

# Financial Services Alert

Goodwin Procter LLP, a firm of 700 lawyers, has one of the largest financial services practices in the United States.

## New Subscribers, Past Issues and Background

**Material:** If you would like anyone else to receive issues of the Financial Services Alert, would like to receive any past issues, or would like the background materials for any of the matters discussed in this issue, please contact **Greg Lyons, Eric Fischer, Elizabeth Shea Fries** or **Jackson Galloway** at 617.570.1000 or at the e-mail addresses referenced at the end of this newsletter.

## Alert on the Web:

Back issues of the *Alert* are available at [www.goodwinprocter.com/Publications/Financial%20services%20Alerts.aspx](http://www.goodwinprocter.com/Publications/Financial%20services%20Alerts.aspx)

## Disclaimer:

This publication, which may be considered advertising under the ethical rules of certain jurisdictions, is provided with the understanding that it does not constitute the rendering of legal advice or other professional advice by Goodwin Procter LLP or its attorneys.

©2007 Goodwin Procter LLP  
All rights reserved.

## *In this issue:*

### *Developments of Note*

1. Federal District Court Dismisses 401(k) Excessive Fee Litigation
2. OCC Issues Guidance Clarifying its Capital and Liquidity Expectations for National Trust Banks
3. FRB Amends Regulation E to Exempt Transactions of \$15 or Less from Receipt Requirement
4. Banking Agencies Determine Bank Merger Act Not Applicable to Bank/Thrift Acquisition of Credit Card Portfolios with Small Credit Balances
5. OCC Issues Report Concerning Best Practices Used by Loan Servicers to Prevent Foreclosures
6. SEC Issues Release Proposing Electronic Filing and Revised Information Requirements for Form D
7. OCC Confirms National Banks May Honor Items Relating to Deposit Accounts with Insufficient Funds and Charge Overdraft Fees

### *Other Items of Note*

8. SEC Extends Temporary Exemption of Banks from Definition of “Broker” under Securities Exchange Act of 1934
9. SEC Eliminates Short Sale Price Tests

## *Developments of Note*

### ► **Federal District Court Dismisses 401(k) Excessive Fee Litigation**

Over the last nine months, plaintiffs’ class action firms have filed at least fifteen lawsuits across the country on behalf of participants and beneficiaries of some of the largest defined contribution plans in the nation, alleging that the plans were charged excessive and undisclosed fees. Defendants in these suits typically are the employer-sponsor of the employee benefit plans, and also can include the individuals or committees within the sponsor organization responsible for the plans. In a limited number of these cases, the plaintiffs have also named the plans’ service providers as defendants -- *i.e.*, the trustee and recordkeeper of the plans as well as the investment adviser to the funds offered as plan investment options. These cases all allege violations of fiduciary duties under the Employee Retirement Income and Security Act of 1974, as amended (“ERISA”). Fourteen of these cases have been brought by the same plaintiffs’ firm, Schlichter, Bogard & Denton, based in St. Louis.

On June 20, 2007, the United States District Court of the Western District of Wisconsin (the “Court”) issued the first dispositive decision in a suit that named both the service providers and the plan sponsor as defendants, dismissing entirely a purported class action lawsuit filed on behalf of participants in the 401(k) plans offered by John Deere & Co. (“Deere”). The issues addressed in the Court’s opinion are relevant to these cases across the country.

*ERISA does not require Specific Disclosure of so-called Revenue Sharing.* The Court rejected plaintiffs’ claim that Deere had a fiduciary duty to disclose that the investment manager of the funds available to participants “shares” some of the revenue received by it from the funds with the plan’s service provider. In light of current initiatives underway at the Department of Labor to modify Form 5500 disclosure requirements, and the plain text of ERISA’s disclosure requirements, the Court

concluded that to require disclosures of so-called “revenue sharing” would “require judicial expansion of the detailed disclosure regime crafted by Congress and the Department of Labor pursuant to its statutory authority.”

*Fees were not Excessive for Mutual Fund Investment Options.* The Court also rejected as a matter of law plaintiffs’ claims that defendants breached their fiduciary obligations by offering investment options with unreasonably high fees. The retail mutual funds offered as investments had expense ratios ranging from seven (7) to one hundred and one (101) basis points, all of which fees were fully disclosed on the funds’ prospectuses. In addition, the Court observed that more than 2,500 additional funds were offered to participants. The Court concluded that participants had exercised control over their investments, and “were in a position to consider and adjust their investment strategy based in part on the relative costs of investing in [the] funds.” Accordingly, the Court found that ERISA’s safe harbor provision, Section 404(c), barred plaintiffs’ claims.

*Service Providers were not Relevant ERISA Fiduciaries.* The Court also found that neither of the service providers -- the trustee/recordkeeper or the investment adviser to the plan investment options -- possessed relevant fiduciary authority such that they could be liable under ERISA for any alleged failure to disclose or imprudent choice of investment options.

