GIBSON DUNN

Recent Developments at the New York State Department of Financial Services

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Department Overview

- The New York State Department of Financial Services ("DFS") is the state's primary regulator of financial institutions and insurance companies with jurisdiction over approximately 1,500 financial institutions and 1,400 insurance companies.
- The agency's new leadership has been focused heavily on consumer protection in the absence of federal regulation, and asserting its authority over emerging areas of significance to New York's banking and insurance industries.

Roadmap

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1.
New Department Leadership and Organizational Structure

New Department Leadership and Organizational Structure

- Superintendent Linda Lacewell became acting head of DFS in February 2019 and was confirmed in June 2019.
- She was previously a longtime aid to Governor Andrew Cuomo, most recently serving as his chief of staff. She also served as the State's first chief risk officer and spent nine years as an AUSA in the Eastern District of New York.
- She has signaled an emphasis on bringing resources to bear on the financial technology ("fintech") industry, and curbing new threats to data privacy and technological infrastructure.

New Department Leadership and Organizational Structure

Superintendent Lacewell has overseen the creation of new divisions focused on emerging trends and areas of concern in the financial industry.

- In April 2019, she announced a new **Consumer Protection and Financial Enforcement Division**, which combines several prior DFS Divisions.
  - Led by **Katherine Lemire**, former partner at a compliance and investigative consulting firm and prosecutor in the Manhattan District Attorney's Office and the United States Attorney's Office for the Southern District of New York.
- In May 2019, she announced a new **Cybersecurity Division** focused on protecting consumers and industries from cyber threats, enforcing the agency's new cybersecurity regulations, and overseeing a wide range of cyber matters.
  - Led by **Justin Herring**, former Chief of the Cyber Crimes Unit at a U.S. Attorney's Office.
- In July 2019, she announced a new **Division of Research and Innovation**, intended to keep abreast of financial services developments and supervise and license virtual currencies on the heels of DFS's 2015 BitLicense regime.
  - Led by **Matthew Homer**, former head of policy and research at a New York fintech company.

New Department Leadership and Organizational Structure

- In April 2020, Richard Weber became the **General Counsel** of DFS. He replaced Acting General Counsel, Kevin Bishop, who is now the Executive Deputy General Counsel.
  - Prior to joining DFS, Weber was the head of Financial Crime Prevention for the Americas at UBS and Deutsche Bank.
  - He also has been Chief of the Criminal Investigation Division at the IRS and held senior roles in the New York County District Attorney's Office and United States Attorney's Office.

- In May 2020, Nina Chen became the first **Director of Sustainability and Climate Initiatives**. She will develop environmental policies at the intersection of finance and climate risk mitigation.
  - Chen was previously a Director of Conservation Investments at the Nature Conservancy and has a broad career in finance.

New Leadership

- In November 2019, DFS announced that My Chi To would become the new **Executive Deputy Superintendent of the Insurance Division**.
- She was previously a partner in a large New York law firm and has spoken about the division's commitment to "protecting consumers while encouraging growth in the insurance industry."

Remaining Leadership

- Shirin Emami remains with DFS as the **Executive Deputy Superintendent of the Banking Division**.

2.
COVID-19 Developments

COVID-19 and Health Insurance

- Since March, DFS has taken a number of steps to address the **novel coronavirus** that have impacted the **health insurance industry**:
  - In March, insurers were instructed to **waive cost-sharing associated with testing** for the coronavirus. They also were required or advised, among other things, to keep New Yorkers informed of benefits and offer telehealth services.
    - This mandate was soon expanded to require insurers to **waive cost-sharing for in-network telehealth visits**, regardless whether related to coronavirus.
    - DFS also subsequently required insurers to **cover coronavirus testing**.
  - In March, DFS announced a **special health insurance enrollment period** that would be available to New Yorkers and subsequently extended it until June.

COVID-19 and Health Insurance (Cont'd)

- In April, DFS required health plans to **defer the payment of insurance premiums** due under individual and small group health commercial insurance plans for businesses and individuals experiencing financial distress due to the pandemic.
  - DFS required insurers to continue paying claims during this period without reporting late payments to credit rating agencies.
- In April, DFS directed health insurers to **immediately pay hospital claims** and **suspend preauthorization requirements** for hospital services.
- In May, DFS required health insurers to **waive out-of-pocket costs for in-network mental health services** for frontline essential workers.

