The CFPB— A POWERFUL NEW COP

— by DYLAN W. HOWARD AND TRACY L. STARR —

The Consumer Financial Protection Bureau represents financial law enforcement on steroids. What you don't know about it can hurt you.

Chief Justice of the United States John Roberts' dissent in *City of Arlington v. FCC [Federal Communications Commission]* refers to our modern-day administrative agencies as the "headless fourth branch of government," noting that they combine broad legislative, executive and judicial powers. ¶ While not writing specifically about the Consumer Financial Protection Bureau (CFPB), the CFPB's activities during its short existence demonstrate, as Roberts stated in his dissent, the accumulation of these broad powers in the same hands—which has become a "central feature of modern American government."

Recent actions by the CFPB

Although it just celebrated its second birthday, the CFPB has quickly established itself as an aggressive enforcer. Many of the regulatory and enforcement functions of other agencies have been transferred to the CFPB. Recent actions of note include the following.

Lawsuit over bonus for mortgage borrower upcharges

On July 23, 2013, the CFPB sued a mortgage company and two of its executive officers in Utah for awarding bigger quarterly bonuses to loan officers who led consumers to take out higher-interest mortgages after the practice was banned in 2011. According to the lawsuit, the company did not have a written policy about its program but the policy was shown in payroll records. The case was referred to the CFPB by investigators with the Utah Department of Commerce, Division of Real Estate.

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Capital One Bank enforcement action for $210 million

The CFPB made its presence known in July 2012 with this record-setting settlement against this credit-card issuer for deceptively marketing add-on products, for failing to enact programs to prevent unfair and deceptive practices, and for what the CFPB termed unfair billing practices. The $210 million includes $150 million in refunds to affected customers including approximately 2 million customers who enrolled in the add-on products, and $60 million in penalties paid to the CFPB.

The consent order also imposes ongoing substantial compliance obligations on Capital One. Capital One has further agreed to stop marketing any of the applicable add-on products until a compliance plan is submitted to and approved by the CFPB.

Discover Financial Services enforcement action for $214 million

The Capital One action was quickly followed by a $214 million settlement with Discover as a result of an investigation initiated by the Federal Deposit Insurance Corporation (FDIC), which the CFPB joined in 2011. The joint investigation involved Discover's marketing of credit-card services, including use of scripts that failed to disclose material terms and conditions of credit-card protection products.

As restitution, $200 million of the settlement will go to more than 3.5 million consumers. As part of the action, Discover has also agreed to submit a compliance plan to the CFPB and the FDIC that includes changes to its telemarketing practices, and to submit to an independent audit. It will also pay a $14 million penalty—$7 million of the penalty will be paid to the U.S. Treasury and the remaining $7 million will be paid to the CFPB's Civil Penalty Fund.

American Express Companies enforcement action for $85 million consumer restitution/$27.5 million in civil penalties

Following these actions, the CFPB reached a settlement with American Express Companies with respect to credit-card practices, including deceptive marketing and unlawful late fees allegedly committed by three American Express subsidiaries. This action was based on an investigation started by the FDIC and the Utah Department of Financial Institutions. Portions of the fine will be paid to various agencies including the CFPB, the FDIC, the Federal Reserve and the Office of the Comptroller of the Currency (OCC). The enforcement order also requires specific changes in the American Express subsidiaries' marketing and debt-collection policies, with compliance to be verified by independent auditors.

Criminal action

As if these actions were not enough to make its presence known, the CFPB on May 7, 2013, teamed up with the Department of Justice (DOJ) to bring criminal charges against debt-relief companies for fraud and deception. Based upon referrals from the CFPB, DOJ charged New York–based Mission Settlement Agency, its owner and employees, with criminal conspiracy, mail fraud and wire fraud in an alleged scheme to obtain illegal fees for bogus debt-settlement services. The owner and three employees were arrested in connection with this case, and two former employees have agreed to plead guilty. The CFPB has also filed parallel civil actions.

