



# CONSUMER FINANCIAL SERVICES COMMITTEE NEWSLETTER

February 2017

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## Important Dates



### [Business Law Section Spring Meeting](#)

April 6-8, 2017  
New Orleans, LA

## Newsletter Editors

Yolanda Gamboa  
Bank of America, N.A.  
312/992-9620

Judy Mok  
Morrison & Foerster LLP  
212/336-4073

Sabrina Neff  
Hughes Watters Askanase, LLP  
713/328-2816

## Membership Minute

**CFSC by the Numbers:** As of December 2016, total members = 1,540, which represents a small decrease compared to December 2015. Keep spreading the word about joining the ABA's CFSC - encourage your clients and colleagues to check it out!

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## Leadership Message



Andrew Smith, Chair  
Consumer Financial Services Committee

In this Chairman's Message, we will provide details of our upcoming Spring Meeting in New Orleans-including a financial literacy initiative sponsored by our Pro Bono Subcommittee on the afternoon before the CLE programming begins-and recap our recent success at the Winter Meeting in Carlsbad, California.

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## Subcommittee Spotlight

### **Housing Finance Subcommittee's Panel on RESPA and PHH at Winter Meeting** By Peter Cockrell, McGlinchey Stafford, PLLC

At this year's Winter Meeting in Carlsbad, CA, the Housing Finance Subcommittee put together a panel presentation covering recent developments in Real Estate Settlement Procedures Act ("RESPA") law. The panel, which was moderated by the Subcommittee's Co-Chair David Permut, featured Consumer Financial Protection Bureau ("CFPB") alumna Sarah Auchterlonie of Carlton Fields PA, The United States Department of Housing and Urban Development ("HUD") alumnus Ken Markison of the Mortgage Bankers Association, and Jim Milano of Weiner Brodsky Kider PC. The discussion focused on the D.C. Circuit's recent decision in *PHH Corporation v. CFPB* and its implications for RESPA practice and enforcement. In addition to holding that the CFPB's structure is unconstitutional, the D.C. Circuit decision reversed the CFPB's imposition of a \$109 million penalty against PHH for use of a captive mortgage reinsurance arrangement as a violation of RESPA Section 8.

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## Legal Features

### **Supreme Court Appears Deeply Divided Over Bankruptcy Proof of Claim Case** By Caren Enloe, Smith Debnam Narron Drake Saintsing & Myers, LLP

On January 17, 2017, the Supreme Court heard *Midland Funding, LLC v. Johnson, No. 16-348* (argued Jan. 17, 2017). Its decision is anticipated to resolve a circuit split as to whether the filing of a proof of claim for time-barred debt violates the Fair Debt Collection Practices Act (the "FDCPA") and whether the Bankruptcy Code precludes the FDCPA's application to proofs of claim.

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### **Texas Home Equity Gets Some Clarity** By Paul Kellogg, Hughes, Watters & Askanase, LLP

The Texas home equity law has long bedeviled practitioners and lenders with its complexity and lack of clarity and precision. Some issues have been open to interpretation for almost two decades. Faced with a lack of regulatory guidance or court cases, lawyers and lenders have been forced to make difficult and uncertain choices. In the past year, a flurry of Texas Supreme Court cases have upended some of those

## Meeting Highlights

### **Panel on the Future of the CFPB** By Andrew Smith, Covington & Burling LLP

At the CFSC Winter Meeting in Carlsbad, California, in early January, an all-star group of panelists-including a former Chief of Staff for the House Financial Services Committee, a former Associate GC at the Federal Reserve Board, and the former Assistant to the Solicitor General handling PHH's appeal-discussed the possible fate of CFPB Director Richard Cordray, the fate of the CFPB itself, and the fate of the CFPB's rulemaking agenda.

Since the panel was held in the second week of January, momentous events have occurred, including the inauguration of President Trump and a series of Executive Orders limiting the issuance of new rules, but, confounding the predictions of many pundits, there continues to be very little resolution as to the future of the CFPB.

### **The Fate of Director Cordray**

With respect to the fate of Director Cordray, the panelists noted that, although then-President-Elect Trump had reportedly interviewed successors for Mr. Cordray, the President-Elect had not expressed any specific intentions with respect to removing Mr.

long-existing practices but also provided some welcome clarity on these "open issues".

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**A Survey of Activities Identified as Unfair, Deceptive, or Abusive Under the Dodd-Frank Act**  
By Adam D. Maarec, Davis Wright Tremaine LLP  
and John C. Morton, Gordon Feinblatt LLC

This is our latest article in a series that surveys activities identified as unfair, deceptive or abusive acts or practices (UDAAPs) by the Consumer Financial Protection Bureau (CFPB), and state attorneys general and consumer financial services regulators, using federal UDAAP powers created by the Dodd-Frank Act. This article covers relevant UDAAP activity that occurred between July 1, 2016 and December 31, 2016, and surveys enforcement actions and other statements by the CFPB in reports that discuss UDAAP violations. These activities provide insight into the specific types of practices that could be considered UDAAP violations in the future.

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Cordray from his position. Despite continued speculation that Director Cordray's days are numbered, as of this writing, there is still no public statement from the White House expressing support for his removal.

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## Leadership Message

In this Chairman's Message, we will provide details of our upcoming Spring Meeting in New Orleans—including a financial literacy initiative sponsored by our Pro Bono Subcommittee on the afternoon before the CLE programming begins—and recap our recent success at the Winter Meeting in Carlsbad, California.

### Business Law Section Spring Meeting

Our Committee is convening again April 5-8 at the [ABA Business Law Section Spring Meeting](#) in New Orleans. All of our events are at the Hyatt Regency New Orleans – make your reservations ASAP, as the room block closes on March 15. As you make your travel arrangements, please plan to arrive on Wednesday and depart on Saturday (or Sunday for those of you who are staying for the Annual ACCFSL Dinner).

We have a full schedule of meetings planned:

- We begin on Wednesday, April 5, at 1:00 PM with our Pro Bono Subcommittee's **Public Service Project** – financial literacy training for older adults at sites throughout New Orleans. Please sign up by emailing our Pro Bono Subcommittee Chair, David Esquivel ([desquivel@bassberry.com](mailto:desquivel@bassberry.com)).
- Our formal programming begins at 4:00 PM on Wednesday, April 5 with **Beer & Basics**, followed by a **Welcome Reception** with the Banking Law Committee.
- On Thursday, April 6, we have a full day of CLE programming. Thursday's CLE programs include presentations on:
  - A retrospective on the CFPB enforcement program;
  - Financing ancillary products;
  - The CFPB's short-term credit rule;
  - Online small business lending;
  - Privacy implications of blockchain;
  - The intersection of bankruptcy and debt collection in the *Midland v. Johnson* case; and
  - Our timely selection of Roundtable presentations, as well as the In-House Counsel Roundtable.
- On Thursday evening, our **Committee Dinner** will be held at [Brennan's Restaurant](#), a French Quarter institution. Dinner is being generously sponsored by the McGlinchey Stafford and Burr Forman law firms. Tickets are \$150 each, and can be purchased online [here](#).
  - To add a dinner ticket to your existing meeting registration, click on "Register Now," which will prompt you to log-in with your ABA credentials. After logging in, click on "View Registration." Find the "Select Events" header and click on "Edit"—this will take you to the list of ticketed events to select.

- On Friday, April 7, we have another full day of CLE programming which we are holding jointly with the Banking Law Committee, including the venerable Fisher Memorial Program. Friday’s CLE programs include presentations on:
  - Consumer protection exams and the bank examination privilege;
  - The CFPB and “regulation by enforcement;”
  - The HMDA final rule and fair lending supervisory and enforcement trends; and
  - Fintech, bank partnerships, and true lender issues.
  
