

Consumer Finance Monitor (Season 5, Episode 13): A Look at the CFPB's First Months under Director Rohit Chopra, with Special Guest Chris Peterson, John J. Flynn Endowed Professor of Law, University of Utah's S.J. Quinney College of Law

Speakers: Alan Kaplinsky and Christopher Peterson

Alan Kaplinsky:

Welcome to Consumer Finance Monitor podcast, where we explore important developments in the world of consumer financial services. I'm Alan Kaplinsky, senior counsel at Ballard Spahr. I'm formerly the chair of the Consumer Financial Services Group, and I will be moderating today's webinar. Today, I have another very special guest from outside Ballard Spahr, someone that has been on our podcast show before, but actually I think it was before the pandemic. I'm very pleased to introduce Chris Peterson. Chris, welcome to the show.

Christopher Peterson:

Hey, Alan. It's good to be with you again.

Alan Kaplinsky:

It's a pleasure. Let me tell you a little bit about Chris, for those of you our listeners that aren't familiar with him. He's the John J. Flynn Endowed Professor of Law at the University of Utah's S.J. Quinney College of Law. He previously served as special advisor in the office of the director of the Consumer Financial Protection Bureau. He was also a special advisor in the office of legal policy for personnel and readiness in the US Department of Defense and senior council for enforcement policy and strategy at the CFPB. He's written dozens of scholarly articles and published three books on consumer finance. He's been a frequent witness at Congressional hearings dealing with consumer finance issues. He's also a fellow of the American College of Consumer Financial Services and has won many, many awards that there are too many to mention them all.

Alan Kaplinsky:

But Chris, put it mildly has a very impressive bio and I would say more often than not, has a different point of view than yours truly. Although, I'm finding over the years that on many of the issues my position and Chris's position is getting closer together on certain things. In any event, what we're going to do today is talk about a potpourri of issues. A lot of our discussion will be focused on the CFPB, but not exclusively. Let me begin with this question, Chris. We're, I think, six months since Rohit Chopra has been director, is that about right?

Christopher Peterson:

Yeah, yeah. I think that's about right, Alan.

Alan Kaplinsky:

Yeah, and I know before he actually got sworn in, I remember being interviewed by some media and I predicted to the media that it wouldn't take him very long to announce some major enforcement action against a big financial institution, because I felt he would want to begin his tenure at the CFPB with a splash. Something that will get a lot of print and would scare the

hell out of a lot of the larger banks. But surprisingly, that's not happened. I was totally off base. What I'd like to find out is from an enforcement perspective, what's happened so far, Chris, and were you surprised as well?

Christopher Peterson:

First off, thank you so much for the kind introduction, Alan. I actually enjoy visiting with you too and it's important to talk to people that you don't necessarily always agree with to check your assumptions and to help yourself think about things. That's part of why I'm willing to join you on your podcast and talk through some of this stuff, have some dialogue.

Christopher Peterson:

But yeah, I do try to follow the CFPB enforcement cases, both because I used to work in that office, but also I'm just interested as a law professor and a citizen. They do have some interesting cases that they've announced over the past six months. But I guess it's fair to say you're right, that the number of cases has not been maybe as high as it's been at other times in the history of the bureau. I try to track that stuff fairly carefully and to my count as of the day that we're recording this, and it'll be a little bit of delay when the podcast is released, but right now there are five cases over the past half year or so. Some of them are interesting cases and things that I think that the CFPB's enforcement staff can and should be proud of. But there is not a barn bursting case against a major financial institution.

Alan Kaplinsky:

No headline grabbers. I mean, you haven't seen any major and am I right of the five cases in six months, they're against smaller, I think non-banks largely if not entirely.

Christopher Peterson:

Well, there is one against Trustmark National Bank.

Alan Kaplinsky:

Oh, okay.

Christopher Peterson:

That's a big case. But you're right that the cases are not giant cases like we saw sometimes in the past. That JP Morgan Chase credit card case on debt collection back during the Cordray years which was, I forget the exact number. That was a \$3 billion, \$4 billion case, something along those lines.

Alan Kaplinsky:

All the credit card add-on products during the Cordray era, that got him off on a trajectory where he did go against all the major banks.

Christopher Peterson:

That's true. I will say though, if you read between the lines and pay attention carefully to some of the rhetoric that's being used, there are some interesting things in these cases that are signaling, maybe if you're willing to read the tea leaves so to speak, the direction of the bureau. For people that pay careful attention to this, are maybe in some ways exciting or I suppose exciting from my perspective, maybe troubling from yours, Alan.