Kickbacks to mortgage lenders

In April 2013, the CFPB announced enforcement actions and proposed settlements to end improper kickbacks paid by mortgage insurers to mortgage lenders in exchange for business. The proposed orders imposed $15 million in total penalties against Genworth Mortgage Insurance Corporation, United Guaranty Corporation, Radian Guaranty Inc. and Mortgage Guaranty Insurance Corporation (MGIC).

According to a CFPB press release, these companies received lucrative business referrals from lenders in exchange for kickbacks. In addition, these kickbacks were a "common practice in the years leading up to the financial crisis" and these four companies were "key players during that time," according to the CFPB press release. The Office of Inspector General (OIG) at the Department of Housing and Urban Development (HUD) initiated this investigation and in July 2011, HUD's authority was transferred to the CFPB.

In a May 2013 action, the CFPB fined a Texas home builder in connection with kickbacks it received for referring mortgage origination business. This settlement resolved violations of the Real Estate Settlement Procedures Act (RESPA) and the CFPB became aware of this conduct through a referral from the FDIC, which separately fined one of the banks involved.

Proposed regulations—in mortgage servicing

These enforcement strategies are not simply of concern in their own right, but deserve attention specifically because the proposed rule amendments issued by the CFPB effective

Jan. 10, 2014, insert the agency into areas of banking and mortgage servicing where the government previously had little or no role.

One of the primary areas of concern involves the proposed revisions to the Real Estate Settlement Procedures Act and the Truth in Lending Act (TILA). These include dramatic new requirements for lenders/mortgage servicers faced with delinquent borrowers.

For example, after Jan. 10, mortgage servicers must establish or make a good faith effort to establish live contact with a borrower within the first 36 days of the borrower's delinquency and inform the borrower if loss-mitigation options are available. The servicer must then follow up with a clear and conspicuous written notice of available loss-mitigation options by the 45th day of a borrower's delinquency.

In addition, all non-exempt servicers must have in place specific procedures to ensure that every delinquent borrower is specifically assigned personnel with whom the borrower can communicate about the loss-mitigation process. Also, those servicers must make sure that the assigned personnel are available and have access to the borrower's complete record, including his/her payment history and all written information provided by the consumers with regard to loss mitigation.

Once a borrower is delinquent, the revised rules provide stringent new requirements for loss-mitigation procedures for mortgage loans secured by the borrower's principal residence. Once an application for loss mitigation is submitted, the lender is generally required to acknowledge receipt in writing within five days. When a complete loss-mitigation application is received more than 37 days before a foreclosure sale, the servicer is given 30 days to evaluate the application for all loss-mitigation options and to provide a written decision to the borrower providing an explanation for any denial.

The new rules do not provide specific criteria for loss-mitigation review, but do require servicers to have in place policies reasonably designed to allow the proper evaluation of borrowers for loss mitigation pursuant to the requirements of the owners or investors in the mortgage loan.

If a borrower submits a complete loss-mitigation application at least 90 days prior to a foreclosure sale (or at any time when a foreclosure has not been scheduled), and a loan modification is denied, the borrower is provided with additional rights to appeal the denial.

The appeal must be conducted by separate personnel independent from those who evaluated the initial application. Within 30 days of an appeal, the servicer must notify the consumer of its decision on the appeal and must then give the borrower at least 14 days to accept or reject any offer made at that point.

The new rule also targets "dual tracking"—the previously common occurrence where a servicer evaluates a borrower for loss mitigation while it prepares to foreclose.

As of Jan. 10, a servicer will not be permitted to foreclose until a mortgage loan is more than 120 days delinquent. Then, if the borrower submits a complete loss-mitigation application before the servicer has initiated foreclosure, the servicer may not initiate foreclosure unless it 1) informs the borrower that he/she is not eligible for loss mitigation and any appeals have been exhausted; 2) the borrower rejects all loss-mitigation offers; or 3) a borrower accepts a loss-mitigation offer but fails to comply with its terms. If a complete loss-mitigation application is submitted after foreclosure has been commenced but more than 37 days before an actual sale, the servicer is not permitted to conduct a sale or move for a foreclosure judgment until one of the above referenced conditions has been met.

