

Client Alert

March 20, 2017

Court Finds CFPB Case Against Payment Processor Lacking

By Steven M. Kaufmann and Oliver I. Ireland

On March 17, 2017 the United States District Court for the District of North Dakota granted the motion of Intercept Corporation (“Intercept”) and its senior executives to dismiss the complaint filed almost a year ago by the Consumer Financial Protection Bureau (“CFPB”).¹ Intercept is a payment processor that initiates ACH transactions to consumer accounts on behalf of its merchant-customers. This case is one of the few to go forward where the court is confronted with defining the parameters of the CFPB’s authority under the Dodd-Frank Consumer Financial Protection Act (“CFPA”).

In our June 2016 client alert we noted that the Intercept CFPB complaint was somewhat novel in that it alleged that Intercept and its owners were “covered persons” under the CFPA, even though Intercept acts as an agent of the merchant-customer, but not as an agent to the consumer whose account is being debited. We noted that the CFPB’s approach expands the reach of CFPA enforcement for unfair, deceptive, or abusive acts or practices to include within the definition of “covered person” entities that provide payment processing or “other financial data processing” services to businesses that do not offer consumer financial products or services. Practically speaking, this theory means that any entity that processes payments (or offers other financial data processing services) is responsible for monitoring the business practices for every person for whom it processes payments.

The Court gave very short attention to this issue and did not reject the CFPB’s legal theory as the Court might have on a motion to dismiss. The Court noted summarily that, “Intercept is a ‘covered person’ and a ‘service provider’ under the CFPA. [Its principal owners] Smith and Dresser are ‘related persons’ under the CFPA because of their status as officers of Intercept.”² The Court went on to find that “the complaint sufficiently alleges facts that, if proven, would support a finding that defendants are ‘covered persons’, ‘service providers’, or ‘related persons’ under the CFPA.”³

Instead, the Court dismissed the case because it found that the CFPB did not sufficiently allege facts to show a violation of the CFPA or show that the defendants engaged in “unfair, deceptive, or abusive acts or practices,” as defined by the Act. Instead, the complaint impermissibly relied on conclusory statements regarding Intercept’s allegedly unlawful acts or omissions. For example, the complaint alleged that Intercept ignored ‘red flags’ tending to show that it was processing for merchants that engaged in fraud. The Court found the complaint inadequate because it “simply does not sufficiently identify particular clients whose actions provided ‘red flags’ to Intercept or how Intercept’s failure to act upon those ‘red flags’ caused harm or was likely to cause harm to any identified

¹ See Order Granting Defendants’ Motion to Dismiss the Complaint, *Consumer Financial Protection Bureau v. Intercept Corporation, et al.*, No. 3:16-cv-144 (D.N.D. Mar. 17, 2017) (“Order”).

² Order at 2-3.

³ *Id.* at 8.

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consumer or group of consumers.”⁴ The Court noted that “the complaint indicates that Intercept was required to follow certain industry standards, [but] it fails to sufficiently allege facts tending to show that those standards were violated.”⁵ The Court found that “although the complaint contains several allegations that Intercept engaged in or assisted in unfair acts or practices, it never pleads facts sufficient to support the legal conclusion that consumers were injured or likely to be injured.” Similarly, the Court found that the complaint did not meet the CFPB standards in alleging facts to show “whether any potential injury was or was not counterbalanced by benefits to the consumers at issue.”

The Court’s analysis hinged on the theory that the complaint failed to provide the “defendants fair notice of the grounds for the claim and at least a general indication of what the litigation involves.”⁶ The Court relied on basic Fed. R. Civ P. Rule 8 and Rule 12 pleading standards and did not analyze the claim under the stricter pleading standards of Rule 9(b) requiring that a party alleging fraud or mistake, “must state with particularity the circumstances constituting fraud or mistake.”

At this stage, the CFPB has the option to: (1) resolve the case through settlement or dismissal under this record; (2) amend the complaint to attempt to meet the deficiencies noted by the Court; or (3) rest on the pleading record established and seek appeal following dismissal of the case. Most litigants would follow path two, but the CFPB, even in this environment, is not a normal litigant and the parameters of what are unfair, deceptive, or abusive practices under the CFPB are far from clear.

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⁴ *Id.* at 9.

⁵ *Id.* at 9.

⁶ *Id.* at 6.

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