- On Saturday, April 8, our programming ends at 12:30 PM, and includes CLE presentations on
  - payment processing;
  - the intersection of Regulation C and Regulation Z;
  - the new proportionality standard for federal court discovery; and
  - the evolving ethics of incentive compensation (2.0 hours of ethics credits!).
  
- On Saturday evening, the American College of Consumer Financial Services Lawyers will host its annual dinner for the Fellows of the College. Details to follow directly from the ACCFSL.

### Winter Meeting Recap

We had another successful stand-alone CFSC meeting on January 12-15, 2017, at the [Park Hyatt Aviara Resort](#) in Carlsbad, California. We had strong representation from the CFPB, FTC, banking agencies, state regulators, and the consumer advocate community, as speakers and in the audience.

Program materials, including audio recordings of CLE presentations, are located [here](#).

Attendance was very good—although not at the level of last year’s ski meeting in Park City (or the 2015 meeting in New Orleans, which remains the high-water mark)—it was our third-best attended meeting ever. As you will see, below, our meeting attendance has held up nicely, even during the down years of the financial crisis:

<b>YEAR</b>	<b>LOCATION</b>	<b>TOTAL</b>
2017	Carlsbad, CA	263
2016	Park City, UT	277
2015	New Orleans, LA	290
2014	Park City, UT	245
2013	Naples, FL	217
2012	Park City, UT	172
2011	Naples, FL	160
2010	Park City, UT	150
2009	Scottsdale, AZ	168
2008	Park City, UT	166
2007	Dana Point, CA	221
2006	Park City, UT	153
2005	Key Biscayne, FL	108
2004	Park City, UT	127

Although we are not the largest Committee in the ABA Business Law Section—that distinction belongs to the Mergers & Acquisitions Committee—we are among the most enthusiastic, with attendance at our stand-alone meetings, and at our CLE programs at the Business Law Section Spring and Annual Meetings, frequently setting new records.

## Housing Finance Subcommittee's Panel on RESPA and *PHH* at Winter Meeting

By Peter Cockrell, McGlinchey Stafford, PLLC

At this year's Winter Meeting in Carlsbad, CA, the Housing Finance Subcommittee put together a panel presentation covering recent developments in Real Estate Settlement Procedures Act ("RESPA") law. The panel, which was moderated by the Subcommittee's Co-Chair David Permut, featured Consumer Financial Protection Bureau ("CFPB") alumna Sarah Auchterlonie of Carlton Fields PA, The United States Department of Housing and Urban Development ("HUD") alumnus Ken Markison of the Mortgage Bankers Association, and Jim Milano of Weiner Brodsky Kider PC. The discussion focused on the D.C. Circuit's recent decision in *PHH Corporation v. CFPB*<sup>1</sup> and its implications for RESPA practice and enforcement. In addition to holding that the CFPB's structure is unconstitutional, the D.C. Circuit decision reversed the CFPB's imposition of a \$109 million penalty against PHH for use of a captive mortgage reinsurance arrangement as a violation of RESPA Section 8.

Mr. Markison began the discussion by providing an overview of the PHH case and insight into HUD's historical interpretation of Section 8, which generally prohibits kickbacks and referral fees in conjunction with real estate settlement services. He pointed out, however, that Section 8 also provides that "nothing" in the section "prohibits payment to any person of a bona fide salary or compensation or other payment for goods or facilities actually furnished or for services actually performed." He framed HUD's efforts as regulator as seeking to reconcile the prohibition with the exemption by determining for various types of transactions whether payments were bona fide and reasonable and for actual necessary and distinct services, notwithstanding that they might be arrangements among settlement service providers.

HUD as regulator articulated its views through several rules, policy statements, opinions and Frequently Asked Questions that HUD arrived at after reaching out to the public and stakeholders. Mr. Markison characterized the PHH case as a conflict between HUD's analysis of Section 8 and the CFPB's competing interpretations of Section 8 and its exceptions, which the CFPB announced through enforcement actions rather than the regulatory process. He stated that since the CFPB departed from settled interpretations in this and other cases, it should have gone through the rulemaking process.

Ms. Auchterlonie, who during her time at the CFPB directly supervised enforcement counsel in the CFPB's action against PHH, described the CFPB enforcement division's reliance on traditional liability theories while also asserting in the *Lighthouse Title* and *PHH* matters novel and more probing interpretations of Section 8(c)(2). For example, in *PHH*, enforcement alleged that the home loan lender automatically sent loans only to mortgage insurers who purchased "deep cede" reinsurance—where almost 40% of the insurance premiums that consumers paid were ceded to PHH's subsidiary. The 40% split departed from prior and post-crises standards that limited the premium cedes to around 25%.

In light of these facts, enforcement argued that conditioning referrals on the purchase of the unwanted deep cede product could violate Section 8 even if fair market value is paid. While prior HUD guidance focused on the fairness of value paid for goods and services exchanged between settlement service

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<sup>1</sup> No. 15-1177 (D.C. Cir. Oct. 11, 2016).

providers, the statutory language actually requires bona fide compensation. Where payments are clearly tied to referrals—as shown by e-mails, allocation of loans in market shares that correspond to purchases of the unwanted good, and third-party assessments of the sold goods’ actual utility—the CFPB has argued that determining whether compensation represents a fair market value is no longer the end of the inquiry into the bona fide question. Rather, the CFPB looks at the entire arrangement to assess whether the existence of the arrangement itself (*e.g.*, buying something unneeded) constitutes illegal compensation to the seller who is in the position to make settlement services referrals. Ms. Auchterlonie noted that the CFPB has applied this theory elsewhere as well, such as in its action against *Lighthouse Title* in 2014. In addition, she warned against divorcing either enforcement action from the particular facts of the case.

Mr. Milano wrapped up the discussion by providing three themes (theory, structure, and implementation) for practitioners to consider as they advise clients regarding Section 8 compliance. First, the theory that should prevail after the D.C. Circuit’s decision is HUD’s original interpretation of Section 8. Second, practitioners must ensure that any arrangement is carefully structured to fall squarely within one of the Section 8 exceptions. And third, companies should emphasize implementation through training and monitoring of employees.

## Supreme Court Appears Deeply Divided Over Bankruptcy Proof of Claim Case

By Caren Enloe, Smith Debnam Narron Drake Saintsing & Myers, LLP

On January 17, 2017, the Supreme Court heard *Midland Funding, LLC v. Johnson*, No. 16-348 (argued Jan. 17, 2017). Its decision is anticipated to resolve a circuit split as to whether the filing of a proof of claim for time-barred debt violates the Fair Debt Collection Practices Act (the "FDCPA") and whether the Bankruptcy Code precludes the FDCPA's application to proofs of claim.

### Background

As many know, *Johnson* was the Eleventh Circuit's follow-up decision to *Crawford v. LVNV Funding, LLC*. In *Crawford*, the Eleventh Circuit ruled that the filing of a proof of claim was an attempt to collect a debt and that the filing of a proof of claim on time-barred debt violated the FDCPA. *Crawford v. LVNV Funding, LLC*, 758 F.3d 1254 (11th Cir. 2014), *cert. denied* 135 S. Ct. 1844 (2015). Since *Crawford*, copycat cases have been filed all over the country, and a number of circuits have issued opinions that directly conflict with *Crawford*. See, e.g., *Dubois v. Atlas Acquisitions (In re Dubois)*, 834 F.3d 522 (4th Cir. 2016); *Owens v. LVNV Funding, LLC*, 832 F.3d 726 (7th Cir. 2016); *Nelson v. Midland Credit Mgmt.*, 828 F.3d 749 (8th Cir. 2016).

Despite the growing weight of authority against its position, the Eleventh Circuit remained firm in deciding *Johnson*, not only reaffirming its prior position that the filing of a proof of claim for time-barred debt violates the FDCPA but also expanding it to address the issue left unanswered in *Crawford*: whether the Bankruptcy Code precludes the FDCPA's application to proofs of claim. *Johnson v. Midland Funding, LLC*, 828 F.3d 1334 (11th Cir. 2016).

