

Client Alert

January 23, 2015

The CFPB 2015 Forecast: Continued Cloudiness, Thunderstorms Likely

By Donald Lampe, Leonard Chanin and Joseph Rodriguez

This will be a busy year at the Consumer Financial Protection Bureau (CFPB), and that certainly means it will be a busy year for financial institutions as well.

In addition to exercising its supervisory and enforcement authorities, the CFPB is poised to issue a number of proposed rules and finalize several other rules it proposed in 2014. Furthermore, the gargantuan TILA-RESPA integrated disclosure rule will become effective in 2015, posing the most significant operational challenges to mortgage originators since the Truth in Lending Act was enacted. All in all, 2015 will be a hectic time. The following lists the most significant rulemakings and other activities the CFPB will be working on in 2015.

ANTICIPATED PROPOSED RULES

Debt Collection Practices. In November 2013, the CFPB issued an advance notice of proposed rulemaking (ANPR) seeking information about debt collection practices. The CFPB asked more than 150 questions in the ANPR, many with multiple parts. The questions focused on a wide array of issues and several asked about the activities of so-called first-party “original” debt collectors. If the proposed rule is anything like the ANPR, it will be massive and broad-ranging. We anticipate the CFPB will issue a proposed rule in the Spring or Summer of 2015. It is virtually certain that the proposed rule will cover original creditors as first-party debt collectors, as well as those who buy debts from creditors and others. Take a deep breath. You may not want to exhale.

Short-Term Small Dollar Lending. Not to be outdone by the looming debt collection proposal, the CFPB also is scheduled to issue a proposed rule (or more accurately multiple proposed rules) dealing with short-term credit products. Specifically, we expect the CFPB will issue the long-awaited, and, for some institutions, the long-feared, proposal dealing with payday loans. While the payday loan proposal may affect only a limited number of financial institutions, other short-term credit proposals are likely to sweep far more broadly. Spring of 2015 appears to be the most likely issuance date for a proposed payday lending rule.

The other short-term credit proposal we are awaiting will address overdrafts offered in connection with deposit accounts. In July 2014, the CFPB issued a short report on overdrafts, with Director Cordray stating that “consumers who opt in to overdraft coverage put themselves at serious risk when they use their debit card.” It seems as though the writing is on the wall. And, we fear the approach taken by the CFPB in its proposed rule dealing with prepaid cards that offer overdrafts maybe a sign of things to come. For depository institutions, now may be the winter of our discontent; do not expect a glorious summer. This proposal will presumably be issued in 2015, but perhaps not until early Summer.

Client Alert

And, if that isn't enough, there may be a proposal on deposit advance products. The CFPB has been relatively quiet about these products, no doubt due to the guidance issued in late 2013 by the OCC and FDIC, which seemed to have all but eliminated such products.

ANTICIPATED FINAL RULES

HMDA/Regulation C. In August 2013, the CFPB issued proposed changes to Regulation C to implement statutory amendments made to the Home Mortgage Disclosure Act (HMDA), plus many other provisions not in the amended statute. The proposed rule would greatly expand the types of loans covered by Regulation C as well as the types of data collected, and, for larger HMDA reporters, would require "earlier" reporting of data to the CFPB or other applicable federal agencies. The CFPB has to address challenging consumer privacy issues posed by the collection of such massive amounts of data. Thus, some sort of privacy "proposal" will be issued by the CFPB to address these issues. The CFPB faces challenging issues in finalizing this rule, which is why the Bureau may not issue a final rule until late in 2015.

Prepaid Cards. Just in time for the holidays, in December 2014, the CFPB published massive proposed changes to Regulation E and Regulation Z addressing prepaid accounts. Far from simply addressing disclosures for prepaid cards, the proposal has a bit of everything for everyone: coverage under Regulation Z credit card rules of any prepaid card that offers overdrafts, and proposed coverage of tax refund cards and student financial aid cards, as well as certain digital wallets. The comment period closes on March 23, 2015, and then "the fun really begins." Given the sheer heft of the proposal and the number of comments that the CFPB is receiving, it is hard to say whether the CFPB will be able to issue a final rule before the end of 2015. But no doubt some at the CFPB will push hard to finalize the rule by year-end.

Mortgage Rule Revisions. The CFPB issued two proposed rules in late 2014 to amend Regulation Z and Regulation X. One rule was proposed in October 2014, and the other was proposed in December 2014. The former addresses provisions in the TILA-RESPA Integrated Disclosure (TRID) Rule and other rather esoteric issues. The latter is an extensive, highly technical proposal covering many detailed aspects of the CFPB's Regulation Z/Regulation X servicing rules effective in January of 2014. Issues addressed include clarifications sought by the industry and correction of obvious deficiencies recognized by the agency. There is in this proposal, however, no substantive retreat from rigorous consumer protection, particularly with respect to default servicing. The CFPB adopted final rules under the TRID proposal earlier this week. Other than one aspect of the proposal, the CFPB adopted the rules as proposed in October.¹ We do not expect the comprehensive mortgage servicing rules to be finalized until late in 2015.

