AMERICAN BANKER

Year In Review

Reg Overhaul Complicates a Slow Recovery

By Rob Blackwell and Paul Davis and Marc Hochstein and Jeff Horwitz and Andrew Johnson and Heather Landy and Matt Monks and Jodi Schneider and Daniel Wolfe

Robert Voth, Partner

The banking industry got back on its feet in 2010, but the ground beneath remained shaky.

On the one hand, it was a time of healing as credit metrics improved measurably, profits strengthened or returned at many institutions and some banks grew stronger through acquisitions.

On the other hand, regulatory reforms in Washington, stagnant lending and revenue declines raised serious questions about how banks would earn money in the future once reductions in credit losses and expense cutbacks subside. Doubts about the housing market and the economy, coupled with accusations that banks may have improperly seized borrowers' homes, prevented confident forecasts.

There were signs that losses firmly peaked in late 2009, as credit costs fell through 2010 at large and midsize lenders. JPMorgan Chase & Co., Bank of America Corp. and Citigroup Inc. in particular benefited from steadier payments from credit card holders and homeowners. Healthier consumers let all three cut loan loss reserves through 2010, boosting earnings.

JPMorgan Chase and Citi's credit provisions, meanwhile, fell to their lowest levels since 2007 in the second half of the year. Bank of America Chief Executive Brian Moynihan proclaimed in October that "the worst is over" for credit card losses at the biggest bank in the country, as fewer layoffs meant that more consumers were staying current.

Easing losses let JPMorgan Chase begin returning capital to shareholders through stock repurchases. It hopes to raise its dividend in 2011. Citigroup, meanwhile, said in October that it aimed to deploy excess capital in 2012.

Banks' credit problems aren't over, though. Losses are falling, but they're still high by historical standards. The unsteady housing market remains an issue. Bank of America and JPMorgan Chase set aside special reserves to cover lawsuits in connection with accusations of improper foreclosures. Those two companies and Citigroup also had to set aside additional reserves for buying back unsound loans sold to Fannie Mae and Freddie Mac.

"Clearly, the legacy of this housing market crisis is going to be long-lasting," said Roger Lister, chief credit officer for U.S. financial institutions with the rating agency DBRS Ltd.

Deterioration in the commercial real estate, meanwhile, weighed on regional institutions.

The problem became evident at First Horizon National Corp. of Memphis, Tenn., in the second half of the year. Its overdue loans rose for the first time in more than a year in the third quarter because, it said, a "couple of larger commercial credits" became delinquent.

Meanwhile, from new rules on overdraft fees to the passage of the Dodd-Frank Act, it was a year of intense and expensive regulatory changes for the industry — though exactly how expensive remains anyone's guess.

Big banks may have felt singled out by provisions designed to end or at least contain the "too big to-fail" problem. But on the whole they emerged from the regulatory reform in relatively good shape: they weren't ordered to break up, and nothing

close to a reinstatement of the Glass-Steagall Act came to pass despite the advice of former Federal Reserve Chairman Paul Volcker. Volcker did, however, inspire a complicated set of new rules limiting banks' involvement in certain speculative businesses. (See Lifetime Achievement story)

The Volcker Rule notwithstanding, regulatory actions in 2010 focused more on consumer-related aspects of banking rather than the esoteric corners of finance that came to notorious prominence early in the financial crisis. Regulation E, for instance, was amended with new rules on overdraft fees that by some estimates will lower annual fee income at the top 25 banks by a combined $2.5 billion.

"It seems to us the impacts are more manageable on the capital markets side than on the consumer side" of banking, said Guy Moszkowski, an analyst at Bank of America-Merrill Lynch.

The past year introduced several fresh faces to the CEO ranks, just in time to confront a new set of challenges.

Bank of America's Moynihan, Regions Financial Corp.'s O.B. Grayson Hall Jr. and Synovus Financial Corp.'s Kessell Stelling all gained high-profile promotions in 2010. They will have to steer their banks through a sluggish recovery, unemployment hovering around double digits, stagnant loan demand and a flurry of new regulations.

"There are significant problems with asset quality and earnings that command leadership," said Rod Taylor, a founding partner at Taylor & Co., an executive recruiting firm.

