair Credit Reporting Act to mandate that each high-cost mortgage creditor (including the successor creditor) report the debtor's complete payment history to certain consumer reporting agencies. The bill has been referred to the Subcommittee on Financial Institutions and Consumer Credit. Also, Rep. Jan Schakowsky (D-IL), a member of the House Financial Services Committee, introduced a bill (H.R.2531) intended to protect consumers from predatory lending by prohibiting, among other things, laons made without regard to the ability to pay; financing fees that are more than 3% of the total loan or $600; unilateral balloon payments that force consumers to refinance at a high interest rate and pay higher fees; and mandatory arbitration clauses. No bill has yet been introduced in the Senate although Senator Paul Sarbanes (D-MD) has drafted a bill that is expected to be introduced soon.

■ DEPOSIT INSURANCE

(See February 5, 2001 *Banking Journal*, page 34, for background; available on the web at nyba.com.)

In November 2000, NYBA's Board of Directors unanimously endorsed the following policy statement that responded to the Federal Deposit Insurance Corporations options paper on deposit insurance reform:

"1. NYBA supports full coverage of public deposits as a top priority. The elimination of collateral requirements for municipal deposits will relieve banks of all sizes of a significant expense and create increased opportunities for banks to compete for deposits that may have moved to public or private investment vehicles. At the same time, NYBA recognizes that permitting unlimited insured deposits in any single bank could create a moral hazard and would support appropriate safeguards.

2. NYBA also strongly supports the indexation of coverage by the deposit insurance fund sufficient to adjust for inflation since 1980, the last time deposit insurance limits were raised. The new coverage level, thus, would be approximately $180,000. The increase in coverage could be phased in, perhaps over three years, subject to semiannual review by the Federal Deposit Insurance Corporation (FDIC). The Corporation should have the authority to defer the phase-in at any point that it threatens to reduce the deposit insurance required reserve below 1.25% of insured deposits. NYBA would also support the merger of BIF and SAIF.

3. Newly-chartered banks and those that enjoy a dramatic increase in insured deposits should be required to pay an entrance fee sufficient to cover the manageable cost of insuring fully public deposits and of compensating for future increases in inflation."

Most of the provisions of the policy statement have been adopted by the national trade groups as part of their deposit insurance reform positions and legislation has been introduced in Congress to implement, in some form, all of NYBA's recommendations. However, the critical issue of full deposit insurance coverage for municipal deposits, which NYBA has identified as its highest deposit insurance reform priority, has not yet been incorporated in the ABA deposit insurance policy. During the American Bankers Association annual Spring Summit Meeting, NYBA President Michael P. Smith offered a proposal that was approved to establish a task force of State Bankers Association Executives to consider whether to recommend full insurance coverage of municipal deposits. Mr. Smith also was named to chair the Task Force. In addition, NYBA contracted for a study of the costs of implementing its deposit insurance policy, including, in addition to 100% coverage of public deposits, indexation of deposit insurance coverage and an entry fee for new and fast-growing institutions. The study, which was completed in March, found that the cost of providing 100% coverage of public deposits was manageable. In late July, NYBA Chairman Peter Humphrey presented the State Association Division Task Force's recommendation for full deposit insurance coverage of public deposits at the ABA Summer meeting.

Subsequently, in testimony before the Senate Bank-

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ing Committee Subcommittees on Financial Institutions, the ABA, for the first time, endorsed consideration of full coverage of deposit insurance as part of any comprehensive legislation on deposit insurance reform. Also, as part of such a consensus bill, the ABA recommended consideration of adjusting deposit insurance coverage for inflation. The ABA's testimony strongly apposed any increase in deposit insurance premiums when the FDIC reserve exceeds 1.25%.

The change in leadership of the U.S. Senate has accelerated the consideration of deposit insurance reform issues. Former Senate Banking Committee Chairman Phil Gramm (R-TX) opposed an increase in deposit insurance coverage and did not include deposit insurance reform on the Committee's agenda. New Committee Chairman Paul Sarbanes (D-MD) and Financial Institution Subcommittee Chairman Tim Johnson (D-SD) have both expressed support for reform and Senator Johnson held a hearing on the issue in late July. House Financial Services Committee Chairman Michael Oxley (R-OH) has already held a hearing on the issue, but is awaiting the recommendations of new FDIC Chairman Donald Powell before taking any further action on the issue. During his confirmation hearing, Mr. Powell said that he had not completed his review of the issue, but did not believe that reform could only be accomplished in a comprehensive legislative package.

