CADWALADER

CABINET NEWS

Research and commentary on regulatory and other financial services topics

Mid-Summer Momentum

August 8, 2024

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Cadwalader Enhances Financial Regulation Team With Partner Christopher Horn

August 8, 2024

Cadwalader recently added **Christopher Horn**, a widely recognized industry leader in the regulation of securitization transactions, as a partner in the firm's New York office.

"We're thrilled to welcome Chris to our firm," said Cadwalader Managing Partner Pat Quinn. "He has deep experience in legal and regulatory issues that are highly important to our clients involved with securitizations and structured financings. Chris's arrival augments what's already a deep bench of senior regulatory lawyers who are integrated into our core capital markets, financial services, corporate and litigation teams."

With over 25 years of experience advising clients on regulatory matters, Chris is a leading contributor to critical industry initiatives, overseeing high-profile projects for the Structured Finance Association and the Securities Industry and Financial Markets Association. Chris, who is also a member of the American Bar Association's Securitization and Structured Finance Committee, frequently speaks with the media and before industry associations, writes for leading journals and teaches future generations of practitioners as an adjunct professor at the NYU School of Law, where he has taught "Law of Securitization" for over 15 years.

The addition of Chris is the latest enhancement to Cadwalader's continued strategic expansion of its financial regulation capabilities. In less than two years, the firm has welcomed former FDIC Deputy General Counsel and banking industry veteran Andrew Karp, top UK financial regulatory partner Alix Prentice, CFTC regulatory partner Peter Malyshev, and former FTC lawyer and leading fintech and consumer financial services partner Mercedes Tunstall, as well as a host of new partners in related practices.

"I'm grateful for the chance to join a market-leading financial regulation practice," Chris said. "Cadwalader is synonymous with cutting-edge transactional work, and I look forward to contributing my regulatory background and experience to advance our clients' goals."

As Cadwalader continues to advise clients who are subject to increasing regulatory oversight or engaged in evolving and novel financings, such as capital relief transactions, Chris brings a substantial level of reliable, thoughtful and respected experience. Notably, he is a leader of the SFA's Basel III Endgame and SIFMA's SEC Rule 192 task forces.

"Having an elite regulatory practice is critical to our transactional capabilities – and what sets our firm apart," said Cadwalader Financial Services Co-Chair Jamie Frazier. "Chris has a unique blend of knowledge and experience that will add tremendous value to our clients."

Changing US Banking Regulations Keep Cadwalader Hire on Alert

August 8, 2024

Cadwalader partner **Christopher Horn** was interviewed by *IFLR* for a recent article, “Changing US Banking Regulations Keep Cadwalader Hire on Alert.”

The article noted that, in the past two years, Cadwalader has made five hires in its growing financial regulation practice; the team has recently been advising clients on the Basel III Endgame and the U.S. Securities and Exchange Commission’s recently adopted Rule 192, among other developments.

Speaking to *IFLR* about his move, Chris said: “I was drawn to Cadwalader’s involvement in cutting-edge transactional and regulatory work, particularly on the banking side. The firm is a thought leader in the structured finance industry, and I very much look forward to carrying on that tradition.”

Read it **here**.

Banking Regulators' Request for Information on Bank-Fintech Arrangements

August 8, 2024

By Mercedes Kelley Tunstall
Partner | Financial Regulation

By Christopher Horn
Partner | Financial Services

On July 25, 2024, the Fed, the OCC and the FDIC (the "Banking Regulators") released a "Request for Information on Bank-Fintech Arrangements Involving Banking Products and Services Distributed to Consumers and Businesses" (the "RFI"). The RFI was **published in the Federal Register** on July 31, 2025. The Banking Regulators also issued a **joint statement** on the RFI.

Responses to the RFI must be received on or before September 30, 2024.

The RFI states that the Banking Regulators "support responsible innovation and banks pursuing bank-fintech arrangements in a manner consistent with safe and sound banking practices, and with applicable laws and regulations..." and that "Bank-fintech arrangements can provide benefits." But . . . "supervisory experience has highlighted a range of potential risks with these bank-fintech arrangements."

Of course, for practitioners in this space, the contracts put into place between banks and fintechs attempt to address the potential risks and ensure that full compliance with law occurs. While the RFI recognizes that contractual allocation of duties to ensure compliance is standard in these relationships, it reveals that the Banking Regulators seem to be uneasy about whether allocation of duties is a valid means for reaching compliance. Considering that the Banking Regulators are fully aware that banks use a wide variety of third parties to ensure compliance for their day-to-day obligations, the wariness of bank-fintech contractual arrangements seems to be outsized.