Alan Kaplinsky:

Let's dig a little deeper into the cases that he has actually brought and I'd like you to do a little reading of the tea leaves.

Christopher Peterson:

Well, all right. The first case then that I'll mention, and before we do that, I'll be candid, you're right. I'm a little surprised that there haven't been more cases. I think frankly, it's a bit of a problem. That is a challenge that people who are cheering for the CFPB to be a vigorous enforcer of the law, are justifiably concerned about. If you see the pace of cases that the bureau had at different times in its history, this is about on par with the very early years of the Trump administration, when the CFPB was in the most turmoil. But that being said, that could change and just a handful of weeks.

Alan Kaplinsky:

That was under the Acting Director Mulvaney, right?

Christopher Peterson:

Correct. Yeah, yeah. We're seeing about the same pace of cases as back then. But-

Alan Kaplinsky:

Maybe this is the lull before the storm.

Christopher Peterson:

That's exactly right.

Alan Kaplinsky:

I mean, I know our office, it has several cases that have been ongoing for a while and nothing is moving toward finalization at this point. But we don't know what the actual inventory of cases is. That, I guess, is the bigger question.

Christopher Peterson:

Well, I certainly don't. I mean, I still have some friends inside the agency, but it's not polite to ask and they can't tell you even if you did. For those of us that are on the outside watching, we just have to wait and see. Getting back to reading the tea leaves-

Alan Kaplinsky:

Yeah let's get back to the cases, yeah.

Christopher Peterson:

I mean, look, the first case that I think is interesting is the JPay case, the bureau's case against this company called Jpay. It's a Florida company and what they do is have contracts with state corrections departments, the departments and state governments that incarcerate prisoners convicted of crimes. One of the things that's common across the country is to have what's called date money. When prisoners are released to give the former inmates some cash to try to get out and find somewhere to stay and get something to eat while they look for another job and transition back into life on the outside.

Christopher Peterson:

JPay was providing a prepaid card service for the state departments of correction and the bureau got them for violating Regulation E, the electronic funds transfer acts prohibition of requiring the use of a particular financial service provider as a condition of receiving government benefits. I think that's a pretty clear cut violation of Regulation E and they also got them on some inaccurate disclosures, and there were some fees that were being charged in some instances that were not provided for in the contracts. Those are both pretty clear UDAB; unfair or deceptive trade practices violations.

Christopher Peterson:

But the thing that was most interesting about the case to me is that there was some language in the way that the bureau was describing the case that was not the rhetoric that I had heard for a long time. They were complaining of the level, the size of the fees, and they accused JPay of, I'm quoting here from some of the ancillary materials that describe the consent order, "abusing its market dominance." The idea, I think, being that JPay had a captive audience that could not easily pick another financial service provider and they used the stickiness of that product base to have inflated prices.

Christopher Peterson:

Part why I think that's so interesting, is it really does sound like some of the rhetoric that you actually hear in antitrust cases, as opposed to unfair deceptive trade practices cases. That's very interesting. To be clear, I'm not saying that this is an antitrust case. In fact, I mean, the word that I've been using in my own mind, and I'm actually writing a law review article about this, maybe a type of quasi antitrust claim where the policies of trying to ensure market competition are protected are enforced through deceptive trade practices or unfair practices statutes, both at the federal level and the state level across the country.

Alan Kaplinsky:

I detected the same thing that you have, Chris, not only in the JPay case, but it's come up time and time again in some of the pronouncements of Director Chopra. I guess that maybe it's a reflection of the fact that he just spent several years at the Federal Trade Commission. And of course the FTC has as one of its missions, the enforcement of the antitrust laws and fostering of competition. Do you think that's where this thing is coming from?

Christopher Peterson:

It may be part of it. The other place I think it's coming from, frankly, is that the CFPB is now under the managerial oversight and control of the White House and President Biden has expressed one of his priorities in the State of the Union address, and a lot of his rhetoric about ensuring fair competition across the country. So it very well could be coming from the White House and not just Dr. Chopra as well, though he's the mouthpiece of it for those of us that follow consumer finance closely.

Alan Kaplinsky:

Yeah. Well, and there is, as I recall, some very general language in the Financial Consumer Protection Act, or the CFPA, I guess, which just states that one of the purposes of the CFPB is to foster competition. I guess that would be the hook for them.