The major bills pending in Congress on deposit insurance reform are:

- S.128, the "Meeting America's Investment Needs in Small Towns Act," sponsored by Sen. Tim Johnson (D-SD), would adjust the basic $100,000 insurance level, in $1,000 increments, to account for inflation;
- S.227, the "Municipal Deposit Insurance Protection Act of 2001," introduced by Sen. Robert Torricelli, would provide 100% coverage for in-state deposits;
- H.R.557, sponsored by Rep. Frank Lucas, entitled the "Fairness and Economic Opportunity Act," would use the surplus in the FDIC deposit insurance reserve to pay the interest on Financing Corporation bonds, until they are redeemed, and then to pay it over to insured institutions;
- H.R.746, the "Federal Deposit Insurance Corporation Adjustment Act," sponsored by Rep. Joel Hefley, would index deposit insurance coverage for inflation;
- H.R.1293, introduced by Rep. Bob Ney, the "Deposit Insurance Stabilization Act," would impose an entrance fee on newly-chartered and fast-growing institutions;
- H.R.1355, the "Deposit Insurance Funds Merger Act," introduced by Rep. John LaFalce, would merge the Bank Insurance Fund (BIF) with the Savings Association Insurance Fund (SAIF); and
- H.R.1899, sponsored by Rep. Paul Gillmor, the "Municipal Deposit Insurance Protection Act of 2001," would insure aggregate municipal deposits up to the amount of equity capital in a depository institution.

In April, the FDIC released its recommendations for deposit insurance reform, in a report entitled "Keeping the Promise: Recommendations for Deposit Insurance Reform." The FDIC identified four weaknesses with the current system of deposit insurance: insurance is provided by two insurance funds at potentially different prices; it cannot be priced effectively to reflect risk; premiums are highest at the wrong point in the business cycle; and the value of coverage does not keep pace with inflation in a predictable fashion. To address these weaknesses, the Corporation recommends that: 1) BIF and SAIF be merged now; 2) the current statutory restrictions on the FDIC's ability to charge risk-based premiums should be eliminated, with the Corporation charging regular premiums for risk regardless of the reserve in the fund; 3) sharp premium swings triggered by adherence to a "hard" 1.25% designated reserve ratio should be eliminated through gradual premium increases below a target ratio and gradual rebates above it; 4) rebates should be based on past contributions to the fund, rather than the current assessment base; and 5) deposit insurance coverage should be indexed to maintain its real value, with Congress determining the base level for indexation. The FDIC indicated that the recommendations are not intended to alter significantly the assessment burden on the industry, but to spread it more fairly and evenly over time. FDIC Chairman Don Powell is expected to review these recommendations and release his views on them later this year.

■ EXPANDED MONEY MARKET DEPOSIT ACCOUNT

For the past five years, the New York Bankers Association has been among the few state and national bank trade groups opposing legislation calling for the immediate or short-term repeal of the prohibition on the payment of interest on demand deposits. The practical effect of repeal of the prohibition would be to permit interest on corporate checking accounts, since all other types of accountholders are eligible for NOW accounts. NYBA twice unsuccessfully petitioned the Board of Gov-

ernors of the Federal Reserve System to use its regulatory authority to increase from six to 24 per month the number of authorized withdrawals from a money market deposit account, an amendment that would, in effect, permit daily payment of interest on idle transaction account balances. NYBA also urged that any repeal of the prohibition on the payment of interest on corporate checking accounts be accompanied by the longest possible transition and be coupled with payment of interest on sterile reserves.

In April, the House of Representatives passed H.R.974, the Small Business Interest Checking Act of 2001, sponsored by Representative Sue Kelly (R-Westchester) by voice vote. Congresswoman Kelly, along with Senator Schumer, has been a stalwart on this issue, several times introducing legislation and amendments to defer the effective date of interest checking repeal. The bill represents a compromise between Congresswoman Kelly's original version of the legislation, which would have delayed repeal of the prohibition for three years, and efforts by the House Republican leadership to repeal the prohibition in a much shorter time frame. H.R.974 would also authorize upon enactment 24 Money Market Deposit Account (MMDA) transfers and provide the Federal Reserve Board with both authority to pay interest on sterile reserves at a short-term market rate and greater flexibility in setting reserve requirements. NYBA has indicated its acceptance of the three-year transition period in the original version of H.R.974.

In the Senate, two bills repealing the prohibition on the payment of interest on demand deposits have been introduced. Senator Chuck Hagel (R-NE) introduced S.229, the Interest on Business Checking Act of 2001, which provides for repeal of the prohibition two years from date of enactment along with immediate authorization for 24 transfers and payment on interest on sterile reserves. Senator Richard Shelby (R-AL) sponsored S.601, the Small Business Checking Regulatory Relief Act of 2001, which provides for an immediate increase to twenty-four transfers, no interest on sterile reserves and repeal of the prohibition effective Sept. 1, 2002. It appears unlikely that either bill would be considered in the Senate as stand-alone legislation. However, the new Chairman of the Senate Committee on Health, Education, Labor and Pensions, Senator Edward M. Kennedy, has expressed strong support for legislation to increase the minimum wage. Legislation to provide for interest on corporate checking accounts is considered by Senate leadership as one possible offset for the cost of the higher minimum wage for small business interests, which have been the major proponents (along with the thrift industry) of this legislation.

■ BANKRUPTCY REFORM

(For background, please see the February 5, 2001 *Banking Journal*.)