Taylor said he expects more CEO changes in 2011 and 2012. Several banking companies, including PNC Financial Services Group Inc. and SunTrust Banks Inc., made moves in 2010 that seemed to line up potential heirs apparent. Taylor estimated that three-fourths of banks with assets of more than $1 billion have succession needs that involve the CEO or another top executive.

Robert Voth, a managing partner at the executive search firm CTPartners, said he expects banks to be more open to hiring from outside the industry given the radical changes in recent months.

"Banks are looking at their management structure, compensation and where they identify talent through a new lens," Voth said. "Succession planning is open to a wider suite of experiences and the breadth and depth of knowledge outside the industry is potentially as important as the traditional route."

A clear example came at Bank of America, when Moynihan went outside the industry and hired Charles Noski, a former executive at the defense contractor Northrop Grumman Corp., as chief financial officer.

Moynihan's other moves since his Jan. 1 promotion have drawn him the most attention among the incoming CEO class. So far this year, he has reached out to consumers, investors and the government in an all-out effort to improve Bank of America's image.

Taylor said he planned to keep a close eye on the banks that face difficulties with succession planning since it can often serve as a reason for a company to try to sell itself.

"Maybe the CEO problem gets solved with a merger," he said.

Finding new revenue sources will be one of executives' biggest challenges next year.

Early in 2010, it was easy to dismiss the shrinkage in lending as a reasonable response to the possibility of another shock and banks' pressing need to restore capital. Besides, with spread income as strong as it was, said Sandler O'Neill analyst Kevin Fitzsimmons, banks could out produce strong net interest margins simply by running off higher-cost deposits. But that trick only works for so long.

"Banks are putting their money into lower-and-lower-yielding stuff, and you're running out of CDs to reprice," Fitzsimmons said.

The declines increasingly vexed industry executives, some of whom see a period of stagnant growth and market share fights to come.

"You've now got record capital in the industry, but you have no loan demand, and that makes for competition," said Rene Jones, executive vice president and CFO of M&T Bank Corp., remarked in September.

As Fitzsimmons put it: "It seems nine out of 10 banks will tell you, 'We're on the lookout for small-business C&I.' When it comes to pricing, that's concerning right there."

WASHINGTON

Under the time-tested Washington rulebook, regulatory reform legislation was supposed to get weaker in 2010, as the bill was taken up by the Senate, where Republicans held more sway and their support was seen as necessary to push through a final product.

But a funny thing happened: the bill got significantly tougher, and passed without a GOP deal.

By the time the Senate passed its legislation in May, it had added brand new restrictions, including a ban on proprietary trading, that weren't included in the House-passed version, while also tacking on unrelated items, such as restrictions on interchange fees.

From the industry's point of view, the year began ominously enough when President Obama suggested adding new items to regulatory reform.

Smarting from Democrats' loss of a Massachusetts Senate seat in January, Obama looked to regain political traction by embracing a big-is-bad mantra. Among other things, he endorsed Volcker's proposal to ban proprietary trading and limit investment in hedge funds and private-equity firms.

Pundits almost immediately declared the idea dead on arrival, arguing it had come too late in the process and was too politically driven.

They were wrong.

The Volcker Rule did anything but disappear; it gained steam as part of the regulatory reform bill. In the end, even with a last-minute drive to weaken or eliminate it, the Volcker Rule made it into the final legislation.

As Obama added new requirements for "real" reform, he made Senate Banking Committee Chairman Chris Dodd's job more difficult. The Connecticut Democrat, after announcing in early January his intent to retire at yearend, had been trying to cut a deal with Sen. Richard Shelby, the banking panel's lead Republican, for several months.

Talks officially broke down on Feb. 4, with Shelby concerned a proposed consumer financial protection agency would have too much power and independence, and Dodd worried that its wings would be clipped and that it would be subservient to other regulators.

Within a week, Dodd had announced a new negotiating partner: Sen. Bob Corker, R-Tenn. Though Corker is relatively junior on the committee, Dodd clearly thought that if he could strike a deal with him, at least a few Republicans would come along.

By late February, Dodd and Corker had agreed on issues including the creation of a single prudential bank regulator, the structure and powers of a systemic-risk council and a new bankruptcy process for bank holding companies. But once again, consumer protection proved a stumbling block.

