

Consumer Finance Monitor (Season 5, Episode 23): CFPB Director Rohit Chopra: Do His Words Speak Louder Than His Actions?

Speakers: Alan Kaplinsky, Michael Gordon, Tom Burke, and Michelle Hogan

Alan Kaplinsky:

Welcome to Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer finance. I'm Alan Kaplinsky, senior counsel and former practice group leader of our consumer financial services group, Ballard Spahr.

Alan Kaplinsky:

I'm very pleased that you have downloaded the podcast this morning, as we're going to talk about a topic that we covered not very long ago in a very popular webinar that we produced, and that is about the CFPB, which, of course, is our favorite subject. The title of that webcast was CFPB Director Rohit Chopra: Do His Words Speak Louder Than His Actions?

Alan Kaplinsky:

So let me first ... Before I tell you a little bit more about what we're going to cover today in the podcast, let me remind you that our podcast show is available on Apple Podcasts, Google Play, Spotify, or whatever your favorite podcast app may be. You should look for a new episode of our show every week on Thursday morning, except during a couple of holiday weeks.

Alan Kaplinsky:

So let me turn to our topic today. Director Chopra has been in office for about six months. He's given many speeches, issued several requests for information, or we refer to them as RFIs. He otherwise has shared his views on a wide variety of consumer finance issues.

Alan Kaplinsky:

However, much to the surprise of those in the financial services industry, the CFPB has only filed about a handful, or maybe two handfuls, of enforcement actions and consent orders. He's done very little of a public nature on the regulatory front, except for activity related to Section 1071 of Dodd-Frank, which deals with data collection on small business loans.

Alan Kaplinsky:

Even that activity was mandated by a court proceeding arising out of the fact that the CFPB got sued for being dilatory in promulgating a regulation on that topic. It's something which they really should have done toward the beginning of their existence and not 11 years in.

Alan Kaplinsky:

So in today's podcast, we're first going to explore the public enforcement and regulatory actions that Director Chopra's taken during his first six, seven months in office. We'll then discuss his public speeches, his RFIs, and other activity during this time period. Throughout, we will give you our views on how companies should respond to Director Chopra's words. We also will share our views on topics like arbitration that have not been given any public attention by Director Chopra.

Alan Kaplinsky:

Let me cover the topic of arbitration, because many consumer advocates, most notably Professor Jeff Sovern at St. John's University Law School, have been strongly advocating for the CFPB, that they do something, again, with arbitration, that they reinitiate or relaunch another rule-making proceeding dealing with arbitration.

Alan Kaplinsky:

So far, those pleas from the consumer advocates have fallen on deaf ears. I'm going to tell you why I strongly believe that Director Chopra is not going to spend any of his time and effort dealing with arbitration.

Alan Kaplinsky:

Those of you that have been following the CFPB since its inception know that there is a provision in the Dodd-Frank Act which required the CFPB to conduct a study of consumer finance arbitration. Then, at the end of the study, to decide whether there was a need for rulemaking, whether it was in the public interest and necessary for the protection of consumers for there to be either an all-out ban on arbitration or some regulatory restrictions that would be imposed upon the use of predispute arbitration provisions.

Alan Kaplinsky:

After a couple of years in office, Director Cordray finally did launch that arbitration rulemaking, and it went on for many years. This was not something that got done in a matter of months or even in a matter of a couple of years. There were several public hearings that were conducted. I testified myself at three of them on behalf of the consumer finance industry.

Alan Kaplinsky:

At the end of the day, the bureau issued roughly a 700 or 800-page report dealing with consumer arbitration. In a nutshell, what it found is they didn't have enough information to ban the use of consumer arbitration. The data did not show that it was harmful to consumers, but they thought they had enough information to ban the use of class action waivers in consumer arbitration provisions.

Alan Kaplinsky:

So the next thing that happened was that Congress got involved, under the Congressional Review Act, in taking a fresh look at the new CFPB regulation, because under the Congressional Review Act, through a joint resolution of the House and the Senate, signed by the President, any regulation issued by an agency like the CFPB can get thrown out.

Alan Kaplinsky:

That is precisely what happened by a very, very close margin with the then Vice President Pence breaking a tie vote in the Senate. It got rejected. That was the end of consumer arbitration.

Alan Kaplinsky:

Now under the Congressional Review Act, there is no right of the CFPB to adopt another regulation that is substantially similar to the one that got rejected by Congress. They just can't do it.

Alan Kaplinsky:

So it's unclear at the very start what the CFPB can do in this area. Could they adopt an all-out ban on arbitration? I think probably not, but it's not exactly clear. Maybe they could do it, but they clearly couldn't do it on the record they originally created that culminated in this 800-page report, because that record would not support an all-out ban on arbitration. The CFPB said so in that report when it was issued many years ago.

Alan Kaplinsky:

So essentially they'd have to start from scratch. That means a lot of staff would have to get involved, which would take up a lot of bandwidth. A lot of money would have to be involved, because they not only would need staff to do the report, but there were other things that the bureau got involved in. They did survey work to see what consumers thought about arbitration, and that is very costly and time-consuming.

Alan Kaplinsky:

And, let's face it, Rohit Chopra conceivably might have no more than two and a half years left in his term because at the end of his term, a new president, whether it'd be Republican or Democrat, could remove Director Chopra and put someone else in there.