Early in February, both the Senate and House Judiciary Committees held hearings on bankruptcy reform legislation. In the Senate, at a hearing on S.220, Committee Chairman Orrin Hatch (R-UT) said that "bankruptcy reform is clearly the will of the Congress and much needed for all American consumers." In the House, two days of hearings on H.R.333 led to the scheduling of a full Judiciary Committee markup, bypassing the Subcommittee approval process. On February 14, the House Judiciary Committee approved the bill by a vote of 19-8, clearing it for floor action.

The House of Representatives passed H.R.333, the "Bankruptcy Reform Act of 2001," by the overwhelming vote of 306-108 on March 1. Sixteen New York Members joined the majority supporting the bill, while 12 voted against and three did not vote. NYBA wrote all Members of the New York delegation urging a vote in favor of the bill and asked that all member banks and Team 21 members contact their representatives to ask for a "yes" vote. New York Members of Congress who voted for the bill were: Reps. Sherwood Boehlert (R-Oneida), Joe Crowley (D-Queens), Vito Fossella (R-Staten Island), Felix Grucci (R-Suffolk), Amo Houghton (R-Steuben), Steve Israel (D-Suffolk), Sue Kelly (R-Westchester), Peter King (R-Nassau), Carolyn McCarthy (D-Nassau), John McHugh (R-Jefferson), Gregory Meeks (D-Queens), Jack Quinn (R-Erie), Tom Reynolds (R-Erie), John Sweeney (R-Saratoga), Nydia Velazquez (D-Brooklyn) and Jim Walsh (R-Onondaga). Not voting were: Reps. Gary Ackerman (D-Queens), Ben Gilman (R-Westchester), and Ed Towns (D-Brooklyn).

The bill as passed is very similar to the bankruptcy bill that was "pocket vetoed" by President Clinton in December. During floor consideration, amendments were adopted that included: a managers' amendment making technical and conforming changes; a Jackson-Lee amendment that would include a debtor's monthly public school expenses as an allowable expense under the means test; a Green (WI) amendment removing the names of children from bankruptcy filings to protect

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Federal Legislative Developments, continued

their privacy; and an Oxley/LaFalce amendment that updates the bill to reflect changes made by Congress in the Commodity Futures Modernization Act, passed late last year, and certain market developments not obvious when the bill was being considered last year.

The Senate Judiciary Committee favorably reported a somewhat amended version of the bankruptcy reform bill, S.220, on March 2 by a vote of 10-8, with Senator Charles Schumer continuing his opposition. Among amendments adopted to the Senate bill were a Feingold/Hatch privacy amendment that would limit the sale of customer lists of companies in bankruptcy and two Feingold amendments on family farm bankruptcies. A new version of the bankruptcy reform bill, S.420, was introduced by the Judiciary Committee Leadership to reflect changes made during Committee consideration.

The full U.S. Senate, after passing a cloture motion to cut off debate on the bill by a vote of 80-19, passed S.420, the "Bankruptcy Reform Act of 2001," by a vote of 83-15 on March 15. Both New York Senators Charles Schumer and Hillary Rodham Clinton voted to pass the bill. NYBA strongly urged all Members of the New York delegation to support the bill. During debate the Senate rejected numerous amendments designed to restrict the rights in creditors in bankruptcy. Among the few adopted on the floor, however, was an amendment by Senator Schumer to transfer liability for fair lending violations on predatory loans to companies that purchase them from bankrupt lenders. The Senate also approved an amendment by Senator Schumer that is likely to prove highly controversial in conference with the House. The amendment is designed to preclude parties convicted of violence against abortion clinics from avoiding civil liability for their actions through the bankruptcy process.

The evenly divided U.S. Senate was unable to agree on a procedure to go to conference with the House of Representatives on controversial legislation, including bankruptcy. The reorganization of the Senate as a result of the switch from Republican to Democratic control permitted new Senate Majority Leader Tom Daschle (D-SD) to make a motion to proceed to consideration of bankruptcy reform to which Senator Paul Wellstone (D-MN) objected. Senator Daschle then filed the first of what is expected to be a series of cloture motions to cut off debate on Senator Wellstone's numerous objections to the Senate proceeding to conference with the House on bankruptcy reform. It is expected that it will take the Senate much of the rest of July to overcome Senator Wellstone's filibuster, after which a conference with the House may be very contentious.

The following is a short summary of the bankruptcy reform bills, prepared by NYBA, with the major areas of disagreement between House and Senate highlighted:

BANKRUPTCY REFORM BILL SUMMARY

Both S.420 and H.R.333 are intended to move towards a needs-based system of bankruptcy, encouraging those who can pay a portion of their unsecured debt to do so. In addition to provisions affecting consumer bankruptcies (Chapters 7 and 13), the bills would also amend Chapter 11 with regard to businesses and Chapter 12 on agricultural bankruptcies. The bills are quite similar and are both based on legislation that passed Congress last year, but was vetoed by President Clinton. This Summary will focus on the major provisions of the bills, as well as discussing some of the differences that need to be reconciled before a bill can be sent to President Bush's desk. The President has indicated that he will sign a bankruptcy reform bill similar to either version.

