

Payday Lending May Face Greater CFPB Scrutiny Under Biden

By Katherine Kirkpatrick, Andrew Michaelson and Steven Miller

Law360 (February 8, 2021, 12:32 PM EST) -- With the change of administration in Washington, the Consumer Financial Protection Bureau is widely expected to assume a posture of aggressive enforcement of consumer protection laws. One area that we anticipate will receive heightened scrutiny is payday lending, a form of lending that typically involves small, short-term loans at high interest rates.

Under new leadership, the CFPB may seek to require that payday lenders assess a borrower's ability to pay. And even absent such a requirement, the CFPB may pursue enforcement actions against lenders for lending that the CFPB considers predatory or unfair, and therefore putatively in violation of the Consumer Financial Protection Act.

Banks and other financial institutions operating in the payday loan space should closely monitor the bureau's approach to payday lending and evaluate current business practices against this changing regulatory landscape. In particular, they should focus on supporting and documenting the reasonableness of credit extended to consumers affected by the COVID-19 pandemic.

Some reports have suggested that searches for payday loans increased around July 2020, when expanded unemployment benefits under the Coronavirus Aid, Relief and Economic Security Act ended. We anticipate that the CFPB will look closely at lending to retail consumers affected by the pandemic.[1]

Background on the CFPB's Payday Loan Rules

The rules governing payday loans and other forms of short-term lending have long been a focus for the CFPB. Established under Title X of the Dodd-Frank Act in 2010, the bureau has authority to investigate, and file federal complaints against, financial institutions offering products to consumers that are unfair, deceptive or abusive.[2]

Pursuant to this authority, the CFPB has, from its earliest days, focused attention on payday lenders.[3] The bureau began to consider rules specific to short-term lending shortly after it was created, though the CFPB did not issue its first proposed rule on short-term



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loans until June 2016. That proposed rule was aimed at payday loans, auto title loans, deposit advances and other products that were, according to the CFPB, "aimed at financially vulnerable consumers."^[4]

In October 2017, toward the very end of President Barack Obama-appointed Director Richard Cordray's tenure at the bureau, the CFPB issued a final rule on the subject.^[5] The 2017 rule prohibited lenders from attempting to debit borrowers' accounts after two consecutive attempts had failed.^[6]

The 2017 rule also contained mandatory underwriting provisions that required lenders to determine whether borrowers had the ability to repay their loans. These provisions applied to various types of short-term loans with repayment terms of 45 days or less, as well as longer-term loans with a balloon payment — a one-time payment at the end of the loan term that is generally more than two times the average monthly loan payment.^[7]

The mandatory underwriting provisions contained in the 2017 rule prohibited lenders from providing covered loans without first making a reasonable determination of a borrower's ability to repay those loans.^[8]

These provisions purported to require lenders to take various steps to determine a borrower's ability to repay the loan, including:

- Obtaining a written statement from the consumer about that consumer's net income and the amount of payments required to meet their financial obligations;
- Verifying the consumer's net monthly income and the amount of payments required for the consumer's major debt obligations;
- Determining a consumer's ability to repay the loan by projecting either the consumer's residual income or debt-to-income ratio during the calendar month with the highest payment(s) under the loan; and
- Ensuring that the loan would not result in the consumer having a sequence of more than three covered short-term or balloon payment loans taken out within 30 days of each other.^[9]

The 2017 rule became effective on Jan. 16, 2018, while most of its provisions had a compliance date of Aug. 19, 2019.^[10] However, after President Donald Trump appointed Director Kathy Kraninger — who resigned after President Joe Biden's inauguration — the CFPB officially delayed the compliance date for the 2017 rule's mandatory underwriting provisions to Nov. 19, 2020, while the bureau considered comments on a proposal to ultimately rescind them.^[11]

The CFPB rescinded the mandatory underwriting provisions when it issued a new final rule in July 2020. In announcing the rule, the CFPB argued that the 2017 rule's mandatory underwriting provisions lacked sufficient legal and evidentiary bases, and that revoking the provisions "ensures that consumers have access to credit and competition" in states that allow small dollar lending.^[12] The 2020 rule also revoked other sections from the 2017 rule.^[13]