COVID-19 and Other Insurance

- In March, DFS clarified that **travel insurers** may offer **"cancel for any reason" policies** in addition to providing for cancellation due to COVID-19.
  - Six global and national insurance companies agreed to offer such policies.
- In March, DFS mandated **deferral of payments on life insurance premiums** for 90 days and on **property/casualty insurance premiums** for 60 days. Extended in June.
  - The mandate received significant industry support from LICONY.
- In June, DFS directed insurers to **accelerate resolution and payment** of claims by businesses and individuals who were damaged by looting.
  - DFS stated that insurers should recognize that policyholders may have limited documentation due to ongoing burdens relating to COVID-19 and social unrest.

COVID-19 and Financial Institutions

- In March, DFS permitted **temporary relocation** and **remote meetings**, and **waived various reporting requirements** for 45 days.
- In March, DFS required mortgage providers to provide **90-day mortgage relief**, including waiver of payments due to financial hardship, no negative reporting to credit bureaus, and postponement of foreclosures.
  - DFS also required banks to **eliminate ATM, overdraft, and credit card late fees**.
  - In June, however, DFS granted mortgage servicers a 60-day extension to comply with new periodic statement requirements.
- In April, DFS reached agreement with the private student loan industry to permit borrowers facing hardship due to COVID-19 to seek **90-day student loan relief**.
- In April, DFS permitted chartered financial institutions to **conduct virtual stockholder meetings** and extended **deadlines for annual stockholder meetings**.
- In June, DFS reached agreement with credit reporting agencies to provide **free credit reports** and urged financial institutions to minimize negative reporting.

3.
Insurance

Guidance Regarding Unlicensed Insurance Sales Activity

In September 2019, DFS issued **new guidance to life insurers and producers** on **unauthorized activity**, with the goal of "protect[ing] New York pension holders from unlicensed activity in New York's pension risk transfer market."

- DFS reiterated that an insurer's employees or representatives may not solicit, negotiate, sell, or service group annuity contracts through in-person meetings, phone calls, mail, emails, access to web portals, or in any other manner from any location in New York if the insurer is unauthorized to do so in the State.
- DFS also warned that an insurance producer or other person may not aid or call attention to any unauthorized life insurer in New York, with potential penalties including fines, license suspension, and license revocation.
- This rule contains a limited exception for certain "back office" activities in New York, such as gathering information about the insurance industry or assembling policies on non-New York risks, but not if they constitute solicitation or sale of insurance.

Amendments to Insurance Regulation 187

In August 2019, a new **best-interest rule (Insurance Regulation 187)** came into effect, requiring insurers to establish standards and procedures to supervise recommendations by agents and brokers with respect to life insurance policies and annuity contracts so that any transaction concerning such policies is in the **"best interest" of the consumer** and appropriately addresses the consumer's insurance needs and financial objectives at the time of the transaction.

- Imposes expanded obligations on producers to act in the consumer's "best interest" when making recommendations regarding product purchase, replacement, or modification.
- Expands the supervisory obligations of insurers by requiring them to develop and maintain procedures to prevent financial exploitation and decline a transaction unless there is a reasonable basis to believe the transaction is suitable for the consumer.
- Various insurance agents and brokers challenged the new regulation in state court, asserting among other things that it exceeded DFS's authority and was vague and confusing. The court upheld the regulations as "proper exercise" of authority. An appeal is pending.

Insurance Regulation Enforcement Actions and Defense

DFS has undertaken significant actions to **enforce or defend regulations**.

- In April 2020, DFS announced that a retirement services company would pay $45 million for violations relating to **unlicensed solicitation, communication, and performance** of pension risk transfer business.
  - DFS is investigating other violations in this market.
- In September 2019, six life insurers agreed to pay more than $1.8 million in penalties and restitution for allegedly **violating Insurance Regulation 187** by persuading customers to switch from "deferred" annuities to "immediate" policies without properly notifying them if it was suitable.
  - In April 2020, three additional life insurers agreed to pay $1.1 million in penalties and restitution for allegedly violating Regulation 187.
  - DFS's industry-wide investigation into deferred to immediate annuity replacement practices remains ongoing.