I. Needs-Based Bankruptcy – Both bills create an objective, needs-based test for determining whether a consumer is abusing a Chapter 7 bankruptcy filing (permitting discharge of debts), but the test is applicable only to consumers with income in excess of the state median income level. Provisions are included to protect low-income filers, single parents, children and others in need. Small differences exist in these provisions with the House bill generally more protective of creditors. The Office of U.S. Trustee is *required* to file a motion to dismiss a Chapter 7 petition by a debtor with more than 150% of the median income who fails the needs-based test.

II. Limits of Discharge – Categories of non-dischargeable debt are increased, including cash advances and charges for "luxury goods and services" and debts incurred to pay state or local taxes. Limits are placed on the ability to shelter real estate from bankruptcy with the House bill prohibiting shelter of more than $100,000 when the debtor has moved into a state within two years while the Senate bill sets a flat $125,000 ceiling on homestead shelters. This provision is likely to be one of the most contentious in any House-Senate compromise negotiation.

III. Debtor Requirements – Conditions consumer eligibility for bankruptcy on completion of credit counseling and financial education; requires debtors to sub-

mit tax returns, available to creditors on request; increases the length of Chapter 13 repayment plans to five years.

IV. Creditor Requirements – Consumer lenders are required to make extensive new disclosures regarding minimum payments, "teaser rates," late payment deadlines and fees, the tax consequences of home equity loans, and, for lenders over $250 million in assets, additional information through an "800" number. Standardized disclosures and explanations must be used to obtain valid reaffirmations.

Additional retirement programs and education IRAs and tuition program credits are sheltered from creditors. Limits are placed on the use of non-public customer information purchased from a bankrupt debtor.

V. Secured Loans – Secured creditors gain additional protection under both bills, with debtors filing for Chapter 13 plans required to continue making payments on secured loans while approval of the repayment plan is pending. "Cramdowns" of debt secured by personal motor vehicles are prohibited if the vehicle was purchased within three years of the filing under the Senate bill and five years under the House bill. A secured creditor under Chapter 13 retains its lien until a debt is repaid or a debtor discharged. And the value of claims secured by personal property is specified as replacement value, without deduction for marketing or sales costs, with Chapter 7 filers required to reaffirm or redeem a loan within 45 days or surrender the property.

VI. Commercial and Administrative Provisions – The bills establish an expedited form of Chapter 11 reorganization for businesses with less than $3 million in outstanding debts; allow creditors to be represented by non-attorneys at the first creditor's meeting; lengthen the permissible time periods between prior bankruptcy discharges and new Chapter 7 or 13 filings; and allow direct appeals of bankruptcy court rulings to the U.S. Court of Appeals under certain circumstances.

More extensive summaries of the Senate and House bills, along with copies of the bills themselves, may be obtained from the Library of Congress legislative website, "Thomas."

■ PERSONNEL CHANGES

New York Representatives Vito Fossella (R-Richmond) and Joseph Crowley (D-Queens) have been added to the House Financial Services Committee, bringing to eleven (out of seventy) the number of New York Members on the Committee. In addition, as a result of the changeover in control of the Senate, Senator Charles Schumer is expected to become Chairman of the Senate Banking Committee's Economic Policy Subcommittee and the Judiciary Committee's Administrative Oversight and the Courts Subcommittee (responsible for reviewing all judicial nominations).

■ MISCELLANEOUS LEGISLATION

Passed as part of this year's budget resolution was an amendment precluding President Bush from imposing **examination fees on state-chartered banks**. The amendment passed both Houses. It was sponsored in the Senate by Senator Schumer. NYBA contacted key members of the New York delegation urging their support.

Also passed in both Houses was a bill to **reduce significantly the fees** paid by issuers and investors for securities issues. Sponsored in the House of Representatives by Reps. Vito Fossella (R-Staten Island) and Carolyn Maloney (D-Manhattan), H.R.1088, the Investor and Capital Markets Fee Relief Act, passed on June 14 by a vote of 404-22. The Senate passed a similar bill, S.143, on March 22 by unanimous consent with New York Senator Schumer as a cosponsor. The bill is intended to reduce fees paid to the SEC to the level necessary to fund SEC operations and to increase the pay of SEC employees to competitive levels. It is expected to save capital market participants more than $14 billion over the next ten years.

In Washington, the House of Representatives passed, by a vote of 407-24, H.R.10, the **Portman-Cardin Pension Reform Act of 2001**. Designed to make pensions portable, the bill would, among other things, increase IRA contribution limits for both traditional and Roth IRAs from $2,000 to $5,000 per year by 2003 and index these limits for inflation thereafter. The annual contribution limit for 401(k)-type pension plans would be increased from $10,500 to $15,000 by 2005, with workers older than 50 authorized to make catch-up contributions up to $5,000. The bill is pending in the Senate.