The RFI seeks public comment on 41 discrete questions (by a tally of the question marks) and provides the public 60 days to answer them. Among these questions is a query whether "additional clarifications or further guidance" would be helpful for banks. To our minds, the Banking Regulators already have provided guidance on most of the topics covered by the RFI, which is to say that as long as the bank and the fintech work together to ensure that the bank has sufficient information and sufficient agency to fulfill its obligations with respect to its own safety and soundness, liquidity, and capital requirements, as well as its obligations to comply with consumer protection, privacy and security laws, then specific guidance for the bank-fintech relationship is not really necessary.

Having said that, we think there are a couple of areas where a statement from the Banking Regulators could set expectations and make things a bit smoother at the negotiating table. Specifically:

- To the extent the fintech's compliance obligations are lesser than the obligations a bank must meet, the fintech must instead meet the bank's compliance obligations.
- Proper due diligence by the bank for the program with the fintech should identify parameters for when a certain amount of growth will give rise to liquidity, capital reserves or safety and soundness challenges.
- The contract should provide a means for banks to throttle back the program with the fintech in case the growth is such that liquidity, capital reserves or safety and soundness thresholds cannot be shifted quickly enough.
- While banks and fintechs may continue to negotiate ownership of data generated from the program, banks should be assured a broad enough and long enough license to such data that will allow them to meet compliance obligations.

In sum, we think that the Banking Regulators should tread lightly in this area, which sentiment is consistent with this **statement** regarding the RFI, by Federal Reserve Board Governor Michelle W. Bowman -- she stated that while she supports the RFI, she is "concerned that the agencies continue to publish piecemeal guidance and other documents based on an incomplete understanding of current bank-fintech relationships" and that any guidance or rulemaking that arises from the RFI poses "the risk of pushing out innovation from the regulated banking system."

FDIC Proposes To Exercise Now-Dormant Authority Under the Change-in-Bank Control Act

August 8, 2024

By Andrew Karp
Partner | Financial Regulation

The board of directors of the Federal Deposit Insurance Corporation ("FDIC") recently proposed a rule change that would reassert its now-dormant authority to review changes in bank control involving bank holding companies. Under the Change-in-Bank Control Act (the "CIBCA"), 12 USC 1817(j), the FDIC has statutory authority to review and approve or reject proposals that would result, directly or indirectly, in changes of bank control, as defined in the CIBCA.

Under the CIBCA, an investor (excluding those that would be captured by the Bank Holding Company Act), may not acquire "control" (generally defined as the "power, directly or indirectly, to direct the management or policies [of a bank] or to vote 25 per cent or more up of any class of voting securities of a bank]") without submitting prior written notice of the transaction. In practice, a rebuttable presumption of control is triggered at a 10 percent voting securities ownership position, and the federal banking agencies require the notice at that level.

The statute's reference to indirect changes in control entitles the FDIC to review changes in control of bank holding companies that own or control banks principally supervised by the FDIC. However, the FDIC has long ceded that authority to the Federal Reserve, which has authority to review changes in bank control in respect of bank holding companies.

If adopted as proposed, this rule would reverse that concession. The proposal is a response to the FDIC's perception of the influence of large asset managers on the banking system as a result of their investment in bank holding companies. As the preamble to the notice of the proposal states, the FDIC is concerned that "recent development in the equity markets may be contributing to elevated risk of excessive indirect control or concentration of ownership in FDIC-supervised institutions." See FDIC Press Release **PR 63-2024**, Notice of Proposed Rule, Amendment to Regulations Implementing the Change in Bank Control Act, July 30, 2024 (the "Proposal Release".)

The FDIC's concern is two-fold. First, it notes that large asset managers have been acquiring and hold significant interests in many bank holding companies partially as a result of the growth of passive investment vehicles, such as mutual funds and exchange-traded funds that track popular indices. Second, while the positions often are subject to the Federal Reserve's review under the CIBCA, the Federal Reserve, has, in the case of holdings below the 25 percent trigger, often dispensed with the notice process in favor of negotiated agreements with the investors, whereby the investors commit to remaining passive by abiding by a set of generally standardized commitments.

