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CFPB

The Quarterly Review

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In the second quarter of 2016, the CFPB continued its strong pace of activity, initiating two major rulemakings, issuing multiple industry reports and resolving several notable enforcement matters.

The CFPB Speaks

Regulatory agenda update

On May 18, CFPB's Office of Regulations posted its semiannual update on the rulemaking agenda. Key takeaways include:

- **Supervision of Larger Participants ("LP") in Installment Loan and Vehicle Title Loan Markets.** With the agency extending the completion of pre-rule activities from September 2016 to December 2016, we do not expect a proposed rulemaking for this rule until the first half of 2017 at the earliest. Given the pace at which prior LP rulemakings proceeded, the CFPB's authority to supervise entities in this space would not take effect (even assuming a proposal in the first half 2017) until 2018.

- **Small Business Lending Data/Regulation B.** Similar to the Installment Loan LP rulemaking, the CFPB extended the completion of pre-rule activities for this rule from September 2016 to December 2016. Unlike the LP rulemaking, however, which, as discussed in a prior client alert, could face obstacles to obtaining a robust data source, the small business lending pre-rulemaking activities are well under way. Of note, on April 12, the CFPB announced that it hired a former high ranking Small Business Administration official, Grady Hedgespeth, to serve as the Assistant Director for the CFPB's Office of Small Business Lending Markets.

- **Debt Collection.** For the fourth consecutive time, the CFPB extended the date for completion of pre-rule activities for the debt collection rule. Initially set for December 2014, the agency indicated that it would complete such activities by June 2016; however, to date the CFPB has not issued its outline of proposals under consideration. We anticipate that it will likely do so at an upcoming debt collection field hearing that will be held on July 28 in Sacramento, California. Industry participants now anticipate that, in August 2016, the agency will convene small business representatives (pursuant to the Small Business Regulatory Enforcement Fairness Act) to solicit information on the impact a rule would have on small businesses and to obtain recommendations for regulatory alternatives. If other rulemakings are any indication, a proposed rule would likely not be issued until at least 2017 with a final rule in late 2017 or 2018. This would mean a final debt collection rule would not become effective until 2019 or 2020. As a result of the delays in this rulemaking, the industry should expect the CFPB to continue to oversee this space through a combination of supervisory activities and enforcement actions.

- **Gramm-Leach-Bliley Act/Regulation P.** On July 11, the Federal Register published the CFPB's proposed rulemaking to make "minor technical modifications and clarifications to Regulation P" to incorporate a new section of the Gramm-Leach-Bliley Act ("GLBA"). On December 4, 2015, President Obama signed into law the Fixing America's Surface Transportation Act, which contains a provision that modifies the GLBA's annual privacy notice requirement. Under new section 503(f) of the GLBA, a financial institution is no longer required to provide annual privacy notices as long as (1) it only shares nonpublic personal information as permitted by the GLBA without providing consumers with notice and opt-out rights, and (2) there have been no privacy policy changes since the last time consumers received a privacy notice. Comments are due August 10, 2016.

The CFPB weighs in

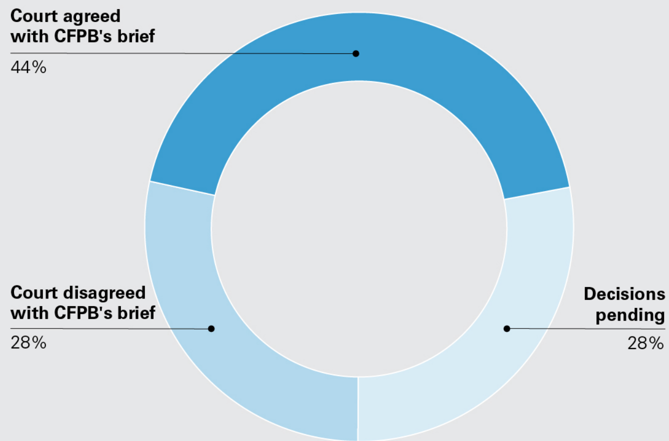
In a 6-2 decision in *Spokeo v. Robins*, issued on May 16, the Supreme Court held that Article III standing requires a concrete injury "even in the context of a statutory violation," making clear that a statutory violation does not by itself establish constitutional standing. Perhaps realizing that more consumer suits would become susceptible to dismissal in the wake of the *Spokeo* decision, the CFPB filed three *amicus* briefs on the standing requirement in June 2016 alone:

- On June 3, the CFPB filed a supplemental *amicus* brief with the US Court of Appeals for the Third Circuit in *Bock v. Pressler & Pressler, LLP,* a civil suit brought under the Fair Debt Collection Practices Act ("FDCPA") against a debt collection law firm that entered into a consent order with the CFPB on April 25 (as discussed below). Like the CFPB's related enforcement action, the complaint alleged that the firm made false and deceptive representations in attempting to collect debts in violation of the FDCPA by filing a complaint without "meaningful review by an attorney." In its supplemental brief, the CFPB asserted that the FDCPA granted the plaintiff "a legally protected interest in not being subjected to misleading debt-collection communications" and an invasion of that legally protected interest amounted to an "actual" injury sufficient to give rise to standing.

- On June 16, the CFPB filed an *amicus* brief with the US Court of Appeals for the Ninth Circuit in *Keen v. JP Morgan Chase Bank*, a civil suit brought under the Truth in Lending Act ("TILA") for the company's alleged failure to accurately disclose the finance charge on a mortgage loan. In its brief, the CFPB posited that receiving a disclosure that incorrectly states the finance charge in violation of TILA is a concrete harm sufficient to confer Article III standing because the borrowers were "depriv[ed] of a right to receive information to which one is entitled by law." Further, the CFPB argued that the allegation that the company violated the borrowers' "right not to be given false information" satisfies Article III.

- On June 17, the CFPB filed an *amicus* brief with the US Court of Appeals for the Second Circuit in *Strubel v. Comenity Bank*, another civil suit brought under TILA for the company's alleged failure to provide statutorily mandated account-opening disclosures. The CFPB again argued that a consumer has a concrete injury, meeting Article III standing, when she is deprived of the right to receive information to which she is entitled by law.

Number of Appellate Decisions (*Amicus*): 2011 – 1H 2016

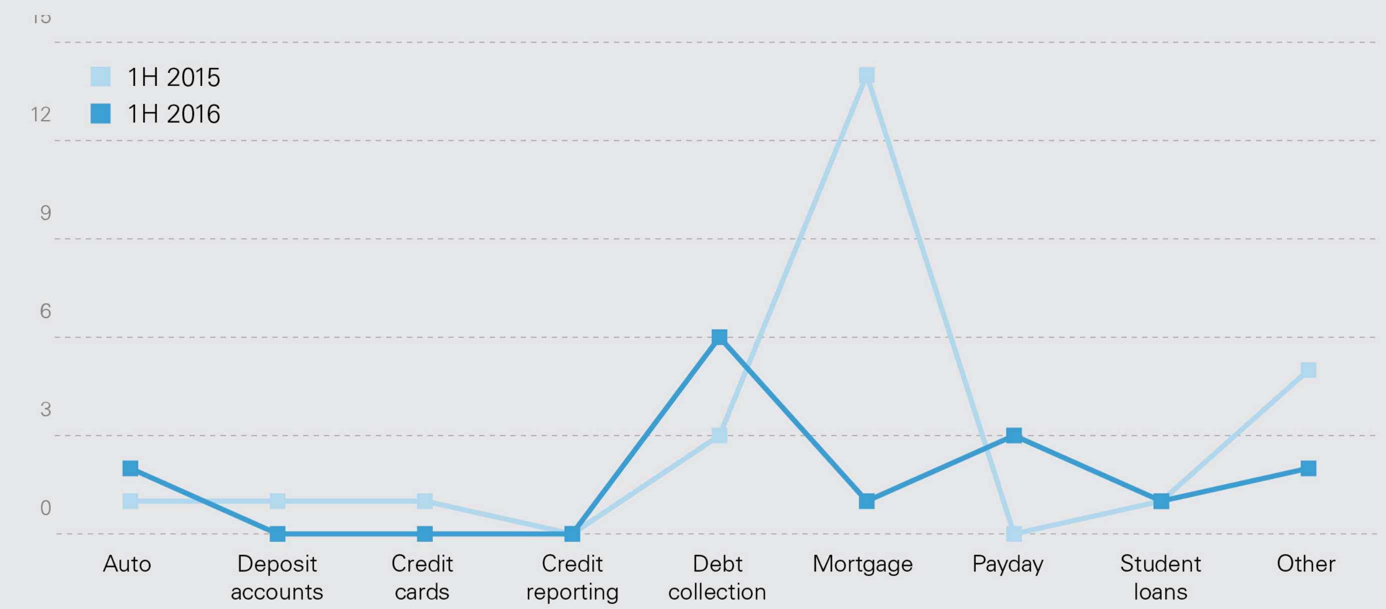


Between 2011 and 1H 2016, there were a total of 32 briefs filed.