Significant bill introductions include:

The Community Savings and Investment Act of 2001 (S.605/H.R.1220) that exempts the first $250,000 of corporate income from Federal taxes for qualified community lenders. The next $750,000 of such income would be taxed at 15%. Qualified community lenders would be defined as non-publicly traded institu-

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tions with less than $1 billion in assets with a CRA rating of “satisfactory” or better, at least 60% of its loans in its local area, and at least two-thirds of its shares owned by residents of its home state.

The Small Business and Financial Institutions Taxpayer Relief Act of 2001 (H.R.1263), to ease formation of Subchapter S banks by increasing the number of permitted shareholders from 75 to 150, permitting Sub S shares to be held in IRAs, excluding interest and dividend income from the passive investment rules, exempting national bank directors’ qualifying shares from shareholder limit calculations, and allowing bad debt chargeoffs to offset reserve recapture. A parallel bill was introduced in the Senate (S.936, the Small Business and Financial Institutions Tax Relief Act of 2001) that would also reduce the shareholder consent requirement for conversion from unanimity to 90%. ▼

State Regulatory Developments, continued

tition seeking amendments to Banking Board regulations pertaining to appraisal requirements for loans secured by real estate made by State-chartered entities. In its response, the Department stated its belief that a “wild card” amendment was not required. The Department proposed making regulatory amendments which would eliminate any reference to appraisals in the relevant Banking Board regulations (specifically Parts 80, 82 and 84), and issuing an interpretive letter stating that the requirement found in Section 103(4) of the Banking Law for a “signed certificate of an appraiser appointed by the board of directors” would be satisfied by a written “evaluation of real property collateral that is consistent with safe and sound banking practices.” While NYBA believes that this proposal is a significant improvement over current regulatory requirements, on April 7, l999, NYBA submitted additional comments which, if adopted, would result in greater parity between national and State-chartered banks. To date, NYBA's requested amendments have not been submitted to the Banking Board for approval or for public comment.

5. Wild Card Petition - Underwriting of Municipal Revenue Bonds

On March 16, 2000, NYBA filed a wild card petition with the New York State Banking Department requesting that State banks be provided the authority to underwrite municipal revenue bonds given to national banks by the Gramm-Leach-Bliley Act (GLBA). The petition cites Section 151 of the GLBA, which provides the municipal revenue bond underwriting authority for national banks as the basis to trigger the applicability of the wild card statute. The petition notes that, in the absence of comparable authority for State-chartered banks and trust companies, national banks will have a distinct competitive advantage not only in the competition for underwriting revenue bonds, but also in their ability to compete for all municipal deposits, loans, underwritings and services. To date, the Department has not submitted NYBA’s petition to the Banking Board for approval or for public comment.

■ INTERSTATE TRUST TAXATION

The Department of Taxation and Finance drafted a regulation, which NYBA strongly urged, that clarifies the tax treatment of trusts established by New York grantors in the out-of-state offices of New York banks. Under current law, for a trust to be subject to New York income tax, both the grantor and the trustee must be New York domiciliaries. With the advent of interstate branching, the question arose whether branches of New York banks outside the State were New York domiciliaries for tax purposes. Other states that addressed this question (e.g., California and Virginia) ruled that the mere change in corporate form from an affiliate to a branch of the out-of-state office of a bank does not subject a trust administered in that office to state tax law. In 1999, then Tax Commissioner Michael Urbach, in response to a letter from NYBA President Michael P. Smith, stated the Tax Department’s intention to issue a ruling clarifying that trusts administered in the out-of-state offices of New York banks would not give rise to New York tax liability. In April, the Tax Department shared a draft regulation with NYBA that would accomplish that goal. NYBA filed a comment letter in May generally supporting the draft. NYBA suggested several wording changes in the draft and urged that it be published for public comment.

In November 2000, NYBA met with the Tax department and discussed amendments to the draft regulation. The Department is currently reviewing the comments it received. ▼

■ Federal Regulatory Developments

■ PREDATORY LENDING

The Office of the Comptroller of the Currency (OCC) sent all national banks and OCC examiners an advisory letter detailing abusive lending practices that may violate fair lending and other consumer protection laws. While not attempting to define “abusive” or “predatory” lending, the OCC advised lenders to review and correct activities that may be in violation of the law. The OCC suggested that significant differences in the proportion of minority or female applicants or loans made between a lender’s prime lending and sub-prime lending affiliate could suggest the potential for fair lending violations.

Similarly, the Fed has proposed several amendments to the regulations implementing the Home Owners Equity Protection Act (HOEPA). Among the changes proposed are a decrease in the trigger interest rate from 10 percentage points to 8 percentage points over the comparable Treasury rate; inclusion of optional as well as mandatory single premium credit insurance premiums in the fees that trigger HOEPA coverage; a requirement that any refinancing of a HOEPA loan within 12 months of origination be for the benefit of the borrower; and inclusion of the face amount of the note in the disclosures that must be provided three days before closing. Comments were due by March 16, 2001 but no final rule has been issued yet.