Christopher Peterson:

Yeah, I think that's one hook. Another hook too, is that the statutory hook in the Federal Trade Commission Act that the FTC uses for its antitrust law, is the term unfair competition. But that's in the same sentence in section five, as unfair competition and unfair or deceptive practices. For a lot of us that divide up our law practices or our academic pursuits, or just in the classes that law students take in law school, antitrust is usually cordoned off as a separate discipline from consumer law, more generally speaking. But I don't know that the origins of the law are that cleanly divided.

Christopher Peterson:

The Federal Trade Commission also does that too with its competition bureau and its consumer protection bureau. But I think that right now, one of the things we're seeing in the marketplace are a lot of companies that are coming up with creative ways to sit between the two zones in a zone defense, so to speak. In a soft spot where it's not squarely within the orbit of the competition bureau at the FTC or the consumer protection bureau at the FTC, or related for the purposes of our discussion, the CFPB. I think that Dr. Chopra is onto something there and that may signal something about the kind of cases that could be coming in the future.

Alan Kaplinsky:

Yeah, let's talk. I mean, you talked about the JPay case, any of the other cases worthy of mention?

Christopher Peterson:

Yeah, I think so. I mean, there are important cases. I don't think that there's anything in there that struck me as really innovative or different than the kinds of cases we've seen in the past. We also already mentioned a case against Trustmark National Bank from Jackson, Mississippi. That was a joint case with the OCC and it was a redlining case that focused on the Memphis metropolitan area. They settled the case because there was an accusation that they had a lack of branch locations and loan officers in Black and Hispanic neighborhoods. That they had inadequate self-monitoring program to ensure that they were not discriminating against their potential customers on the basis of race. In the case, they agreed to \$3.5 million, \$4 million loan subsidy program to try to correct some of that past mis-practice or misbehavior and also \$5 million in civil money penalties. It's an interesting case.

Christopher Peterson:

There's also a Military Lending Act case against a large pawn shop chain, First Cash Incorporated and Cash West America. Cash West America is a subsidiary of First Cash and First Cash is, I think, the largest pawn shop chain. In any event, they have thousands of pawn shop locations across the country and their interest rates are often above the permissible 36% that you can charge active duty military service members. But the CFPB is alleging that the pawn shops were still making illegal pawn loans to service members. I was a little surprised that case didn't settle because presumably the CFPB has the documents to prove that those loans were made. The other thing too, is that the predecessor to First Cash, which was Cash America, they had a consent order way back when I was at the CFPB in 2013, where they had made some illegal loans to service members. This is their second offense, at least within the larger umbrella in predecessors and interest at that particular company. Interesting to see how that one goes.

Christopher Peterson:

Then there's also a pretty typical debt collection case for some illegal debt collection tactics against some debt buyers in Colorado and New York. Also, some deceptive marketing by American Advisors Group, which is the largest reverse mortgage lender in the country. They had some marketing materials that were indicating that perhaps the borrowers couldn't lose their homes and that's not true. There are some circumstances where you can lose your home in a reverse mortgage. They were also using inflated estimates of the value of homes to give a sense that the reverse mortgage payments for the borrowers were going to be larger than they actually were, which made the loans more enticing.

Christopher Peterson:

Important cases and the kind of thing that the bureau is supposed to be doing as part of its core mission.

Alan Kaplinsky:

Right. Well, okay. Thank you very much for a good summary of the work product that we're able to observe so far coming out of the enforcement area. But it seems strange to say it, but it's been unlike the history of the CFPB, where enforcement seemed to be most of the activity. That is, most of the observable activity of the CFPB used to be in enforcement. We're now finding there's still a lot coming out from the CFPB, a lot of statements by Director Chopra, covering a lot of different areas that I'd like to get your reaction to that.

Alan Kaplinsky:

I'm thinking, for example, the statement or the RFI that he came out with recently regarding so-called junk fees. Not an enforcement issue, no proposed regulation, although maybe this is a precursor to a regulation, although I doubt it. I'm wondering if you could comment on not just the junk fee, let's call it initiative for lack of a better term, but also other jawboning activities; overdraft fees. He castigated overdraft fees several months ago and that led to some major banks

eliminating overdraft fees. Now we see the junk fee thing and there are other examples. I'm wondering if you could comment on that generally and specifically?