Alan Kaplinsky:

So a lot of hoops for Rohit Chopra to jump through. At the end of the day, he also knows there's going to be a lawsuit challenging what he has done, and he could never get anything accomplished during his term in office.

Alan Kaplinsky:

And it's also part of the old regime. While he aligns himself, and he's certainly, politically, I think, very close to former Director Cordray, he is charting his own path. As we have seen in some of the things that he's done already, he's taking a fresh look at a lot of things. I don't think he's going back to revisit something that Director Cordray didn't get accomplished. So that's my feeling.

Alan Kaplinsky:

Now let me now introduce our other presenters today on our podcast. First of all, and leading off, I'm very happy to introduce Mike Gordon, who very recently joined Ballard. He's a partner in our consumer financial services group.

Alan Kaplinsky:

He's a former senior official at the CFPB, with two decades of experience in consumer financial services law. In addition to being a former regulator, Mike has also been general counsel of a fintech lending platform.

Alan Kaplinsky:

Mike was on the startup team that established the CFPB, and he served for five years in senior roles at the agency, including senior counselor to the director. Indeed, Mike is of the people that we've had from the CFBP within our consumer financial services group. He's certainly by far has had the most experience with the CFBP and held the highest position at the agency.

Alan Kaplinsky:

So at Ballard Spahr, Mike is concentrating on enforcement defense, not just with the CFPB but the FTC and state attorney's general, compliance and exam readiness for the CFPB, and banking and bank partnerships, blockchain and digital assets, consumer and commercial credit payments, regulatory strategy, and risk management for a range of clients.

Alan Kaplinsky:

He is a fantastic lawyer. If any of you have anything of concern pertaining to the CFPB, he is our go-to person at Ballard Spahr right now.

Alan Kaplinsky:

Let me also introduce Tom Burke, who is not new to our firm. He is a litigation partner within our consumer financial services group and our white-collar group. He litigates enforcement actions across the country on behalf of lenders and loan servicers.

Alan Kaplinsky:

Tom has represented clients in major enforcement actions brought by the CFPB and state attorneys general, as well as in class actions and preemptive regulatory actions, with particular focus on student lending and loan servicing.

Alan Kaplinsky:

Last but not least, let me introduce to you Michelle Hogan. Michelle is an associate in our commercial litigation group, focusing on white collar and commercial litigation matters. Prior to joining Ballard Spahr, Michelle served as an assistant attorney general in the fraud and special prosecutions group within the Arizona Attorney General's Office. So let me now turn our podcast show over to Mike Gordon.

Michael Gordon:

Thank you, Alan. To get started, I thought I would set the table with some observations about the CFPB and Director Chopra to better understand what they've done, why they've done it, and what might be coming.

Michael Gordon:

So we'll start with Director Chopra, leadership matters. I had the opportunity to work with Rohit during my time at the bureau. He was the student loan ombudsman at that time.

Michael Gordon:

I observed that he was quite aggressive in using the press and establishing a leadership position on issues of student lending. He took what was a position without really much actual authority, ended up becoming the spokesperson across the federal government for student lending issues, in my recollection, even leading the Department of Ed to places it wasn't going. He could do that with minimal authority.

Michael Gordon:

I think now coming back as a director, with his temperament and intelligence, I expect him to continue to expand the reaches of the bureau's authority. I think we saw some of that in his most recent post as an FTC commissioner as well.

Michael Gordon:

I would say that never before have we had an incoming director as well positioned as Rohit is to have a huge impact and to have it quickly. He knows the agency. He knows what he wants to accomplish. He's savvy with the press. He's also rowing in the same direction as much of the middle management of the bureau, which remains from the early days, and is like-minded to his goals and viewpoint.

Michael Gordon:

As for the bureau itself, it's in a different place than when I worked there in the early years for Director Cordray. We certainly wanted to have an impact and get results, and there were a number of accomplishments. But there were also a number of things on our agenda that we didn't have control over and we had to devote resources to in a way that Director Chopra doesn't have to worry about.

Michael Gordon:

So, for example, we had a number of rulemakings that were mandated by Congress that took a lot of resources and time. We were also focused still on building the agency, building the plane while flying it. We also were very aware of the need to establish credibility, and it tempered some actions that we were taking and how we set up our priority list in the early days, because we were a new agency.

Michael Gordon:

Finally, there were constitutional questions hanging over the bureau, and that cloud also affected certain activities at the bureau in a way that probably is not the same today. I would hasten to say that there is a constitutional issue that has now emerged through a concurrence in a recent Fifth Circuit decision having to do with the funding source for the bureau and whether that would pass constitutional muster.

Michael Gordon:

So I think there is a bit of a cloud brewing there, but I would say, overall, the agency's on a much firmer ground than when it was in the cradle. It gives Rohit, I think, more freedom of motion.

Michael Gordon:

Finally, I would point out that the bureau is more closely tied to the President, President Biden in this case, than ever before in two ways. One is that after the CLO law decision, now that the director can be removed for any reason at will by the President, it makes the bureau closer to the White House and have to heed perhaps closer to the White House agenda than in earlier years.

Michael Gordon:

Secondly, Rohit Chopra has to assume that his term ends with the end of the first term of the Biden administration. That could be the end for him and, therefore, he's on the clock in a way that prior directors may not have felt.

Michael Gordon:

So imagine that you're Rohit Chopra and you show up at the bureau and you have a lot of priorities. You've got a lot of resources committed to supervisory activity, to rulemaking, and you've got this big and growing enforcement staff. Your goal is to change market behavior quickly with the least amount of resources you can commit to the effort.

