

# The Unique Ethical and Legal Challenges in Advising Regulated Institutions

**IBA Bank Counsel Conference**

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**Presented By:**

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with special guest

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Former General Counsel, FRB

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# Regulatory Relations

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## Regulatory Engagement

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- Supervision vs. litigation
- Preserving your client's relationship
- Obtaining good feedback and outcomes
- Examiner treatment

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# Understanding the Client

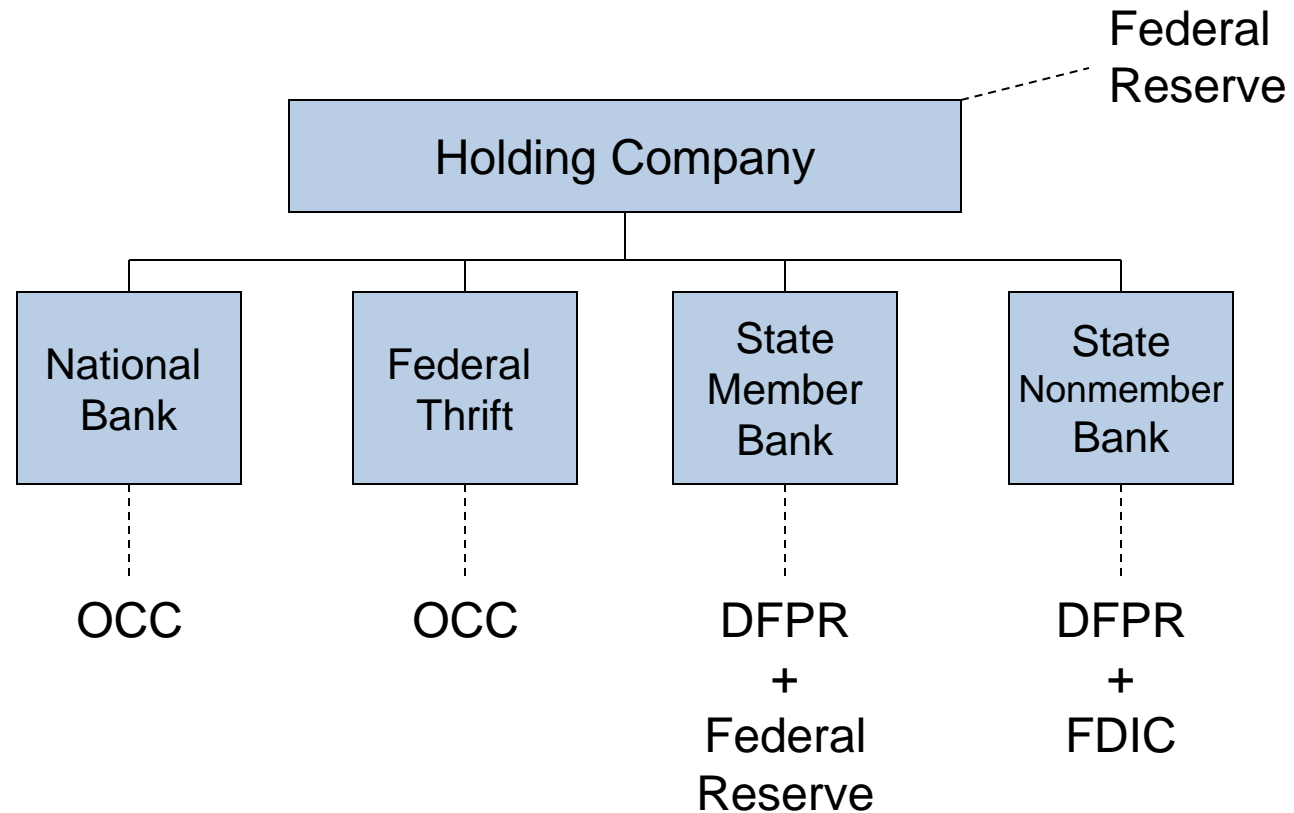
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## Institution Information

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- FDIC/ BankFind Suite
- Federal Reserve/ National Information Center (NIC)
- FDIC/ Call Reports
- FFIEC/ Uniform Bank Performance Report (UBPR)
- Reports of Examination and regulatory correspondence
- Enforcement actions
- Governance documents
- Others

# Organizational Structure and Regulators



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# Understanding the Sources

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## Legal and Regulatory

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- Statutes
- Regulations/ Federal Register
- Supervisory guidance
- Examination handbooks
- Reports of Examination and regulatory correspondence
- Enforcement actions
- Failed bank reports
- Speeches and Congressional testimony
- Others