### Johnson in the Lower Courts

Aleida Johnson filed her Chapter 13 bankruptcy petition in 2014. Midland Funding, LLC, a debt buyer, filed a proof of claim which disclosed on its face that the claim was barred by the applicable statute of limitations, listing the date of last transaction as May 2003. Johnson sued Midland in federal court, alleging that Midland had violated sections 1692e and 1692f of the FDCPA by filing a proof of claim for time-barred debt.

### In the District Court

Midland moved to dismiss, asserting that Johnson's FDCPA claims were precluded by the Bankruptcy Code. The district court concluded that the Bankruptcy Code expressly provides for the filing of a claim, irrespective of whether the underlying debt is time barred, so long as the creditor has a right to payment that has not been extinguished by state law while the FDCPA prohibited debt collectors from doing so. The district court further concluded that the Bankruptcy Code and the FDCPA were in irreconcilable conflict and that the later statute, the Bankruptcy Code, impliedly repealed the earlier statute, the FDCPA. *Johnson v. Midland Funding, LLC*, 528 B.R. 462, 470 (S.D. Ala. 2015).

## In the Eleventh Circuit

On appeal, the Eleventh Circuit reversed, holding that the Bankruptcy Code and the FDCPA were not in irreconcilable conflict. Instead, "[t]he FDCPA easily lies over the top of the Code's regime, so as to provide an additional layer of protection against a particular kind of creditor." *Johnson*, 823 F.3d at 1341. The court concluded that the two statutes could be reconciled because "they provide different protections and reach different actors." *Id.* at 1340. While the Bankruptcy Code allows creditors to file proofs of claim even with respect to time-barred debt, it does not require that they do so, and such creditors "are not free from all consequences of filing these claims." *Id.* at 1339.

## Supreme Court

The significance and divisiveness of the issues led both the petitioner and respondent to agree that the issues merited review. The parties' consensus fast tracked the court's consideration of the petition, and the following issues were certified for appeal in October: (a) whether the filing of an accurate proof of claim for an unextinguished time-barred debt in a bankruptcy proceeding violates the FDCPA; and (b) whether the Bankruptcy Code, which governs the filing of proofs of claim in bankruptcy, precludes the application of the FDCPA to the filing of an accurate proof of claim on an unextinguished time-barred debt.

On oral argument, the Court appeared sharply divided. Justices Ginsburg, Sotomayor and Kagan all appeared troubled with Midland's premise that the Bankruptcy Code allows for the filing of a proof of claim for time-barred debt. Meanwhile, Chief Justice Roberts, as well as Justices Kennedy, Breyer and Alito, expressed concerns of various degrees with the legal and jurisdictional implications of Johnson's argument. Specifically, the Court was troubled by:

- **Whether the Bankruptcy Code's definition of a claim includes an implicit requirement that the claim be enforceable.** Justices Sotomayor and Kagan seemed particularly troubled by Midland's position that a "claim" is defined broadly and does not impose upon the creditor any duty to certify that there is no valid statute of limitations defense to its claim under the provisions of the Bankruptcy Code. Justice Sotomayor expressed some affinity with the position that a claim required both a right to payment and an enforceable obligation.
- **Johnson's position that a "debt collector has to have a good faith belief that they have a right to payment under the code and have a valid and enforceable debt."** Chief Justice Roberts, Justices Breyer and Alito expressed concerns over the "good faith" standard, posing questions as to whether "good faith" was a subjective or objective test and as to which court would make the determination. Chief Justice Roberts noted that, with respect to the statutes of limitations, the issue is not always patently clear. A number of justices additionally appeared concerned with the scope of Johnson's enforceability argument and the unintended implications of extending it to affirmative defenses other than the statute of limitations.
- **Jurisdictional implications.** Both Chief Justice Roberts and Justice Breyer raised concerns with the jurisdictional implications of Johnson's position and the potential of not hearing bankruptcy matters in bankruptcy court. Justice Breyer particularly expressed his concerns regarding the proof of claim being adjudicated in the bankruptcy court and then a different court (the district court) ascertaining whether the filing of the proof of claim was in good faith or violated the FDCPA.
- **Reconciliation of the statute of limitations as an affirmative defense and Johnson's position.** Justice Kennedy posed a number of questions to Johnson's counsel and the Department of Justice (appearing as *amicus curiae*) raising concerns with Johnson's assertion that a debt collector can

violate the FDCPA by filing a proof of claim for time-barred debt. Justice Kennedy's questions seemed to reflect a two-fold concern. First, that, by its inherent nature, the statute of limitations is an affirmative defense and, secondly, that, in a majority of states, the running of the statute of limitations does not extinguish the debt. Both Justices Kennedy and Alito seemed to share a concern with reconciling those concepts with the position of Johnson which would place an affirmative duty on the claim filer not to file the proof of claim for time-barred debt rather than upon the trustee or other interested party to object.

- **The practical effect of allowing the filing of proofs of claim for time-barred debt and the burden it imposes upon other parties in a bankruptcy case.** Both Justices Kagan and Sotomayor expressed concerns with the practical effects that allowing creditors to file proofs of claim on time-barred debt would have on the bankruptcy system, the burden it would impose upon trustees, and the diminishing effect that allowing proofs of claim for time-barred debt has on other creditors' claims. Conversely, Chief Justice Roberts, as well as Justices Alito and Breyer, seemed less concerned, noting that considering the documentation filed with the proof of claim, it should be obvious to the trustee as to which claims to object.

A decision is expected sometime this spring. For those interested, the Spring Business Law Meeting will include a panel discussion of *Midland Funding, LLC v. Johnson* including counsel for the parties.

## Texas Home Equity Gets Some Clarity

By Paul Kellogg, Hughes, Watters & Askanase, LLP

The Texas home equity law has long bedeviled practitioners and lenders with its complexity and lack of clarity and precision. Some issues have been open to interpretation for almost two decades. Faced with a lack of regulatory guidance or court cases, lawyers and lenders have been forced to make difficult and uncertain choices. In the past year, a flurry of Texas Supreme Court cases have upended some of those long-existing practices but also provided some welcome clarity on these “open issues”.

Two of the most important issues have been (1) whether a defective home equity loan is void or voidable, and (2) what statute of limitations (SOL) applies to claims by borrowers. Historically, lower courts in Texas have held that a defective home equity loan was voidable and subject to a 4-year SOL. Moreover, the statutory process to cure a defective loan arises only if the borrower notifies the lender of the defect. If there was no notification, no cure was required. Accordingly, many practitioners advised their clients to “let sleeping dogs lie” while the SOL ticked away.

That changed last May. In *Wood v. HSBC Bank USA, N.A., et al.*, the Texas Supreme Court held that the lien was invalid (void) until cured. Fortunately, the Court emphasized that cure renders the lien valid. If uncured, the loan might remain void for the entire life of the loan, creating a continuing cloud on title. As such, the owner has an ongoing right to sue to remove that cloud and therefore, no SOL applies. What lender would gamble that a defect goes unnoticed for up to 30 years? Now it only makes sense for a lender to be proactive and cure defects it finds through audit or otherwise.

The only event that cuts off the borrower’s right to sue to quiet title is if an innocent purchaser for value buys the home at foreclosure. However, that same provision of the statute allows the borrower to sue for wrongful foreclosure. The remedy could be drastic, depending on the facts and circumstances.

Fortunately, most home equity loan defects can be cured. The law provides for five types of cures for five categories of defects, and a sixth “catch-all” or “do-over” cure for defects that don’t fit within the other categories. The “catch-all” allows the lender to cure “the failure to comply by a refund or credit to the owner of \$1,000 and offering the owner the right to refinance the extension of credit with the lender or holder for the remaining term of the loan at no cost to the owner on the same terms, including interest, as the original extension of credit with any modifications necessary to comply with this section or on terms on which the owner and the lender or holder otherwise agree that comply with this section.”

