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Asserting Bank Examination Privilege in Litigation

Determining the Legal Basis and Working With Regulators to Assert and Defend the Privilege

WEDNESDAY, MAY 15, 2019

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

Eric Epstein, Special Counsel, **Pillsbury Winthrop Shaw Pittman**, New York

Michelle K. Ng, Attorney, **Pillsbury Winthrop Shaw Pittman**, New York

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The Bank Examination Privilege

Presenters:

Eric B. Epstein
Michelle Ng

May 15, 2019

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Our Background

- We are members of Pillsbury's China-focused litigation team
- We have extensive experience defending regulatory privileges in litigation
- Notable publications:

  1) The American Bar Association treatise The Bank Examination Privilege (2017)

  2) Yale Journal on Regulation, *Why the Bank Examination Privilege Doesn't Work as Intended* (2017)

- Feel free to contact us at:

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Overview of the Privilege

- Protects banks' regulatory examination records during litigation
- Federal common law
- Recognized in every federal circuit – at circuit court level or district court level

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The SAR Privilege

- Bank Secrecy Act: Do not notify "any person involved in the transaction that the transaction has been reported." 31 U.S.C. § 5318(g)(2).
- "A SAR, and any information that would reveal the existence of a SAR, are confidential," and "shall not be disclosed." 12 C.F.R. § 21.11(k).
- "[A]n unqualified discovery and evidentiary privilege" with respect to SARs. *Whitney Nat'l Bank v. Karam*, 306 F. Supp.2d 678, 682 (S.D.Tx. 2004).

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FOIA Exemption 8

- Information "contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions." 5 U.S.C. § 552(b)(8).
- Proposed Federal Rule of Evidence 509 – information "not otherwise available to the public pursuant to 5 U.S.C. §552."

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28 U.S.C. § 1828x

- "Privileges not affected by disclosure to banking agency or supervisor."
- Submitting privileged information during a bank examination ≠ waiver.

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BERPA

- Bank Examination Report Protection Act (BERPA)
- Would have added a “Bank Supervisory Privilege” to federal statutory law.
- “All confidential supervisory information shall be the property of the Federal banking agency that created or requested the information and shall be privileged from disclosure to any other person.”
- Would have prohibited litigants from requesting examination reports directly from regulated banks.

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Regulatory Policy

- "Non-public OCC information" includes examination records. 12 C.F.R. § 4.32(b)(1).
- "It is the OCC's policy regarding non-public OCC information that such information is confidential and privileged." 12 C.F.R. § 4.36(b).
- "Unauthorized disclosures prohibited. All non-public OCC information remains the property of the OCC. No supervised entity . . . may disclose non-public OCC information without the prior written permission of the OCC . . ." 12 C.F.R. § 4.36(d).

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Origins of the Privilege

In re Subpoena Served upon Comptroller of the Currency, 967 F.2d 630 (D.C.Cir. 1992).

- Shareholders' class action and derivative suit against bank and bank officers – in federal court in Rhode Island
- Demanded that bank produce confidential communications with OCC and Federal Reserve
- "[A] unique and objective contemporaneous chronicle of the true financial status of [the bank] and defendants' knowledge."
- Bank refused – plaintiffs then made a similar demand on OCC and Federal Reserve – and then sued to enforce in District of Columbia federal court

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Origins of the Privilege

In re Subpoena Served upon Comptroller of the Currency, 967 F.2d 630 (D.C.Cir. 1992).

District Court

- Rejects assertion of privilege
- Sending examination reports to banks = waiver of privilege
- "Don't send [examination reports] to the banks, then you don't have a problem."

Appellate Court

- Sending examination reports to banks ≠ waiver
- Providing examination reports to the bank "is a fundamental part of the regulatory process."
- "To hold that the privilege is waived or even weakened merely because the regulator provides the report to the bank would quickly render the privilege a dead letter."

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Rationale for the Privilege

1. "Bank management must be open and forthcoming in response to the inquiries of bank examiners, and the examiners must in turn be frank in expressing their concerns about the bank." *In re Subpoena Served upon Comptroller of the Currency*, 967 F.2d 630 (D.C.Cir. 1992).
2. "[D]isclosure of confidential portions of a bank report might breed public misunderstanding and unduly undermine confidence in the bank." *Delozier v. First Nat'l Bank of Gatlinburg*, 113 F.R.D. 522 (E.D.Tenn. 1986).