The Fed has also proposed numerous changes to Regulation C, which implements the reporting requirements of the Home Mortgage Disclosure Act (HMDA). Some of the changes are proposed simplifications and some are to require reporting of additional information on each HMDA-reported Loan. Among the changes, which could have a significant impact on banks’ regulatory reporting burdens, is a proposed new requirement that all home equity lines of credit (HELOCs) be reported, as well as the annual percentage rate (APR) on each loan. The final rule is not expected to be issued until early Fall.

Additionally, in February, the Federal Reserve, OTS, OCC and the FDIC issued examiner guidelines offering an extensive definition of subprime lending and recommending that banks hold significantly more capital for subprime loans. The Agencies defined subprime portfolios as those made up of loans to borrowers with higher risk characteristics, including: a Fair, Isaac & Co. score of 660 or lower, or an equivalent credit rating; two or more 30-day delinquencies in the past year; bankruptcy in the last five years; a debt service-to-income ratio of 50% or more; and a foreclosure, repossession, or chargeoff in the preceding 24 months. The guidelines apply to institutions that have a subprime asset concentration of 25% of Tier 1 capital or higher. Examiners are instructed to require these financial institutions to hold capital that is one-and-one-half to three times higher than that typically set aside for prime assets.

NYBA is currently working with U.S. Senator Charles Schumer (D-NY) to address disparities in lending patterns in minority geographic areas. A subcommittee of the working group formed to address this issue met several times during the Winter and Spring of 2001 to lay the groundwork for a pilot program involving conventional mortgage lenders and faith-based community leaders in New York City.

The program, called the House Equity Lending Project (H.E.L.P) which provides a link between potential homeowners and bank home lenders in Southeast Queens and Central Brooklyn, was announced by Senator Schumer, NYBA President Michael P. Smith, Vice Chair of Fannie Mae Jamie S. Gorelich, Reverend David Cousins of Bridge Street AME Church, Brooklyn; and the Reverend Jesse Jackson, at a joint press conference held on May 30, 2001 at the Senator’s New York office. The H.E.L.P. program went live in July 2001.

NYBA also was a co-sponsor of the Predatory Lending Forum sponsored by the Northeast Region of the Federal Trade Commission (FTC) on April 3, 2001. NYBA President Mike Smith made opening remarks and NYBA General Counsel Roberta Kotkin participated in a panel discussion regarding federal and state regulatory and legislative initiatives.

As a result of the Forum, NYBA is now participating in a Task Force comprised of representatives of among other entities, the FTC, the AARP, the New York State Attorney General’s Office, the NAACP and the Better Business Bureau, with the goal of developing predatory lending education initiatives.

■ "PUSH OUT' PROVISIONS

On July 9, 2001, NYBA sent a letter to the Securities and Exchange Commission (SEC), expressing its concerns about the final interim rules addressing the exceptions from broker-dealer registration, which the SEC recently released. In its comment letter on the “push-out” provisions contained in Title II of the

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Gramm-Leach-Bliley Act (GLBA), NYBA stated its belief that the SEC has interpreted the GLBA too strictly in several key instances thereby appearing to contradict Congressional intent when enacting the GLBA. For example, NYBA noted that the SEC has interpreted that the GLBA provision that employees may not receive incentive compensation for any brokerage transactions prohibits year-end bank bonus programs. NYBA stated that such an interpretation would appear to raise questions concerning the continued legality of many bank bonus programs, thus having an impact on many lines of business beyond securities.

Additionally, NYBA stated its concern that the final interim rules impose significant regulatory burdens on banking entities. NYBA pointed out, for example, that the rules provide that the bank must conduct a "chiefly compensated" calculation annually on an account-by-account basis. According to statistics cited by the American Bankers Association (ABA) in its June 4, 2001 comment letter on the SEC's interim final rules, such a requirement would require yearly analyses of fees charged to over 19 million accounts nationwide, and valued at over $22 million. Also, because banks can only judge their compliance with the "chiefly compensated" test after the fact, they may learn too late that they have violated the law by operating as an unregistered broker-dealer, thus creating the potential for litigation by customers seeking to undo unprofitable transactions. This possibility may leave banks with little choice but to "push out" almost all securities business – an eventuality not intended by Congress nor currently required of traditional securities firms affiliated with banks or trust companies. For these reasons, NYBA asked the SEC to withdraw the final interim rule and promulgate new rules. In a letter to the SEC sent in early July, the Federal Reserve, the OCC, and the FDIC, bank regulators similarly stated that the final interim rule instituted "overly complex, costly, and unworkable requirements" for banks.

In response to comments such as those submitted by NYBA, the SEC announced on July 18 that it would extend the compliance deadline from Oct. 1, 2001 to May 12, 2002. The Commission also extended the comment period of the rules from July 17 until Sept. 4, 2001 and said that it expects to extend the compliance deadline further in response to any changes it makes to the rule.