Insurance Regulation Enforcement Actions and Defense

- In January 2019, DFS entered into a consent order with an insurance company, under which the insurance company would pay a $19.75 million penalty and more than $189 million in benefits for its 2017 self-report that it had **not sufficiently located and notified** 30,000 retirees that they were **eligible for retirement benefits**—significantly larger than a similar $1 million fine by regulators in Massachusetts.
- In February 2020, DFS announced that an insurance company and insurance producers that assist wireless communications equipment venders would pay $4 million for providing **inadequate disclosures and improperly bundling insurance products** in violation of agency guidance.
- After two years of litigation, DFS partially prevailed on the title insurance industry's **challenge to Insurance Regulation 208**, with an appellate ruling invalidating the regulation's restrictions on certain closer and ancillary fees, but upholding its restrictions on marketing and advertising-related expenditures.
  - Subsequent proceedings struck down the regulation, but reversed on appeal.

4.
Data Privacy

Cybersecurity Regulations

DFS's **cybersecurity regulations** went into effect in March 2017 (with some provisions not effective until March 2019). They require:

- A detailed data security plan;
- Increases in monitoring of third-party vendors;
- Appointment of chief information security officers;
- Reporting of breaches to DFS within 72 hours.
- Monitoring and testing of vulnerability;
- Control measures such as multi-factor authentication and encryption of nonpublic information.

Data Privacy Enforcement

DFS has continued pursuing enforcement actions for data privacy.

- In July 2019, DFS entered into a settlement with credit reporting company, which agreed to pay $10 million in penalties to DFS for a 2017 data breach.
  - According to DFS, the breach exposed sensitive information of nearly 8.5 million New Yorkers. The settlement comes after DFS and NYOAG initiated separate investigations into the credit rating agency's practices and the communications surrounding its data breach, the latter as part of a multi-state investigation.
  - As a result of the Attorney General's investigation, the company agreed to pay $9 million to the State of New York and provide New York consumers restitution in connection with settlements that have been reached in multi-district class action suits and settlements with the FTC and CFPB.

5.
Fintech and Cryptocurrency

Litigation with the Office of the Comptroller of the Currency

In October 2019, DFS prevailed against the federal Office of the Comptroller of the Currency (OCC), obtaining an order **setting aside OCC's regulation** permitting non-depository fintech institutions to obtain **special purpose national bank charters**. See *Lacewell v. OCC*, No. 18 CIV. 8377, 2019 WL 6334895 (S.D.N.Y. Oct. 21, 2019).

- DFS challenged OCC's authority to accept fintech charter applications under the National Banking Act on the ground that non-depository institutions are not in the "business of banking" and are therefore outside OCC's regulatory ambit.
- The district court agreed with DFS and denied OCC's motion to dismiss. Following that decision, DFS and OCC negotiated but failed to agree on proper relief.
- The OCC has appealed to the Second Circuit, where the case remains pending.

Cryptocurrency Guidance

DFS issued **new guidance governing virtual currencies** in New York.

- DFS requires creators, investors, and traders to obtain a "BitLicense," which requires Bitcoin exchanges and other virtual currency operators to comply with anti-money laundering, consumer protection, and other requirements.
- The BitLicense reportedly led to an "exodus" of cryptocurrency companies.
- The new guidance provides general "frameworks" for establishing an online list of digital coins approved for business in New York and allowing licensed companies to self-certify compliance and listing or adoption of new coins.
- The guidance became final in June 2020.

New Approvals

DFS has continued to **approve virtual currencies** under its BitLicense regime.