Michael Gordon:

I think keeping that in mind helps to understand why some of the things that we're going to talk about today have occurred, and gives you clues as to how Director Chopra might tackle problems in the future. We know he's going to be aggressive, but the question is what are his best tools to accomplish his goals?

Michael Gordon:

In terms of priorities, I would say some of the priorities have been made clear already from day one. Fair lending. It's hard to overstate how important fair lending is and racial equity issues generally to this administration.

Michael Gordon:

I think the bureau's going to be looking with a fair lending lens at just about everything they do in the supervisory and enforcement context to see if there is a concern there. They want to make cases in the fair lending arena.

Michael Gordon:

Secondly, I would say they've talked about focus on big players and, relatedly, anticompetitive behavior in markets. I'm going to talk a little more about that later.

Michael Gordon:

Third, easing the financial impact of the COVID crisis. It seems like that might feel a little dated, but in point of fact, the way that institutions handled the COVID crisis is going to be a subject of scrutiny for the bureau for the next couple of years.

Foreclosures are already starting to pick up again, particularly in the mortgage industry but also others. I expect to see the bureau bringing cases about how companies handled relief programs or other actions they took during the height of the crisis.

Michael Gordon:

Finally, I would say tech and fintech, and the use of data more generally, are a clear priority of the bureau based not only on the experience that the FTC that Rohit Chopra has, but it's very timely that the growth of fintech ... And we hear the bureau talk a lot about the use of data, the impact of AI and machine learning and algorithms and alternative data and how that affects consumers, particularly different sets of consumers.

Michael Gordon:

So the strategies that we see them employ and that I think the bureau will continue to employ, first, a return to enforcement first. We may be a little surprised that in the first six months, the actual number of enforcement matters hasn't been shockingly large. But I expect that number to go up and to go up significantly over the next year as cases become ready and as new enforcement matters are initiated.

Michael Gordon:

I think there'll be more guidance, more talk, and less rulemaking. Alan alluded to that with respect to his view of the arbitration issue. But I think more broadly, generally, rulemakings are very resource-intensive, and with the prospect of court challenges, can be uncertain.

Michael Gordon:

Other than the small business credit lending, which is a rule they have to get done, and perhaps the consumer access to data rulemaking that they teed up, I mean how many resources do they have to devote? How many other big rulemakings could they do in the next few years? One, two, then may do some smaller rules.

Michael Gordon:

But it's much quicker for Director Chopra to speak to an issue through guidance or a speech or a policy, these other tools we're going to talk about today, and try to influence industry behavior more quickly than the longer process of a rulemaking. That's true even when rulemaking may be the better choice from a policymaking standpoint.

Michael Gordon:

Finally, I think that you will see him testing the boundaries of the CFPB's authority. Agencies don't know where that boundary is until they test it. As a new agency on a little firmer footing, I expect the bureau to take more aggressive legal positions. It may even be the case that they're willing to lose a few in order to gain ground elsewhere and find out where the boundaries are and expand those boundaries.

Michael Gordon:

Finally, perhaps the most obvious one, strategy is what we're getting at with the title today, which is the use of the bully pulpit and the power that the CFPB has by speaking to certain issues and setting expectations for industry conduct, even if they don't use their other regulatory authorities.

Michael Gordon:

I do think there's a bit of a false choice in the title, the way we set it up, in the sense that it's not words versus actions in the sense that words can lead to the results in the industry and to the actual change that Director Chopra wants in certain circumstances without having to take actions.

Michael Gordon:

I think we've seen that a little bit. There have been examples of it. The most prominent one that comes to mind is probably overdraft, where in part, because of the focus and the condemnation of overdraft practices that Director Chopra took, many banks in recent months have started changing their practices without any change in rule or guidance or official regulatory expectation.

Michael Gordon:

So we're going to discuss a number of topics now, and for each, we'll try to get at what the bureau has said and what they've done and also what might be coming. So let's start with the junk fees request.

Michael Gordon:

This may be the most obvious example of using the bully pulpit and speaking to an issue without perhaps a clear regulatory objective or authority to rely upon. The bureau did a request for information in January on what they called junk fees that aren't subject to competitive processes that ensure fair pricing.

Michael Gordon:

A huge number, something like 25,000 comments received are more ... And very critical comments from industry, basically along the lines of like this is more words and it's more confusing than it really is action, because the word junk fees, of course, has no legal meaning and it seems to include a whole bunch of disparate ideas. First of all, it includes fees that are regulated at the state and federal level already, including on amount, and it lumps together different types of fees and circumstances, including legitimate fees for services that consumers want and that provide real benefit.

Michael Gordon:

But there's different context. An insufficient fund fee is a much different scenario than a fee paid voluntarily to purchase an ancillary product, for example, that a consumer might choose to do. They're all lumped together as areas of concern, and the bureau's focused on large totals of dollars of fees that the consumers are paying. The implication is they shouldn't be paying most of those without examining some of the benefit side of what the consumers might be getting for those fees paid.

Michael Gordon:

The CFPB said it's going to use the information it gathers to craft rules, to issue guidance, and to identify legal practices through supervision and enforcement for my money. Enforcement, probably using the UDAAP authority, is much more likely than rulemaking. Perhaps they'll do a guidance document or policy of some kind on some corner of the world in terms of fees.