But what if none of the cures is applicable, even the “catch-all”? For example, what if the borrower has paid off the loan and then the lender fails to comply with the statute (such as by failing to provide the cancelled note and a release of lien document as required)? The Texas Supreme Court decided this issue in *Garofalo v. Ocwen Loan Servicing, L.L.C.* The statute states that the homestead is “protected from forced sale [i.e., is not subject to foreclosure] for the payment of all debts” except the 8 types of liens listed in Section 50(a) – home equity debt being only one of those types. The Court held that the home equity statute prohibits foreclosure but does not give borrowers substantive rights, such as the right to require forfeiture of principal and interest, except where the statute specifically provides for that remedy (such as for failure to cure a defect). In *Garofalo*, the loan had been paid in full before the suit was filed, so none of the cure provisions were applicable or would provide effective relief (it being

impossible to offer to refinance a loan that no longer exists). Perhaps to avoid a “draconian” penalty on the lender for a technical violation of the home equity requirements, the Court held that Garofolo had other remedies – a suit for breach of contract and the remedies of actual damages or specific performance. (But also note that, if the loan is brought into compliance with the home equity statute, a breach of contract claim on other grounds would be subject to the general 4-year SOL that applies to contracts in Texas.) Of course, this is a very narrow exception. In almost any other situation – if there had been any remaining balance due on the loan – there would have been a clearly applicable cure that the lender was obligated to undertake.

One should also note that the “catch-all” requires only an *offer* to refinance the loan on compliant terms at no cost to the borrower. It does not require the lender to obtain the borrower’s consent or cooperation. The lender has met its duty with the offer. This view is affirmed in the official regulations.

What if the refinance is not feasible? For example, what if it would fail the underwriting standards of the lender, or not comply with the federal ability-to-repay rules? In some situations, the lender may be able to enter into a modification of the loan to work around these issues and resolve certain loan defects. In a 2014 case, *Sims v. Carrington Mortgage Services, L.L.C.*, the Texas Supreme Court held that the lender could recapitalize past-due amounts owed under the terms of the initial loan (such as monthly payments, taxes, and insurance premiums) without creating a new “extension of credit”, since the original debt instrument was not satisfied and replaced. The payment of these amounts by the lender was not a loan of “new money” because these were amounts the borrower was already obligated to pay. The Court also stated that the test of whether the transaction is a true modification (versus a refinance) is “whether the secured obligations are those incurred under the terms of the original loan.” Most importantly, because the recapitalization was not a new extension of credit the modification did not have to comply with the home equity statute. Really? Not at all?

One of the home equity provisions requires the loan to be “scheduled to be repaid in substantially equal successive periodic installments”. The narrow question in *Sims* was whether the original repayment schedule could be altered by changing the monthly payment to accommodate the capitalization of past-due amounts. The Court held that the original schedule could be changed. A subsequent Texas appeals court decision (*Graze v. Nationstar Mortgage, LLC*), which the Supreme Court declined to hear on appeal, considered the question of whether a modification could provide for interest-only payments for several months followed by a period of amortizing payments. The court considered this a valid change to the payment schedule. The court also made a very sweeping statement: “The Texas Supreme Court has recently held . . . that section 50, which applies to new home-equity loans, does not apply to restructured home-equity loans. . . If Graze's . . . loan modifications do not meet the [Supreme] court's definition of a new ‘extension of credit,’ they are not subject to the requirements of article XVI, section 50(a)(6)”. This should not be treated as a *carte blanche* to ignore statutory limitations such as the aggregate 3% cap on fees over the life of the loan or the requirement that the installments ultimately amortize the debt (i.e., no balloon payment). For example, a balloon payment would be a substantial change from the original loan terms. Second, although the *Sims* court and the *Graze* court approved of changes in the monthly payment, both plans ultimately resulted in substantially equal amortizing monthly payments. On the other hand, if properly structured, the lender should be able to implement remedial repayment plans, forbearance agreements, changes to the interest rate and changes to the monthly payment as a result of large prepayments of principal.

Although the Texas home equity law still has many mysteries, these clarifications should help many practitioners and lenders resolve some common and fraught issues with existing loan portfolios and new transactions.



## **A Survey of Activities Identified as Unfair, Deceptive, or Abusive Under the Dodd-Frank Act**

by Adam D. Maarec, Davis Wright Tremaine LLP  
John C. Morton, Gordon Feinblatt LLC

American Bar Association Consumer Financial Services Committee  
Compliance Management and Federal and State Trade Practices Subcommittees

January 6, 2017

### **I. Introduction**

This is our latest article in a series that surveys activities identified as unfair, deceptive or abusive acts or practices (UDAAPs) by the Consumer Financial Protection Bureau (CFPB), and state attorneys general and consumer financial services regulators, using federal UDAAP powers created by the Dodd-Frank Act.<sup>1</sup> This article covers relevant UDAAP activity that occurred between July 1, 2016 and December 31, 2016, and surveys enforcement actions and other statements by the CFPB in reports that discuss UDAAP violations.<sup>2</sup> These activities provide insight into the specific types of practices that could be considered UDAAP violations in the future.<sup>3</sup>

We intend to publish periodic updates to this article cataloging new UDAAP activity based upon the federal UDAAP powers contained in the Dodd-Frank Act.

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<sup>1</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, 12 U.S.C. §§ 5301 *et seq.* (the “Dodd-Frank Act”); *see, e.g.*, 12 U.S.C. § 5552 (2016).

<sup>2</sup> We have attempted to make this survey as comprehensive as possible; however, it is not exhaustive and there may be other relevant actions that are not discussed in this paper. Also, it must be noted that this area of law is rapidly evolving and new actions arise regularly.

<sup>3</sup> The term “unfair” is defined in the Dodd-Frank Act as an act or practice that “causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers [and the] injury is not outweighed by countervailing benefits to consumers or to competition.” 12 USC § 5531(c)(1). The term “deceptive” is not statutorily defined, but it is defined in the CFPB’s examination manual as “a material representation, omission, act or practice that misleads or is likely to mislead a consumer, provided the consumer’s interpretation is reasonable under the circumstances.” CFPB Examination Manual V.2, UDAAP 5 (October 2012), available at [http://files.consumerfinance.gov/f/201210\\_cfpb\\_supervision-and-examination-manual-v2.pdf](http://files.consumerfinance.gov/f/201210_cfpb_supervision-and-examination-manual-v2.pdf). The Dodd-Frank Act introduced the term “abusive” and defined it as an act or practice that either:

[1] materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or

[2] takes unreasonable advantage of [either]:

(A) a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;

(B) the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or

(C) the reasonable reliance by the consumer on a covered person [such as a bank or other financial institution] to act in the interests of the consumer. 12 USC § 5531(d).

## **II. Overview: Identification of Unfair, Deceptive, or Abusive Acts or Practices**

Between July 1, 2016, and December 31, 2016, the CFPB engaged in 11 public enforcement actions involving alleged UDAAP violations. Past UDAAP actions can provide a road map for industry participants to identify and better understand acts or practices that are considered problematic by law enforcement authorities. UDAAP enforcement actions during the period of this summary involved marketing, servicing, debt collection, debt sales and debt settlement. The CFPB highlighted other UDAAP issues involving production incentives in a bulletin, and debt collection, student loan servicing, and automobile loan servicing in its Supervisory Highlights report. During this period there were no enforcement actions filed independently by state regulators or attorneys general alleging violations of the federal UDAAP prohibition. We provide an update on two litigated cases that were resolved within the period.

The summaries of each UDAAP action below appear in chronological order and are intended to provide a straightforward identification of the specific acts or practices that were alleged to be unfair, deceptive, or abusive by the CFPB, state attorneys general and/or state regulators.