- In July 2019, DFS approved BitLicenses for **Seed Digital Commodities Market LLC and Zero Hash LLC**. The former will serve as a matching engine for buyers and sellers will cater to institutional investors. Zero Hash will serve as Seed Digital's money transmitter.
- In December 2019, DFS granted a BitLicense to **SoFi**, clearing the way for trades in cryptocurrencies such as Bitcoin, Ethereum, and Litecoin on SoFi's platform.
- In September 2019, DFS authorized the sale of PAX Gold, a digital cryptocurrency backed by physical gold. The currency is sold by **Paxos Trust Company LLC**, which also received approval to issue Binance USD, a U.S. dollar-backed cryptocurrency.
- In May 2020, DFS approved **Eris Clearing, LLC**, as a licensee of virtual currency. The license allows Eris to be a clearing entity for contracts bought and sold on its platform, **ErisX**. Eris Clearing joins 20+ entities engaging in virtual currency business in New York.

Developments in Cryptocurrency and Fintech

- In June 2020, DFS signed a **Memorandum of Understanding ("MOU") with France's** Autorité de Contrôle Prudentiel et de Résolution (ACPR) to ease entry of fintech companies into the New York and French financial markets.
  - DFS and ACPR will recommend fintech companies to one another, exchange information, and collaborate to implement regulatory and supervisory expertise.
- In June 2020, DFS launched its **FastForward program** to support innovation in Fintech, InsurTech, and HealthTech in the COVID-19 era.
  - Companies engage with DFS to explore regulatory issues relating to their innovations.
  - The FastForward program builds upon an InsurTech pilot, "Project WhiteHall."
- In June 2020, DFS proposed a new **"conditional licensing framework"** for start-ups to partner with approved entities for operational and other support.
- DFS also signed an **MOU with SUNY** expressing an intent to launch a virtual currency program, "SUNY BLOCK," to make use of conditional licenses.

6.
Confidential Supervisory Information

Confidential Supervisory Information

In November 2019, DFS **proposed a new regulation** allowing regulated entities to share **"confidential supervisory information"** with counsel and independent auditors.

- In exercising authority over banking organizations, DFS has long mandated that reports, memoranda, or correspondence relating to investigations and examinations be deemed "confidential" and not be subject to disclosure without DFS approval.
- Counsel often must obtain approval before considering such information and can be impaired from providing timely and thorough advice as to compliance with banking statutes.
- The new regulation would have provided a "limited exception," so the information could be shared with counsel and auditors, assuming they entered into a written agreement stating that the information would be used solely for "legal representation or auditing services" and would be disclosed solely to employees, directors, or officers on a "need to know" basis.
- The new regulation would place DFS closer in line with other regulators of financial institutions.

According to the State Register, DFS **withdrew the proposed regulation** in June after a comment period and stated that the agency must prepare a new version of the regulation.

7.
Other Enforcement Priorities

Bank Enforcement Actions

- In April 2019, DFS announced that a bank would pay a fine of $180 million and agree to a variety of oversight and compliance measures as part of a global settlement for alleged **transactions in sanctioned countries** like Iran, Syria, and Sudan.
- That month, DFS announced that a bank would pay $405 million and agree to disciplinary review, hiring, oversight, and compliance measures as part of a global settlement for alleged **transactions in sanctioned countries** like Iran, Libya, and Sudan.
- In April 2020, DFS announced that a bank would pay $35 million and submit plans to revise its compliance program as a result of alleged violations of the Bank Secrecy Act and Anti-Money Laundering laws. The bank had purportedly failed to prevent large-scale **fraud and money-laundering** schemes in its New York branch.
- In April 2020, DFS announced that a bank would pay $220 million for knowingly **facilitating its customers' tax evasion** and initially failing to cooperate with DFS's investigation. The bank also agreed to improve its policies and procedures.

Investigations and New Powers

- In August 2019, DFS announced that it would lead a multistate investigation into the **payroll advance industry**.
  - The investigation focuses on allegations that industry members collected illegally high interest rates in the form of "tips" or other fees, and forced improper overdraft charges on vulnerable low-income consumers.
- DFS recently launched an investigation into the **student "debt relief" industry**, subpoenaing eight debt relief companies concerning advertising and fees.
  - The investigation focuses on allegations that companies failed to alert borrowers of federal programs that offer the same programs for free, or that they have otherwise misrepresented the relief they can achieve.
- In April, the Financial Services Law was amended to empower DFS to **regulate and sanction student loan consultants** and create a private remedy.
  - The new Article 7 will require student debt consultants to enter contracts (with disclosures), permit cancellations, and refrain from abusive practices.

Conclusions

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