Christopher Peterson:

Well, first off, I'm not a big fan of junk fees myself. I mean, they're often not the most easy way to shop for consumers in the marketplace to protect themselves because they could be more difficult to compare than baseline interest rates or more upfront charges. I'm not sure I'd necessarily agree that there might not be some regulation in the works. I mean, there's the potential for some amendments of existing rules. It's been a while since anybody's taken a look at the CARD Act and that's a classic area, it's within the CFPB's jurisdiction to identify whether not there might be some fees that have crept up higher and higher in the CARD Act that are within the scope of the way that the CARD Act has been implemented that need a second look.

Alan Kaplinsky:

You see Chris, that's exactly the thing. Look, I understand, I don't like paying junk fees myself either. There's nothing more annoying when you go into a hotel and you find you get some general charge for recreational activities, \$25 dollars a day. Something that covers a penumbra of things that you might do. But here's the thing with the respect to the junk fee thing that bothered me, a lot of the fees that he attacked were either outside his area of jurisdiction, he actually mentioned hotel fees that doesn't have anything to do I don't think with the jurisdiction of the CFPB, but he went beyond that.

Alan Kaplinsky:

A lot of fees are specifically authorized under state law. A lot of these things companies generally, if you're a licensed consumer or finance company, the state statute will specify the precise fees that you can charge and then there will very often be a sentence saying that you can't charge any other fee in connection with this loan if it's not expressly authorized. Some are authorized under federal law, he didn't even acknowledge that. Such as the late fee that's permitted on credit cards. Specifically authorized by the CFPB many years ago under the CARD Act and there was no acknowledgement of that in his RFI. I just thought that was a little disingenuous, a little bit unfair. What do you think?

Christopher Peterson:

Well, look, I'm not going to second guess the packaging or the rhetoric. I mean, I do think that it is absolutely within the core of the director of the CFPB's responsibilities to gather information on fees that are being charged that are within the competence, the jurisdiction of the bureau to see what's being charged. Gather information about potential enforcement cases, help target exams on the companies that pose the highest risk to consumers and also consider updating regulations or potentially even new rule makings that might address common practices. The mere fact that one state may authorize it, well, we also know, we may talk about this later in the podcast, that one state authorizing it may actually lead to being imported across the country or to consumers in other jurisdictions. And just because it's okay in one state doesn't mean that it's legal under federal law or that it should be something that we all as a society are willing to accept.

Christopher Peterson:

Nobody in all the other states in the country need to agree to how one particular state decides to establish its laws at the outset of an inquiry. But look, I mean, your broader question was about a lot of press releases and a lot of talk. I see that too. There's some value in engaging with the popular press and providing content for conversation and Dr. Chopra, he's got a knack for getting some newsprint and good for him. That's part of the way that he's got to his position and I think that consumers want to see somebody in the federal government that's speaking up for them and that's advocating on their behalf. That being said, I also want to see some cases and I want to see some good cases. I think we will, we've already seen some and we're going to see more.

Alan Kaplinsky:

But the one thing, and I will grant you, it's not just him getting newsprint, it does really have an impact on the industry. Because after that junk fee RFI came out, I can't begin to tell you the number of calls that our office got saying, "Hey, are we charging any of those things that he's talking about?"

Christopher Peterson:

Of course, they are. They're worried that those enforcement cases are going to come. You already said one of the best examples with his focus on overdraft fees. I think there are other factors too. There's some market competition at play here. There are some new technologies, new financial services that are providing competition to avoid those overdraft fees. But Director Chopra beating the drums on this, is I think one of the factors that's likely to nudge banks to pull back on overdraft fees, which are often one of the most aggressively priced financial services that are imposed on people who are struggling. Not just hotel fees, but single moms and families that are struggling to pay their rent and their utilities and have enough food in the kitchen to feed the children. I think it's a positive step to the extent that the United States government is encouraging financial institutions to look for ways to remain profitable, make some money, but do so without putting unnecessary burdens on those working Americans who are struggling to make ends meet.

Alan Kaplinsky:

Yeah. Let's talk about some of the other initiatives or jawboning. He's had a lot to say about the use of technology. Doesn't seem to be such a fan of things like artificial intelligence. He's talked about digital redlining and he has called out the growing reliance on artificial intelligence models that companies are using to do underwriting. He's worried about whether these models may have buried within them, I guess the seeds of discrimination. But he's made everybody very, very nervous. There are a lot of people who are thinking, "Gee, he's blocking technology," and technology in general, the use of it is a good thing. A good thing for companies, a good thing for consumers, a good thing for the economy. Then of course, very early in his tenure, he issued a request for information to practically every big tech company. They all got hit with requests for information.

Alan Kaplinsky:

What's your take on what Director Chopra's thinking is in that area?