## **III. CFPB Enforcement Actions**

### **a. Santander Bank, N.A. – July 2016 (Marketing)<sup>4</sup>**

Santander Bank, N.A., entered into a consent order with the CFPB related to allegedly deceptive practices when asking consumers to opt-in to deposit account overdraft services for ATM and one-time debit transactions. The CFPB alleged that the company engaged in the following deceptive practices:

- With respect to the cost of overdraft services, misrepresenting in telemarketing calls that consumers would:
  - Not have to pay for the overdraft service when the service carried fees;
  - Only be charged one overdraft fee, either at the time of an overdraft or on the sixth day after, when charges would be imposed in connection with both events;
  - Not be charged any fees if the overdraft amount was repaid in five days, when charges were incurred at the time of an overdraft;
  - Only have to pay a fee in emergency situations when fees were applied in all situations; and
  - Be charged overdraft and other fees if they did not opt-in to the overdraft service when such fees would not be charged absent an opt-in;
- Misrepresenting the nature of telemarketing sales calls by claiming the calls were to inform consumers of their “opt-in status” and an attempt to “reenroll” consumers in the overdraft service; and
- Misrepresenting that the overdraft services would apply to all transactions when the solicited services only applied to ATM and one-time debit transactions.

Pursuant to the consent order, the company agreed to pay a \$10 million civil money penalty to resolve the above allegations of deceptive conduct, along with alleged violations of Regulation E.

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<sup>4</sup> *In the Matter of: Santander Bank, N.A.*, File No. 2016-CFPB-0012, Consent Order (July 14, 2016).

b. First National Bank of Omaha – August 2016 (Marketing and Servicing)<sup>5</sup>

First National Bank of Omaha entered into a consent order with the CFPB to resolve allegations of unfair and deceptive practices in connection with the marketing, sales, and administration of credit card add-on products, namely debt cancellation and credit monitoring products.

Specifically, the CFPB alleged that the company engaged in the following deceptive enrollment practices:

- Implying that cardholders calling to activate a credit card were required to listen to a sales pitch;
- Misrepresenting the nature of a telemarketing call by stating that the call was about an important feature of the consumer’s account and that the product was being offered “as our way of saying thanks”;
- Enrolling consumers in debt cancellation products without conveying the existence of a purchase by:
  - Representing that a welcome kit would be sent for the consumer to review the product; and
  - Construing consumers’ verification of their city of birth as approval to enroll;
- Misrepresenting the debt cancellation products terms, exclusions, and benefits by:
  - Not disclosing eligibility limitations to consumers that disclosed their ineligibility for certain product benefits;
  - Claiming that consumers were “eligible” for the product without information to make such an assessment; and
  - Not properly stating (or perhaps omitting) limitations on product benefits; and
- Misrepresenting that consumers could cancel a debt protection product “anytime”, “immediately”, and with “no questions asked” when call center representatives were paid a bounty to prevent consumers from cancelling, often rebutted cancellation requests several times before agreeing to cancel, and permitted cancellations only if consumers demanded it “multiple times in succession.”

The CFPB also alleged that the company engaged in the following unfair practices:

- Preventing debt cancellation product holders from obtaining promised benefits by:
  - Imposing exclusions to deny benefits, such as a “pre-existing condition” exclusion that refused coverage for conditions occurring before or up to six months after the product was purchased;
  - Imposing onerous administrative requirements, such as a 15-day window to apply for unemployment benefits, between the 30<sup>th</sup> and 45<sup>th</sup> day of unemployment, and monthly “continuation forms” proving continued illness, disability, or unemployment; and
  - Failing to disclose these exclusions and requirements prior to enrollment, and approving only 9% of all claims for benefits; and
- Billing the full fee for credit monitoring products when the credit monitoring services were not actually provided.

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<sup>5</sup> *In the Matter of: First National Bank of Omaha*, File No. 2016-CFPB-0014, Consent Order (August 25, 2016).

Pursuant to the consent order, the company agreed to provide \$27.75 million in consumer redress and pay a \$4.5 million civil money penalty to the CFPB to resolve the above allegations of unfair and deceptive conduct. In a parallel enforcement action focused on the company's allegedly unfair credit monitoring billing practices, the Office of the Comptroller of the Currency imposed a \$3 million civil money penalty.<sup>6</sup>

c. Wells Fargo Bank, N.A. – September 2016 (Servicing)<sup>7</sup>

Wells Fargo Bank, N.A., entered into a consent order with the CFPB involving allegedly unfair and abusive conduct in connection with a series of unauthorized activities, including the opening of deposit and credit card accounts, transferring funds, ordering and activation of debit cards, and enrolling consumers in online account access.

The CFPB alleged that the company engaged in unfair conduct by opening unauthorized credit card accounts and deposit accounts (with simulated funding by transferring funds from other accounts) without consumers' knowledge. The CFPB also alleged that this conduct was abusive since it interfered with consumers' ability to understand the terms and conditions of the accounts that were opened, and it took unreasonable advantage of consumers' inability to protect their interests in selecting consumer financial products or services.

The CFPB also alleged that the following conduct was abusive (without including an unfairness claim):

- Enrolling consumers in online banking without their knowledge, because the company took unreasonable advantage of consumers' interests in having these services activated: 1) after affirmative agreement; and 2) after having the opportunity to protect themselves from security and other risks; and
- Issuing debit cards without consumers' consent, because the company took unreasonable advantage of consumers' inability to protect their interests in selecting or using a consumer financial product or service.

The company agreed to provide \$5 million in consumer redress and pay a \$100 million civil money penalty to the CFPB. In related settlements, the company agreed to pay a \$35 million penalty to the Office of the Comptroller of the Currency<sup>8</sup> in connection with alleged safety and soundness deficiencies (not unfairness claims) and a \$50 million penalty to the City and County of Los Angeles<sup>9</sup> in connection with allegedly unlawful, unfair, and fraudulent sales and related business acts and practices in violation of California's Unfair Competition Law.

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<sup>6</sup> *In the Matter of: First National Bank of Omaha*, File No. AA-EC-2015.71 (August 25, 2016).

<sup>7</sup> *In the Matter of: Wells Fargo Bank, N.A.*, File No. 2016-CFPB-0015, Consent Order (September 8, 2016).

<sup>8</sup> *In the Matter of: Wells Fargo Bank, N.A.*, File No. AA-EC-2016-67, Consent Order (September 8, 2016).

<sup>9</sup> *The People of the State of California v. Wells Fargo & Company, et al.*, Stipulated Final Judgment, Case No. BC580778 (C.D. Cal. September 13, 2016).

d. Wells Fargo Bank, N.A. – August 2016 (Servicing)<sup>10</sup>

Wells Fargo Bank, N.A., is the second-largest private student lender in the United States, originating and servicing private student loans through its division, Educational Financial Services. The company entered into a consent order with the CFPB in connection with allegations that the bank engaged in illegal private student loan servicing practices that increased costs and unfairly penalized certain student loan borrowers.

Specifically, the CFPB alleged that the following practice was deceptive:

- Misrepresenting to borrowers that paying less than the full amount due in a billing cycle would not satisfy any obligation on an account when, in reality, if a consumer made a partial payment on an account with multiple loans that was sufficient to cover at least one of the payments due in full for a loan in the account, then such partial payment would advance the next payment due for that loan.

The CFPB also alleged that the following practices were unfair:

- Failing to disclose its payment allocation methodology to consumers and failing to disclose to consumers the ability to provide payment instructions on how to allocate payments, while allocating payments in a manner that maximized late fees;
- Failing to aggregate multiple partial payments submitted within the same billing cycle that would have satisfied the total amount due if aggregated;
- Charging late fees to consumers who paid on the last day of their grace period, and charging late fees to consumers who paid multiple partial payments instead of one single payment; and
- Failing to update and correct inaccurate information reported to credit reporting companies.