Michael Gordon:

But I expect the most of the action, the follow up here would be enforcement. They could try to base one on the size of the fee, but I think it's much easier for them to bring actions based on how the fee is communicated or collected. And so, that's what I would expect to see.

Michael Gordon:

And which types of fees are in the crosshairs of the bureau? It might be easier to ask which fees aren't, I mean in a sense that there's a long list that they identify as fees and sectors that they're concerned about. But you can categorize them. One way to think about it is for different groups of fees, one is fees charged for things that a consumer believed was included in the base price of the product or service. Another is other unexpected fees that come later in the process.

Michael Gordon:

A third is fees that are really greatly disproportionate to the cost of the service that the service provider is giving. Fourth, fees where the reason for the fee is unclear. Convenience fees are maybe the paradigmatic example that the bureau talks about in this regard. It's gotten notice from other quarters as well. I noticed that the Democratic attorneys general around the country wrote a letter in response to the RFI that focused really on convenience fees alone.

Michael Gordon:

So there's a lot of scrutiny of those, but there are others. Really, I think the ones that the bureau would naturally be most focused on are fees actually be that you incur for not having enough money, whether they're late fees or penalties or insufficient funds or other similar types of fees.

Michael Gordon:

So it's a good reminder to review your fee structure. We've been helping a lot of clients do this, not only to look at the legality of the fees that you're charging, but also the associated fee practice and what are the risks associated with those practices in light of the bureau's increased scrutiny or their signaling in this area.

Michael Gordon:

But it is true that there are real limits to the bureau's ability to regulate in this area. As I mentioned, state and federal law already regulate fees in many cases. Also, the bureau's not a price-setting entity. They don't have the authority to say you charge \$5 instead of \$10 for a certain fee, just like they can't set an interest rate cap. And so, there are real limits here.

Michael Gordon:

But I do think that the UDAAP authority is flexible enough for them to attack practices that are egregious, or that they think are egregious, with respect to charging the fees.

Michael Gordon:

The next topic I wanted to turn to is the request that the bureau made to large household name tech companies that operate payment platforms, Amazon, Apple, Facebook. The bureau seems to be asserting itself as the primary regulator of these large tech companies' consumer finance activities in a way that they hadn't in the past.

Michael Gordon:

It was rather bold in that sense. The bureau's state of concern is that these payment system developments present new risks to consumers and to a fair, transparent, and competitive marketplace.

Michael Gordon:

They use the market monitoring authority, which is distinct from enforcement authority or supervision. This authority had been used before, but not very often. It's an unusual kind of authority that the agency has, and Congress essentially foresaw that the bureau might need to monitor markets that it doesn't already have supervisory jurisdiction or isn't otherwise tracking as new risks emerged.

Michael Gordon:

And so, they wrote this catchall authority saying you can issue these orders and request really broad swaths of information with very little procedural certainty. So, for example, the breadth of the requests here included not only how the products and services work, but revenues earned, and perhaps most critically how consumer data is harvested and used and monetized.

Michael Gordon:

In terms of procedures, the statute didn't really limit the scope. So you can get very broad requests like this, and there's not an established process for challenging these orders. You don't have the same procedural safeguards that you would have, for example, if you were issued a CID from the enforcement division.

Michael Gordon:

Finally, I would say, from a procedural aspect, you might be concerned as a company about the potential disclosure by the CFPB of some information disclosed in this process. As I said, I mean these are information about how Google or others use consumer data and monetize it. I mean those are crown jewels kind of sensitive commercial information. It'll be interesting to see if there are any challenges to the bureau's authority in this regard.

Michael Gordon:

I would say that this request to the large tech firms illustrates Director Chopra's leadership style in a number of ways. First, an example of him using every tool in the toolbox; second, focus on big players; third, a focus on tech and fintech; fourth, a theme of anticompetitive behavior being a concern that runs throughout this request; and, five, an attempt perhaps to influence conduct without necessarily exercising the traditional enforcement on supervised and rulemaking authorities.

Michael Gordon:

Let's turn to this theme of anticompetitiveness. Obviously, as an antitrust regulator at the FTC, Director Chopra was focused on antitrust and enforcing antitrust laws. The bureau doesn't have that same authority, but he seems to be using this antitrust and competitiveness lens more than any prior director had used before.

Michael Gordon:

I will note that this is not only Director Chopra's personal background and mindset perhaps, but it's also a Biden administration priority. The White House directed all agencies to use their existing authorities to promote increased competition in their areas of regulation.

Michael Gordon:

In doing so, the bureau puts a lot of weight on a single clause in the bureau's authorizing statute, which is a purposes clause, where one of the purposes of the bureau is to ensure that markets are fair, transparent, and competitive. They cite to this often when using this lens, and they're making competitive there do a lot of work if, in fact, competitive is supposed to mean competitive from an antitrust viewpoint.

Michael Gordon:

What does the bureau consider anticompetitive? As I see what they're doing, I think there's two categories. There's the traditional antitrust category concern about market concentration and use of market power.

Michael Gordon:

You saw that with the tech companies' information request that I just discussed. We saw them mention it even in the credit card industry, where they had an announcement recently and they were concerned about credit card companies using their power. There were eight companies that had 70% of the market, and they were worried that they were moving in concert on issues around credit reporting in a way that they found anticompetitive. They took pains to point that out.