Christopher Peterson:

Well, I don't know that I have anything. I mean, I know Director Chopra, we've worked together a couple different times. But I don't want to represent that I have any direct insights on his thoughts, other than what he said publicly. You're certainly right that he has spoken out about his concerns about the information technology industry, the information that the industry gathers about us, the way it's used to influence our credit scores, our privacy. Also, I think in my view rightly so, about whether or not there may be unforeseen consequences for providing credit fairly across the different vulnerable groups that have been traditionally excluded from wealth in our society. That's something that we need to be vigilant about. He's fortunately speaking on that to try to encourage that vigilance.

Christopher Peterson:

I think the concern is that everybody agrees it's illegal to discriminate in say, providing a mortgage loan. But suppose for a moment that you've got a sophisticated artificial intelligence machine learning underwriting system that has 500, 600 different variables, and those variables combine in surprising ways to create a proxy for race or for sex or sexual preference or some other protected class that we're concerned about discrimination against. And that we unintentionally replicate those same patterns that we as a society are struggling to overcome. I don't think that there is any rule that the director has discussed and certainly not that I've heard anybody advocate for, that prohibits using artificial intelligence. But it's a mistake for us not to maintain some vigilance about discrimination creeping in.

Christopher Peterson:

One other thing I'll mention too, it also has the potential to sharpen marketing in ways that could be troubling to some of us. If you have extensive transactional information on when a consumer's paycheck is coming into their bank account and when the money's being paid, you might be able to calibrate your advertising and marketing practices to have a very sharp insight into when consumers might be at their most vulnerable decision making point and induce them to take out a loan that is not in their best interest, that a majority of Americans would characterize as a predatory loan.

Christopher Peterson:

I agree you with you, that technology and progress is something to hope for and to strive for and to achieve, but let's not be naive. Technology can be an instrument for positive social change, but it can also be a tool of oppression. And if anything we've learned over the history of technological change, whether that's the introduction of steel, or bronze, or iron, it can also be used to hurt people. That's something that our consumer protection agency must protect against.

Alan Kaplinsky:

Yeah, while we're on the subject of discrimination, let's talk about one of the most recent things that he came out with and that is a revision to the examination manual dealing with the use of the unfairness prong of UDAP to go after forms of discrimination that aren't banned by the Equal Credit Opportunity Act, or by the Fair Housing Act. That really got a lot of people very stirred up in the industry, I can tell you that. Wondering what you think about the process. I want to talk about the process and I want to talk about the substance of what he's done here. But first of all, let's talk about the process. Shouldn't this have been done in a more formal way through a notice of proposed rulemaking something under the Administrative Procedures Act?

Christopher Peterson:

It's funny you want to talk about the process first, I want to talk about the substance first.

Alan Kaplinsky:

Well, talk about both.

Christopher Peterson:

Okay. Well, let's just take a gut check here. I mean, the thing that my students in my consumer law class are sometimes surprised to learn, is that in 2022 America, there is still no explicit federal law that prohibits affirmative deliberate discrimination in a financial service that's something other than credit. The Equal Credit Opportunity Act is an important civil rights statute, the Fair Housing Act in housing, but suppose a deposit account or a remittance, there's not an affirmative statute that says that's illegal, which is a bit astonishing, isn't it?

Alan Kaplinsky:

I haven't done a thorough search or research on this, but there are a lot of state laws, public accommodations laws I'm thinking of that I think might be broadly construed to cover certain types of non-credit discrimination.

Christopher Peterson:

Yes, in some states, but not in others. In some states, one of the ways that consumers have challenged alleged discrimination in financial services that are not credit, is by using state unfair and deceptive or UDAP statutes. So there is some precedent for this that's behind this change. It's not like this is completely out of nowhere. The other thing I'll mention too, is that there's a number of case where the implied obligation of good faith and fair dealing. The UCC, the Uniform Commercial Code and also other common law doctrines of good faith have also been interpreted in a lot of jurisdictions to prohibit discrimination.

Christopher Peterson:

Look, of course, we have lots and lots of anti-discrimination laws all across the country, going all the way back to the equal protection clause within the constitution, which obviously is not applicable in this context of private, non-credit based financial services. But it's not a surprise. Nobody should be surprised that there are federal regulators that might be concerned about discriminating against racial minorities or one gender or another in providing deposit accounts or remittances.