■ FAIR CREDIT REPORTING ACT

On Oct. 20, 2000, the federal regulatory agencies published for comment in the *Federal Register* proposed regulations implementing the provisions of the Fair Credit Reporting Act (FCRA) that permit banks, under certain circumstances, to share information with their affiliates without incurring the obligations of consumer reporting agencies. These provisions authorize banks to freely communicate transaction and experience information with their affiliates, and to communicate "other information" to affiliates, provided that the consumer has been given notice and an opportunity to opt out. "Other information"which is referred to in the proposed regulation as "opt out information" is defined generally as information (i) that bears on a consumer's credit worthiness, credit capacity, character, general reputation, personal characteristics, or mode of living, (ii) is used or expected to be used or collected for one of the permissible purposes listed in the FCRA (for example, a credit transaction) and (iii) is not solely transaction or experience information. The proposed regulations, which are intended to conform to the final Title V privacy provisions of the GLBA, explain how to comply with the affiliate information sharing provisions.

NYBA submitted comments generally supportive of this proposed rule; however, in its comments, among other things, NYBA urged that the Agencies provide an adequate period of time to implement the final rule. As many banks were in the final stages of preparing their GLBA privacy notices, NYBA asked that the final rule not require financial institutions to meet the new FCRA affiliate sharing opt-out notice requirements with respect to existing customers until the first annual GLBA notices are required to be provided. Additionally, NYBA suggested that for new customers (those who established relationships with financial institutions on or after July 1, 2001) the final FCRA rule should be effective on the earlier of July 1, 2002 or the date by which the first annual notice must be provided for that relationship. As the proposed rule can also be interpreted as expanding the type of information it covers beyond what is defined as a "consumer report" under the FCRA, NYBA's comments urged that the final rule be clarified to ensure that no such expansion of the FCRA take place. In response to these and other similar comments from the banking industry, the agencies announced that the rule would be delayed in order to resolve technical issues.

■ INTERNATIONAL BANKING

International regulators, the Basel Committee on Banking Supervision, issued a proposal that gives financial institutions the opportunity to tailor capital requirements to each bank's individual risk profile. The proposal provides a complex combination of options for banks to use in determining the amount of capital they must hold against outstanding loans and offers three options for setting capital requirements for credit risk. In reaction to the large number of comments it received calling for changes in the proposed ruling, the Basel Committee announced in late June 2001 that it would delay new rules by approximately one year. The Committee said that a new version of the rule would be proposed in the first quarter of next year, with a final rule to be issued in 2002. It is currently anticipated that banks will have two years to prepare for compliance.

■ REAL ESTATE BROKERAGE & MANAGEMENT

In January, the Board of Governors of the Federal Reserve System, in consultation with the Treasury Department, published for public comment a proposal to authorize financial holding companies and the financial subsidiaries of national banks to engage in real estate brokerage and management activities. The proposal was in response to a petition from the American Bankers Association (ABA) urging that these activities be considered "financial in nature or incidental to a financial activity" under the provision of the Gramm-Leach-Bliley Act that authorizes financial holding companies and national bank financial subsidiaries to engage in any such activities.

NYBA filed a comment letter in April strongly supporting the proposal. NYBA noted that their home is the largest single financial asset owned by most Americans and their mortgage the largest financial commitment. One of the definitions adopted by Congress for activities that are financial in nature is "arranging, effecting or facilitating financial transactions for the account of third parties," a definition within which brokering a transaction in real estate or managing real estate comfortably fits. Moreover, NYBA also pointed out that real estate brokerage and management are certainly incidental to the financial activity of investing in real estate through the purchase or lease of a real estate asset. NYBA's comments also noted the ability of many real estate brokerage companies to offer "one-stop shopping" for their customers by combining brokerage of real estate with mortgage lending, and argued the need for banks to remain competitive by being able to engage in similar transactions.

With the release of the Fed/Treasury proposal, national trade groups representing the real estate brokerage industry began a grass roots campaign to persuade the regulators not to approve real estate brokerage and management as financial activities or as incidental to banking. In addition, they are urging Congress to preclude the regulators from making such a determination. While the banking industry filed several hundred letters in support of real estate brokerage and management authority with the Fed and Treasury prior to the expiration of the comment period, the real estate industry filed more than 40,000 in opposition. Moreover, the realtors have inundated Congress with more than 100,000 letters, while bankers have sent far fewer.

There is no current legislation pending that would preclude the regulators from deciding whether financial holding companies and national bank financial subsidiaries could be involved in real estate brokerage and management. However, should the proposal be approved by the Federal Reserve Board and Treasury Department, it seems clear that the Realtors will strongly renew their legislative efforts to block the regulation from going into effect. The regulators have not indicated when they will consider the proposal.

■ INTERSTATE TRUST ACTIVITIES

In December, the Comptroller of the Currency's Office published a proposal to codify previous rulings that make clear that national banks have the ability to provide trust services outside the states in which they are headquartered. NYBA supported the Comptroller's proposal in a February comment letter that noted that the Comptroller's ruling would clarify long-standing opinions that national banks may provide trust services in any states that permit State-chartered banks to exercise trust powers. The proposal also made clear that a national bank in one state could accept appointment as trustee in another state so long as it complies with appropriate state laws, such as those requiring bonding or the deposit of securities for the protection of certain charitable or private trusts. NYBA stated that the codification of these rulings will assist national banks seeking entry in other states and, through the dual banking system, may encourage states to ease entry requirements

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for State-chartered banks and trust companies.