Republicans were resistant to the idea of a consumer agency in the first place, but a few appeared willing to accept it if other regulators had a say in its operations. They argued that the agency must take into account safety and soundness of institutions, fearing the consumer agency could force banks to engage in practices that might boost homeownership, for example, but lead to shoddy lending.

Democrats rejected such a view, arguing that the consumer agency would be created to police abuses, not to create sweeping new mandates. Dodd in particular feared that if other regulators could veto the agency's actions, it would be doomed from the start.

At some point, the two sides appeared to agree on a deal where the consumer protection agency would be placed under the Federal Reserve Board, but maintain much of its independence. Major media outlets breathlessly declared that a deal between Dodd and Corker was imminent.

But this being 2010, everyone should have been prepared for the unexpected. A little more than a month after publicly pledging to negotiate with Corker, Dodd abandoned the talks, saying that he would have to compromise too much with no sign of widespread Republican support.

Corker and Dodd "were at the 5-yard line," Corker said at the time, "and suddenly the lights went out."

Dodd finally unveiled a new version of the reg-reform bill on March 15, which reflected some of his negotiations with Corker, including putting the Consumer Financial Protection Bureau — downgraded from full "agency" status — under the Fed.

With the bill out in the open and Dodd still looking to make a deal with Republicans, the industry scrambled to analyze all of it and decide which parts were most threatening to them. For some, it was the preemption provisions, which many predicted would upend existing legal precedents and set off a wave of lawsuits challenging national banks' exemption from state laws.

For others, it was the CFPB itself. The Chamber of Commerce warned that the bureau's powers were so vast it would target even the neighborhood butcher and baker (the candlestick maker's status was unclear).

The Senate Banking Committee approved the bill largely untouched on March 22 with no Republican support, but most issues had yet to be resolved.

The Fed began a campaign in earnest to dial back some of Dodd's bill. Dodd proposed to allow the Fed to keep supervision of large banks with more than $50 billion of assets, and divvy up supervision of small bank holding companies between the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corp.

With the release of the bill, Fed presidents began lobbying Capitol Hill on the issue. By confining central bank oversight to big banks, the Dodd plan was essentially cutting the number of its supervised entities from around 6,000 to 55. Several Fed districts would have been left without any entity under their supervision, raising the question of why they should continue to exist at all.

The conventional wisdom at the time was that the pushback against the Fed had momentum, and appeared to have the support of many Republicans. But, as throughout much of the financial crisis and its aftermath, the conventional wisdom turned out to be wrong.

Far from being stripped of its powers, the Fed emerged as one of the few clear-cut winners from the final legislation. It kept its existing supervisory powers and expanded its oversight to cover all systemically risky companies, including nonbanks.

While much of the credit for that victory goes to the Fed bank presidents, state regulators and anxious community banks, the central bank also had to thank the Treasury Department, which lobbied hard on the Fed's behalf.

Although Dodd was clearly not happy with keeping the Fed's powers intact, he acknowledged that he just didn't have the votes to push the issue through the Senate.

He was far more successful with other parts of his bill. His legislation called for the creation of the CFPB, the formation of an interagency regulatory council to track systemic risks and the creation of a new resolution regime for large firms. The final bill included all those elements.

After the Banking Committee approved the bill, even more issues became intertwined with its fate.

Sen. Dick Durbin, D-Ill., who had fought for years to restrict interchange fees, successfully won passage May 13 of a provision that would let the Fed write rules restricting such charges for debit cards.

Senate Agriculture Committee Chairman Blanche Lincoln, meanwhile, won passage of a provision that would force all banks to spin off their trading desks.

Democrats vied to find just enough GOP support to pass the bill, finally approving it 59 to 39 on May 20.

It had taken months of work to get to that point. The hard part was just starting.

Within a week, the Senate had named negotiators to meet with House lawmakers in a rare formal conference committee to reconcile differences between the two bills.

Over two weeks in June, the committee met in public, and negotiated in private, on every controversial issue in the bill — and a few that hadn't even been part of it. At times it felt as though Dickens' Ghost of Christmas Past had showed up to rehash every banking debate of the last decade.