Alan Kaplinsky:

Yeah, but isn't this such a important issue? And I agree with you, this is an important issue, isn't it the kind of thing that Congress ought to be focused on? Congress has very thoroughly looked at credit discrimination. The ECOA, the Fair Housing Act, there are other civil rights statutes. This sounds like a great subject for Congress to do a study of and to perhaps enact some laws in the area to provide very definite guidance. What I'm troubled about here is there are no boundaries. I mean, I don't know where it begins and it ends, I don't know who's in the protected class anymore under this new theory of applying unfairness to get rid of discrimination.

Alan Kaplinsky:

Let me give you an example, get your reaction to this, Chris. Let's say I want to open up a deposit account at an institution. I'm on vacation in Florida. I want to open up an account down there and I go in and they say to me, "Sorry, Mr. Kaplinsky, you don't live in our market area and our policy is we can't give you a deposit account." Anything wrong with that?

Christopher Peterson:

Well, I'd have to think about it some more. I mean, normally the law professor gets to make up the hypotheticals, Alan. If I were in Congress, I would certainly support legislation that prohibits discrimination in articulating what those specific classes are. But I don't know if you noticed Alan, that the United States Congress is a bit paralyzed with gridlock and has been for a long time. I guess for those folks, my friends out there in the industry that are saying that this is the wrong tool choice or the wrong process through which to effectuate the change that everybody that I've ever spoken to agrees that the substance is correct. I'm sure that there are some folks that don't, those misguided and disturbed souls don't need to be a part of this particular conversation, I think.

Christopher Peterson:

But choosing what process is not that easy. Each of the processes, each of the tool choices that you look at are going to have a lot of challenges and notice-and-comment rulemaking takes a long time. As I recall, the last time I was on your podcast, we were talking about the payday loan rulemaking, which is still tied up in the courts all these years later. In Congress, it takes 60 votes to get past a filibuster and any Senator can grind things to a halt. They do pass laws once in a while and there's hope from time to time. It's not that easy. This one is fast, it does not lay to rest all of the uncertainty that financial institutions will face, but financial institutions already face that uncertainty. I think what's happening is that some of the general councils that these businesses are waking up that, oh yeah, I guess you're right. We probably shouldn't discriminate in the provision of our remittances or checking accounts.

Christopher Peterson:

Of course, that's the case, that should not be surprising. There may be, I think, some soul searching and maybe some more self-testing and some more compliance work to be done. I'm sure that will be a little bit stressful and will cause some costs and it will be probably hardest on the smaller business that have thinner margins. But the country has to move forward in dealing with the racial challenges and divisions in our society, as we progress towards a more perfect union. Look, the other thing is that this is going to get to court at some point. It's not that there is no boundaries, Alan, there'll be one or two or more federal judges that will eventually get to have a say about this. I suspect that there is at least a strong chance that when a federal judge looks at the underlying elements of the unfairness doctrine which causes, or is likely to cause substantial injury, that the injury

is not avoidable by consumers and that the injury is not outweighed by countervailing benefits to consumers or to competition, racist behavior in providing checking accounts or remittances seems to me to qualify as unfair.

Alan Kaplinsky:

Mm-hmm (affirmative), okay. Let's turn to another area and I know this is an area very near and dear to you, and that's the 36% federal rate cap. Under the Military Lending Act, members of the military, you can't charge more than 36% and it's an all in rate cap. There was a bill, and there still is a bill I think. Although, I don't know where it is right now, that would apply that 30% all in rate cap to all people, not just members of the military or active duty members of the military. I think, I hope I have this right, I'm not misstating things. But I think you predicted that something like that was going to get through, that would become an act. Maybe I'm thinking of one of your other colleagues who told me that, but I have it in my mind it was you Chris. Am I wrong?

Christopher Peterson:

Well, I don't know that I predicted it would get through. I mean, it's called the Veterans and Consumers Fair Credit Act. The first a version of it was an appendix of a law review article that I wrote with Paul Cantwell, who was my boss when I was working on the Military Lending Act at the Pentagon. I drafted the original version of the legislation, so obviously I support it. I don't know that I ever predicted that it would pass. I do think that there is a lot of public support for it. I mean, the public polling on a traditional interest rate cap of 36% gets a super majority of Republicans in my home state of Utah, which a very conservative state. And it also gets a super majority of Democrats all across the country as well, so the public overwhelmingly wants that.