Pursuant to the consent order, the company agreed to pay \$410,000 in redress to consumers and a civil money penalty of \$3.6 million.

e. Prime Marketing Holdings, LLC (d/b/a Park View Credit, National Credit Advisors, and Credit Experts) – September 2016 (Debt Sales/Debt Collection)<sup>11</sup>

The CFPB filed a lawsuit in federal district court against Prime Marketing Holdings, LLC, a credit repair company that has operated under various names, including Park View Credit, National Credit Advisors, and Credit Experts (together “the company”). Since 2014, the company has marketed, offered, and provided credit repair services to consumers across the country. In addition to alleged violations of the federal Telemarketing Sales Rule, the CFPB’s complaint alleges that the company engaged in deceptive acts and practices.

Specifically, the CFPB alleged that the following practices were deceptive:

<sup>10</sup> *In the Matter of: Wells Fargo Bank, N.A.*, File No. 2016-CFPB-0013, Consent Order (August 22, 2016).

<sup>11</sup> *Consumer Financial Protection Bureau v. Prime Marketing Holdings, LLC (d/b/a Park View Credit, National Credit Advisors, and Credit Experts)*, Case No. 16-cv-7111 (C.D. Cal. September 22, 2016).

- Misleading consumers about the costs of its services. The company charged consumers an automatic monthly fee but often failed to disclose such fee or stated that such fees were incurred only if consumers elected to continue services beyond the initial 60 days.
- Failing to disclose limits on the company’s “money-back guarantee.” The company represented that it offered a “money-back guarantee” but failed to disclose certain restrictions. For example, consumers had to pay for at least six months of services to be eligible for the “money-back guarantee.”
- Misleading consumers about the benefits of its services. The company misrepresented that its credit repair services would, or likely would, result in the removal of negative entries on consumers’ credit reports, and would, or likely would, result in a substantial increase to consumers’ credit scores.

This case was not resolved at the time of publication.

f. Flurish, Inc., d/b/a LendUp – September 2016 (Marketing and Servicing)<sup>12</sup>

LendUp is an online lending company that offers single-payment loans and installments loans. The company markets its loans as a way for consumers to build credit and improve their credit score, and as consumers make progress, they are able to obtain more favorable loan terms. The CFPB alleged that the company engaged in deceptive and unfair practices.

Specifically, the CFPB alleged that the following practices were deceptive:

- Advertising that consumers could graduate to lower-priced loans when, in reality, such loans were not available outside of California for most of the company’s existence;
- Failing to disclose the annual percentage rate of its various loans in ads, as required by the Truth in Lending Act and Regulation Z;
- Understating the annual percentage rate. First, the company retained a portion of the expedited processing fee charged for processing certain loans more quickly. These fees should have been included in the annual percentage rate calculation, and, because they were not, the disclosed finance charges were inaccurate. Second, on certain loans issued in California, APRs were inaccurate and understated; and
- Failing to report loan information to credit reporting companies and failing to have any written policies and procedures about the accuracy and integrity of information actually furnished to consumer reporting agencies.

The CFPB also alleged that the following practice was deceptive and unfair:

- Reversing origination fee discounts when consumers extended repayment dates. These discounts were given when borrowers selected an earlier repayment date, but the discount would be reversed if the consumer subsequently extended the repayment date. The CFPB alleged that such discount reversals were not properly disclosed in applicable loan agreements.

Pursuant to the consent order, the company agreed to provide approximately \$1.83 million in consumer redress and pay a \$1.8 million civil money penalty.

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<sup>12</sup> *In the Matter of: Flurish, Inc., d.b.a. LendUp*, File No. 2016-CFPB-0023, Consent Order (September 27, 2016).

g. Bridgepoint Education, Inc. – September 2016 (Marketing)<sup>13</sup>

Bridgepoint Education, Inc. offered students at its for-profit colleges private student loans to pay for tuition. The CFPB alleged in a consent order that the company engaged in deceptive practices when, in connection with the marketing of its private student loans, its representatives made oral statements that students could repay those loans with monthly payments as low as \$25 when “in many instances” a typical monthly payment was more.

Pursuant to the consent order, the company agreed to provide \$23.5 million in consumer redress through loan forgiveness and refunds and pay an \$8 million civil money penalty.

h. TMX Finance LLC – September 2016 (Marketing and Debt Collection)<sup>14</sup>

TMX Finance LLC offers short-term automobile title loans through a subsidiary in various states, some of which allow for multiple loan renewals or extensions. The company used a “Payback Guide” in its sales pitches that contemplated multiple title loan renewals or extensions but only showed the finance charge and principal paid in each individual 30-day period, without disclosing the total cost of the transaction.

The CFPB alleged in a consent order that the company’s “Payback Guide” and sales pitch resulted in an abusive practice because it materially interfered with consumers’ ability to understand the terms and cost of credit, including:

- That the title loan was a 30-day transaction;
- That the “Payback Guide” was not an actual repayment plan;
- That renewals or extensions would affect the total cost of the transaction;
- That renewals or extensions caused the loan to be more expensive; and
- Whether the consumer should pay off the loan over a longer period.

The CFPB also alleged that the company engaged in unfair debt collection practices when it authorized in-person visits to a consumer’s home or place of employment and visits to a consumer’s references, exposing the existence of a debt to third parties and causing or likely causing substantial injury in the process.

Pursuant to a consent order, the company agreed to pay a \$9 million civil money penalty.

i. Navy Federal Credit Union – October 2016 (Debt Collection)<sup>15</sup>

Navy Federal Credit Union is a federal credit union that offers a wide range of consumer financial products and services, including deposit accounts and loans. The CFPB alleged that the company engaged in deceptive and unfair debt collection practices.

Specifically, the CFPB alleged that the following practices were deceptive:

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<sup>13</sup> *In the Matter of: Bridgepoint Education, Inc.*, File No. 2016-CFPB-0016, Consent Order (September 16, 2016).

<sup>14</sup> *In the Matter of: TMX Finance LLC*, File No. 2016-CFPB-0022, Consent Order (September 26, 2016).

<sup>15</sup> *In the Matter of: Navy Federal Credit Union*, File No. 2016-CFPB-0024, Consent Order (October 11, 2016).

- Falsely threatening to take legal action and garnish wages unless consumers made a payment when the company rarely took legal action and had no intention or authority to garnish wages;
- Falsely threatening to contact commanding officers to pressure servicemembers to repay when the company had no intention of ever actually doing so and was not authorized to do so even if it did have such an intention; and
- Misrepresenting to consumers the credit consequences of falling behind on a loan by telling consumers that obtaining additional credit would be “difficult, if not impossible” and implying that Navy Federal Credit Union could raise or lower a consumer’s credit rating.

The CFPB also alleged that the following practice was unfair:

- Illegally freezing members’ access to their deposit accounts when they became delinquent on a Navy Federal Credit Union credit product. By freezing members’ access to their deposit accounts, the company was, in turn, shutting down consumers’ debit cards, ATMs, and online banking access.

Pursuant to the consent order, the company agreed to provide \$23 million in consumer redress and pay a \$5.5 million civil money penalty.

- j. Douglas MacKinnon, Mark Gray, Northern Resolution Group, LLC, Enhanced Acquisitions, LLC, and Delray Capital, LLC – November 2016 (Debt Collection)<sup>16</sup>

Douglas MacKinnon and Mark Gray operate a network of debt collection companies, including Northern Resolution Group, Enhanced Acquisitions, and Delray Capital (together “the company”). In a joint complaint, the CFPB and New York Attorney General alleged that the company engaged in unfair and deceptive debt collection practices.

Specifically, the CFPB and New York Attorney General alleged that the company engaged in both unfair and deceptive practices by adding a \$200 fee to each consumer debt acquired when state law prohibited the fee and implying in collection efforts that consumers were obligated to repay the fee.