Michael Gordon:

So that's one area is traditional market power dominance and misuse of that market position. But the second, which is much broader and could affect a lot more companies, frankly, is where competitive pressures are diluted for a variety of reasons, but that consumers basically can't vote with their feet or their pocketbook. You don't get to choose your service provider.

Michael Gordon:

I think of servicing debt collection, credit reporting, data aggregation. Anytime they would say where fees are not disclosed on the front end but on the back end is a trap that the consumer can't avoid and they can't vote with their feet at that point.

Michael Gordon:

I expect the bureau to focus, and try to make cases when they can, regarding practices where companies are making it difficult for consumers to easily switch their providers. We've seen them mention that many times.

Michael Gordon:

Finally, if you think about what their current authorities may allow them to do in the area of this competitiveness concern, abusiveness has already popped up once. I think it's worth pausing on this for a minute.

Michael Gordon:

There was a case recently called JPay case. It involved people who were incarcerated, who were leaving prisons, and did not have a choice of the method by which they were going to receive funds they were entitled to at that moment. JPay, I think, was the provider of the card on which the money was placed.

Michael Gordon:

The bureau took an action against them and took pains to talk about this in the antitrust, anticompetitive way that I've been mentioning here, which is, first of all, the abusiveness prong itself was used, the one that says you're taking an unreasonable advantage of consumers who can't protect their own interests. They made a claim based on that.

Michael Gordon:

In his statement, Director Chopra went even further than the language of the consent order and stressed that the laws that JPay had violated were designed to prohibit abuses of dominance, as he called it.

Michael Gordon:

So here was a case where consumers couldn't vote with their feet. They were captive in some sense, and the bureau made pains to add to their other claims this particular abusive claim and this notion of anticompetitiveness of it.

Michael Gordon:

It's an open question if abusiveness will continue to be used in this way to target anticompetitive behavior, but it's certainly something to look out for. It's a risk to consider now for companies whose services affect consumers who are somehow captive or have limited ability to choose.

Michael Gordon:

The next step I want to address is the bureau's focus on fintech and tech more generally. In the broader context of what's going on in Washington, the bureau's focus on this is part of a larger government increase in scrutiny on the fintech sector, which is to be expected when a sector grows and becomes more important in the economy. But we see it all across a government.

Michael Gordon:

Some of the concerns I've already addressed in terms of the fair lending aspects of AI and modeling of decisions and here, though, what do we expect to see in terms of what the bureau's going to actually do about it in terms of, you said, the real authorities. I mean I'd be surprised if we see rulemaking in this area.

Michael Gordon:

A year ago, I might have given better than 50-50 odds that the bureau would write a larger participant rule that would allow them to supervise a whole bunch of non-banks that are in this space, fintechs. Now I'm less confident that's going to happen because of their recent announcement on invoking their risk-based supervision to supervise non-banks.

Michael Gordon:

So I don't expect a lot of rulemaking one or the other. Maybe they'll still do the larger participant rule. But certainly enforcement of fintech companies and other uses of the bully pulpit to send signals about practices that the bureau has strong views about.

Michael Gordon:

I do want to talk briefly about this announcement on risk-based supervision authority, because I thought it was really interesting. Unlike some of the announcements the bureau has made about extending their legal interpretation, and Tom's going to talk about that in the context of fair lending and its connection with UDAAP, this is one where it's pretty clear the bureau has this authority. It just hadn't been used in this way.

Michael Gordon:

So to remind folks, the bureau has three ways it can exert supervisory authority. Some markets were delineated in the Dodd-Frank Act that they would have this authority. Others they designate through larger participant rulemaking.

Michael Gordon:

But the third is this catchall that they said we're going to start using. This is the risk-based, where they have a reasonable cause to determine that a company's engaging in conduct that poses risk to consumers. If they see that, they can swoop in on a single company where they believe that risk exists and exert their supervisory authority.

Michael Gordon:

I found this notable for several reasons. First, it's consistent with the bully pulpit approach, because I really see this as much about signals sending by the bureau in the future than about actual supervision, because the bureau made an exception to the typical confidentiality rules that apply to supervisory activity and said for this authority, we actually want to have the ability to publish this risk determination that tell the world what we thought was risky about this company and potentially even the name of the company.

Michael Gordon:

That allows the bureau to quickly supervise in a new market, but equally importantly to send a quick message to others in the industry before the supervisory or enforcement work has been completed, but to send signals about practices they're concerned about.

Michael Gordon:

I would say the standards in this are unclear in the sense that what counts as reasonable cause for risk to consumers, there's not guidance about that in the statute about what that standard is. The bureau hasn't delineated one, really. But it's safe to expect that the Bureau's interpretation of that risk won't always match what industries' interpretation is.

Michael Gordon:

Again, this is an example where the standard won't be tested unless the targeted company sues. Even in that case, the result from that might come long after the bureau has accomplished its signal-sending objective.

Michael Gordon:

There's great risk for reputational harm if the bureau actually names names, because the basis for the risk determination that the bureau makes to identify a particular company can be just about anything. There's a wide variety of sources for that reasonable cost determination, including consumer complaints and press reports.

Michael Gordon:

So in other words, based on unsubstantiated consumer complaints, a company could be on the receiving end of one of these risk determinations and have their conduct called out as risky before supervisory activity has even begun much less any findings of wrongdoing.

Michael Gordon:

Adding insult to injury here, the normal rules about confidentiality of supervisory activity remain. So a company might be limited in its ability to refute the allegations at that point in time.