Lawmakers unexpectedly added provisions to the bill to revamp the deposit insurance system, including permanently setting the limit at $250,000, extending a program to provide unlimited guarantees for certain accounts and giving the FDIC more power to set premiums.

In another surprise, the conference committee removed a ban on paying interest on business checking accounts — a legislative action banks had unsuccessfully sought for years.

Toward the end of the conference, two big issues remained outstanding: how tough the Volcker Rule should be and whether banks should have to spin off their derivatives units.

In a bid to finish the conference with enough time for lawmakers to pass the final bill before the July 4 recess, the committee went on a legislative bender, holding a marathon 21-hour session to work out those issues and smaller one out. Banks won a crucial exception from Lincoln's provision while the Volcker Rule stayed mostly intact.

In the early morning hours of June 25, lawmakers officially named the bill the Dodd-Frank Act, and called it a day.

This being regulatory reform, it wasn't quite over yet. Within a few days, problems had surfaced on the Senate side. Sen. Robert Byrd, D-W.Va., died, leaving the Democrats without a needed vote, and Sen. Scott Brown, R-Mass., a key swing vote, turned against the bill, citing the last-minute addition of a tax on "systemically important" financial institutions.

In an unprecedented move, Dodd reopened the conference committee, removed the proposed tax and instead raised the minimum ratio of federal reserves to insured deposits to 1.35%.

Over the July 4 recess, Dodd lobbied Brown and a few other swing votes. On July 15, the bill passed 60 to 39, just barely getting the necessary support to avoid a potential Republican filibuster.

President Obama signed the legislation into law on July 21.

That effectively was the end of the year in Washington. With the upcoming mid-term elections and lawmakers and lobbyists exhausted from the reg-reform roller coaster, there was little appetite to wade into new issues. The only significant banking legislation that Congress passed after reg reform was a bill that would create a $30 billion small-business lending fund. President Obama signed the measure into law on Sept. 27, though whether any banks will use the fund remains an open question.

While lawmakers were off campaigning, federal regulators were busy implementing the hundreds of rules required by the Dodd-Frank Act.

In many cases, lawmakers had left the hardest tasks to the agencies, ordering them to create a tighter oversight system for systemic banks, including higher capital, liquidity and leverage requirements, but leaving the details up in the air.

The Fed took the lead in systemic risk regulation, while the FDIC had to set up a new resolution system for "too big to fail" entities. The OCC, meanwhile, was left to integrate the OTS into its operations.

The administration, meanwhile, took steps to set up the Consumer Financial Protection Bureau. Rather than appointing Harvard professor Elizabeth Warren (who had conceived the agency in 2007) as director of the agency, which would have

subjected her to a contentious Senate confirmation process, the administration made her its top official in charge of starting the CFPB. (See the Innovator story)

While regulatory reform may be the most sweeping change to the financial system since the Great Depression, the next big banking bill is already on the horizon.

The administration and lawmakers have pledged to tackle the future of the government-sponsored enterprises and the housing finance system next year. It may be the only thing that could make this past year look easy by comparison.

COMMUNITY BANKING

Many community banks in 2010 came to the stark realization that they had to grow or would die.

Some healthy banks went out and raised capital — either through public offerings or private placements — that they then used to shop for other banks or move into new lines of business.

Others expanded through acquisitions of failed banks, while some ailing banks — and others worried about the uncertain banking environment — sold themselves to local rivals, getting out for a decent price while they could.

Behind much of this activity was a growing sense that smaller banks, no matter how healthy, could not survive on their own given the rising costs of regulatory compliance and the continued pressure to raise capital.

Jay Sidhu, the former chairman and chief executive of Sovereign Corp., who is building his New Century Bank largely through acquisitions, put it well when he explained why the $150 million-asset Berkshire Bank in Wyomissing, Pa., was willing to sell to New Century.

"It is very, very difficult for small community banks to survive in this kind of environment," said Sidhu, who took the reins at New Century in June 2009. "You have to have the resources to live in this environment. The days of being able to successfully run a bank under $1 billion in assets are gone."

Plenty of small and regional institutions raised capital not to grow but merely to hang on, especially if they were operating under regulatory orders.