# Asset Threshold Issues

Asset Threshold(s)	Provision(s)
\$48 million	Home Mortgage Disclosure Act reporting requirements
\$50 million	Management interlock restrictions , Insurance activities
\$150 million	Streamlined SEC reporting requirements
\$300 million	Expedited acquisition eligibility and/or streamlined acquisition reporting requirements
\$330 million	Community Reinvestment Act requirements
\$500 million	BHC risk-based capital requirements, Corporate governance requirements
\$1 billion	Corporate governance requirements, Flood insurance escrow requirements
\$1.322 billion	Community Reinvestment Act requirements
\$2.23 billion	High-priced mortgage threshold
\$3 billion	Expedited acquisition eligibility and/or streamlined acquisition reporting requirements, Corporate governance requirements, Small BHC Policy Statement, Collins Amendment exemption, 18-month examination cycle, Streamlined stock buyback and redemption reporting requirements
\$5 billion	Tailored call reports
\$7.5 billion	Expedited acquisition eligibility and/or streamlined acquisition reporting requirements
\$10 billion	CFPB primary regulator for consumer compliance, Interchange fee cap ("Durbin Amendment"), Volcker Rule, Portfolio QM, Mortgage escrow requirements, CBLR eligibility, Swap margin and capital requirements
\$20 billion	Thrift charter opt out

Source: Congressional Research Service (2021)

## “Secret Law”

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[M]any of the control doctrines . . . have been unwritten, or have been written but not well publicized, or in some cases even disseminated. And as a result, the practical determinants of when the Board will deem one company to control another, can in some cases not be discovered except through supplication to a small handful of people who have spent a long apprenticeship in the subtle hermeneutics of Federal Reserve lore, receiving the wisdom of their elders through oral tradition in the way that gnostic secrets are transmitted from shaman to novice in the culture of some tribes of the Orinoco.

Randal Quarles (FRB Vice Chair for Supervision)

April 23, 2019

## Case Study

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### Control Definitions

- Bank Holding Company Act/ Regulation Y
- Change in Control Act/ Regulation Y
- 23A/B of the Federal Reserve Act/ Regulation W
- Regulation O
- Illinois Banking Act

## Case Study

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### Dividends for Illinois State Member Banks

- Illinois Banking Act
- Federal Reserve/ Regulation H
- Federal Reserve/ SR 09-4
- Examination findings
- Enforcement actions

## Case Study

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### Affiliate Transactions

- Dodd-Frank Act revises 23A/23B of the FRA
- Changes to covered transactions, collateral requirements, credit exposure, investment funds, exemptions
- Regulation W not yet revised accordingly

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# Understanding the Mission

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## Legal vs. Business/Policy Advice

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- “What may I do?” vs. “What should I do?”
- Identify pros and cons
- Outside counsel vs. in-house role

## Regulatory Opinion Types

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### Options

- Confidential vs. disclosed
- Informal vs. formal interpretations

### Factors

- Engagement considerations
- Certainty
- Timing



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# Attorney-Client Privilege

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## Examination and Visitation Authority

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DFPR	205 ILCS 5/48
FDIC	12 U.S.C. 1820
FRB	12 U.S.C. 248
OCC	12 U.S.C. 481

## Unfettered Access?

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The Federal Reserve examines, on a regular basis, institutions for which we have been granted supervisory authority by Congress and, through that authority, has complete and unfettered access to an institution's most sensitive financial information and processes, including information that would otherwise be privileged and not subject to public disclosure.

## Statutory Exception

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The submission by any person of any information to [banking agencies] for any purpose in the course of any supervisory or regulatory process of such [agency] shall not be construed as waiving, destroying, or otherwise affecting any privilege such person may claim with respect to such information under Federal or State law as to any person or entity other than such [agency].

12 U.S.C. 1828(x)

## Common Issues

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- Legal advice
- Examinations
- Proactive disclosures
- Internal investigations
- Enforcement

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# Conflicts of Interest

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## Potential Clients

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- Bank
- Employees
- Board of directors
  - Inside vs. outside
  - Board factions
- Holding Company
- Shareholders

## Potential Conflict Situations

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- Dominant management/ significant shareholder
- Mergers and acquisitions
- Enforcement actions
- Troubled banks
- Others



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# Regulatory Confidentiality Issues

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# Confidential Supervisory Information

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- Scope of definition
  - Examination reports and ratings
  - Regulatory correspondence
  - Other information

## Confidential Supervisory Information (cont.)

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- Disclosure situations
  - Insurance companies
  - Securities disclosures
  - M&A
  - Others