Michael Gordon:

So non-banks that aren't currently subject to a supervisory authority of the bureau should at this point be considering whether they have in place the robust compliance management systems that the CFPB is going to expect to see, if they do come knocking. With that, I'll hand it over to Michelle.

Michelle Hogan:

Thank you. I'm going to touch on the market monitoring request that the CFPB sent to BNPL providers on December 16th. Just as background, BNPL really exploded in the global market. It now represents about \$100 billion in e-commerce transactions. Low interest rates have really helped this BNPL space grow.

Michelle Hogan:

BNPL products are in very high demand because BNPL transactions typically offer 0% interest and consumers repay them in four fixed monthly installments. The first payment being, at the point of sale, 25% of the purchase price.

Michelle Hogan:

The way these products are set up is rather than charging consumers any fees for use of BNPL, BNPL providers typically receive 6% of the purchase price. So the merchant is actually paying the BNPL provider to give this service to their consumers. Merchants have agreed to this setup because it really appeals to a more broader base of consumers.

Michelle Hogan:

And so, basically the way it works, it offers this frictionless checkout where the approval for BNPL is almost instantaneous. Also, it's just a straightforward installment plan. So the consumer knows the exact cost of each installment fee going forward.

Michelle Hogan:

In the past, the average transaction price for BNPL has been \$200, but we anticipate the next stage of BNPL growth will be fueled by bigger ticket items. As an example, Klarna has recently partnered with some luxury merchants like Saks and Balenciaga. And so, these sales are going to range into the thousands. As more BNPL providers partner with luxury merchants, the average BNPL transaction is going to increase.

Michelle Hogan:

Due to all this rapid growth, it has become an obvious target for regulatory attention because of the way it's set up. As I described, BNPL products do not charge interest and are paid in four or fewer installments. BNPL providers have taken the position that the Truth in Lending Act and its associated disclosures do not apply to their products.

Michelle Hogan:

Because of that, senators wrote a letter to the CFPB, raising concerns that BNPL providers intentionally structured their products to avoid obligations under the Truth in Lending Act. Given that BNPL falls into a regulatory gap, consumers may be unaware that BNPL providers operate without any meaningful oversight.

Michelle Hogan:

So getting back to the market monitoring request from CFPB, some of their concerns are accumulating super consumer debt. So some questions the CFPB has is how are BNPL providers tracking aggregate loans to a single consumer, particularly because BNPL providers don't report these loans to the credit bureau. So one BNPL provider doesn't know how much loan amounts another BNPL provider has granted one consumer, and then also how are BPL providers determining a maximum loan amount.

Michelle Hogan:

So the CFPB is asking questions about the underwriting process. Given that really it's instantaneous, the providers really ask just for basic identifying information. There's stock credit pull. I assume they're also using data from previous consumers to assess their credit risk. There is a concern that the BNPL providers aren't determining the consumer's ability to repay these installment loans.

Michelle Hogan:

So the very flexibility is a concern that it's harming BNPL consumers who are taking on several plans they can't afford. Also, they're responsible for tracking multiple dates, if the consumer takes out multiple loans and could have multiple deadlines for repayment in a single month. There is at least some evidence that the delinquency rate on BNPL repayment is higher than on traditional credit payments.

Michelle Hogan:

And so, again, another concern is that it really falls into a regulatory void as part of this market monitoring. 19 state attorney generals took the position that BNPL products are credit and are urging for oversight.

Michelle Hogan:

As Mike mentioned, another concern is harvesting and monetization of consumer data. Typically that has been the province of the FTC. But again this isn't the only instance of the CFPB reviewing how companies treat data and their privacy policies.

Michelle Hogan:

This isn't the first alternative consumer financial product that the CFPB has reviewed, but it's certainly one of the most popular. Once the CFPB finishes its review, we expect that it will use more words, as the theme of this presentation, to express any displeasure with certain features of BNPL rulemaking is possible, but the much more likely result will be enforcement activity or additional guidance.

Michelle Hogan:

Finally, I am turning to junk fees. The CFPB recently sent out a press release that overdraft fees and account maintenance fees are fees for not having enough money. Again, regarding Mike's comments on looking back to the pandemic, this press release

highlighted that the bank revenue from overdraft fees and non-sufficient fees surpassed \$15 billion in 2019, during the pandemic. The same press release also highlighted that credit card companies charged \$14 billion in late fees during the same time period.

Michelle Hogan:

Even before that press release, the CFPB had criticized banks for harvesting billions in overdraft fees from Americans during the pandemic, and stated that overdraft fees were a clear market failure and a lack of competition.

Michelle Hogan:

Shortly after these statements, many banks had already changed their overdraft fee policies. For example, JPMorgan Chase made changes to their overdraft fees, and many of the major banks shifted away entirely from non-sufficient funds fees and overdraft fees in some circumstances.

Michelle Hogan:

So, again, pointing to what Mike said earlier, sometimes words can result in action without the CFPB exerting its actual authority. I will turn it over to Tom at this point.

Tom Burke:

Thanks very much, Michelle. So I have a couple topics I'd like to take the opportunity to cover today. The first of those is very important changes to the way that the CFPB intends to use its UDAAP authority with respect to non-credit discrimination.