Two noteworthy deals were completed in the second half of the year. Gerald Ford's Ford Financial poured $500 million into the troubled Pacific Capital Bancorp in Santa Barbara, Calif. And the even more troubled Sterling Financial in Spokane, Wash., completed its $730 million recapitalization led by Warburg Pincus and Thomas H. Lee Partners, along with several private placements.

Pacific Capital and Sterling were among the lucky ones. Some companies that desperately needed capital weren't able to raise it.

The investor Steven Hovde called off his recapitalization of Anchor BanCorp Wisconsin in Madison because he couldn't persuade U.S. Bancorp to take a discount on its $116 million line of credit.

Failures were plentiful this past year as regulators worked their way through the pipeline of banks badly damaged from the real estate busts in several regions.

As of Nov. 15, 146 banks had failed in 2010, nearly all of them community banks. Meanwhile, the number of troubled banks continues to increase. As of June 30, 829 banks were on the FDIC's problem-bank list, up from 702 as of Dec. 31. And more than 1,200 banks had been hit with enforcement actions made public by federal regulators since the start of 2008, and analysts said they expected that pace to continue in coming months.

While the bulk of the failed banks were taken over by community institutions in their own markets, well-known names with backing from private-equity and big-time investors got into the failed-bank game this past year. On July 16, North American Financial Holdings, bolstered by $900 million in capital from the private-equity firm Crestview Partners, picked up three failed banks in the Southeast, two of them in Florida. A week earlier, Hovde Acquisition, a Washington private-equity firm, used its new thrift charter to buy the failed $282 million-asset Bay National Bank in Baltimore.

This PE-infused bidding reflected a shift. Private-equity leaders, including the billionaire financier Wilbur Ross, have said existing banks hold an advantage in failed-bank deals because they can bid higher, anticipating cost savings during integration. Ross notably said early in the year that he was no longer interested in Florida — as failures there had become too expensive — and was instead going after acquisitions in Michigan. Yet the PE-backed groups sought to make deals in markets that were key to their strategy, and with a short time frame to deploy the capital, acquiring failures became a good option.

Community bank M&A picked up as the year went on. Most of the deals were between healthy buyers and struggling sellers — until August, when First Niagara Financial Group of Buffalo, N.Y., announced it had agreed to acquire NewAlliance Bancshares of New Haven, Conn., for $1.5 billion, a deal that would create a top-25 U.S.-based commercial bank. NewAlliance's decision to sell was surprising. It was not only healthy, it was sitting on a pile of cash from a $1 billion initial public offering six years earlier. Observers had been waiting to see whom it would acquire.

Most community bank M&A remained between in-market rivals. For a number of banks, impending regulatory changes led them to make deals close to home.

"As the ominous clouds of regulatory oversight and souring economy gather, naturally, the people we've already talked to in the past are the ones you hear from now," said David Rainbolt, the president and CEO at BancFirst Corp. in Oklahoma City. The $4.6 billion-asset company announced four acquisitions of smaller banks in its home state in 2010 and closed on the purchase of Union National Bancshares Inc. in Chandler on Oct. 8.

Analysts said they expect to see more recapitalizations and in-market deals, and perhaps even bigger mergers like that of First Niagara and New Alliance union, in the remainder of 2010 and into 2011, especially as the regulatory overhaul begins affecting community banks' operations.

MORTGAGES

In normal times, a year in which mortgage rates dropped to record lows would be a happy one for the home lending industry.

But in 2010, the business struggled with its continued reliance on government secondary market agencies; increasingly contentious relationships with those agencies; weak demand for home purchases; low pull-through rates on loan applications; and above all, a festering foreclosure crisis.

Early in the year, there were signs that things might turn out differently. In February, the Mortgage Bankers Association's chief economist, citing encouraging delinquency data, ventured that "the end may be in sight" for the foreclosure crisis. And in April, Redwood Trust Inc. pulled off the first private securitization of newly originated residential mortgages — that is, the first such deal that did not have federal backing — in about two years. The $238 million bond sale, backed by high-quality jumbo mortgages, rekindled hope that there might once again be a robust secondary market for mortgages that were too large to bear the stamp of Fannie Mae, Freddie Mac or the Federal Housing Administration. But jumbos remained, by and large, a product that banks originated for their own portfolios.