## Suspicious Activity Reports

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- SARs (and existence) confidential, except for BSA responsibilities
- Existence/ non-existence of SARs confidential, including SAR information if reveals SAR existence
- If impermissibly asked to disclose SAR (or SAR information), decline to produce and notify FinCEN/federal banking agency

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# SEC Issues

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## SEC “Up-the-Ladder Rule”

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- Report material violations to CLO / CEO
- If futile, report to Audit Committee, Independent Committee, or Board
- If inappropriate response, report reasons to CLO, CEO, and directors
- Disclose to SEC if:
  - prevents substantial injury
  - prevents perjury/fraud
  - rectifies consequences of material violation that caused substantial injury

## **Speech by SEC Commissioner Allison Herren Lee (March 4, 2022)**

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- Revisiting “Up-the-Ladder Rule”
- Legal advice should reflect interests of corporation/shareholders
- Independent/rigorous analysis of materiality issues
- Minimum standards for attorney competence/experience
- Continuing legal education requirements
- Obligation to investigate red flags
- Law firm oversight

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# Potential Liability

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## IAP Liability

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### Institution-Affiliated Party

- any director, officer, employee, or controlling shareholder (other than a BHC/SLHC) of, or agent for, a bank;
- any other person who has filed or is required to file a change-in-control notice;
- any shareholder (other than a BHC/SLHC), consultant, joint venture partner; or any other person who participates in the conduct of the affairs of a bank; or
- any independent contractor (including any attorney, appraiser, or accountant) who knowingly or recklessly participates in violations, breaches of fiduciary duty, or unsafe or unsound practices, which caused or are likely to cause more than a minimal financial loss to, or a significant adverse effect on, the bank

## FDIC Professional Liability Recoveries and Expenses

Type of Claim	Total Recoveries – 2007-2022	
Securities		
RMBS	\$2,043,643,910	(45.5%)
Other	\$65,002,496	(1.4%)
D&O Liability	\$1,326,494,017	(29.5%)
Accountant Malpractice	\$461,635,367	(10.3%)
MMF	\$241,442,946	(5.4%)
Bond	\$204,239,458	(4.6%)
Appraiser Malpractice	\$45,738,132	(1.0%)
Attorney Malpractice	\$44,424,157	(1.0%)
Other Professional Claims	\$34,413,216	(0.8%)
Insurance Issuer	\$22,478,837	(0.5%)
Financial Instruments – LIBOR	\$767,300	(0.0%)
<b>Total</b>	<b>\$4,490,279,836</b>	<b>(100.0%)</b>

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## Other Issues

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## Hot Spots

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- State law issues
- Dealing with the media
- Deposit insurance
- Troubled bank situations
  - Advance retainers
  - Document retention
- Others

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## Questions?

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## John M. Geiringer



**John M. Geiringer**

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As the Regulatory Section Leader of BFKN's Financial Institutions Group, John advises a wide variety of financial institutions around the country about the full spectrum of legal, regulatory, and supervisory issues that they face. He is a frequent speaker and author in the financial institutions area on issues surrounding banking regulations, examinations, and enforcement actions, as well as on cybersecurity.

John devotes significant time to anti-money laundering, counter-terrorist financing, and related national security issues. In this regard, he lectures and advises institutions around the country, engages with relevant organizations, and has published on the subject.

Prior to joining BFKN in 1999, John worked as a bank regulator and also as a compliance consultant. He served as legal counsel for the Illinois bank regulatory agency, now the Illinois Department of Financial and Professional Regulation. John also obtained practical experience with respect to bank operations and compliance issues as a regulatory consultant with a regional accounting firm, performing compliance reviews and training for a variety of financial institutions.

## Special Guest -- Scott G. Alvarez

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Scott G. Alvarez served as General Counsel to the Board of Governors of the Federal Reserve System and the Federal Open Market Committee for 13 years, retiring in September 2017 after serving a total of 36 years as an attorney for the Board of Governors. As the chief legal officer for the Board, he provided legal and policy advice on a wide range of regulatory, administrative, organizational, legislative and other issues related to the duties and operations of the Federal Reserve Board, Federal Reserve System, and FOMC.

Currently, Scott is an Adjunct Professor at Georgetown University Law Center. He was an Adjunct Professor at the Boston University Law School and has been a guest lecturer at the Yale School of Management, Columbia University Law School, New York University Law School, Duke Law School and the UNC Law School.

He was also a contributor to *First Responders: Inside the US Strategy for Fighting the 2007-2009 Global Financial Crisis*, Edited by B. Bernanke, T. Geithner, and H Paulson. Scott received his JD from Georgetown University Law Center and an A.B. in Economics from Princeton University.