

2023 TCFA Membership Meeting

Legal Update

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Today's Topics

- FTC Safeguards Reminder
- CFPB Update
 - CFPB Constitutionality Lawsuit
 - Nonbank registration and registry of contract terms
 - Abusive acts and practices statement
- Litigation Trends
 - FCRA direct dispute investigations
- Texas Legislation of Interest

FTC Safeguards Reminder

- Amendments effective June 9, 2023
 - You must be in compliance now
 - Expect OCC to inquire during audits and exams
 - TCFA circulated a template for members
- General requirements
 - Ensure security and confidentiality of customer info
 - Protect against threats or hazards to security of customer info
 - Protect against unauthorized access to or use of customer info

FTC Safeguards Reminder

- Information security program
 - Designate a qualified individual to implement and supervise
 - Conduct a risk assessment
 - Design and implement safeguards to control the risks identified
 - Periodically review access controls
 - Know what you have and where you have it
 - Encrypt customer info on your systems and in transit
 - Assess your applications
 - Multi-factor authentication for anyone accessing customer info
 - Dispose of customer info securely
 - Evaluate changes to your information systems and network
 - Maintain a log of authorized users' activity
 - Regularly monitor and test safeguards, and keep the program current
 - Train your staff
 - Monitor service providers
 - Create written incident response plan

CFPB Constitutionality Lawsuit

- *Cmt. Fin. Servs. Ass'n of Am. vs. CFPB*, 5th Circuit Court of Appeals, Oct. 19, 2022
 - Held that CFPB's funding mechanism was unconstitutional
 - Not funded through Congressional appropriations
 - Federal Reserve approves yearly funding requests from CFPB director, as long as 12% or less of Federal Reserve budget
 - Court stated CFPB is "double-insulated" from Congressional appropriations and oversight
 - This violates separation of powers
 - Vacated the Payday Lending Rule

CFPB Constitutionality Lawsuit

- Since the 5th Circuit decision
 - Numerous entities have challenged CFPB enforcement authority in other lawsuits
 - CFPB has not slowed its aggressive enforcement and rulemaking activity
 - 2nd Cir. Court of Appeals issued a conflicting ruling, finding the funding structure does not violate the US Constitution
 - US Supreme Court has agreed to hear the 5th Circuit case, and parties have filed briefs (decision likely in early 2024)

CFPB Nonbank Registry

- Proposed rule issued Feb. 1, 2023 (12 CFR pt 1092)
 - <https://www.govinfo.gov/content/pkg/FR-2023-02-01/pdf/2023-00704.pdf>
- Summary: will require supervised nonbank entities to register and provide data concerning contract terms
 - Registration would be completed electronically
 - Registrants would have to annually submit reports on their use of form contracts containing certain “covered terms or conditions”

CFPB Nonbank Registry

- Who is covered? Nonbank covered persons subject to supervision and examination
 - Residential mortgage lenders or services
 - Student loan lenders
 - Payday lenders
 - Should not cover traditional installment lenders, but remains unclear given Payday Rule coverage
 - Larger participants subject to supervision
 - So far, only applied to consumer reporting, debt collection, student loan servicing, and international money transfers, but could try to apply this to installment lenders in future.
 - Risky nonbanks – a nonbank the CFPB has reasonable cause to believe is engaging in conduct that poses risks to consumers regarding consumer financial product or service
 - Has been dormant, but CFPB announced in 2022 its intent to use this

CFPB Nonbank Registry

- Exceptions – does not apply to:
 - Nonbanks that have less than \$1 million in annual receipts from offering or providing consumer financial product or service
 - De minimis use of form contracts containing the covered terms (defined as entering into form contracts less than 1,000 times during previous year)
- Bottom line:
 - Does not appear to directly apply to traditional installment lenders, but could apply if deemed risky or considered payday or become larger participant.
 - Notably, the rule explanation contains multiple references to installment loans and short-term small-dollar lending

CFPB Nonbank Registry

- Covered terms or conditions that must be reported:
 - Restrict consumer from bringing legal action
 - Specify a forum or venue for legal action
 - Limit ability to file legal action seeking relief for others or participate in legal action filed by others (i.e., class action)
 - Limit liability to consumers (i.e., damage caps or remedy limitations)
 - Waive a consumer's cause of action
 - Limit consumer's ability to review, assess, or complain about your product or service
 - Waive a legal protection afforded by law
 - Require arbitration (end run around the rejected arbitration rule)

CFPB Nonbank Registry

- **Additional items to be reported**
 - What products or services the form contract covers, jurisdictions where used, and details on type and scope of limitations
 - Whether registrant has received a decision regarding the enforceability of any covered term or condition by a court or arbitrator and the details related to the decision
- **Publication**
 - CFPB plans to publish the information in a publicly available database on a periodic basis
 - Actual content unclear