In light of the increasing number of such agreements, the FDIC has reconsidered its prior concession policy in favor of a proposal to subject such investments to its review under the CIBCA, in addition to the review of the Federal Reserve, in order that the FDIC "may more appropriately assess the effects of any control exerted over [the target and its subsidiary FDIC-supervised banks]. See the Proposal Release **here**. The proposal would effectuate this policy change by deleting section 303.84(a)(8) of its regulations, 12 C.F.R § 303.84(a)(8). That section currently exempts bank holding companies, and therefore indirectly any FDIC-supervised subsidiary bank, from the FDIC's scope of authority under the CIBCA.

As a result, asset managers acquiring triggering positions in bank holding companies that own or control banks principally supervised by the FDIC would be required to submit a prior notice to the FDIC. Under the CIBCA, a subject transaction may be completed only if the applicant receives written notice that the appropriate federal banking agency does not object, or the agency fails to decline to approve within the statutory time period. The banking agency will decline to approve a notice if the proposal fails to satisfy the CIBCA's statutory analysis factors, which include competition, financial condition of the proposed investors, future prospects of the target, and the competence, experience and integrity of the investors and managers. The proposal would also direct FDIC examiners to monitor compliance with any relevant passivity commitments, a significant change from the Federal Reserve's approach of company self-certification.

The proposed policy change can be expected to add a level of uncertainty to the timing and reception of subject investments. It remains to be seen if, and how, the Federal Reserve will respond to the FDIC's proposal. More broadly, the FDIC's action also reinforces the recent signals of a lack of harmony between the FDIC and the Federal Reserve.

This has been evident in recent FDIC actions in which it has asserted a more stringent position than the Federal Reserve in matters as to which the agencies have similar or overlapping authority. The FDIC's approach can be seen in its recent proposal to substantially modify its policy on the **Bank Merger Act** to impose much different standards than those applied by the Federal Reserve, and its application of more stringent resolution planning standards to certain bank holding companies, a matter in which the agencies have joint authority.

Public comment on the proposal will be open for 60 days following publication of the proposal in the Federal Register, which has not yet occurred as of the date of this note.

A Classic Commodity Ponzi Scheme Raising Novel Issues for Pools and Carbon Credits

August 8, 2024

By Peter Y. Malyshev
Partner | Financial Regulation

The Federal U.S. District Court for the Northern District of Illinois entered an **Order** granting summary judgement for the U.S. Commodity Futures Trading Commission on July 1, 2024 and ordered $83 million in restitution and $36 million in disgorgement against Sam Ikkurty and his affiliated companies. This would have been a garden variety “classic Ponzi scheme” case but for two novel issues.

First, the court agreed with the CFTC’s interpretation that for an investment vehicle to qualify as a “commodity pool” it need not actually “trade” any “commodity interests,” i.e., derivatives – such as commodity swaps, futures or options. Instead, merely the “solicitation of funds” from participants to invest in a vehicle for purposes of trading in derivatives (*e.g.*, in the future) – would be enough to qualify this vehicle as a “commodity pool.” Thus, the court agreed with the CFTC that Ikkurty’s investment vehicles were “commodity pools” even though they had no positions in derivatives, and therefore the operator of the pool acted as an unregistered commodity pool operator (“CPO”) and as such committed fraud.

The court found that investment vehicles operated by Ikkurty invested in Bitcoin, Ethereum and other cryptocurrencies, that under ***CFTC v. My Big Coin Pay**, Inc.* 334 F. Supp. 3d 492, 498 (D. Mass 2018) would qualify as “commodities,” triggering the CFTC’s anti-fraud jurisdiction under § 180.1 of the CFTC regulations.

Secondly, the court also agreed with the CFTC that certain carbon credits also qualify as “commodities” and that Ikkurty had misappropriated customer funds through a “carbon offset program” that resulted in a $20 million shortfall for carbon offset program participants. The Order does not provide a lot of detail on how the carbon offset program operated, but it is notable that this Order is the first instance where the CFTC was able to successfully prosecute fraud in connection with trading environmental commodities, such as carbon credits.

This enforcement action is significant because it confirms the CFTC’s position that even if an investment vehicle may not have any positions in derivatives, merely stating (orally or in writing) that it may establish these positions in the future, would qualify as a “commodity pool” and the operator would become a CPO with all attendant compliance obligations.

Further, this Orders confirms the CFTC’s view that carbon credits are “commodities” and that the CFTC will continue investigating and prosecuting fraud in related carbon credits and other environmental commodities.