Auto Finance Larger Participant Rule. In October 2014, the CFPB issued a proposed rule to define who would qualify as a "larger participant" for purposes of the provision of automobile financing. This rule, when finalized, will determine the nonbank entities that provide automobile financing over which the CFPB has supervisory authority. We anticipate a final rule in 2015, perhaps by Spring.

¹ With respect to the proposal to allow creditors to redisclose the Loan Estimate one business day after the interest rate is locked, the CFPB is extending the timing requirement to three business days after the rate is locked.

Client Alert

RULES ISSUED PREVIOUSLY THAT BECOME EFFECTIVE IN 2015

On December 31, 2013, the CFPB adopted final changes to Regulation Z and Regulation X, implementing integrated mortgage disclosures under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z). The final rule will become effective August 1, 2015, so plan your summer vacations accordingly. The final rule is the result of a multi-year rulemaking effort by the CFPB, dubbed “Know Before You Owe,” and involved consumer testing of disclosures as well as quantitative study of the proposed disclosures. Time will tell how the approach will work. One thing is likely: the CFPB will not revisit the fundamental building blocks of the rule for a long time. So mortgage lenders and settlement service providers can settle in and get comfortable.

SUPERVISION PRIORITIES

As required by the Dodd-Frank Act, the CFPB generally chooses which institutions to examine based on a risk-weighted priority for each Institution Product Line (IPL) (e.g., “Bank of MoFo” – Mortgage Origination). However, examination scheduling is subject to certain constraints. For example, at smaller institutions in which policies and procedures, compliance, and governance may be shared across lines of business, the CFPB may decide that the most efficient use of its resources is to examine the entire institution rather than a single IPL. Certain smaller institutions also have been used as training opportunities for new examiners before they move on to larger and more complex institutions. Furthermore, aside from any fancy risk-weighted prioritization, the Bureau likely wants to have some supervisory interaction with even the smallest depository institutions under its jurisdiction (i.e., those with more than \$10 billion in assets) at least every two to three years.

Accordingly, every year the CFPB has to make decisions about where it will use its supervisory resources. Despite its guaranteed funding from the Federal Reserve’s coffers, the Bureau only has so many examiners and each examiner can only participate in so many exams over the course of the year. That means the CFPB has to decide which IPLs it will examine among its continuously supervised institutions,² “smaller” banks and credit unions (to the extent one thinks \$10 billion in consumer assets is small), and non-depository financial services companies. That said, even if your institution is not scheduled for an examination, that doesn’t mean you won’t get a “visit” from the CFPB (see Enforcement Priorities below).

Reading the CFPB tea leaves - it may be a bitter brew for some - our sense is that the Bureau’s focus in 2015 likely will continue to be on compliance with the new mortgage origination and servicing rules that went into effect in January of 2014. It appears that the CFPB started focusing on such issues in the second half of 2014, mostly to allow sufficient transactional data to accrue for testing purposes. Thus, a number of larger institutions have not yet been examined for compliance with the new mortgage origination and servicing rules. Given the significance of those rules, such exams will almost certainly be a priority for the Bureau in 2015.

Further within mortgage origination and servicing, we also expect the CFPB to continue to focus on fair lending (ECOA and HMDA) and unfair, deceptive or abusive acts or practices (UDAAP). In light of the loan originator compensation rule (within Section 36 of Regulation Z), we think the Bureau’s fair lending analysis will emphasize

² Continuously supervised institutions are generally, but not always, the largest banks under the Bureau’s jurisdiction. They typically are subject to at least one, and frequently multiple, examinations during any given 12-month period.

Client Alert

underwriting issues, rather than pricing, within the origination space. For example, we understand that the CFPB has been conducting targeted redlining inquiries of mortgage lenders. Thus, for 2015, mortgage lenders would be wise to consider whether their compliance management systems effectively monitor for such risks. And, of course, HMDA compliance will, as it has been since the CFPB commenced examining mortgage originators, be a concern of the agency as it underpins fair lending mortgage exam work. As it pertains to UDAAP, we expect that the CFPB will wield that authority to fill perceived gaps in its rules, particularly in the servicing business. For example, the supplemental rules the Bureau proposed for mortgage servicing in December 2014 likely will not become effective until late 2015 at the earliest.

In addition to those lines of business, with a few exceptions we think the Bureau's supervisory priorities will likely closely track its rulemaking initiatives. Thus, large diversified financial institutions should be preparing for CFPB examinations covering deposits/overdrafts, debt collection, indirect auto financing,³ and credit cards. Not surprisingly, we see the Bureau looking closely at overdraft programs and compliance with Regulations E, DD and perhaps B, as well as UDAAP issues such as posting order, holds and fee disclosures. Regarding debt collection, our strong sense is that the Bureau will be conducting both first-party and third-party exams. UDAAP and FCRA/Regulation V compliance will certainly be a focus in both types of exams, with FDCPA compliance prominent for the third-party collectors, and the specter of fair lending arising for first-party collectors.