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Scope of the Privilege

- "[A]gency opinions and recommendations and banks' responses thereto." *In re Bankers Trust Co*., 61 F.3d 465, 471 (6th Cir. 1995).
- The "iterative process of comment by the regulators and response by the bank." *In re Subpoena Served upon Comptroller of Currency*, 967 F.2d 630, 633 (D.C.Cir. 1992).
- "[P]urely factual material falls outside the privilege, whereas opinions and deliberative processes do not." *Merchants Bank v. Vescio*, 205 B.R. 47, 42 (D.Vt. 1997).

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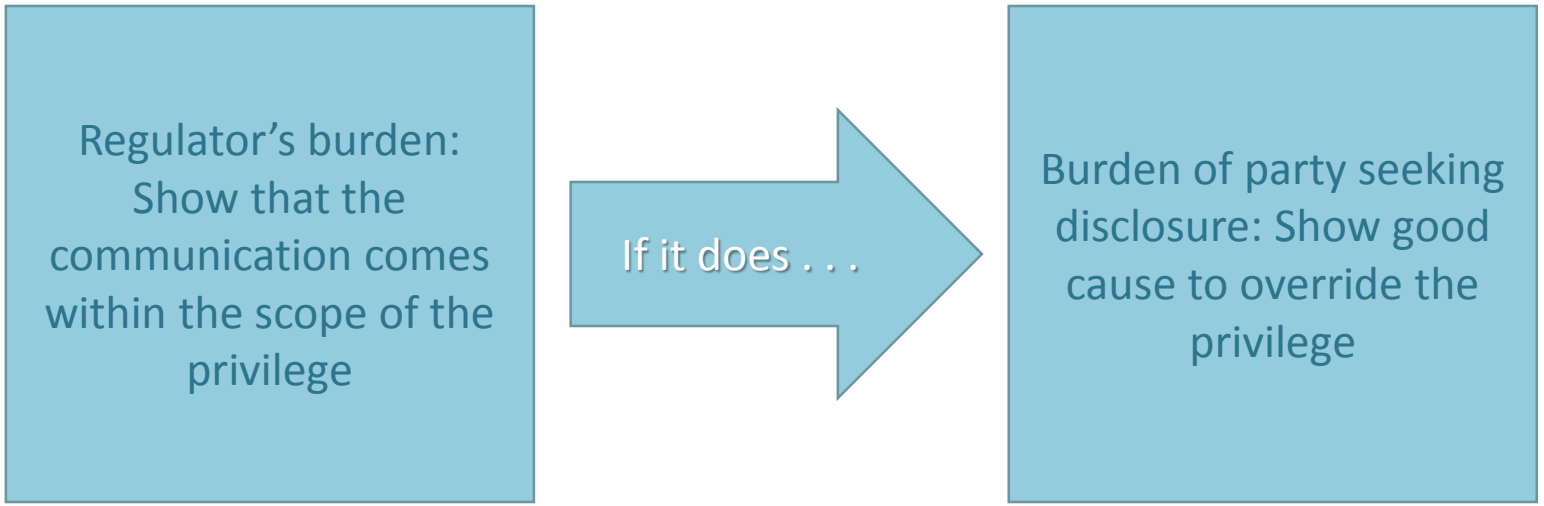
Burden-Shifting Framework



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Good Cause Test

Factor	Significance
1. Relevance	More relevant = favors disclosure
2. Availability of other, non-privileged sources of evidence	Other evidence available = weighs against disclosure
3. Seriousness of the litigation	Serious case = favors disclosure
4. Role of government in litigation	Governmental role = favors disclosure
5. Possible chilling effect of disclosure on future examinations	Likely chilling effect = weighs against disclosure

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Recent Developments

- Extending the bank examination privilege to consumer protection exams?
- Interplay between bank examination privilege and state privilege law.
- The role of sovereign immunity.

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Consumer Protection Exams

U.S. v. Ocwen Loan Servicing, U.S. District Court, E.D.Tx., No. 4:12-cv-00543.

- June 2016: CFPB intervenes to assert the bank examination privilege.
- The CFPB's position: The privilege does cover CFPB supervisory information.
- Case settled before Court resolves the issue.

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Consumer Protection Exams

Lawrence E. Jaffe Pension Plan v. Household Int'l, Inc., 239 F.R.D. 508 (N.D.Ill. 2006).

- Securities fraud class action
- Plaintiff seeks state regulatory documents with respect to various Household branch offices.
- Several states assert the bank examination privilege.
- The Court rejects these assertions of the bank examination privilege because "it is undisputed that the regulated entities at issue here are not banks."

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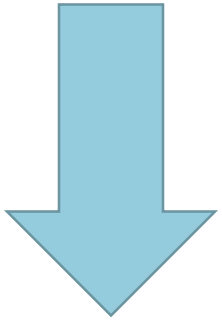
Consumer Protection Exams

Federal Housing Finance Agency v. JPMorgan Chase & Co., 978 F. Supp.2d 267 (S.D.N.Y. 2013): FHFA may assert the bank examination privilege.