Oversight of other mortgage-related practices

Another area of CFPB oversight that is being greatly expanded involves debt collection. On July 10, 2013, the CFPB made it clear that all debt collectors subject to its jurisdiction must ensure they are not engaging in any unfair, deceptive or abusive acts or practices (UDAAP) in connection with debt-collection activities.

The Fair Debt Collection Practices Act (FDCPA) generally applies to third-party debt collectors such as collection agencies, and the CFPB now has imposed the requirements of the FDCPA on creditors or first-party debt collectors. In so doing, the CFPB described the acts and practices that it regarded as UDAAPs, including charging additional amounts not expressly authorized by the agreement creating the debt or permitted by law; revealing the consumer's debt without consent; and misrepresenting that a debt-collection communication is from an attorney.

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Other examples of areas subject to investigation by the CFPB include qualifications and screening standards for loan originators (including ethics, education and financial responsibility requirements); the prohibition of incentives to loan originators for steering borrowers to more expensive loans; the prohibition both of contractual rights waivers and of mandatory arbitration provisions; and servicer policies with regard to escrow accounts, force-placed insurance and borrower communication, including monthly mortgage statements.

The CFPB indicates that it understands the extent of the necessary revisions to mortgage bankers' systems and policies necessary to comply with these new rules. It further states that it will work to help the industry achieve implementation on a timely basis. Nevertheless, the CFPB maintains the right to examine and enforce servicers' and originators' compliance with these extensive new rules as of the effective date.

CFPB's complaint and investigative process

In addition to its broad substantive mandate, the CFPB has implemented a specific complaint process that will certainly affect the way financial institutions do business. The CFPB

created a centralized website where consumers can log complaints directly with the agency, making it extraordinarily easy for consumers to voice their concerns.

Since July 2011, the CFPB has launched complaint channels for many types of financial products and, to date, consumers can use the website to file complaints related to mortgages, banking accounts and banking services, credit cards, credit reporting, debt collection, money transfers, student loans and vehicle or consumer loans.

The CFPB divided the complaint process into six stages. The initial section, titled "complaint submission," requests a narrative from the consumer describing the concern, his/her desired resolution and specific details on the financial product or service at issue. Consumers receive email updates and can log in to track the status of a complaint.

The narrative information provided by consumers, however, will not be made public until the CFPB has carefully reviewed the privacy risks of making such information public. To that end, the CFPB reports that it is considering ways to give submitting consumers a meaningful choice of narrative disclosure options.

Once a complaint is received, the CFPB forwards the complaint to the company and works with the company to get a response (see www.consumerfinance.gov/complaint). The company is then tasked with reviewing the complaint, communicating with the consumer and reporting back about the steps taken to address the complaint.

The CFPB notifies the consumer when the company submits a written response to the complaint, and allows consumers the opportunity to review the submission and provide feedback. Responsive company narratives—like the consumer complaint narratives—will not be published by the CFPB.

The CFPB's investigative, pre-adjudication process is modeled on the procedures of other law-enforcement agencies, specifically the Federal Trade Commission (FTC) and the Securities and Exchange Commission (SEC). The CFPB has significant discretion to determine whether and when to open an investigation, but only the assistant director or any deputy assistant director of the Office of Enforcement has the actual authority to open an investigation.

Similarly, only the director, the assistant director of the Office of Enforcement and the deputy assistant directors of the Office of Enforcement are authorized to issue civil investigative demands (CIDs) for documentary material, tangible things, written reports, answers to questions or oral testimony. These demands may be enforced in federal district court.

The CFPB's investigators may conduct investigational hearings pursuant to CIDs for oral testimony and, after notice of what conduct is at the root of the alleged violation and the applicable provisions of law, may compel information and testimony from individuals.