The CFPB and New York Attorney General also alleged that the company engaged in deceptive practices by:

- Threatening consumers with arrest, imprisonment, or other legal action when the companies had no intention of ever taking such action; and
- Impersonating law-enforcement officials, court officials, and other entities.

This case was not resolved at the time of publication.

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<sup>16</sup> *Consumer Financial Protection Bureau & the People of the State of New York, by Eric T. Schneiderman, Attorney General for the State of New York v. Douglas MacKinnon, Mark Gray, Northern Resolution Group, LLC, Enhanced Acquisitions, LLC, and Delray Capital, LLC*, Case No. 1:16-cv-00880 (W.D. NY) (November 2, 2016).

k. Moneytree, Inc. – December 2016 (Marketing and Debt Collection)<sup>17</sup>

Moneytree, Inc. offers payday loans and check-cashing services. The CFPB alleged that the company engaged in the following deceptive practices:

- Running an online advertising campaign that advertised tax-refund check-cashing services for “1.99”, either expressly or impliedly represented that the fee for these services was “1.99 dollars” when in fact the fee was “1.99 percent” of the tax refund.
- Threatening repossession of consumers’ vehicles if consumers did not make past due payments on their installment loans, even though the loans were unsecured.

The CFPB also alleged that the company violated the Electronic Fund Transfer Act when it failed to obtain written authorization for preauthorized electronic-fund transfers. Pursuant to the consent order, the company agreed to provide \$255,000 in consumer redress and pay a \$250,000 civil money penalty.

**IV. CFPB Guidance**

a. Detecting and Preventing Consumer Harm from Production Incentives – November 2016 (Marketing)<sup>18</sup>

Programs to incentivize the sale of consumer financial products and services by employees and service providers were identified as a potential source of UDAAP violations. Specific practices that were considered to encourage deceptive conduct include:

- Sales benchmarks that encourage the marketing of products to consumers that may not benefit from or be eligible for the product; and
- Unrealistic sales quotas.

**V. CFPB Supervisory Highlights**

The CFPB periodically issues Supervisory Highlights reports that summarize its supervisory activity over a period of time and identify, among other things, allegedly unfair, deceptive or abusive conduct that may not have otherwise been publicly disclosed in enforcement actions.

a. Fall 2016 Supervisory Highlights (published in October 2016)<sup>19</sup>

The CFPB’s Fall 2016 Supervisory Highlights report identified UDAAPs in connection with automobile loan servicing, debt collection, and student loan servicing.

With respect to automobile loan servicing, the following practices were considered unfair:

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<sup>17</sup> *In the Matter of: Moneytree, Inc.*, File No. 2016-CFPB-0028, Consent Order (December 16, 2016).

<sup>18</sup> CFPB Compliance Bulletin 2016-03, Detecting and Preventing Consumer Harm from Production Incentives (November 28, 2016).

<sup>19</sup> CFPB Supervisory Highlights, Issue 13 (October 2016), available at [https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/Supervisory\\_Highlights\\_Issue\\_13\\_Final\\_10.31.16.pdf](https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/Supervisory_Highlights_Issue_13_Final_10.31.16.pdf).

- Detaining or refusing to return personal property found in a repossessed vehicle until a consumer paid a fee, even if the fee was permitted by contract; and
- Charging an undisclosed fee to store personal property found in a repossessed vehicle.

With respect to debt collection, the following practices were considered deceptive:

- Impersonating consumers when calling a creditor’s consumer-facing automated telephone system to obtain information about a debt; and
- Falsely claiming that the ability to settle a debt would be revoked or would expire.

With respect to student loan servicing:

- The following practices were considered unfair:
  - Improperly denying or not approving requests for income-driven repayment plans;
  - Not allowing consumers to allocate their payments among multiple outstanding student loans, where the inability to allocate payments could cause a financial detriment to consumers; and
  - Due to a systems error, causing the last payment to be smaller than the payment identified in the borrower’s repayment plan.
- The following practices were considered deceptive:
  - Where consumers had paid ahead, providing billing statements that misled consumers to believe that additional payments before or after the paid-ahead period would be applied to principal; regarding how much interest would accrue or had accrued; and as to how payments would be applied after the paid-ahead period.

## ***VI. Updates on Past Cases***

### **a. Pension Funding, LLC – July 2016 (Marketing)<sup>20</sup>**

In August 2015, the CFPB and the New York Department of Financial Services (NYDFS) jointly filed a civil complaint against Pension Funding, LLC, along with a related company and related individuals, in connection with the offering of lump sum “pension advances”. The company claimed in its marketing materials that the products were not loans but were purchases of the right to future pension payments. The CFPB and NYDFS alleged that the pension advances were actually loans, that the company’s marketing claims were deceptive, that the company engaged in abusive practices, and that the loan’s undisclosed effective interest rate exceeded New York’s usury cap.

In February 2016, all but one defendant entered a stipulated judgment to resolve these allegations. In July 2016, a default judgment was entered against the one remaining defendant in which the court agreed with the CFPB’s and NYDFS’s allegations that the pension advances were loans. The court found that the company’s marketing claims indicating that the advances

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<sup>20</sup> *Consumer Financial Protection Bureau et al. v. Pension Funding, LLC et al.*, Case No. CV-01329-JLS-JCG (C.D. Cal. July 11, 2016)

did not have an interest rate and that the interest rate was lower than the effective interest rate of the advances were unfair, deceptive, and abusive practices. The defendant was ordered to disgorge \$578,182 in profits.

b. CashCall, Inc. – August 2016 (Loan Servicing)<sup>21</sup>

We previously reported that the CFPB had filed a civil complaint in December 2013 against CashCall, Inc., alleging that the company purchased, serviced, and collected consumer installment loans that state usury and/or licensing laws rendered void or limited the consumer's obligation to repay. The CFPB's UDAAP allegations were based on the company's actions in servicing and collecting debts that were void under state law.

The company filed a motion for judgment on the pleadings in November 2015, arguing that the CFPB's UDAAP allegations should be dismissed because they were predicated solely upon violations of state law and that the agency was attempting to establish a usury limit, which is prohibited by statute. The court denied the company's motion, finding that the company's alleged conduct in collecting payments on debt that consumers did not actually owe fell within the broad range of conduct covered by the federal UDAAP prohibition and that prohibiting such conduct did not amount to the establishment of a usury limit.

On June 30, 2016, the CFPB filed a motion for partial summary judgment, which the court granted. The court found that: (1) the laws of the borrowers' home states apply to the loan agreements and, as a result, (2) CashCall violated the Consumer Financial Protection Act when it engaged in the deceptive practice of creating the impression that the loans were enforceable and that borrowers were obligated to repay when the loan agreements were void under state law and/or the borrowers were not obligated to pay.

According to a Joint Status Report filed on November 14, 2016, CashCall intends to file a motion for stay and request to certify interlocutory appeal. If CashCall's motion for stay and request for certification are denied, a trial will be set for damages.

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<sup>21</sup> *Consumer Financial Protection Bureau v. CashCall, Inc., et al.*, Case No. CV 15-7522-JFW (RAOx) (C.D. Cal. August 31, 2016).

## About the Authors

### Adam Maarec

Davis Wright Tremaine LLP  
Washington, District of Columbia  
[adammaarec@dwt.com](mailto:adammaarec@dwt.com) | 202-973-4217



### John Morton

Gordon Feinblatt LLC  
Baltimore, Maryland  
[jmorton@gflaw.com](mailto:jmorton@gflaw.com) | 410-576-4176



Adam Maarec is a member of Davis Wright Tremaine LLP's Payments Team, located in Washington, D.C. He concentrates his practice on consumer financial services, primarily advising financial institutions on regulatory compliance matters involving payment and credit product structures, marketing, and servicing. Adam has experience with a broad range of financial services laws including Dodd- Frank, the Truth in Lending Act, the CARD Act, the Gramm-Leach-Bliley Act, the Fair Credit Reporting Act, and the Real Estate Settlement Procedures Act, as well as state-based insurance regulations. His regulatory practice involves helping companies comply with various laws and regulations, drafting rulemaking comment letters, meeting with government agencies, and responding to regulatory investigations.