However, the 2020 rule ratified the 2017 rule's payment provisions that prohibit lenders from making new attempts to debit funds after two consecutive attempts have failed, unless the consumer consents to further withdrawals.^[14] The payment provisions also require lenders to provide consumers with

written notice before making their first attempt to withdraw payment and before subsequent attempts that involve different dates, amounts, or payment channels.[15]

Current Legal Challenges to the Payday Loan Rules

There are currently at least two competing federal court challenges to the CFPB's payday loan rule, one challenging the constitutionality of the 2017 rule and another seeking to reinstate the mandatory underwriting provisions to the 2020 rule. Back in 2018, two trade groups sued the CFPB in the U.S. District Court for the Western District of Texas, asserting that the 2017 rule is unconstitutional, and that the payment provisions are arbitrary and capricious.[16]

On Nov. 6, 2018, the court stayed the 2017 rule's Aug. 19, 2019, compliance date, which was subsequently pushed back under Kraninger.[17] In an amended complaint filed in August 2020, the plaintiffs argued that the entire 2017 rule was invalid when adopted because the U.S. Supreme Court found that the CFPB director was unconstitutionally insulated from removal by the president.[18]

They further argued that the 2020 rule's ratification of the payment provisions without notice-and-comment rulemaking was legally insufficient to make those provisions effective and cure the 2017 rule's constitutional defects.[19]

The plaintiffs further assert that the 2017 rule contained "draconian ability-to-repay provisions" and that because the payment provisions placed unwarranted limits on consumers' ability to preauthorize payments from their bank accounts, consumers would face greater risks of late-payment fees and loan defaults.[20] The parties recently completed briefing on motions and cross-motions for summary judgment, and a ruling from the court is forthcoming.

Separately, in October 2020, the National Association for Latino Community Asset Builders sued the CFPB in the U.S. District Court for the District of Columbia to try to overturn the 2020 rule's revocation of the mandatory underwriting provisions.[21] Among other arguments, the group alleges that no-underwriting lending is harmful to consumers, and the CFPB's requirement of "robust and reliable"[22] evidence for determining whether consumers can reasonably avoid the harms of no-underwriting lending is unfair, abusive, and unreasonably favors the industry over consumers.[23]

The resolution of these lawsuits, which address both the payment provisions and the mandatory underwriting provisions, may affect the regulatory landscape and could embolden, or chasten, the bureau's enforcement efforts in this space.

Renewed Focus on Payday Lending, Including by Large Financial Institutions

Biden has nominated Rohit Chopra, currently a member of the Federal Trade Commission, to be the CFPB's next director.[24] During the Obama administration, Chopra served at the bureau as an assistant director and as student loan ombudsman, a watchdog role in which he was known for publicly pushing lenders on their treatment of student borrowers.[25]

Based on his previous experience at the bureau and his current post at the FTC, observers agree that Chopra's nomination likely means that the CFPB's priorities will be moving to a more active and aggressive posture. At the FTC, Chopra has been known for favoring tougher enforcement actions and encouraging the commission to provide stronger consumer protections through more aggressive rulemaking.[26]

In the payday lending space, the new director could make it a priority to revise the 2020 rule on short term lending in order to reincorporate the mandatory underwriting provisions from the 2017 rule.[27] But even without the mandatory underwriting provisions, the bureau may pursue payday lenders on a case-by-case basis for lending practices that it considers to be predatory or unfair.

Under Cordray, the CFPB asserted that payday lenders' practices harmed consumers in numerous ways, including: debiting consumers' bank accounts without their express, informed consent; lying about consumers' rights; threatening to report consumers to credit reporting agencies; and deceiving consumers with false threats of legal action.[28]

Depending on the facts and circumstances, the bureau could — as it did under Cordray — bring enforcement actions against payday lenders for unfair practices in violation of the CFPB.

Notably, in the wake of the COVID-19 pandemic, Sens. Elizabeth Warren, D-Mass., and Sherrod Brown, D-Ohio,, articulated a need to "prohibit debt collectors from using predatory and intrusive measures" during the pandemic and criticized the CFPB for "enabling" predatory lending.[29]

These statements suggest that the bureau, under the Biden administration, may focus its enforcement efforts on creditors that have extended loans on terms it deems unfavorable to consumers directly affected by the pandemic.

