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M E M O R A N D U M

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To Our Clients and Friends

Re: Interagency Guidance on Unfair or Deceptive Acts
or Practices by State-Chartered Banks

The Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation (the “Agencies”) have issued guidance outlining standards that they will consider in determining if acts or practices by state-chartered banks are unfair or deceptive. Unfair or deceptive acts or practices are illegal under the Federal Trade Commission Act (“FTC Act”).

The Agencies also provide strategies for managing risk in this area and guidance on best practices to avoid engaging in unfair or deceptive acts or practices. The guidance focuses on those areas that are particularly prone to unfair or deceptive practices: advertising and solicitations, servicing and collections and the management and monitoring of employees and third-party service providers.

The Agencies warn that acts and practices deemed unfair or deceptive under the FTC Act may also violate other federal or state statutes; and conversely, an act or practice may be in technical compliance with other applicable laws but violate the FTC Act. State-chartered banks are advised to pay particular attention to the Truth in Lending and Truth in Savings Acts, Equal Credit Opportunity and Fair Housing Acts and the Fair Debt Collection Practices Act.

STANDARDS FOR UNFAIR ACTS OR PRACTICES

To be considered unfair an act or practice must meet all of the following criteria:

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- The act or practice must cause or be likely to cause substantial injury to consumers.

Substantial injury usually involves monetary harm. An act or practice that causes a small amount of harm to a large number of people may be deemed to cause substantial injury. Emotional impact or speculative harm will not ordinarily make an act or practice unfair.

- Consumers must not reasonably be able to avoid the injury.

Consumers cannot reasonably avoid injury from an act or practice if it interferes with their ability to effectively make decisions. An act or practice may also be unfair where consumers are subject to undue influence or are coerced into purchasing unwanted products or services.

- The injury must not be outweighed by countervailing benefits to consumers or to competition.

The act or practice must be injurious in its net effects. Offsetting benefits may include lower prices or a wider availability of products and services. Costs that would be incurred for remedies or measures to prevent the injury will also be taken into account in determining whether an act or practice is unfair. Such costs may include direct costs to the bank as well as costs to society as a whole of any increased burden.

Public policy considerations (e.g., a particular practice violates a state law or banking regulation or is permitted under state law) may be considered in determining whether an act or practice is unfair but will not serve as the primary basis for determination.

STANDARDS FOR DECEPTIVE ACTS AND PRACTICES

To be considered deceptive a representation, omission or practice must meet all of the following criteria:

- There must be a representation, omission or practice that misleads or is likely to mislead the consumer.

The Agencies will evaluate the representation, omission or practice in the context of the entire advertisement, transaction or course of dealing. Examples of acts or practices that have the potential to be deceptive include making misleading cost or price claims; using bait-and-switch techniques; offering a product or service that is not available; omitting

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material limitations or conditions from an offer; selling a product unfit for the purposes for which it is sold and failing to provide promised services.

- The act or practice must be considered from the perspective of the reasonable consumer.

The test is whether the consumer's expectations or interpretation are reasonable in light of the claim made. When representations or marketing practices are targeted to a particular audience, the standard is based upon the effects of the act or practice on a reasonable member of that group. If a representation conveys two or more meanings to reasonable consumers and one is misleading, the representation may be deceptive. An act or practice may also be deceptive if a significant minority of consumers in a relevant class is misled even if the majority in that class is not. In determining how a reasonable consumer would respond, the Agencies will consider the entire advertisement, transaction or course of dealing.

- The representation, omission or practice must be material.

The representation, omission or practice must be likely to affect a consumer's decision regarding the product. The following are considered to be material: information about costs, benefits or restrictions on the use or availability of product or service; express claims made with respect to a financial product or service; an implied claim when it is demonstrated that the institution intended that the consumer draw certain conclusions based upon the claim; claims made with the knowledge that they are false; and omissions when the financial institution knew or should have known that the consumer needed the omitted information to evaluate the product or service.

The interagency guidance can be found on our web site at http://www.schwartzandballen.com/whats_new.html.

If you have any questions, please call Gilbert Schwartz, Robert Ballen or Tom Fox at (202) 776-0700.