Guidance on consumer deposit account discrepancies

On May 18, the CFPB along with the Federal Reserve Board, the Federal Deposit Insurance Corporation, the National Credit Union Administration and the Office of the Comptroller of the Currency issued guidance outlining their supervisory expectations on how financial institutions should handle consumer deposit discrepancies.

The interagency guidance calls on financial institutions to adopt policies and practices that are "designed to avoid or reconcile discrepancies, or designed to resolve discrepancies such that customers are not disadvantaged." In particular, the guidance indicates that entities are expected to comply with Regulation CC, which implements the Expedited Funds Availability Act, in addition to other applicable laws and regulations, Number of Enforcement Actions by Product or Service



including prohibitions on unfair, deceptive and/or abusive practices in the FTC and Dodd-Frank Acts. Further, the interagency guidance notes that financial institutions should provide accurate information to their customers regarding their deposit reconciliation practices and "implement effective compliance management systems that include appropriate policies, procedures, internal controls, training, and oversight and review processes to ensure compliance with applicable laws and regulations, and fair treatment of customers."

Fair lending report

According to its April 29 Fair Lending Report, the CFPB's supervisory and enforcement actions resulted in approximately US$108 million in remediation and other monetary payments in 2015.

- **Supervision.** CFPB examinations revealed deficiencies in adverse action notices, violations of the Equal Credit Opportunity Act ("ECOA") and Regulation B related to the treatment of protected sources of income, including income provided under the Section 8 Housing Choice Voucher Homeownership Program, and underwriting disparities resulting from illegal discrimination.
- **Enforcement.** The CFPB's enforcement actions remain centered on mortgage lending and auto financing.

In the mortgage space, CFPB partnered with the Department of Justice ("DOJ") in two enforcement actions. The first action, which represents the largest redlining settlement in history, resulted in the company paying US$25 million in direct loan subsidies to qualified borrowers in the affected communities, US$2.25 million in community programs and outreach, and a US$5.5 million penalty. The second action resulted in a settlement by a private mortgage company that allegedly charged disparate brokers' fees and was required to pay US$9 million to harmed borrowers.

In auto financing matters, the CFPB again partnered with the DOJ in two actions, one against the ninth largest depository auto loan lender in the country and the other against the fourth largest captive auto lender. In each matter, the government alleged that the entity's indirect lending policies resulted in minority borrowers paying higher discretionary markups in violation of ECOA. Both companies agreed to change their pricing and compensation systems by substantially reducing or eliminating discretionary markups to minimize the risks of discrimination. The bank also agreed to pay US$18 million in restitution to affected borrowers and the nonbank agreed to pay US$24 million in restitution.

Auto title lending report

We reported in our inaugural quarterly review that the CFPB plans to focus on "debt traps," involving practices that trigger a cycle of debt. We also noted that one of the agency's nine priorities is increasing its understanding of how consumers use auto title lending. Thus, it comes as no surprise that, on May 18, the CFPB released a report, examining consumer usage, default and rates of vehicle seizure for single-payment vehicle title loans.

Among other things, the agency found that over 80 percent of vehicle title loans are reborrowed on the same day a previous loan is repaid, and nearly 90 percent are reborrowed within 60 days. According to the agency, such reborrowing often results in long "loan sequences," around half of which involve ten loans or more. The CFPB further concluded that these sequences have high default rates. Roughly a third of loan sequences result in a default, while 20 percent result in the repossession of the borrower's vehicle. With auto title lending clearly within the CFPB's crosshairs, we expect the CFPB to issue a rulemaking proposal to supervise the larger participants of this market in 2017.

Rulemaking

Arbitration

On May 5, the CFPB issued a Notice of Proposed Rulemaking ("NPRM") that, if finalized as proposed, would ban class-action limitations in arbitration agreements. The NPRM has two main components:

- Prohibitions on pre-dispute arbitration agreements ("PDAAs") that bar consumers from filing or participating in class action lawsuits; and
- Requirements that entities involved in arbitration proceedings pursuant to a PDAA submit certain arbitral records (such as arbitral claims and awards) to the CFPB.