Furthermore, under the Biden administration, the bureau is expected to widen the lens of its enforcement program. Whereas in recent years the bureau's payday loan enforcement efforts have focused on smaller lenders, going forward, the bureau will likely take a careful look at larger financial institutions involved in short-term lending.

Conclusion

For financial services companies involved in any form of payday lending, now is the time to consider the following:

- State of compliance with the payment provisions contained in the bureau's 2020 rule, which is currently stayed pending litigation in the Western District of Texas;
- The extent to which current practices involve a determination of the borrower's ability to repay, given the potential for renewed rulemaking and likelihood of heightened enforcement scrutiny of practices that may be considered predatory and/or unfair;
- Reasonableness of terms and disclosures to consumers affected by the pandemic;
- Consumer complaints concerning payday lending terms and operations; and
- Reviewing lending practices to assess whether any programs or conditions could be considered unfair, even if the programs are accurately described and represented to consumers.

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[1] See Emily Stewart, Americans are falling through the safety net. The government is helping predatory lenders instead, Vox.com (Aug. 26, 2020), <https://www.vox.com/policy-and-politics/2020/8/26/21401493/payday-loans-cfpb-occ-fdic-rent-bank-covid-19>.

[2] 12 USC §§ 5531, 5561-64. § 5531 defines an act or practice as unfair if it causes or is likely to cause consumers substantial injury that they cannot reasonably avoid, and that injury is not outweighed by the benefits to consumers or competition.

[3] See, e.g., CFPB Takes Action Against ACE Cash Express for Pushing Payday Borrowers Into Cycle of Debt, CFPB Press Release (July 10, 2014), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-ace-cash-express-for-pushing-payday-borrowers-into-cycle-of-debt/>.

[4] Consumer Financial Protection Bureau Proposes Rule to End Payday Debt Traps, CFPB Press Release (June 2, 2016), https://files.consumerfinance.gov/f/documents/CFPB_Proposes_Rule_End_Payday_Debt_Traps.pdf.

[5] Executive Summary of the Payday, Vehicle Title, and Certain High-Cost Installment Loans Rule, CFPB Press Release (Oct. 5, 2017), https://files.consumerfinance.gov/f/documents/201710_cfpb_executive-summary_payday-loans-rule.pdf.

[6] 12 CFR § 1041.8.

[7] 12 CFR § 1041.3 defines a covered loan as "closed-end or open-end credit that is extended to a consumer primarily for personal, family, or household purposes" that are not excluded under the section. Certain types of credit are excluded from the definition of covered loans in § 1041(d), including real estate secured credit, credit cards, student loans, wage advance programs, and non-recourse pawn loans.

[8] 12 CFR § 1041.5(b).

[9] Executive Summary of the Payday, Vehicle Title, and Certain High-Cost Installment Loans Rule at 4.

[10] CFPB Statement on Payday Rule, CFPB Press Release (Jan. 16, 2018), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-statement-payday-rule/>.

[11] Executive Summary of Delay Final Rule's Amendments to the 2017 Payday Lending Rule, CFPB Press

Release (June 6, 2019), https://files.consumerfinance.gov/f/documents/201906_cfpb_executive-summary_payday-delay-final-rule.pdf.

[12] Consumer Financial Protection Bureau Issues Final Rule on Small Dollar Lending, CFPB Press Release (July 7, 2020), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-issues-final-rule-small-dollar-lending/>.

[13] The 2020 Rule specifically revoked: § 1041.4 identifying an unfair and abusive practice; § 1041.5 governing the ability-to-repay determination; § 1041.6 providing a conditional exemption from §§ 1041.4 and 1041.5 for certain covered short-term loans; § 1041.10 governing information furnishing requirements; § 1041.11 regarding registered information systems; § 1041.12(b)(2) and (3) detailing record retention requirements that are specific to the mandatory underwriting provisions; and § 1041.15(d) identifying November 19, 2020 as the compliance date for the mandatory underwriting provisions.