Fairholme Funds, Inc. v. United States, 128 Fed. Cl. 410 (2016), *aff'd in relevant part*, 2017 U.S. App. LEXIS 2059 (Fed. Cir. Jan. 30, 2017): Agrees that FHFA may assert the bank examination privilege.

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State Law

Example – 5 Del. C. § 145, entitled "Financial Institution Supervisory Privilege":

"[A]ll confidential supervisory information shall be the property of the [State Bank] Commissioner and shall be privileged and protected from disclosure to any other person and shall not be discoverable or admissible into evidence in any civil action; . . ."

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State Law

Example – Or. Rev. Stat. Ann. § 706.720(5):

"The records are subject to production if the court before which a civil or criminal action is pending finds that the examination and production is essential for establishing a claim or defense."

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State Law

Example – Wash Rev. Code Ann. § 32.04.220(6):

"In any civil action in which the reports are sought to be discovered or used as evidence, any party may, upon notice to the director [of the Washington State Department of Financial Institutions], petition the court for an *in camera* review of the report. The court may permit discovery and introduction of only those portions of the report which are relevant and otherwise unobtainable by the requesting party."

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State Law

Federal Rule of Evidence 501:

"The common law — as interpreted by United States courts in the light of reason and experience — governs a claim of privilege unless any of the following provides otherwise:

- the United States Constitution;
- a federal statute;
- or rules prescribed by the Supreme Court.

But in a civil case, state law governs privilege regarding a claim or defense for which state law supplies the rule of decision."

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State Law

United States ex rel. Fisher v. Ocwen Loan Servicing, LLC, 2016 U.S. Dist. LEXIS 73759 (E.D.Tx. Jun. 7, 2016).

- Party seeks non-public examination records from West Virginia Department of Financial Services.
- The Court notes: "Clearly, these communications originated with an understanding that they would not be disclosed under state law."
- But the Court applies federal privilege law.
- The Court finds good cause to override the privilege.

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State Law

SBAV LP v. Porter Bancorp. Inc., No. 3:13-CV-00710, U.S. District Court, W.D.Ky.

- Diversity-jurisdiction case.
- Party seeks records of examinations conducted by FDIC and Federal Reserve.
- Mar. 31, 2015 decision: The Court defers to Kentucky privilege law – which does not shield bank examinations – so the records are non-privileged.

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State Law

SBAV LP v. Porter Bancorp. Inc., No. 3:13-CV-00710, U.S. District Court, W.D.Ky.

- Nov. 20, 2015: FDIC and Federal Reserve move for reconsideration (Dkt. No. 241-1).
- Their argument: The bank examination privilege isn't *just* a privilege. It's a substantive federal policy. So, it should override state law.
- Dec. 1, 2015: Based on settlement of case, Court vacates the Mar. 31 decision as moot – does not resolve the motion for reconsideration (Dkt. No. 244).

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State Law

- *Erie v. Tompkins,* 304 U.S. 64 (1938).
- To overcome *Erie*, must show that there are "uniquely federal interests at stake." *Ungaro-Benages v. Dresdner Bank AG*, 379 F.3d 1227, 1233 (11th Cir. 2004).

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Sovereign Immunity

Serving a subpoena on a federal regulator.

- *Yousuf v. Samantar*, 451 F.3d 248, 257 (D.C. Cir. 2006): No need to "graft onto discovery law a broad doctrine of sovereign immunity."
- *U.S. E.P.A. v. Gen. Elec. Co.*, 197 F.3d 592, 597 (2d Cir. 1999): A subpoena would "compel [an agency] to act and therefore is barred by sovereign immunity in the absence of a waiver."
- But the Second Circuit leaves open the possibility of applying the Administrative Procedure Act (APA).

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Sovereign Immunity

Manzo v. Stanley Black & Decker, Inc., 2017 U.S. Dist. LEXIS 48038 (E.D.N.Y. Mar. 30, 2017).

- Notes that the circuit split is still unresolved.
- "Some circuits utilize the arbitrary and capricious standard" set forth in the APA.
- But other circuits "rely on the standards set forth in Fed. R. Civ. P. 26 and 45, which federal courts typically apply in analyzing non-party subpoenas."

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Sovereign Immunity

FDIC v. Crowe Horwath LLP, 2018 U.S. Dist. LEXIS 105880, at **13-15 (N.D.Ill. Jun. 25, 2018).

- Another recent decision describing the status of the circuit split.
- This court decides to review FDIC's position "under the Federal Rules rather than the APA."

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