Fannie and Freddie increasingly bombarded lenders with requests that they repurchase faulty loans. The GSEs also found new reasons to make the originators buy back loans. Two of the most common justifications in 2010 were the discovery that the borrower had debts that were not disclosed to the buyer and problems with appraisals.

The average 30-year fixed mortgage rate sank from the low 5% range in January to 4.19% in mid-October, according to Freddie. But with the economy weak, consumers were skittish about buying homes; economists said that a tax credit for buyers largely expedited purchases that would have been made later in the year. Refinancing application volume climbed throughout the year, but stricter underwriting guidelines made it hard to translate refi requests into closed loans. Total originations dropped to $784 billion in the first half from more than $1 trillion the same period a year earlier, according to the MBA. And increased regulation threatened to erode long-term profitability.

All of this paled in comparison to the foreclosure issues.

Obama administration initiatives like the Home Affordable Modification Program languished, as lenders and consumers alike found the programs overly restrictive and their ever-changing guidelines hard to understand. Another widely noted

impediment to loan modifications, and to other foreclosure alternatives such as short sales, was the refusal of banks that hold second mortgages to take losses.

The foreclosure surge and home seizures devastated neighborhoods throughout the country. But close observers of the industry came to realize something more troubling: mortgage servicers were not initiating or processing foreclosures at the pace they could be. As a result of this "delay and pray" strategy, a so-called shadow inventory loomed over the housing market.

By September, with economists predicting further home price declines, the kick-the-can approach was starting to look dicey. Fannie Mae put its foot down, notifying its servicers that it would begin monitoring them to determine why there were delays in moving delinquent loans into foreclosure. If servicers did not properly account for the holdups, Fannie would assess fees.

It briefly seemed that a day of reckoning on the foreclosure front was near. Then the robo-signing stories surfaced.

In late September, Ally Financial Inc.'s GMAC Mortgage said it was halting evictions and foreclosure sales in the 23 states where the process was being handled by courts as it investigated problems with the way documents were executed. The issue was brought to light in the depositions of an employee who revealed that he routinely signed thousands of documents a month without verifying the information or having a witness present, which is required by law. JPMorgan Chase and Bank of America subsequently discovered similar problems with their documentation processes and instituted similar foreclosure freezes.

The disclosures set off a flurry of investigations by attorneys general. Although the Obama administration resisted calls for a nationwide moratorium, and the banks later geared up to resume foreclosing, it was clear that reverberations of the scandal would be felt for a long time.

TECHNOLOGY

This year has proved that it's no longer a dumb move to embrace the smartphone.

The earliest days of mobile banking were experimental: more banks favored text-message access for its ability to reach more handsets. But in 2010, Apple Inc. and Google Inc. moved fast, rushing consumers from the relatively primitive world of feature phones into the state-of-the-art world of smartphones.

Two milestones in the development of mobile banking involved JPMorgan Chase — one that the company intended and one it did not.

In July, Chase became the first major bank to offer mobile remote deposit capture, a technology that allowed consumers to deposit checks by photographing them with their phones' cameras.

But if Chase was an early adopter of mobile check capture, it was also a late arrival for another trend: the rise of Google's Android operating system as the mobile banking platform of choice for consumers.

In February, a former JPMorgan Chase employee named Jeff Peiffer, too impatient to wait for the bank to come out with its own Android banking app, wrote his own version. It quickly became a top download in the finance category of the Android Market, Google's mobile application store.

The following month, analysts at Javelin Strategy and Research were surprised to learn from their data that the most active mobile banking users were those on Android phones, not those on iPhone handsets.

Smartphones also matured as payment devices this year, most rapidly for Starbucks Corp. The coffee chain expanded its mobile payments program from 16 stores to more than 1,000 in one fell swoop by adapting its mobile application, developed by mFoundry Inc., to work with the scanners at Starbucks locations inside Target Corp. stores.

Bling Nation Ltd., which makes contactless payment stickers that it suggests users attach to phones, became a national player through partnerships with PayPal Inc. and Fifth Third Processing Solutions LLC (a joint venture of Advent International Corp. and Fifth Third Bancorp).