In the July 2 *Federal Register*, the Comptroller of the Currency's Office adopted final regulations clarifying the ability of national banks to engage in trust operations across state lines. The final rule, to take effect August 1, codifies interpretations issued by the OCC in recent years concluding that national banks may operate in a fiduciary capacity in any state, engage in any fiduciary capacity permitted by the state for state-chartered entities, and market to and perform fiduciary services for customers regardless of where the bank is acting in a fiduciary capacity. National banks that wish to exercise fiduciary powers in a state in which they had previously not done so would simply need to notify the OCC of their move. The OCC also indicated that it was continuing to review comments it had received on a related proposal to establish uniform nationwide standards for trust operations, but had not yet concluded whether to proceed with the proposal. NYBA's February comment letter had expressed strong reservations regarding the proposal to create uniform national trust standards.

■ IRS TRUST REGULATIONS

On May 18, NYBA filed comments with the Internal Revenue Service supporting a proposal published in the February 15 Federal Register that would revise the tax definition of income for trust accounting purposes. The proposal would recognize changes made by state laws that both incorporate the equitable adjustment power contemplated by the Uniform Principal and Income Act and that authorize unitrusts that provide annual income between 3% and 5% of the annual fair market value of the trust assets. NYBA's comments noted that the proposal accorded well with pending changes in New York's Principal and Income Act and would provide trustees with additional flexibility in meeting the needs of trust beneficiaries without jeopardizing the marital deduction or other favorable features of the tax treatment of trusts. The IRS has not yet completed its review of the comments it has received.

■ FARM CREDIT SYSTEM

In April, NYBA filed comments with the Farm Credit Administration in opposition to its proposal to create national charters for direct farm lenders in the Farm Credit System. NYBA expressed concern that the Farm Credit System had strayed from its mission of providing credit to farmers for agricultural purposes and that the implicit Federal guarantee supporting Farm Credit System bonds gave the System a competitive advantage over the commercial banking industry in raising funds for agricultural lending. NYBA also commented that the national charter program could lead to Farm Credit System lenders focusing more directly on larger corporate borrowers to the detriment of family farmers. As the second largest agricultural State in the nation, New York is a major focus for agricultural lending. ▼

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mail.[17] Some Internet Service Providers define unsolicited e-mails to include as few as 50 identical messages. The compliance burdens for the increasing number of companies communicating by e-mail could be enormous.

In short, virtual banking has opened a Pandora's box of issues with respect to outsourcing that in turn triggers other issues, such as privacy and security. Issues with respect to outsourcing are complex and demand constant vigilance on the part of financial institutions, their lawyers and regulators. ▼

Footnotes

1 MasterCard International Incorporated v. Meridian Enterprises, Inc. Case No. 94-CV-4105 (Dist. N.J. August 17, 2001) (order, dismissing action n.m.).
[2] Until recently, few insurance policies were designed to cover liabilities relating to on-line banking. The American Bankers Association has announced sponsorship of an Internet Banking Liability Policy to fill that gap. See John Ginovsky, E-Insurance Targets Bank Needs, ABA Bankers News, July 10, 2001.
[3] Silger Livingston Publications, Inc. v. Hamburg Township, No. 93-CV-40295-FL, U.S. Dist. LEXIS (E.D. Mich. Sept. 22, 1993).
[4] 12 U.S.C. §§ 1861-1867 (2001).
[5] 12 U.S.C. § 1867(c) (2).
[6] 64 Fed. Reg., 3109 (Jan. 20, 1999).
[7] OCC Bulletin 99-9 (Mar. 5, 1999).
[8] Federal Reserve Bank of New York, Outstanding Financial Services Activities: Industry Practices to Mitigate Risks (October 1999).
[9] FFIEC, Risk Management of Outsourced Technology Services (Nov. 28, 2000).
[10] OCC Bulletin 2001-12 (Feb. 28, 2001).
[11] OCC Bulletin 2001-12 at 1.
[12] OCC Bulletin 2001-12 at 4.
[13] Fed. Reg. 8,616 (Feb. 1, 2001) (to be codified at 12 C.F.R. pt. 30 (OCC); 12 C.F.R. pts. 208, 225 and 263 (FRB); 12 C.F.R. pts. 308 and 364 (FDIC); 12 C.F.R. pts. 568 and 570 (OTS)).
[14] 15 U.S.C. § 6809(3)(A).
[15] Basel Committee for Banking Supervision, Electronic Banking Group Initiatives and White Papers, (Oct. 2000).
[16] Id. at 16.
[17] See Richard Raysman and Peter Brown, E-Mail Blocking: Spammers (and Alleged Spammers) Fight Back, New York Law Journal, July 10, 2001, at 3.