Tom Burke:

So to preface this, you may have seen that two days ago, the CFPB issued an advisory opinion in which it held that ECOA, which I'm sure pretty much everybody here is familiar with, applies not just to origination but to the life of the loan. So in other words, they're going to be looking at the discriminatory impact of decisions like whether to terminate or close accounts, whether to lower a credit limit, and they're going to be looking for adverse action notices for all of those events.

Tom Burke:

So if your institution happens to be narrowly focusing on equal credit opportunity considerations only with respect to origination, be prepared in the context of future examinations to go broader than that.

Tom Burke:

On the same note, in March 2022, the CFPB announced an intent to identify unfair discrimination in non-credit practices. In other words, go beyond ECOA. So lots of other things. We have reason to think that that includes at least collections, servicing, consumer reporting, payments and remittances, all kinds of things where people have traditionally not necessarily been looking at their practices with respect to a discriminatory impact.

Tom Burke:

That's all going to be subject to the standard definition of unfairness, which is whether the practice causes substantial harm to consumers that they can't reasonably avoid and where it's not offset by countervailing benefits, which, in the CFPB's view, it never is.

Tom Burke:

So, for example, denying access to its checking account based on race. That would not previously have been an ECOA issue or really a CFPB issue, but now it is. You might say, "Well, Tom, come on. Nobody here is denying bank accounts on the basis of race, obviously." However, the question is not the intent of the institution. It's what is happening in practice.

Tom Burke:

So if you happen to be a small institution servicing a local geographic population that is homogenous in terms of the racial makeup or other things, and you're denying bank accounts on the basis of geography, then that may be disproportionately affecting other populations. All of this is suddenly going to come into the scope of what you're being examined about.

Tom Burke:

By the way, the context in which this is happening is a change to the examination manual for supervision. And so, supervised companies are going to have to be ready to show their processes for assessing the risk of discriminatory outcomes, meaning show that it's something you care about, show your documentation on demographics, the impact of products and fees on different demographics. Are you doing proactive monitoring of your processes before they get implemented and afterwards to make sure that this is not a problem, and training? So in other words, all the stuff you've been doing merely in the ECOA space, get ready to start doing it on a much broader basis.

Tom Burke:

One point I'll note is that if you are trying to get a handle on this, you should seriously consider whether you're making these assessments with the benefit of counsel or not, because if it's not with counsel, then it's probably not privileged. If the results are something that you have concerns about, then you may want the opportunity to address that with the assistance of counsel before making it discoverable to regulators.

Tom Burke:

I'm going to move on to another topic here, which is Director Chopra's comments in which he encouraged state attorneys general to start using the CFPB more in their own enforcement actions and to work jointly with the CFPB in the context of enforcement.

Tom Burke:

Now I personally thought of this as the junior deputy approach. What the CFPB does not have the resources itself to handle, it would like the state AGs to pick up the slack. We did see a lot more state AG activity when there was a perception that the CFPB, under a Republican administration, had pulled back. Now what Director Chopra is saying here is that he would like that to continue.

Tom Burke:

So he has literally used the term joint forces. What has happened since December 2021, when he extended this invitation? The answer is not very much. There was recently an announcement of a joint investigation by the CFPB and the New York Attorney General against MoneyGram related to remittance practices. They're bringing that under both the CFPB and New York law.

Tom Burke:

But I personally do not think that we're going to see a tidal wave of CFPB actions by state attorneys general. The reason for that is that, first of all, you're often going to end up in federal court, which state AGs don't always like. They want home court advantage. They want to be in state courts. There'll be federal question jurisdiction for removal in many instances if they bring that CFPB claim.

Tom Burke:

Historically, even though the state of use have always been able to do this, they just haven't done it very much. You've seen some dabbling by Illinois, New York, California in very isolated cases, typically bigger cases, but it hasn't happened too much.

Tom Burke:

All of this is to say if you have a pattern of practice with a potential national scope or something that is a big deal, consider the risk of joint or parallel investigations and whether it's advantageous to try to handle those simultaneously or separately. With that, we are already at our next prompt for CLE credit.

Tom Burke:

So I'll give folks a minute to click the button here, and then I'll move on to a topic that, like many of these other things, we could probably talk for an hour about, but I have to limit it to a few minutes here.

Tom Burke:

In January, the CFPB announced an intent to examine postsecondary schools that extend private loans with respect to those private loans, which historically it has not done. Of course, anyone who is a fed lender or a loan servicer is familiar with the CFPB exams by now. But for many schools that are making their own institutional loans, they have not been examined. The CFPB has said, "Well, this is driven by things like our experience with Corinthian and IIT and we're worried that this is a loophole where we haven't been looking at these things."

Tom Burke:

So this examination process may be relatively new to some of these institutions. There will be a fairly standard focus on CMS, communications about repayment options to these borrowers, as well as collection practices. If you are in the subset of institutions affected by this, go ahead and just download the updated examination procedures and you will see exactly what questions they're going to ask.

Tom Burke:

Again, we could spend all day on it, but take a look at the questions. If you have concerns, obviously we're available to help with that, because we do a fair amount of work in the examination space.

Tom Burke:

Last, Director Chopra's focus on injunctive relief. If you said, "Tom, what keeps up Director Chopra at night? What is he most worried about?" if you look at his public remarks, the thing that comes up again and again is the issue of recidivism. He's specifically thinking here about large institutional actors that have the capacity to weather large financial penalties without it seriously affecting their business.