John Morton is a Member of Gordon Feinblatt's Financial Services Practice Group. He provides legal advice to an extensive range of financial institutions including nationwide, regional and community banks; credit unions; consumer lending companies; sales finance companies; mortgage lenders and brokers; investment advisers; and other regulated businesses.

John provides counsel regarding multi-jurisdictional compliance issues, including advising clients on federal and state credit statutes and regulations; UDAAP and the CFPB; interaction with state and federal regulators; licensing and registration matters; due diligence and transactional matters; and general corporate governance issues.

## Panel on the Future of the CFPB

By Andrew Smith, Covington & Burling LLP

At the CFSC Winter Meeting in Carlsbad, California, in early January, an all-star group of panelists—including a former Chief of Staff for the House Financial Services Committee, a former Associate GC at the Federal Reserve Board, and the former Assistant to the Solicitor General handling PHH’s appeal—discussed the possible fate of CFPB Director Richard Cordray, the fate of the CFPB itself, and the fate of the CFPB’s rulemaking agenda.

Since the panel was held in the second week of January, momentous events have occurred, including the inauguration of President Trump and a series of Executive Orders limiting the issuance of new rules, but, confounding the predictions of many pundits, there continues to be very little resolution as to the future of the CFPB.

### The Fate of Director Cordray

With respect to the fate of Director Cordray, the panelists noted that, although then-President-Elect Trump had reportedly interviewed successors for Mr. Cordray, the President-Elect had not expressed any specific intentions with respect to removing Mr. Cordray from his position. Despite continued speculation that Director Cordray’s days are numbered, as of this writing, there is still no public statement from the White House expressing support for his removal.

Currently, the Dodd Frank Act only permits the President to remove the Director of the CFPB for “malfeasance, neglect of duty and inefficiency”—*i.e.*, for cause. The October 2016 decision of a three-judge panel of the US Court of Appeals for the DC Circuit in *PHH v. CFPB*, however, complicated this calculus holding that the removal only for cause provisions of Dodd Frank are unconstitutional, and that the CFPB Director can be removed at any time by the President with or without cause. The CFPB has petitioned the DC Circuit for rehearing *en banc*, but the court has yet to rule. The panelists agreed that, if the DC Circuit grants rehearing, it could take many months for the issue to be resolved—particularly if the court orders additional briefing and oral argument. If rehearing is not granted, the CFPB might petition the Supreme Court for *certiorari*, but, as pointed out by the panelists, the Dodd Frank Act requires the CFPB to provide notice and a refusal right to the Attorney General before it can appear on its own behalf in front of the Supreme Court.

In the meantime, the panelists thought that now-President Trump could act without waiting for a final ruling from the DC Circuit. For example, President Trump might dismiss Director Cordray for some sort of malfeasance, neglect of duty or inefficiency while in office—at the time of the panel, there had been several editorials and other articles published laying out the basis for a “for cause” removal, and since the panel several more such articles have been published (as well as several articles arguing to the contrary). Although there is little case law and even less consensus as to what would constitute “malfeasance, neglect of duty or inefficiency,” the panelists seemed to agree that it should be more than a policy dispute or difference of opinion.

In addition, the panelists thought that the President could remove Director Cordray without cause, simply on the basis that the agency's structure was unconstitutional and represented an incursion on the President's privilege.

Regardless of the basis for removal, the panelists believed that the President had room to act, and the most likely outcome—should the President decide to remove Director Cordray—would be a letter to the Director removing him both for cause and without cause. The question was then raised about the ability of the Director to challenge his removal. For example, could the Director request a stay of his removal and remain in office while he challenged the President's authority to remove him? Or, would the Director be required to comply with the President's directive and vacate his office, and subsequently sue for reinstatement? The panelists noted that in past similar situations – such as the *Humphrey's Executor* case in the Franklin Roosevelt Administration—the proper remedy was to sue in the Federal Court of Claims for reinstatement. The panelists noted that in prior similar cases courts have not awarded reinstatement, only back pay. In any event, because Director Cordray's term only extends through July 2018, the issue of whether the Director can remain in office while challenging the President's decision to remove him ultimately seems more important in determining Director Cordray's fate than the outcome of the *PHH* case.

### **The Fate of the CFPB**

Regardless of what happens to Mr. Cordray, the Republican majority in Congress has made no secret of its interest in reforming the CFPB. The Financial CHOICE Act, introduced by House Financial Services Committee Chairman Jeb Hensarling in the last Congress, would have created a new Consumer Financial Opportunity Commission, headed by a five-member board (similar to the SEC and FTC) rather than a single individual. The panelists generally agreed that a commission structure would make more sense than a single Director who will constantly be subject to political pressures.

Regardless of the wisdom of a commission structure, since the panel was held in early January, the House Financial Services Committee staff has floated an outline for so-called "CHOICE 2.0," which would leave the CFPB as a single-member agency, but would strip it of its authority to supervise financial institutions and to prohibit unfair, deceptive and abusive practices.

The panelists observed that, to the extent that the Republican Administration sees any need for a change in course at the CFPB, it might be easier to accomplish that correction with a single-Director structure, rather than a bipartisan agency, so perhaps we should not be surprised by the new approach taken in CHOICE 2.0.

### **The Fate of the CFPB's Agenda**

The CFPB has had an active rulemaking agenda recently: the final Prepaid Rule, the proposed Arbitration Rule, the proposed Small Dollar Rule, and promised rules on small business fair lending, debt collection, and installment lending. The Arbitration Rule in particular has been controversial, and the panelists were asked what could be done by the new Administration to undo the Arbitration Rule if issued in final form by the CFPB.

The panelists noted that the Congressional Review Act is a powerful tool to invalidate rules made by agencies against the will of Congress. The Congressional Review Act requires agencies to submit all rules to Congress for review, and Congress has 60 "days of continuous session" to issue a "Resolution of Disapproval." Although Congress can always pass a law to invalidate any specific rule, the Congressional Review Act is particularly appealing, because the Resolution of Disapproval cannot be filibustered in the Senate—that is, it cannot be debated and must be brought to an up-or-down vote by a simple majority of Senators. The panelists noted, however, that the Congressional Review Act is a blunt

instrument—it cannot be used to excise particular parts of rules, but only to invalidate an entire rule. And, once invalidated, the agency cannot make another rule on that same topic without specific permission of Congress (which, as ordinary-course legislation, would be subject to potential filibuster). For that reason, the panelists speculated that the Congressional Review Act may not be an attractive option for all rules.

Since the panel was held, Congress has used the Congressional Review Act to invalidate an SEC rule requiring oil companies to report foreign payments. This is only the second time that the Act has been used to invalidate an agency rule. (The first time was the 2001 transition between the Clinton Administration and the Bush Administration and involved OSHA ergonomics regulations.)

In addition, shortly after taking office, President Trump imposed a moratorium on all new rules until Trump-appointed agency heads were installed, and also issued an Executive Order directing agencies to repeal two rules for each new rule that is proposed. There has been some debate about whether these Executive Orders would apply to the CFPB, which is typically considered to be an independent agency (at least pending the outcome of the *PHH* decision), but the fact remains that no new CFPB rules, including the Arbitration Rule, have been made since the issuance of the Executive Orders.

And, so it goes. Since the panelists spoke, Director Cordray remains in office, the DC Circuit has yet to decide whether to grant the CFPB's petition for rehearing, and the Congressional Review Act has not been used to invalidate any CFPB rules, but the threat, or promise (depending on one's perspective), of major change remains on the horizon.