Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Dem AG Gains May Spur State Financial Services Action

By **Jon Hill**

Law360 (November 16, 2018, 9:39 PM EST) -- Democrats have strengthened their presence in state-level law enforcement after flipping the attorney general's office in several state in the midterm elections, gains that some financial services experts say could make for a tougher enforcement landscape for banks and other financial services firms.

Results from the recent elections show that Democrats have captured state AG offices from Republicans in four states — Colorado, Michigan, Nevada and Wisconsin — while maintaining control of AG seats in New York, California, Illinois and nine other states, plus the District of Columbia.

Combined with the eight states where current Democratic AGs were not up for election and the two states where Democrats have been or will likely soon be appointed as AGs, those results mean that a Democrat will soon be the top prosecutor in a majority of U.S. states — including Iowa, Massachusetts and Maryland, where Republicans will control the governors' mansions.

"Compared to the last few cycles, this was a resurgence on the Democratic attorney general side," said Joe Jacquot, a Foley & Lardner LLP partner and former chief deputy attorney general of Florida. "I think those AGs — not only the ones that won in significant states, like Michigan, Wisconsin and Nevada, but also as a whole — feel a new motivation, and I think you're going to see them press that in enforcement actions."

How hard and where this blue wave lands on the financial services industry will be shaped in part by coordination among these state AGs, according to attorneys who spoke to Law360.

With their comparatively limited resources and jurisdictions, state AG offices have often found it advantageous to team up when going after banks and other financial services firms, when cases might involve business activity in multiple states, need complex investigative work to develop and require even more complex lawyering to pursue successfully.

After the financial crisis, for example, state AGs partnered with each other and the federal government to secure huge settlements of claims related to mortgage lending, servicing and securitization. Such coordination helped produce, among other things, the largest-ever consumer financial protection settlement, when 50 AG offices and the federal government reached the landmark $25 billion national mortgage servicing settlement with five major U.S. banks in 2012.

"Some of the state AGs no doubt played a stronger role at the state level than others, but they all joined the bandwagon during this time," said Kavita Shelat, an associate at Baker Donelson Bearman Caldwell & Berkowitz PC.

What has changed in the Trump era, according to Shelat, is that state AGs have been left more to their own devices as the Consumer Financial Protection Bureau and other federal regulators have pulled back on financial services enforcement activity. That has led many Democratic state AGs to vow they will fill the void and hold financial firms' feet to the fire if the federal government won't, particularly on issues related to consumer protection.

"There are some states that have stepped up their enforcement, like Massachusetts," Shelat said. "But in order to do large-scale supervision, I don't think any state wants to put their necks out on their own."

Now that they will have four more like-minded counterparts in other states, though, Democratic state AGs will have more opportunities to build coalitions and may feel more empowered to act accordingly. In Shelat's view, this is most likely to show up as a greater emphasis on cases brought under state statutes against deceptive acts or practices.

"The importance of the midterms to me is less about the outcome of any individual state," Shelat said. "It is more about how many are the blue team and how many are on the red team."

But beyond the four state AG offices that flipped, the midterms also saw voters in California, Connecticut, Illinois and New York elect new Democratic AG candidates for the first time in years. That fresh blood in those states, which have been very active on the consumer financial protection front, may wind up being a major factor in driving new enforcement activity, according to Jacquot.

"The vast majority of these elections were run against Trump and his policies, whether that be at the CFPB, the Department of Education with student finance, or other areas," Jacquot said. "When you run a campaign on those issues, particularly as a first-time candidate for this office, and you're elected, there's not only an obligation but also a motivation to make good on those promises."

Jacquot said he doesn't see the interest in enforcement coming from solely from blue states, either. Republican state AGs were elected again in Florida, Ohio and Texas, for example, but those states have had strong consumer protection offices and have in the past helped to steer multistate litigation, according to Jacquot.

"I think you will see more and more AG offices on a bipartisan basis looking for opportunities to bring consumer results," Jacquot said. "That doesn't always have to be in opposition to the Trump administration. Republicans aren't necessarily going to pursue enforcement actions that way, but they do have obligations to care for the consumer, and I think they are going to be vigilant in that."

But Jean Veta, a Covington & Burling LLP partner and a member of the firm's financial services practice, is skeptical that the state AG election results will produce a meaningful difference in investigations and enforcement activity for banks.

"While banks may feel some effects of the blue wave, I don't look for banks to be swamped by that wave," Veta said.

Although Veta agreed that more multistate coalitions are likely, she said such coalitions are most effective when they can seize on a hot issue highly salient to the public. Veta pointed to the deluge of foreclosures

that came out of the financial crisis as an example, saying it gave state AGs a clear target for their enforcement efforts and plenty of room to run.
But in the current strong economic environment, she said she doesn't see comparable scope for such an issue to propel a coalition.

"While there's a risk there, I think it would take some work for those kinds of coalitions to gain traction," Veta said. "I think it's conceivable that we'll see some coalitions forming around various consumer protection issues, but I think most banks do pretty well on that score now."

That's where the new majority in the House next Congress may wind up being yet another factor driving state-level enforcement, according to Jacquot. Through investigations and hearings, particularly in the House Financial Services Committee, Democratic lawmakers could help focus public attention in a way that gives state AGs room to maneuver.

"Where they are attempting to push an agenda that may never be accepted and passed as legislation on the Senate side, you'll see AGs picking up on those issues and acting unilaterally where Congress has to act by consensus," Jacquot said.

Payday lending could wind up as such an issue, in Jacquot's view, given that the next Congress will be revving up just in time for the CFPB to begin its controversial rewrite of payday lending regulations that have strong support among Democrats and consumer advocates.

So what, if anything, should banks and other financial firms be doing differently to prepare themselves for this bluer state AG environment?

Shelat said a key task now facing these companies is to work through their trade organizations to continue strengthening their relationships with officials at the state level.

"Those trade organizations have lobbyists and political action committees," Shelat said. "They have people and money invested in building relationships on both sides of the aisle. In fact, one of the reasons so much money has been poured into the state races, especially state AG races, is because there's a recognition that the state level is where there is going to be potentially the most financial regulatory action."

Jacquot, meanwhile, stressed that firms should not think about state AGs the same way they might think about federal regulators and prosecutors, who are not elected officials.

"State AGs care about policy implications, they care about business implications, and they care about political implications," Jacquot said. "What you want to do is make sure you're before them, educating them on your business and industry so they're able to factor through all of those lenses how they should see your company or industry. That's the key difference — not to wait until a subpoena shows up on your door, but to make sure the state AGs understand you beforehand."

--Editing by Emily Kokoll and Peter Rozovsky.