*Hecker et al v. Deere & Company, et al*, No. 06-C-719-S, 2007 U.S. Dist. LEXIS 45275 (W.D. Wis., June 20, 2007). Goodwin Procter LLP was co-counsel for the service provider defendants in this matter.

### ➤ **OCC Issues Guidance Clarifying its Capital and Liquidity Expectations for National Trust Banks**

The OCC issued revised guidance (the “Revised Guidance”) regarding the OCC’s expectations as to capital maintenance and liquidity management by national trust banks (“NTBs”). NTBs provide primarily trust and investment management services, do not offer loans or accept deposits and are not FDIC-insured. The Revised Guidance supersedes OCC Bulletin 2000-26, which covered the same subject matter.

The Revised Guidance emphasizes that: (1) an NTB’s board and management should implement a system to analyze and maintain adequate liquidity and capital; (2) an NTB’s capital and liquidity will be expected to increase beyond initial minimum requirements set forth at 12 C.F.R. Part 3 as its size, complexity and risk profile evolves; (3) capital and liquidity should be evaluated separately, and an NTB’s pledged or encumbered assets should not be viewed as an available source of primary liquidity; and (4) an NTB should develop and maintain forward-looking liquidity risk management procedures and develop contingency funding plans. The Revised Guidance states that OCC examiners will seek corrective action by NTBs when the examiners observe significant capital or liquidity weaknesses or unwarranted risks.

### ➤ **FRB Amends Regulation E to Exempt Transactions of \$15 or Less from Receipt Requirement**

The FRB adopted a final rule (the “Final Rule”) to exempt transactions of \$15 or less from Regulation E’s requirement that receipts be available to consumers for transactions initiated at an electronic terminal. The Final Rule is intended to facilitate the ability of consumers to use debit cards in retail environments where making receipts available may not be practical or cost effective. The effective date of the Final Rule is 30 days from the date of publication in the *Federal Register*.

### ➤ **Banking Agencies Determine Bank Merger Act Not Applicable to Bank/Thrift Acquisition of Credit Card Portfolios with Small Credit Balances**

The four federal banking agencies determined that a bank or thrift need not comply with the application and other requirements of the Bank Merger Act (“BMA”) to acquire a portfolio of credit card accounts from another insured depository institution even if that portfolio includes some credit balances (OCC Interpretive Letter 1083, “Letter 1083”). Letter 1083 provides that the BMA issue arises because by its terms the BMA applies to institutions that “assume liability to pay any deposits,” and credit balances generally are considered “deposits” for purposes of the Federal Deposit Insurance Act. Letter 1083 states, however, that the banking agencies will not consider the BMA to apply if the credit balances represent less than one percent of the value of the credit card receivables transferred and the selling institution is in compliance with section 165 of the Truth in Lending Act (“Section 165”). Section 165 requires institutions to promptly return any credit balances upon request and to take all necessary steps to return such balances within 6 months. Letter 1083 also requires that the selling institution not have advertised the availability of the credit balances as part of the sale, and the balances cannot be transferred to another account or be withdrawn by check or similar means. Finally, Letter 1083 cautions that it only applies to credit card portfolios, and not balances linked to debit or stored value cards.

### ➤ **OCC Issues Report Concerning Best Practices Used by Loan Servicers to Prevent Foreclosures**

The OCC issued a report (the “Report”) on best practices loan servicers are using to improve their contact rate with delinquent mortgage borrowers to help prevent foreclosures. The Report found three main strategies in use around the country for reaching borrowers who are late on mortgage payments. The first two involve direct customer contact by the loan servicer or a nonprofit counseling agency. The third involves providing the borrower with a toll-free telephone number to call either the loan servicer or a housing counseling agency. According to the Report, the five most common direct contact strategies used by loan servicers are:

- *Behavior scoring:* Models used to help determine which late paying borrowers are priority contacts by providing a score that identifies the risk of a borrower going further into delinquency.
- *Non-standard call times:* Calls made on weekends and weekday evenings to contact borrowers when they are home.
- *Customer friendly contact:* Friendly themes used on the phone and in letters to engage the borrower (e.g., we do not want to take your home, in fact we want to help you stay in your home).
- *Options that do not require conversations:* Alternatives for borrowers who do not want to talk to the servicer over the phone such as a website with information about payments and other options and a DVD mailed to delinquent borrowers that identifies foreclosure prevention methods.
- *Door Knockers:* Trained employees go door-to-door to explain repayment options and provide a brochure detailing the options.

