The CFPB and House Republicans Remain at Odds Over Consumer Finance Regulation

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On January 28, 2014, CFPB Director Richard Cordray appeared before the House Financial Services Committee to testify about his agency's fourth Semi-Annual Report. Cordray's written testimony and opening remarks at the hearing focused on the agency's Qualified Mortgage Rule and other new regulations under the Dodd-Frank Act, as well as the CFPB's efforts in the areas of consumer financial literacy and decision-making. Cordray also noted the CFPB's collection of roughly $3 billion in consumer restitution for violations of the financial protection laws.

The hearing was very contentious. Cordray came under fire from House Republicans who questioned him about a variety of topics. For example, committee members asked about the new Qualified Mortgage Rule, which went into effect in January. If a loan meets the standards for a "qualified mortgage" – which include a debt-to-income ratio of no more than 43 percent – then there is a presumption that the lender made a reasonable and good faith determination that the borrower has the ability to repay the loan. If not, then the lender may be subject to liability. Committee members questioned whether the Qualified Mortgage Rule will deter banks from making loans, or even cause mortgage lenders to exit the business altogether. Cordray responded that lenders could still make loans that qualify if they are purchased by a government-sponsored enterprise, and he said that smaller creditors' loans kept in portfolio also get a pass. Notably, he stated that the CFPB would monitor the impact of the Qualified Mortgage Rule on lending markets and would be willing to consider adjustments as needed.

Committee members also criticized the agency's collection of data, asking whether the bureau's data collection practices are threatening consumers' privacy. Cordray responded by explaining that the CFPB collects aggregate data and that much of it cannot be linked to any particular consumer because of the lack of personally identifiable information collected. Other topics of questioning included the bureau's regulation of manufactured housing, the auto finance industry and the cost of renovating the CFPB's headquarters.

Given House Republicans' ongoing criticisms of the CFPB, it was not surprising that the House recently passed H.R. 3193, the Consumer Financial Freedom and Washington Accountability Act, which would make structural and other changes to the agency. H.R. 3193 combines several bills approved in November by the House Financial Services Committee. Among other changes, H.R. 3193 would replace the position of Director of the CFPB with a five-member commission, would change the voting standard for the Financial Stability Oversight Council from a two-thirds majority to a simple majority vote, and would make the agency subject to the congressional appropriations process rather than the current funding system through the Federal Reserve.

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The American Bankers Association expressed its support for H.R. 3193, urging House members to pass the bill. According to the association, the proposed five-member commission structure "would provide needed balance and appropriate checks in the exercise of the Bureau's authority." In addition, "[o] versight by Congress would allow the very consumers who the Bureau was designed to protect to hold it accountable through their elected officials."

The Obama Administration issued a statement strongly opposing House passage of H.R. 3193. The White House criticized the bill, arguing that the proposed organizational structure "would significantly limit the agency's ability to respond effectively to the rapid changes in the dynamic consumer financial products and services market." Moreover, "H.R. 3193 would subject the agency's funding to appropriations, dramatically undermining its ability to carry out consumer protections independent of political pressures." The statement indicated that President Obama's "senior advisors would recommend that the President veto . . . H.R. 3193." As a result, the bill's passage by the current Congress seems highly unlikely.

For-Profit Colleges and the Student Loan Industry Should Take Note of CFPB's Recent Enforcement Action

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In a recently filed lawsuit, the Consumer Financial Protection Bureau (CFPB) has demonstrated its willingness to assert its authority over both the student loan industry and for-profit colleges. The defendant in that lawsuit, ITT Educational Services, Inc., is a nationwide for-profit college accused by the CFPB of predatory student lending relating to the loans its students take out to fund their ITT education. This is the CFPB's first public enforcement action against the for-profit college industry, and may be a sign of actions to come against other for-profit colleges as well as other participants in the student loan industry, including banks and non-bank student loan servicers.