Comments are due August 22. As we mentioned in our client alert on the proposal, it is likely that any final rule would not take effect until 2Q 2017 at the earliest.

Payday lending

Following its April 26 report on online payday loans, on June 2, the CFPB issued another NPRM; this time on short-term lending. As discussed in our previous client alert on the issue, this is the first time the agency has used its rulemaking authority to prevent unfair, deceptive or abusive acts or practices ("UDAAPs"). Though often characterized as the "payday rulemaking," if finalized as proposed, it would also apply to auto title loans, deposit advance products and certain "high-cost" installment loans and open-end loans. Accordingly, the rule would impact a range of entities, including banks and nonbanks as well as traditional and marketplace lenders.

The payday lending NPRM has four major components:

- Requiring covered lenders to determine if a borrower is able to afford certain loans without resorting to repeat borrowing (the "Full Payment Test");
- Permitting covered lenders to forego a Full Payment Test analysis if they offer loans with specific structural features, such as an alternative "principal payoff option" for loans with a term under 45 days or two other alternative options for longer-term loans;
- Requiring notice to borrowers prior to debiting a consumer bank account and restricting repeat debit attempts; and
- Requiring covered lenders to make use of and report to credit reporting systems.

Comments are due September 14. If prior rulemakings are any indication, we expect that any final rule likely would not take effect until 2019.

Debt Collection

Enforcement actions

Of the 11 enforcement actions brought this year, six have involved violations of the FDCPA or UDAAP violations arising from debt collection litigation and the sale of consumer debts to third-party debt buyers.

On April 25, the CFPB announced that it had entered into consent orders with a debt collection law firm and third-party debt buyer in connection with the companies' allegedly unlawful debt collection practices. In its action against the law firm, the CFPB alleged that the firm filed "unfair and deceptive debt collection lawsuits" on behalf of its first-party creditor and third-party debt buyer clients. This is the third enforcement action that the CFPB brought against a law firm in 2016 over debt collection practices. The enforcement action brought against the third-party debt buyer also arose from litigation practices, and specifically the debt buyer's failure to provide original account-level documentation to law firms that it engaged to bring collection suits on its behalf. As noted earlier, the CFPB is engaged in a debt collection rulemaking, and based on questions in its Advanced Notice of Proposed Rulemaking, any final rule is likely to include some requirement around the transfer of debt information from original creditors to third-party debt collectors and debt buyers. Both groups should pay careful attention when the CFPB issues its outline of proposals under consideration for the proposed rule.

Payday Lending

Notwithstanding the CFPB's rulemaking activity in this space, the agency has made clear it will remain aggressive in using its UDAAP enforcement authority to police industry practices.

CFPB targets co-founders of online lead aggregator

The business of online lead generation involves lead generators, lead aggregators and lead purchasers. Lead generators advertise loan products and collect applications from consumers. They then sell to lead aggregators the contact information, which usually consists of a consumer's name, phone number, home address, email address, references and employer information. In turn, the lead aggregator sells to lead purchasers who are online small-dollar lenders, data managers, data brokers and remarketing companies.

On April 21, the CFPB brought suits in federal district court against the co-founders of an online lead aggregator. According to the CFPB, both individuals provided substantial assistance to the company, which had allegedly engaged in unfair and abusive conduct when it bought and sold personal information from payday and installment loan applications. (In December 2015, the CFPB had brought an action against the company for allegedly exposing millions of consumers to harm by allegedly selling leads to purchasers without regard to what lead generators promised to consumers or how the consumers' information would be used.)

The recent suits highlight that the CFPB's enforcement authority over "covered persons" can extend to service providers and to individuals who run these companies.

The agency's actions place pressure on third-party service providers, such as lead aggregators, to engage in independent compliance checks on both sides of their businesses. That is, online lead aggregators should consider independently evaluating not only the representations made by lead generators, but also the compliance infrastructure for lead purchasers.