### ➤ **SEC Issues Release Proposing Electronic Filing and Revised Information Requirements for Form D**

The SEC issued a formal release (the “Release”) proposing mandatory electronic filing of Form D, which an issuer uses to provide information to the SEC regarding an offering that relies on certain securities offering exemptions under the Securities Act of 1933, as amended, most notably Regulation D. The information filed electronically on Form D would be readily available to the public on the SEC website. Consequently, the SEC’s proposal includes a safe harbor from the prohibition in Regulation D against general solicitation and general advertising. To qualify for the safe harbor, an issuer would have to make a good faith and reasonable attempt to comply with the requirements of Form D, which in its revised form would be designed to elicit (and accept) only information in the categories specified.

**Goodwin Procter LLP  
Financial Services  
Partners and Counsel**

Lynne B. Barr  
Gary A. Beller  
Kay E. Bondehagen  
Raymond P. Boulanger  
Agnes Bundy Scanlan  
Margaret B. Crockett  
Eric R. Fischer  
Martin J. Flynn  
Elizabeth Shea Fries  
Jackson B.R. Galloway  
Geoffrey R.T. Kenyon  
Satish M. Kini  
Thomas J. LaFond  
Paul W. Lee  
Gregory J. Lyons  
Robin J. H. Maxwell  
William P. Mayer  
Philip H. Newman  
Sean P. O'Malley  
Christopher E. Palmer  
Regina M. Pisa  
Mark S. Raffman  
Victoria E. Schonfeld  
William E. Stern  
Michael P. Whalen  
Meryl E. Wiener

To e-mail any of the above attorneys, use first initial of first name followed by last name followed by @goodwinprocter.com. For example, the e-mail address for Gregory J. Lyons would be glyons@goodwinprocter.com

The Release also discusses proposed changes designed to update and simplify Form D's informational requirements. In large part, these proposed changes would reorganize the presentation of much of the data Form D currently requires. The proposed changes would also revise the definition of "related persons" to eliminate owners of 10% or more of a class of an issuer's equity securities, leaving only an issuer's executive officers, directors and promoters to be identified as related persons in a Form D filing. The proposed revisions to Form D would spell out the circumstances, such as mistake of fact or changes in certain types of information provided in a prior filing, under which an issuer would need to amend a Form D filing. In an effort to promote federal and state regulatory coordination and "one stop" filing for issuers, the revised Form D would include a section where an issuer could designate states to which a Form D filing would be directed (although, as contemplated, the electronic filing system would not collect any fees levied by the states with respect to an offering described in a Form D filing, and states would have to agree to access Form D filings on the SEC website).

Comments on the mandatory electronic filing of, and proposed changes to, Form D are due no later than sixty days after publication of the Release in the *Federal Register*. The Release indicates that there will be a companion release describing changes to the Regulation D offering exemptions that the SEC voted to propose in conjunction with the changes discussed in the Release.

➤ **OCC Confirms National Banks May Honor Items Relating to Deposit Accounts with Insufficient Funds and Charge Overdraft Fees**

In Interpretive Letter 1082 ("Letter 1082") the OCC confirmed that a national bank may honor items relating to a deposit account with insufficient funds, and charge overdraft fees for providing this service. Letter 1082 states that Section 24(Seventh) of the National Bank Act expressly provides national banks the authority to take deposits, and also permits national banks to engage in any incidental activity. Pursuant to this authority, Letter 1082 provides that a national bank may permit banks to honor items with insufficient funds in an account, even if such deposit accounts include social security deposits.

As to the overdraft fees, Letter 1082 states that Section 7.4002 of the OCC's regulations expressly permits national banks to assess deposit account service charges. The national bank at issue separately provided the analysis required by Section 7.4002(b) to demonstrate that its fees satisfied the factors set forth in that regulation to show that the fees were consistent with safe and sound banking practices. Letter 1082 also confirmed that these overdraft practices are not covered by 7.4007(c)(4) of the OCC's regulations, which provides that state laws pertaining to the "right to collect debts" may apply to national banks. Letter 1082 clarifies that that provision pertains to the existence of a bank's *right* to recover a debt, not the means by which a national bank may pursue that right, and the activities at issue are directly related to the maintenance of a deposit account rather than a typical debt arrangement.

## *Other Items of Note*

➤ **SEC Extends Temporary Exemption of Banks from Definition of "Broker" under Securities Exchange Act of 1934**

The SEC issued an Order extending the temporary exemption of banks from the definition of "broker" under the Securities Exchange Act of 1934. The exemption was extended from July 2, 2007 to September 28, 2007 to allow the SEC and the FRB to consider carefully the over 70 comments received on proposed Regulation R before the SEC and FRB jointly adopt final implementing rules. (See discussion of proposed Regulation R in the December 19, 2006 *Alert*).

➤ **SEC Eliminates Short Sale Price Tests**

Effective July 3, 2007, the SEC amended its rules under the Securities Exchange Act of 1934, as amended, to eliminate all restrictions on the execution prices of short sales and to prohibit any self-regulatory organization from maintaining any restriction on the execution price of short sales.