CFPB's Abusive Acts Policy

- April 3, 2023 - CFPB issued policy statement on abusive acts or practices
 - Available here:
<https://www.consumerfinance.gov/compliance/supervisory-guidance/statement-of-policy-regarding-prohibition-on-abusive-acts-or-practices/>
 - Explains how CFPB analyzes the elements of abusiveness
 - Framework for fellow government enforces to follow
 - Intent to broadly enforce

CFPB's Abusive Acts Policy

- Abusive act or practice defined in federal statute:
 - Materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
 - Takes unreasonable advantage of:
 - A lack of understanding on part of consumer of the material risks, costs or conditions of a product or service;
 - The inability of consumer to protect the interest of the consumer in selecting or using a product or service; or
 - The reasonable reliance by the consumer on a covered person to act in the interests of the consumer.

CFPB's Abusive Acts Policy

- Abusiveness requires no showing of substantial injury to establish liability (conduct is presumed to be harmful)
- Material interference does not require “intent”
 - Some things are so important that failing to convey them prominently or clearly may raise a presumption that the act or omission materially interfered with the consumer's ability to understand
 - Complex products may interfere with an ability to understand if cannot be sufficiently explained

CFPB's Abusive Acts Policy

- “Materially interfering”
 - Acts or omissions to obscure, withhold, deemphasize, or hide relevant information (buried disclosures, complex language, jargon)
 - Digital or physical interference that impedes a person’s ability to see, hear, or understand (withholding or hiding notices, pop-up or drop-down boxes, multiple click-throughs, or dark patterns that make terms less accessible)
 - Overshadowing – prominent placement of certain content that interferes with comprehension of other content

CFPB's Abusive Acts Policy

- “Taking unreasonable advantage” – it is abusive for a lender to take advantage of:
 - Gaps in a consumer’s understanding
 - When consumer does not understand material information, such as likelihood of default; loss of future benefits; monetary costs and non-monetary costs, such as loss of time, loss of use, or reputation harm
 - Unequal bargaining power
 - When consumer lacks practical ability to switch providers, seek more favorable terms, or make decisions to protect interests, such as
 - Onerous steps to protect their interests; lack of monetary means to protect their interests; or no meaningful choice among providers
 - Form contracts, where contractual provisions are not subject to a consumer choice or where person cannot bargain over a clause to protect their interests
 - Outsized market power by certain companies
 - High transaction costs (time, money, or effort) to exit the relationship, which locks them in
 - Consumer reliance on you
 - When you communicate that you will act in consumer’s best interest
 - When you assume the role of acting on behalf of consumers or helping them to select providers in the market, like in a broker scenario (risk of steerage or self-dealing)

Litigation Trends

- Report of Litigation in 2022
 - In general, consumer protection cases have declined for 10 years
 - Class action consumer protection cases have also declined from high in 2017
 - Telephone Consumer Protection Act and debt collection cases have declined
 - However, certain cases are on the rise:
 - Fair Credit Reporting Act – consumer reporting (143% increase since 2013)
 - Impermissible use of credit reports
 - Failure to investigate disputes by consumers (CAUTION!)
 - Plaintiffs bar is casting a wider net on defendants
 - Data Breach cases have also risen markedly

Litigation Trends

- Example of FCRA Violations and Enforcement
 - CFPB Enforcement Action - Phoenix Financial (6/8/23)
 - Debt collector – sent collection letters to consumers who disputed validity or accuracy of debt
 - Violated FCRA and its implementing Regulation V by:
 - not conducting reasonable investigations of consumer disputes;
 - not having reasonable written policies and procedures regarding the accuracy and integrity of the information it furnished to consumer reporting companies.
 - Penalties
 - Pay \$1.675 million fine to CFPB
 - Refund any amounts that affected consumers paid
 - Subject to CFPB supervisory review

Texas Legislation

- A few bills of interest
 - HB 4 – Texas Data Privacy and Security Act
 - Comprehensive data privacy and security law
 - Exception for financial institutions and data subject to federal GLBA and its privacy and security requirements, which includes consumer lenders and data you maintain.
 - HB 2127 – City/County Preemption Bill (eff. Sept. 1, 2023)
 - Prohibits city/county regulations in field of regulation occupied by numerous other state codes, including the Finance Code
 - Exception for regulation of CSOs under Chapter 393, Finance Code
 - Could affect ordinances that regulate Chapter 342 F lenders
 - City of Houston filed suit arguing bill is unconstitutional on various grounds, including that bill violates home rule powers of cities
 - HB 4219 - Prime Rate Adder to E Loans
 - Vetoed by Governor
 - SB 1371 - OCC's Clean Up Bill
 - No substantive changes; cleans up archaic or outdated references or processes