Christopher Peterson:

Any time usury law ever comes up in a ballot measure, it always passes no matter how much opposition the industry puts up against it. The other thing that's interesting, it is a bipartisan bill. In the House, it's sponsored by Chuy Garcia from Illinois on the Democratic side, but it also has a Republican co-sponsor, Representative Glenn Grothman. I visited with him a lot when he was deciding about whether or not to co-sponsor the bill. He's a very conservative guy, a Freedom Caucus type of Republican from Wisconsin. But he takes the Biblical injunctions against usury, I think quite seriously as do a lot of people of faith all across the country. It's not a bipartisan bill in the Senate right now though. They have not been able to find a Republican Senator who will get on board with it. Until they get that, they've got to get some Republican votes in the Senate for it to pass. If there's a courageous Senator that's out there, or some staffers that think they've got a chance, feel free to give me a call and I'll help encourage that to happen.

Alan Kaplinsky:

But in the meantime, little by little, at the state level, a few states have enacted that legislation. The type of legislation I'm thinking of Illinois, I think New Hampshire and I think very recently, New Mexico passed something. There may be some other states where similar legislation is percolating. Am I right?

Christopher Peterson:

Yeah, that's right. Illinois is very similar. It uses the same methodology for calculating the interest rate limitation as the Department of Defense's regulation that they worked on back when I was at the Pentagon. The New Mexico bill was just passed in the most recent New Mexico session, also has similar kinds of all in interest rate caps that include some of the other credit insurance and debt suspension products as part of the calculation of the interest rate limits.

Christopher Peterson:

I mean, one you didn't mention is California. Its calculation of the cap is not quite the same and it also provides for some additional index that varies based on inflation or based on the fluctuation of interest rates. But drawing a line between the extremely priced products that mainstream Americans and essentially all consumer advocates view as unacceptable and then

the products that one fee or another, or some underwriting practice for the collection efforts, but we agree are acceptable in society. Drawing a line between those two things can be politically productive, so I'm excited about some of those reforms.

Alan Kaplinsky:

Yeah. One final thing, before we wrap things up. We've covered a lot of territory, but there is a really important case that recently got filed by a company called Opportunity Financial or OppFi, against the state of California, dealing with the so-called true lender doctrine. I'm wondering if you could tell our listeners what that case is about and why you think it's important?

Christopher Peterson:

Sure. Well, it's about that California interest rate cap that we just talked about. The California legislature imposed an interest rate limit of about 36% on loans of a certain balance, installment loans. That's exactly the kind of loan that OppFi makes or services, depending on who side you take. OppFi has a bank partnership model for making their loans. They work with a bank in my home state of Utah; FinWise bank. As people that listen to this podcast regularly will remember, ever since the 1970s, early 1980s, it's become clear that national banks and state banks, under certain circumstances, can export the bank's home state interest rate cap into the borrower's home state. If you make a loan in my home state of Utah as a bank, which has no interest rate cap, then you can apply that lack of an interest rate cap to borrowers that are borrowing from say, New York City, where there are very aggressive usury laws. Many of the loans that are common in my state are actually a felony under New York law if it's made by a loan that's not a bank.

Christopher Peterson:

The question is whether or not these loans that are being made by FinWise are actually made by FinWise or really whether or not it's this technology platform company, OppFi, that's making the loans. OppFi insists that FinWise Bank, the bank is making the loans. The California regulators are naturally more skeptical about that. They've just been directed by the state legislature of California and the overwhelming public sentiment of Californians, that loans above 36% should be illegal and OppFi's loans are expensive. I mean, they're not payday loan expensive, but they make loans at just right up about 200% APR. Extremely expensive loans by a historical measure. California's trying to stop that and the company, OppFi, has been pretty aggressive about it. They sued California and are seeking a declaratory judgment that says that all of their loans were made by FinWise and are not subject to California's usury law.

Christopher Peterson:

Strikes me that what they're trying to do is get more case law and more certainty that protects their business model. They're trying to dictate the place and the venue in which that decision case law is going to be made. But I also think that the Federal Deposit Insurance Corporation, which is the regulator for FinWise, a state bank, and also even potentially the CFPB should have something to say about it because the true lender doctrine really affects their consumer protection mission and their safety and soundness mission at the FDIC.

Alan Kaplinsky:

Yeah. Well, this is a little bit connected to some regulations that were issued by the comptroller a couple of years ago, one dealing with the Midland Credit case in the Second Circuit. I can't remember the name of the plaintiff in that case right now, where the OCC promulgated regulation, the FDIC promulgated a regulation basically overturning that Second Circuit opinion. Under the regulation, it says that if a loan is valid at inception, if it gets transferred or assigned to a third party, that immunity from the usury law continues to apply. In other words, what applied to the national bank or the state charter bank at origination, that carries through, even if the loan ends up getting acquired by a non-banking institution.

