

# 2022 TCFA Membership Meeting

## Legal Update

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# Today's Topics

- CFPB Update
  - Increased enforcement
  - Encouragement of state enforcement
  - Dormant nonbank oversight
  - Adverse action notices revisited
  - Consumer 'gag' clauses and customer reviews
- New Mexico Small Loan Law
  - HB 132: 36% rate cap
  - Application to loans made to NM residents in Texas

# Increased Enforcement by CFPB

- Escalating enforcement statements
  - Focus on repeat corporate offenders and large market participants
  - Hired 20 more full-time positions
  - Recently identified payday loans, extended payment plan options, and rent-a-bank schemes
- Renewed interest in enforcement of:
  - Prohibited communications with consumers
  - Harassment and threats when collecting a debt
    - False representations about impact of paying debt
  - Improper charges and fees when assessed to consumers
    - Any charge/fee assessed to a consumer not stemming directly from the underlying contract may draw attention

# CFPB Encouraging State Enforcement

- CFPB reiterated States' rights to bring enforcement actions, and encouraged them to do so
  - States can (and have been able to) bring civil actions for violations of
    1. The Consumer Financial Protection Act (CFPA)
    2. The 18 enumerated consumer laws w/in CFPA
    3. Any rule or order prescribed by the CFPB
  - States must consult with CFPB before bringing an action, but can bring complementary actions in most cases
  - Just because the CFPB brought action, doesn't automatically prohibit the State from doing so as well

# CFPB Encouraging State Enforcement

- What a State can (or may want to) pursue depends on statute and violations
  - CFPB announcements and circulars are not law
  - Courts not required to give announcements deference; they are only persuasive to the extent the court finds them so
- States not obligated to bring enforcement actions
- CFPB silent on potential remedies States may recover
  - May be difficulties in seeking civil money penalties under fed law
- Also recently opined States can police credit reporting issues (and enact laws, so long as no conflict with FCRA)

# CFPB's Dormant Nonbank Oversight

- CFPB also announced intent to increase nonbank supervision
  - This supervision not recently exercised
  - Stems from Dodd Frank Wall Street Reform and Consumer Protection Act of 2010
  - In general, allows CFPB to hold nonbank entities to similar standards as banks
    - All nonbank entities in mortgage, private student loan, and payday loan industries may be subject to supervision
    - Applies only to nonbank entities which the CFPB has **reasonable cause** to determine **pose a risk** to consumers

<https://www.consumerfinance.gov/about-us/newsroom/cfpb-invokes-dormant-authority-to-examine-nonbank-companies-posing-risks-to-consumers/>

# CFPB's Dormant Nonbank Oversight

- Risk-Determination Process
  - CFPB plans to increase transparency in decision process of which nonbank entities are subject to supervision
  - Nonbank entities that CFPB has **reasonable cause** to determine **pose a risk** to consumers are subject to supervision
    - Risky conduct may involve:
      - Potentially unfair, deceptive, or abusive acts or practices
      - Practices that may violate federal consumer financial law
  - Risk determination process can be based on:
    - Complaints collected by the CFPB
    - Information from other sources like judicial opinions or admin decisions
    - Whistleblower complaints
    - Statements from federal or state partners
    - News reports

# Adverse Action Notices Revisited

- May 2022 advisory opinion by CFPB notes that:
  - Equal Credit Opportunity Act (ECOA) continues to protect borrowers even after they have applied for and received credit (e.g., renewals)
  - Lenders required to provide “adverse action notices” to borrowers with existing credit (e.g., if adverse action upon renewal)

# Adverse Action Notices Revisited

- Adverse Action includes
  - Denying an application for credit
  - Terminating an existing credit account
  - Making unfavorable changes to the terms of an existing account
  - Refusing to increase a credit limit, etc.
- Notice must specify a reason that was actually relied upon
  - Lender must provide specific principal reason(s) for adverse action
  - Reasons must relate only to factors actually scored in system
  - If there is a factor that was a principal reason in the decision, it may not be excluded, or the notice will not satisfy requirements

<https://www.consumerfinance.gov/compliance/circulars/circular-2022-03-adverse-action-notification-requirements-in-connection-with-credit-decisions-based-on-complex-algorithms/>

# Adverse Action Notices Revisited

- Application to Black Box Algorithms
  - Lenders using artificial intelligence, machine learning, or complex or black box algorithms not exempt from notice requirement
    - A creditor cannot justify noncompliance based on the mere fact the technology it employs is too opaque to understand
  - If a lender does not know the reason for adverse action, they cannot satisfy the requirement

# 'Gag' Clauses and Consumer Reviews

- CFPB issued notice that CFPB prohibits banks or financial companies from:
  - Including contractual 'gag' clauses which prevent completely honest consumer reviews
    - Such clauses may amount to unfair or deceptive practices
    - Threatening to invoke such a clause is separate unfair/deceptive act
  - Creating fake positive reviews
    - Inducing non-customers to create fake positive reviews is similarly deceptive
  - Suppressing or manipulating reviews
    - For example, only publishing positive reviews is prohibited

<https://www.consumerfinance.gov/about-us/newsroom/cfpb-issues-policy-on-contractual-gag-clauses-and-fake-review-fraud/>

# New Mexico Small Loan Act of 1955

- Summary of NM H.B. 132:
  - 36% rate cap
  - Covers cash advances up to \$10,000
  - Applies to loan made to a resident of New Mexico
  - Goes into effect January 2023
- Be aware if have operations near the NM border

# New Mexico Small Loan Act of 1955

- Potential Conflict with Texas Law

- Tex. Fin. Code § 342.005 - says Texas law applies if customer is located in Texas at the time the loan is made (even if a NM resident)
- N.M. Stat. Ann. § 58-15-24: Loans made elsewhere. – No loan made outside this state to a resident of New Mexico in the amount or of the value of ten thousand dollars (\$10,000) or less for which a greater rate of interest, consideration, charge or compensation to the lender than is permitted by the general laws of New Mexico in force governing money, interest and usury has been charged, contracted for or received shall be enforced in this state. Every person in any way participating in such a loan in this state is subject to the provisions of the New Mexico Small Loan Act of 1955. Any loan made to a nonresident of New Mexico in conformity with the law of the state where made may be enforced in this state.

# New Mexico Small Loan Act of 1955

- Which law applies?
  - If person lends to NM resident while that resident is in Texas, arguably that loan is subject to NM law and Texas law
    - New Mexico rates more stringent
    - If loan made under Texas rates, cannot be enforced in NM where customer resides
    - If loan does not comply with any rate or charge in NM law, cannot be enforced in NM
    - Unable to collect, potential usury claim, potential civil penalty or lawsuit
  - “If a party argues that the laws of the state where the right vested conflict with a fundamental public policy of New Mexico, a New Mexico court may refuse to apply that state's law.” See *United Wholesale Liquor Co.*, 108 N.M. at 470, 775 P.2d at 236.

# New Mexico Small Loan Act of 1955

- **WARNING: Don't make loans to NM residents using Texas rates**
  - Consider whether can meet requirements of both NM law and Texas law as to all charges
    - “for which a greater rate of interest, consideration, charge or compensation to the lender than is permitted by the general laws of New Mexico”
    - 36% rate cap, acquisition charge, late fees, returned check fees?
    - Could be other conflicts
- Lenders in Texas, but particularly near NM border, must be cognizant