[14] Payday, Vehicle Title, and Certain High-Cost Installment Loans; Ratification of Payment Provisions, 85 Fed. Reg. 41905 (July 13, 2020). The CFPB ratified the payment provisions in light of the Supreme Court's order in *Seila Law*, which found that the clause that required cause to remove the CFPB director was unconstitutional, but this was severable from the statute establishing the Bureau itself. *Seila Law LLC v. CFPB*, 140 S. Ct. 2183, 2192 (2020). And although the 2020 Rule's compliance date was stayed at that time because of the litigation in the Western District of Texas, the Bureau said it "will seek to have [the payment provisions] go into effect with a reasonable period for entities to come into compliance." See, Consumer Financial Protection Bureau Issues Final Rule on Small Dollar Lending.

[15] Consumer Financial Protection Bureau Issues Final Rule on Small Dollar Lending.

[16] *Comty Fin. Serv. Assoc. of Am., Ltd. et al v. CFPB et al*, No. 1:18-cv-00295 (W.D. Tex. Aug. 28, 2020), ECF No. 1 at 34.

[17] *Id.*, ECF No. 53. The court again extended the stay of the compliance date on May 14, 2020. See *Id.*, ECF No. 70.

[18] *Id.*, ECF No. 76 at 3.

[19] *Id.* at 3-4.

[20] *Id.* at 2.

[21] *Nat'l Assoc. for Latino Comty Asset Builders v. CFPB*, No. 1:20-cv-03122 (D.D.C. Oct. 29, 2020), ECF No. 1.

[22] The CFPB stated that it chose this standard of evidence for determining whether consumers could reasonably avoid injury from loans covered under the rule. According to the Bureau, the "measure of whether evidence is robust and reliable is whether, as a practical matter, the evidence gives the Bureau a level of confidence in the Bureau's conclusion that is commensurate with the dramatic impacts on consumer choice and access to credit that are at stake here." *Payday, Vehicle Title, and Certain High-Cost Installment Loans*, 85 Fed. Reg. 44382, 44400 (July 22, 2020).

[23] *Nat'l Assoc. for Latino Comty Asset Builders*, ECF No. 1 at 23.

[24] Tyler Pager, Zachary Warmbrodt, Katy O'Donnell, and Lead Nylen, Biden taps Warren ally Chopra to lead Consumer Bureau, Politico (Jan. 17, 2021), <https://www.politico.com/news/2021/01/17/biden-rohit-chopra-consumer-bureau-460086>.

[25] Andrew Ackerman and Andrew Restuccia, Biden to Pick Chopra to Lead Consumer-Finance Agency, Wall Street Journal (Jan. 18, 2021), <https://www.wsj.com/articles/biden-expected-to-nominate-rohit-chopra-to-head-consumer-financial-protection-bureau-11610933184>.

[26] Id.; see also Pager, Warmbrodt, O'Donnell, and Nylen, Biden taps Warren ally Chopra to lead Consumer Bureau.

[27] Robert Schmidt & Jesse Hamilton, Wall Street Frets Over a Revived CFPB Trump Left Toothless, Bloomberg (Dec. 7, 2020), <https://www.bloomberg.com/news/articles/2020-12-08/wall-street-frets-over-a-revival-of-cfpb-left-toothless-by-trump>.

[28] See, e.g., CFPB Takes Action Against ACE Cash Express for Pushing Payday Borrowers Into Cycle of Debt, CFPB Press Release (July 10, 2014), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-ace-cash-express-for-pushing-payday-borrowers-into-cycle-of-debt/>; Consumer Financial Protection Bureau Takes Action Against Payday Lender For Robo-Signing, CFPB Press Release (Nov. 20, 2013), <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-takes-action-against-payday-lender-for-robo-signing/>; and CFPB Orders EZCORP to Pay \$10 Million for Illegal Debt Collection Tactics, CFPB Press Release (Apr. 21, 2020), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-ezcorp-to-pay-10-million-for-illegal-debt-collection-tactics/>.

[29] Senators Elizabeth Warren and Sherrod Brown, Congress must provide immediate relief for consumers. Here's how., Medium (Apr. 21, 2020), <https://medium.com/@SenWarren/congress-must-provide-immediate-relief-for-consumers-heres-how-2aeb99672ef9>.