As previously discussed in the January edition of this newsletter, there is approximately $1 trillion in outstanding student loan debt in the United States, and the CFPB has indicated that it considers the student loan industry to be within the CFPB's purview of regulation and supervision. A new CFPB rule took effect on March 1, 2014, that allows the CFPB to oversee non-bank student loan servicers.

In this lawsuit, *CFPB v. ITT Educational Services, Inc.*, filed in the United States District Court for the Southern District of Indiana (Case No. 1:14-cv-292), the CFPB makes numerous allegations relating to purported predatory student lending by ITT. The CFPB first alleges that ITT engages in high pressure tactics to sign up potential students, artificially inflates its job placement figures, and conceals from potential students "the virtual non-transferability of ITT's credits" to other colleges in order to sign up additional students.

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The CFPB also alleges that as part of the sign-up process, ITT used deceptive and high pressure tactics to cause the students to take out student loans which ITT knew that the students would be unable to repay. The CFPB alleges that ITT created a private student loan system whereby it caused students to take out short term loans directly from ITT and then subsequently pushed "students into expensive, high-risk loans that ITT knew were likely to default…for the purpose of window-dressing ITT's financial statements and increasing its stock price."

The CFPB alleges that "ITT students relied on ITT and its Financial Aid staff to act in their interests when they signed up for financial aid packages" and that ITT's "Financial Aid staff solicited students' reliance and trust." The CFPB further alleges that "ITT did not act in the students' interest" and "took unreasonable advantage" of the students' "reasonable reliance to act in their interests" by, among other things, using "aggressive repackaging tactics, including the threat of expulsion" unless students took out additional private student loans. Based on these allegations, the CFPB brought three counts against ITT under the Consumer Financial Protection Act for engaging in unfair and abusive practices, 12 U.S.C. § 5536(a)(1)(B).

Finally, the CFPB also brought a claim against ITT for violation of the Truth in Lending Act, 125 U.S.C. § 1601, et seq. (TILA), and Regulation Z, 12 C.F.R. Part 1026, for failure to disclose a finance charge relating to the short term loans issued to students by ITT. The purported basis of the CFPB's TILA and Regulation Z claim is that ITT offered a 25% discount to students who repaid the short term loan at graduation, but did not give this discount to students who entered into repayment plans to repay the short term loans after graduation. The CFPB alleges that to "the extent that such discounts are not applied" to the post-graduation repayment plans, "ITT is charging students a finance charge in connection with those extensions of credit," and that this charge was not disclosed conspicuously in writing, thus purportedly violating TILA and Regulation Z.

Based upon these claims, the CFPB seeks equitable relief, restitution to borrowers, disgorgement of profits and civil penalties against ITT.

While the target of this enforcement action was a for-profit college, in light of the CFPB's recent statements and rule changes relating to the student loan industry, it is likely that this is the first of many CFPB enforcement actions to come against the student loan industry.

CFPB Continues Grassroots Methods to Obtain Complaints from Borrowers

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Consumer Financial Protection Bureau

In mid-January of this year, Richard Cordray addressed mayors from around the country and explained the many ways that the CFPB is making it easier for disgruntled borrowers to lodge consumer complaints through the CFPB. At the U.S. Conference of Mayors on January 14, 2014, Cordray assured the crowd that the CFPB is making every effort to help prevent constituents from "feel[ing] helpless because they stand alone against a large and powerful financial company." The remarks Cordray prepared for the mayors double as a helpful overview of the many new methods by which borrowers can lodge complaints against mortgage servicers – in fact, some methods allow borrowers to file a complaint in less than 30 minutes. Cordray focused on two ways that U.S. mayors could use the CFPB's resources to help their constituents.