Alan Kaplinsky:

But then the OCC went further to basically promulgate another regulation dealing with this true lender issue. But then Congress ended up using the Congressional Review Act, much to my chagrin, to override that regulation. It's interesting to note that the FDIC never followed the OCC in promulgating a similar true lender regulation. We can speculate as to why that's the case, but I'm sure that people will say, "Well, the FDIC didn't have the same authority as the comptroller." I mean, that's what I've heard. The comptroller gets its authority from the National Bank Act, the FDIC gets it from the Federal Deposit Insurance Act. There were different authorities relied upon by the comptroller that don't exist for the FDIC.

Alan Kaplinsky:

I assume what OppFi is trying to do, is it's trying to get a federal preemption determination, right? That's the key. It's not saying it's a matter of California law, the true lender is FinWise Bank. It's saying that even if California says the true lender is FinWise Bank, there is federal preemption under the Federal Deposit Insurance Act. Am I right?

Christopher Peterson:

Well, it's federal preemption. If FinWise Bank is the lender, then they're going to have the right to export the lack of an interest rate cap in my home state of Utah. But whether or not FinWise Bank is the true lender, in my view, that's not a question of federal banking law. That's a question of contract law. It's a question that's a commercial law question across the country that is the same kind of doctrine, whether or not the original lender is a bank or an Indian tribe. Interestingly, one of the leading cases in California is not a banking case. It's the CFPB case against Cash Call, which was a tribal lending case that took an aggressive view in the federal district court of whether or not a tribal entity had made a loan or whether or not the servicer that was really providing the capital and doing all the collections was a non-tribal entity, who the true lender was. It was not the tribal a lender.

Christopher Peterson:

Look, I think that's part of why there's a real incentive here for the CFPB and also most explicitly the FDIC, to get involved to try to control whether or not the loans that are made in the particular pattern and way that FinWise is making them, or OppFi, depending on your perspective, that's going to control a lot about the scope of the capacity of banks to partner with non-banks and thereby circumvent these same interest rate caps that we were just talking about in New Mexico and Illinois and California. It's a very important case and it seems to me that the federal regulators need to not be asleep at the wheel on this one. Because if they don't get involved and throw their weight around with an Amicus brief, or potentially even frankly, I think there's the potential for an investigation.

Christopher Peterson:

If you look at the complaint that OppFi made to California, if you were in the CFPB's enforcement office and you were looking for the basis on which to open an investigation of OppFi, all these representations that OppFi itself is making about California's position, all are some of the building blocks in making out a UDAP claim against OppFi. In the complaint, OppFi says that California says that OppFi is making the loans, not the FinWise Bank. If OppFi's representation of California's position is correct, well, then that means that OppFi is not just violating the state California usury limit, it's also mischaracterizing in its origination documents, in its collection efforts, the underlying nature of the loan and may be collecting interest that it's not entitled to from those consumers. That's a UDAP violation that's squarely within the CFPB's authority.

Alan Kaplinsky:

I know you would take the position that's the case, even though in the Consumer Financial Protection Act, there is a prohibition against the CFPB imposing any kind of a usury ceiling. Am I right?

Christopher Peterson:

Well, yes, there is a prohibition of the CFPB establishing a usury limit, but that's not the same thing as saying that if a lender violates a state usury law, completely as a matter of state law, and then goes about collecting interest that they're not entitled to, that's not a usury violation at that point. What it is, is a deceptive trade practice. They can't take money they're not entitled to, and that's a federal law question. It's exactly the kind of thing that OppFi might be doing if the state of California is correct that OppFi made those loans and not FinWise.

Alan Kaplinsky:

Right, right. Anyway, Chris really want to thank you very much for participating today. Your views, I always want to hear them, even though very often you and I may disagree on what the particular issue is that we're talking about. Thank you very, very much.

Christopher Peterson:

Well, thank you. I always like hearing your views as well, Alan.

Alan Kaplinsky:

I want to thank all of our listeners today for taking the time to download our podcast show. Want to remind you that it's a weekly show, we release a new version of the show every Thursday. Just if we could toot our horn a little bit, a website called Good To Be Social, within the past several months ranked all of the law firm podcast shows in the country. I'm proud to say that we were ranked second in the country. I'm extremely, extremely happy about that. Enough tooting of our own horn though and I want to wish everybody a good day.