CFPB targets payday lender

On May 11, the CFPB filed a complaint alleging UDAAP violations against an entity that offers check cashing services and originates payday loans. The allegations state that the company refused to reveal fees to customers and deceived consumers about the ability to cancel or reverse transactions. The alleged behavior included making false promises to consumers that they had lower fees than competitors. In addition, the complaint alleged that the company did not notify consumers when they overpaid for a loan and did not return overpayments to consumers. The CFPB also alleged that the company did not properly disclose fees in accordance with applicable state law. This complaint makes clear that, while the CFPB is working to issue a regulation to set minimum standards for payday lenders, the agency intends to use its enforcement and rulemaking authorities in tandem to oversee the industry.

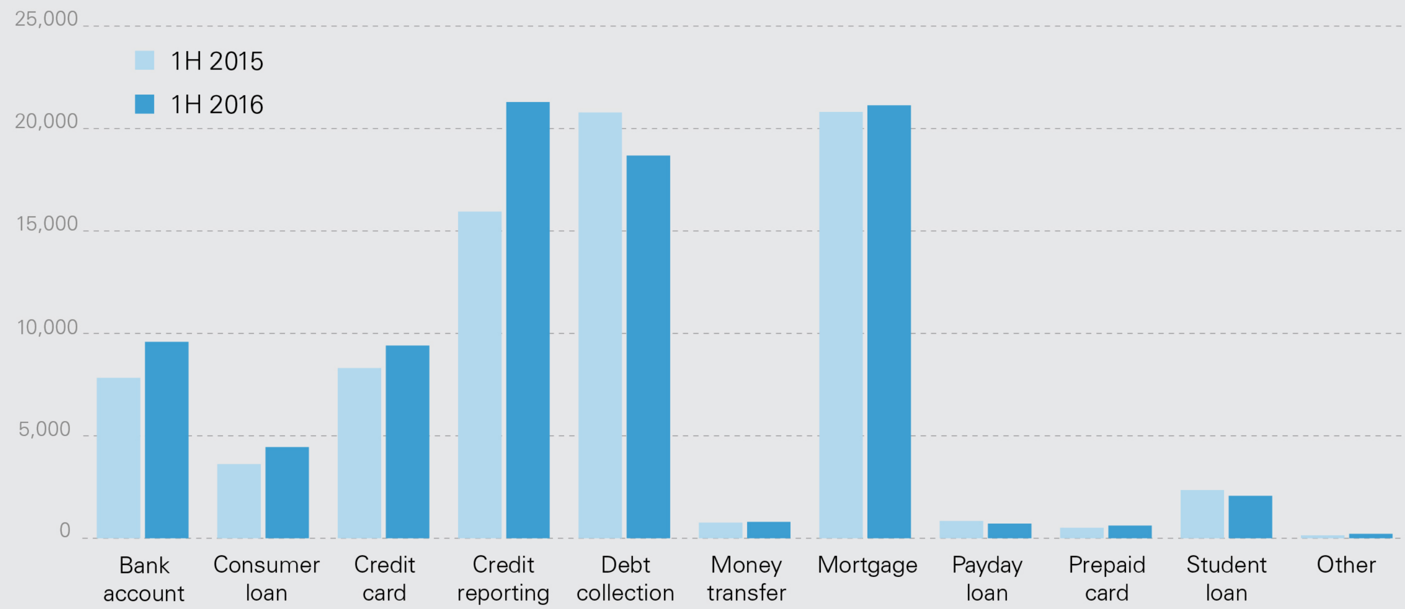
Mortgages

CFPB partners with DOJ

On June 29, in an interagency action against a bank, the CFPB and the DOJ alleged that the institution engaged in discriminatory lending practices against African Americans and other minorities. Specifically, the agencies claimed that the bank implemented an explicitly discriminatory loan denial policy by redlining and denying African Americans loans significantly more often than, or charging them higher prices than, similarly situated non-Hispanic white applicants.

Under the proposed consent order, the company would be required to take a number of remedial measures, including the payment of: US$4 million to a loan subsidy program to increase access to affordable credit, US$2.78 million to African American consumers in restitution, and a US$3 million civil penalty. Additionally, the bank would be required to spend at least US$300,000 on outreach and US$500,000 to partner with community-based or governmental organizations that provide assistance to minority neighborhoods, and to implement policies that require its employees to provide equal assistance to all individuals.