Beware of the Law of Unintended Consequences

August 8, 2024

By Christopher Horn
Partner | Financial Services

A recent study, **Government Litigation Risk and the Decline in Low-Income Mortgage Lending**, provides further evidence that the law of unintended consequences reigns supreme, particularly in the realm of public policy. The study examined the effects of litigation brought by the Department of Justice in the early 2010s against large mortgage lenders for alleged fraud in the origination of Federal House Administration ("FHA") mortgages. The litigation resulted in a $5 billion settlement paid by 31 large FHA lenders to the Federal government.

The study found that the settlement caused large lenders to precipitously exit the FHA market, which significantly reduced low-income households' access to mortgage credit. To make matters worse, the study found no evidence that the litigation led to an improvement in underwriting standards or to a reduction in default risk for FHA loans. The authors conclude that:

"Our findings suggest that fines, while often considered an efficient form of punishment, can still have unintended consequences. In this case, large legal settlements drove large firms out of the market, and ultimately reduced borrowers' access to credit. Our results highlight the importance of considering potential unintended societal costs when disciplining firms."

The study was authored by **W. Scott Frame**, the Chief Economist and Head of Policy at the Structured Finance Association, Kristopher Gerardi of the Federal Reserve Bank of Atlanta, Erik J. Mayer of the University of Wisconsin-Madison, Finance Department, Billy Xu of the University of Rochester – Simon Business School, and Lawrence Chengzhi Zhao, of Texas Tech University – Area of Finance.

The UK Relaxes Its Requirements Around Payment for Investment Research

August 8, 2024

By Alix Prentice
Partner | Financial Regulation

In **Policy Statement PS24/9** on Payment Optionality for Investment Research, the UK's Financial Conduct Authority ("FCA") has set out its final rules on allowing payments for research to once again be 'bundled' (i.e. made jointly) with payments for execution and brokerage services.

As we **reported previously**, the FCA consulted in its Consultation Paper CP24/7 in April of this year on its proposals for unbundling, and the 'guardrails' it was suggesting should be in place to protect consumers. The final rules set out in PS24/9, while not essentially different from CP24/7's proposals, do make some changes in response to concerns about the practical implementation of those guardrails.

These include changes to how firms required to put in place the following guardrails when bundling:

- Budgeting: the new rules now allow flexibility to aggregate when budgeting at the level of an investment strategy or group of clients, and give more latitude on the disclosures that are required when budgets are exceeded;
- Research provider disclosures: the new rules no longer require the disclosure of the most significant research providers and give more latitude on the aggregation of disclosures;
- Price benchmarking: CP24/7's requirement to benchmark the price paid for research has been amended to require firms to ensure that these charges are reasonable, with benchmarking being one means of doing this;
- Cost allocation and disclosure: again, these requirements have been given more latitude and flexibility, including on how firms estimate expected annual costs;
- Separately identifiable research charges: the prescriptive requirement for written agreements with research providers has been broadened to require arrangements to be in place that allow research costs to be identified.

The rules apply from 1 August 2024. As they represent an option that has been added to existing requirements (which allow managers to pay for research from either their own resources or from a dedicated research payment account set up for individual clients), the FCA says that "*if you want to take up the new payment option, you must make sure that you comply with our requirements and that you have updated your internal procedures.*"

Cadwalader Tops 2024 Annual Edition of IFLR1000

August 8, 2024

Cadwalader lawyers and practices once again have been recognized as industry leaders in the **34rd edition of the *IFLR1000***, a publication focused on financial and corporate transactional work.

In the United States, Cadwalader is ranked among the top firms in several core areas including Banking, Structured Finance and Securitization, Equity Capital Markets, Financial Services Regulatory, Investment Funds, Mergers and Acquisitions, Project Development, Project Finance, Real Estate and Restructuring and Insolvency.

You can see the listed attorneys **here**.

Cadwalader Shortlisted for Law Firm of the Year at the 2024 SCI CRT Awards

August 8, 2024

Cadwalader has been shortlisted in the North American Law Firm of the Year category for this year's *SCI* Capital Relief Trade Awards, celebrating the team’s incredible achievements in capital relief trades.

The team was cited for leveraging the firm’s existing relationships with bank and fund clients, its market-leading derivatives and securitization practices, and its deep bench of regulatory and product-level specialists to position Cadwalader as the leading North American law firm in CRT transactions. *SCI* noted that Cadwalader has developed a practice that has become the “go-to” choice for banks, investors and advisors who participate in this market. Read more about our Capital Relief Trades practice **here**.

The winners will be announced during a gala black-tie dinner held at the Royal Institute of British Architects on October 17th. Read more **here**.