We further see indirect automobile lending continuing to be a focus for CFPB examinations, particularly in the second half of the year once the larger participant rule has been finalized. Unless you've been hiding somewhere for the last couple of years – not that we would blame you – you know that the CFPB has been using its fair lending authority under the ECOA to assert that by allowing automobile dealers to “markup” interest rates, lenders in effect are discriminating in funding loans to certain minority car buyers. It is well known, through public securities filings, that for well over a year the CFPB has been conducting numerous fair lending exams and investigations against both bank and non-bank auto financing operations. Pretty clearly, the CFPB is not backing off its position that so-called proxy analysis may lead to proof of disparate impacts on minority car buyers. Moreover, our strong sense is that the CFPB is not done with the automobile financing business and may, for example, start turning its attention in 2015 to so-called “add-on products,” such as gap insurance, vehicle service contracts, and, yes, even the ubiquitous rustproofing and undercoating. We expect the Bureau to wield both its fair lending and UDAAP authorities in such reviews.

Further into the fair lending and UDAAP world, with a healthy dose of TILA/CARD Act and Regulation Z added for good measure, we also expect a number of credit card exams in 2015. Our understanding is that the Bureau has dipped its toe in that water over the past year or so, and we think it's likely that they are ready to jump in full force. So bring your proxy analysis and line up your statisticians and economists, because in our experience a credit card fair lending exam will be a whole new ballgame for many institutions.

Finally, we would be remiss if we didn't mention other businesses that may attract supervisory attention in 2015. Based on the trajectory of the CFPB's examination priorities, these businesses include credit reporting agencies, remittance transfer companies, and student loan servicers. The CFPB is likely to pick a handful of such

³ For the first few months of the year, until its larger participant proposed rule is made final, the Bureau will likely interact with non-bank indirect auto lenders through enforcement investigations.

Client Alert

companies or institutions to examine in order to continue to build its knowledge base about those businesses. The CFPB heavily relies on its consumer complaints database in its risk-weighting process, and based on the agency's recent consumer complaint reporting, these businesses may want to ready themselves for a CFPB visit.

ENFORCEMENT PRIORITIES

As CFPB Supervision has brought more examiners on board and provided them with the necessary training, it appears that a regular pipeline of referrals from Supervision to Enforcement now exists. So while Congress and the President continue to debate the Keystone XL Pipeline, the CFPB "Supervision to Enforcement Pipeline" is up and running. Accordingly, we expect that Enforcement will be looking into similar IPLs and issues as those reviewed in Supervision.

But that's not to say that CFPB Enforcement doesn't set its own agenda, too. In fact, we expect that Enforcement's investigation portfolio likely will contain more non-depository institutions than Supervision's list of targets. Moreover, given the limitations of the Bureau's supervisory authority, in which it has to promulgate a "larger participant" rule in order to supervise a consumer financial product/institution that isn't specifically enumerated in the Dodd-Frank Act, we think it likely that Enforcement will continue to bring groundbreaking actions that press the boundaries of the agency's authority, such as the complaint it recently filed against a cellular provider alleging that certain billing practices were improper. While we don't know precisely what the next such case will be, the CFPB has publically indicated its interest in the mobile payments space, and it wouldn't surprise us to see them garner headlines in that area with an enforcement action.

OTHER MATTERS

In December 2013, the CFPB issued preliminary results of a study of arbitration agreements/provisions. We anticipate issuance of a final study in early 2015; don't expect the CFPB to warmly embrace arbitration agreements. Upon issuance of the study, the CFPB has the authority to propose rules addressing arbitration provisions. Such proposed rules must be consistent with the CFPB's study. How funny is that? Not very.

CONCLUSION

From the perspective of keeping up with new developments and responding to CFPB actions, 2015 will, like 2014, prove to be a very busy time for the financial services industry. Institutions, both depository and non-depository, will continue to have to adjust to a high-velocity stream of new rules, guidance, blogs, examination procedures, consent orders and public statements, as well as anticipate where the Bureau's next rulemaking or enforcement action is going to come down. And, on top of the always expanding supervisory regime and ever enigmatic enforcement process, it's hard to know where to start.

Contact:

Donald C. Lampe
(202) 887-1524
dlampe@mofo.com

Leonard N. Chanin
(202) 887-8790
lchanin@mofo.com

Joseph R. Rodriguez
(202) 778-1610
jrodriguez@mofo.com

Client Alert

About Morrison & Foerster:

We are Morrison & Foerster—a global firm of exceptional credentials. Our clients include some of the largest financial institutions, investment banks, Fortune 100, technology and life science companies. We've been included on *The American Lawyer's* A-List for 11 straight years, and *Fortune* named us one of the "100 Best Companies to Work For." Our lawyers are committed to achieving innovative and business-minded results for our clients, while preserving the differences that make us stronger. This is MoFo. Visit us at www.mofo.com.

Because of the generality of this update, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations. Prior results do not guarantee a similar outcome.