A company must decide within 20 days whether it intends to comply with the CID. Time frames to provide a complete written response, however, are generally longer than the initial 20-day notification period and can differ depending on the scope of information requested in the CID. While extensions are generally disfavored, the assistant director of the Office of Enforcement has the authority to grant an extension for good cause.

A response to a CID should be done with care, as submissions must be made under oath and the information contained therein may become evidence in any subsequent enforcement action. While there are limitations to a responding company's ability to withhold information on the basis of privilege, a respondent may file a petition for an order modifying or setting aside a CID.

The responding company may also obtain copies of or access to documents or testimony relied upon by the CFPB in the investigation. Upon submission of a complete response, the Assistant Director negotiates and approves the terms of compliance with a CID.

Ultimately, a complaint is resolved in one of three ways. The assistant director may close the investigation when the facts indicate an enforcement action is not necessary or warranted. If the bureau determines that the facts warrant further action, an enforcement action may be filed in federal or state court or through administrative proceedings. The CFPB also has the option to refer investigations to other federal, state or foreign government agencies for further investigation or action.

The management of the investigative process by the financial institution at issue can mean the difference between dismissal of the consumer complaint and an enforcement action. The response must be both timely and effective. Thus, upon receipt of a complaint from the CFPB, financial institutions are advised to promptly conduct an internal investigation regarding the circumstances of the complaint and a legal review of and response to the CID.

Anyone unfortunate enough to receive a CID from the CFPB should read the CFPB's Sept. 20, 2012, decision in response to the motion to modify or set aside the large CID served on PHH Corporation, a mortgage services provider. The CFPB's decision denied the motion and made it very clear that the CFPB regards itself as having very broad investigative powers, including the power to ask for materials dating back as far as 17 years—even though the applicable statute of limitations was only three years.

The decision also emphasized the importance of CID recipients participating in "meet and confer" sessions with the staff on narrowing the scope of the requests, including the importance of a recipient making its information technology (IT) personnel available in those sessions. The CFPB also made clear that a burden argument must be specific and detailed on cost and time. The CFPB also was not receptive to requests to extend the deadline for compliance. Finally, companies considering motions to limit should also factor in the fact that their motion and any resulting order may become publicly available.

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CFPB can compel production of privileged information and documents

One final area of concern involves the CFPB's power to compel financial institutions to provide information and documents, including those traditionally protected by various privileges.

When the CFPB was first created, there was deep concern about whether the production of privileged information to the CFPB would result in the institution's waiver of the privilege generally. While the CFPB took the position that the production of privileged information did not constitute a waiver of any privilege, this was of questionable legal value. Recent changes to the Federal Deposit Insurance Act (FDIA) codified this position.

The changes to the FDIA provide that the disclosure of information to FDIA-covered agencies would not result in a waiver of privilege. However, the FDIA would not protect the transfer of this information to non-FDIA agencies, such as the Federal Trade Commission or state attorneys general.

This is significant because the CFPB has taken the position that it has statutory authorization to share both examination reports and confidential supervisory information with agencies, including state attorneys general, who have jurisdiction over the covered entity. Significantly, in its most recent rules issued on the handling of confidential information, the CFPB expressed its intent to exercise this authority "carefully." However, as noted in the summary of the final rule, the CFPB expressly declined to add procedural requirements such as a notice and opportunity to object to these affected financial institutions.

This creates a unique situation where the documentation submitted to the CFPB is protected until it decides to share it with a non-covered agency. Given the lack of procedural safeguards, supervised institutions must simply submit privileged information and material in the hope that the CFPB does not produce this information to other agencies.

It will be interesting to see how the CFPB exercises its discretion in the coming years. Will its role as an advocate for consumers dominate this process, causing privilege material to be shared freely? Or will the CFPB's duties as a regulator win out and it will truly exercise discretion in sharing privileged materials with other agencies and state attorneys general? It also remains unclear at this date whether companies will fight the CFPB position on privilege. **MB**

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