First, and perhaps most notably, Cordray requested that mayors consider participating in a pilot program launched in February 2013. Called the "3-1-1 pilot partnership," the CFPB has partnered with several major cities throughout the U.S. – including Boston, Newark and St. Louis – to allow borrowers to have direct contact with the CFPB simply by picking up their phones and dialing 3-1-1. The program partnered with the city of Jackson, Mississippi, in September 2013 and allows the citizens of Jackson to be connected with the Bureau when they have any sort of financial issue. Said Mayor Chokwe Lumumba, "[w]e understand the challenges that Jacksonians face on a daily basis when it comes to financial services such as loans, debt collection and mortgages. We want to help our citizens become more aware of the financial options and services that are available to them, and what better way than to connect the City's 3-1-1 system with the CFPB." At the Conference of Mayors in January, Cordray announced a goal to have as many mayors and cities as possible join the 3-1-1 pilot partnership by July 2014. In sum, the CFPB is not only making it easy for borrowers to contact it, it is embedding itself in cities across the nation.

Second, Cordray touted the ease and simplicity of filing a consumer complaint online at consumerfinance.gov or by calling the CFPB's toll-free hotline. According to Cordray, even "more intricate" consumer complaints should not take more than 30 minutes to submit. After a consumer submits a complaint, the CFPB reviews it and contacts the complained-about company in order to address the issue. More about how the CFPB brings complaints to mortgage servicers is here. Interestingly, Cordray notes that a large majority of the 270,000 complaints it has received from customers are mortgage-related. Specifically, the CFPB has received 109,000 complaints about mortgage products, compared to 27,000 complaints about credit reporting and 31,000 about debt collection.

Since the most complaints received by the CFPB relate to mortgage loan products, the CFPB's efforts to become entrenched in everyday American society is perceived to pose a particular threat to mortgage servicers and their ilk. Servicers are wise to keep abreast of the CFPB's actions and regulations because it is easier than ever for consumers to lodge complaints and, potentially, lawsuits.

Fidelity Mortgage Consent Order Sends Strong Message the CFPB Will Enforce Laws, No Matter Size of Violator

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On January 16, 2014, the CFPB issued a Consent Order resolving a claim that Fidelity Mortgage Corporation (Fidelity), a mortgage lender, and its president, Mark Figert, violated RESPA Section 8 by paying illegal kickbacks to a bank in exchange for mortgage loan referrals.

The CFPB found that Fidelity entered into an agreement with a bank in which the bank referred borrowers to Fidelity in exchange for kickbacks disguised as payments made by the lender for renting office space within the bank. Fidelity's president was determined to be a "related person" under the Consumer Financial Protection Act because he had managerial responsibility for Fidelity and materially participated in the conduct of its affairs.

According to the Consent Order, Fidelity's monthly rental payments averaged $1,350 per month compared to market rent of $600-$900 per month for similar bank office space. RESPA Section 8(a) prohibits the payment of any "fee, kickback, or thing of value" in exchange for a referral of business related to a real estate settlement services. 12 U.S.C. § 2607(a). RESPA's implementing regulations provide that "when a thing of value...is connected in any way with the volume or value of the business referred," it is evidence that it was given in exchange "for the referral of business." 12 C.F.R. § 1024.14(e). Section 8(c) of RESPA lists exemptions to the prohibitions, including one that permits "payment for goods or facilities actually furnished or for services actually performed." 12 U.S.C. § 2607(c)(2). The Consent Order references a 1996 Housing and Urban Development (HUD) policy statement that analyzed this exemption in the context of office-rental agreements. The policy statement concluded that in determining whether rent payments were disguised referral fees, HUD would look at the general market value of the rental property, not its value to a settlement service provider. As discussed above, the CFPB found that the average monthly rent paid by Fidelity was substantially more than comparable monthly rents and thus violated Section 8(a) of RESPA.

The Consent Order required Fidelity and Mark Figert to pay $27,076 as disgorgement of origination fees Fidelity collected from loans referred by the bank during the relevant period, plus a $54,000 civil penalty paid to the CFPB.

This Consent Order signals that the CFPB is taking a strong stand in investigating and enforcing possible consumer law violations regardless of the size of the financial institution. It also demonstrates that the CFPB will bring actions against individuals, as well as financial institutions.