Tom Burke:

So the first time we heard this, at least on a wide platform, was in his July 2019 dissenting statement with respect to the sufficiency of, believe it or not, a \$5 billion fine on Facebook, which in his view did not go nearly far enough in reading in Facebook's practices that resulted in that FTC action.

Tom Burke:

He reiterated that in a March 2022 lecture at the University of Pennsylvania. Again, the text is out there. It's a couple pages long. You might want to consider reading it.

Tom Burke:

He specifically calls out, again, many institutions that we're very familiar with, Citigroup, JPMorgan Chase, Wells Fargo, and others who have been the subject of repeated enforcement actions or consent orders during the CFPB's tenure.

Tom Burke:

What he has said is, "We are prepared to suddenly start thinking about things that would've been unthinkable as a matter of injunctive relief, because that's the only way that we think you'll take us seriously." That can include things like caps on growth.

Tom Burke:

By the way, of course, some of these were implemented in the Wells Fargo resolution a few years back. I think we saw that they were fairly effective as a pain point, that institutions do not want to incur that sort of thing. We have a list here of potential things that they go from bad to worse, ultimately ending in things like revocation of FDIC insurance or receivership or liquidation.

Tom Burke:

Now there's a very serious question here about how realistic are these things. Many of them, the CFPB, I think, quite clearly does not have the power to do. If you find yourself in a situation where those penalties are on the table, you should seriously talk with your counsel, obviously, about how to combat those threats and how to make clear that some of them are empty threats.

Tom Burke:

So, again, we'd be happy to talk about this all day, but I'm going to pass it now to Alan for comments on payday lending.

Alan Kaplinsky:

Thank you very much, Tom. We're going to wrap it up with a very quick review of what actions Rohit Chopra has taken with respect to payday lending. The answer is he hasn't done a great deal.

Alan Kaplinsky:

But before we get to that, I think it bears noting that there is still litigation pending, and it's been pending for a long time, challenging what's left of the payday loan rule that got promulgated in 2017.

Alan Kaplinsky:

There were two aspects to that rule. There was a mandatory underwriting provision and there are payment provisions. After the change in administrations and with a new director of the CFPB in 2019, there was a proposal that the mandatory underwriting provisions be revoked and that there'd be a delay in the compliance state of the payments provisions.

Alan Kaplinsky:

Then that proposal got finalized in 2020. There has been a lawsuit filed by CFSA, a trade association of payday lenders, against the CFPB, which was originally challenging the entire rule. But after the new director limited the rule to only the payments provisions, the litigation now applies and challenges only the payments provisions.

Alan Kaplinsky:

The federal district court has upheld the validity of the payments provisions in the rule. That's now on appeal to the Fifth Circuit. As I noted and also as Mike Gordon noted, there is now a serious constitutional challenge based on the way the CFPB is funded. It's not subject to congressional appropriations. Rather, it gets its funding directly from the Federal Reserve system. As a result of that, there are certain constitutional scholars and certainly people that are challenging CFPB actions that take the position that that is unconstitutional.

Alan Kaplinsky:

Unlike the issue that got litigated to seal a law, where the unconstitutional provision dealing with the tenure of the director, that he could only be removed for cause by the President, unlike the fact that there was a severability provision that applied to that, which legitimized what the CFPB had done up to that point, there is no such severability provision that would apply in the appropriations with respect to that issue.

Alan Kaplinsky:

And so, there is still a cloud hanging over the CFPB. Here we are 11, 12 years into the existence of the agency and we're still not completely certain that it was constitutionally authorized by Dodd-Frank. What that means is that if you get into litigation with the CFPB, that is a card that you can play, but it's one that needs to be played very carefully, very judiciously, and very strategically.

Alan Kaplinsky:

So let me mention the one action, or I guess the one word, that the CFPB has said about payday lending. It said, first of all, nothing about promulgating another rule dealing with mandatory underwriting or anything else.

Alan Kaplinsky:

It did come out last month with this market snapshot pertaining to the consumer use of state payday loan extended payment plans. In this report, the CFPB noted the prevalence of state laws that provided for no-cost extended payment plans and that the data show that rollover and default rates consistently exceeded extended claim payment plan usage rates.

Alan Kaplinsky:

The CFPB, of course, observed that monetary incentives must have been the reason for that, that encouraged lenders to steer them into rollovers rather than to steer them into extended payment plans where the lender wouldn't earn any additional money.

Alan Kaplinsky:

Well, what do I think is going to happen there? I think this is going to apply primarily in the supervision context. It's something the CFPB will be looking at. If they believe that there has been improper steering of customers of payday lenders into costly rollovers rather than into no-cost extended payment plans and if there has been deception, you can be sure CFPB isn't going to like that.

Alan Kaplinsky:

And so, that's where I see most of the activity with respect to payday lending. I do not think it is at all likely that we are going ... Despite the rhetoric that we've seen, and we know that there's no love lost between Rohit Chopra and the payday lending industry. I just don't see it as being a priority that he's going to take on during his remaining term, doesn't have the bandwidth, and, also, whatever he does in that area, he knows is going to be subject to lengthy litigation. So it just isn't going to be worth it.

Alan Kaplinsky:

Well, I want to thank all of our presenters today, Mike, Tom, Michelle. Also want to thank all of our listeners who downloaded the program today.

Alan Kaplinsky:

Let me again just remind you that our podcasts are available, except for two weeks during November and December, on a weekly basis Thursday morning. Thank you once again.