Number of Complaints in 1H 2015 vs. 1H 2016



Update on PHH

As reported in our inaugural quarterly review, on April 12, the Court of Appeals for the District of Columbia Circuit held oral arguments in *PHH Corp. v. Consumer Financial Protection Bureau*. The appeal arose after the CFPB's administrative order against PHH issued by Director Cordray increased an administrative law judge's penalty from US$6.4 million to US$109 million. The Circuit Panel focused its questions on the constitutionality of the CFPB's unique single-director structure. The panel's questions probed whether the CFPB's structure is problematic, even though the CFPB has argued that no discrete aspect of the CFPB is unconstitutional when considered alone. The panel's questions focused on:

- The concerns related to a single director structure as opposed to a multi-member commission;
- Whether the Director can only be removed "for cause"; and
- The fact that the agency does not rely on Congressional appropriations for funding.

Altogether, it was suggested that these issues culminate in an "unusual structure" that grants "a single person a huge amount of power," which is "very dangerous." Specifically, the judges appeared focused on the coupling of the "for cause" removal provision with the single director structure.

Typically, the President has at-will removal power over appointees to federal agencies headed by a single person. For example, the Comptroller of the Currency serves a five-year term by statute "unless sooner removed by the President, upon reasons to be communicated by him to the Senate." In contrast, the President's authority to change the CFPB's leadership is restricted. Though the CFPB was able to identify a few agencies, specifically the Social Security Administration, Federal Housing Finance Administration and the Office of Special Counsel, that are headed by a single individual removable for cause, these agencies have more limited regulatory authority compared to the CFPB's broad rulemaking, supervision and enforcement authority.

Of note, the attorneys representing PHH sought to make the same constitutional arguments in another case before the Court of Appeals for the Seventh Circuit in an interlocutory appeal of *CFPB v. ITT Educational Services*. There, the CFPB alleged predatory student lending. In response, ITT filed a motion to dismiss on constitutional grounds, which was denied. Thereafter, ITT sought appellate review on the CFPB's constitutionality. On June 16, the appeal was dismissed for lack of jurisdiction. According to the most recent scheduling order, a jury trial at the US District Court for the Southern District of Indiana is scheduled for January 2018.

Actions against individuals

On May 26, the CFPB entered into a consent order with a former bank loan officer for referring a large number of loan closings to an escrow company that shifted its fees from some customers to others at the loan officer's request. The fee-shifting scheme purportedly allowed the loan officer to offer lower-cost escrow services to customers and, consequently, to close more loans. The increased loan closings made the former employee a top-producing loan officer at the bank for four consecutive years.

As a loan officer providing real-estate settlement services within the meaning of RESPA, the employee was a covered person subject to CFPB enforcement jurisdiction. The CFPB has occasionally exercised jurisdiction over individuals engaged in violations of the law, and this case serves as a reminder that financial institution employees may be subject to liability. The order barred the former loan officer from the mortgage industry for a year and imposed a civil money penalty of US$85,000.

Upcoming in 2016

- **Prepaid Final Rule.** According to its updated regulatory agenda, the CFPB anticipates issuing the rule in July 2016, which may be optimistic. The CFPB's Division of Research, Markets and Regulations ("RMR"), which is responsible for rulemakings, has a heavy workload and staff resources are thin, with several officers acting in other capacities at the agency along with the departure of several key managers. All of which suggests the realistic expectation of continued delays for the Prepaid Final Rule.
- **Debt Collection SBREFA.** Industry participants anticipate that, in August, the agency will convene small business representatives (pursuant to the Small Business Regulatory Enforcement Fairness Act) to solicit information on the impact a rule would have on small businesses and recommendations for regulatory alternatives. If other rulemakings are any indication, a proposed rule will not be issued until at least 2017 with a final rule in late 2017 or 2018. Presumably, a final rule would not become effective until 2019 or 2020. Notwithstanding delays in this rulemaking, the industry should expect the CFPB to continue to oversee this space through a combination of supervisory activities and enforcement actions.
- **Amicus Program.** In light of the recent Supreme Court decision in *Spokeo* (see above), the CFPB is certain to file more *amicus* briefs arguing that consumers have met the "concrete injury" requirement when alleging violations of federal consumer financial statutes. With the seemingly contradictory language in the majority opinion (e.g., constitutional standing "requires a concrete injury even in the context of a statutory violation. … This does not mean, however, that the risk of real harm cannot satisfy the requirement of concreteness"), it is unclear whether the decision is a win for the defense bar. Because consumer groups have reacted favorably to the decision, the industry should not expect a marked decrease in consumer suits.

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