As part of that transition, Bling Nation also moved away from its initial practice of putting bank logos on its payment stickers to making stickers that just say "Bling" — and offering them in trendy designs like pink camouflage.

This year's revision to the iPhone did not include an embedded payment chip, but a number of Apple patents emerged showing many different approaches the company was mulling for mobile payments — including some that would not require it to cooperate with banks.

Some companies refocused their mobile strategies as it became clear that consumers wanted an all-in-one package rather than separate mobile apps for separate functions. Obopay Inc., a mobile payments company that initially focused on consumers, recast itself as a vendor to banks and adapted its software to function as part of a bank's existing mobile banking application.

And while much of the industry's attention was on mobile, online banking underwent its own makeover.

More banks are experimenting with personal financial management features, but one pioneer shut its doors this year: Wesabe Inc., one of the earliest companies to show banks the value of allowing consumers to analyze their aggregated transaction data on one website.

As more consumers expressed their preference to view this data on their banks' websites, Wesabe attempted to follow its users there by white-labeling its software to sell to banks. But it did not make enough money to survive.

Wesabe also sought to rewrite the rules for selling software to banks by posting its prices online, but found banks were not willing to give up face-to-face sales talks. Still, the company's peers stayed in business.

Bank of America made headlines with the introduction of an account that required consumers to pay a monthly fee if they wanted to receive a mailed statement. Statements remained free for B of A's other accounts, but this account was seen as a major step toward the eventual elimination of paper statements.

Though a lot of this year's trends had an "in with the new" aspect, there was one noteworthy instance of "out with the old": the replacement of Citigroup's North American core system.

Though Citi has not publicly discussed the project, it was revealed during an earnings call of its vendor, Fidelity National Information Services Inc., that Citi planned to use a core system from FIS that it already used in other parts of the world.

CARDS

This was the year EMV finally came to the United States.

The U.S. has long been a holdout against the EMV Integrated Circuit Card Specifications, commonly referred to as "Chip and PIN." But as the format continued to gain favor worldwide, travelers from the U.S. found it increasingly difficult to use their plain, magnetic-stripe cards in other countries.

In May, United Nations Federal Credit Union, which serves U.N. diplomats and their families, announced that it would be the first U.S. financial institution to issue EMV cards to U.S. residents. The cards are only available to the credit union's members, though, and the move did not trigger an avalanche of followers.

Legislation also substantially reshaped the card market. Most parts of the Credit Card Accountability, Responsibility and Disclosure Act of 2009 went into effect in February. Issuers, expecting to lose revenue under the law's limitations on fees, warned that their rewards programs might disappear due to lack of funding.

Though bank-funded rewards have not yet vanished, the legislation has created an opportunity for providers of merchant-funded rewards programs.

Significantly, this was the year the Durbin interchange amendment of the Dodd-Frank Act came into being, and although the Fed's expected cuts to debit interchange would not take effect until next year, the industry expects those cuts to be significant. One institution, TCF Financial Corp., has even sued the Fed to delay or block those cuts.

In October, the Justice Department reached a settlement with Visa Inc. and MasterCard Inc. over their merchant-acceptance policies. The networks agreed to drop most of the policies that prohibit merchants from steering customers toward using specific cards depending on their cost to the merchant. One effect of this settlement could be the introduction of cash discounts to guide consumer behavior. The Justice Department also sued American Express Co., which refused to join the settlement.

Prepaid cards made real advances, as this year marked the successful initial public offerings of Green Dot Corp. and NetSpend Holdings Inc. The public listings brought these companies — and the prepaid business as a whole — greater legitimacy.

Additionally, prepaid card providers kept adding features more commonly associated with full-fledged bank accounts, such as online bill pay and mobile account access.

The business case for contactless payments is also undergoing a transformation. Initially pitched as a way to speed checkout lines at stores, the technology forged ahead in 2010 as an alternative to closed-loop transit fare systems.

MasterCard's trial in New York pushed into its second phase, going beyond just the subway and inviting Visa users to participate by tapping their cards to pay fares on some buses and underground trains. If the tests prove successful, this system could replace the Big Apple's MetroCard.