

Tik Tok: The Compliance Clock Is Ticking for Small-Dollar Lenders in 2020

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INTRODUCTION

Small-dollar lenders waited through most of 2020 for the Consumer Financial Protection Bureau's ("CFPB's") final rulemaking addressing payday, vehicle title, and certain high-cost installment loans. Meanwhile, the CFPB, the Federal Trade Commission ("FTC"), and various states continued to take action to curtail certain practices. This survey addresses compliance issues related to the small-dollar lending industry over the past year, including federal rulemaking, federal and state enforcement actions, significant court decisions, and state legislation.

FEDERAL RULEMAKING

SMALL-DOLLAR RULEMAKING

In July 2020, the CFPB ratified the payment provisions included in the 2017 final rule governing Payday, Vehicle Title, and Certain High-Cost Installment Loans,¹ rescinding the ability-to-repay provisions of that rulemaking.² The payment provisions prohibit certain conduct, require notices to consumers in certain instances, and regulate how small-dollar lenders making covered loans obtain payment transfers from borrowers.³ At the time of this writing, the U.S. District

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1. Payday, Vehicle Title, and Certain High-Cost Installment Loans; Ratification of Payment Provisions, 85 Fed. Reg. 41905 (July 13, 2020).

2. Payday, Vehicle Title, and Certain High-Cost Installment Loans, 85 Fed. Reg. 44382 (July 22, 2020).

3. See 12 C.F.R. § 1041.7–9 (2020); Justin B. Hosie, K. Dailey Wilson & Erica A.N. Kramer, *Stranger Things: Small-Dollar Lending Updates and the Arrival of a Final Rule*, 73 BUS. LAW. 525, 525–27 (2018) (in the 2018 Annual Survey).

Court for the Western District of Texas has stayed the rulemaking's compliance date in connection with a pending case between the CFPB and trade groups.⁴

NATIONAL CREDIT UNION ADMINISTRATION PAL RULEMAKING

In October 2019, the National Credit Union Administration ("NCUA") Board issued a final rule allowing federal credit unions to offer additional payday alternative loans to their members ("PAL II Rule").⁵ The PAL II Rule grants federal credit unions flexibility to offer members alternatives to traditional payday loans, while maintaining certain key structural safeguards for such loans.⁶ The PAL II Rule allows federal credit unions to offer a loan to a member of any amount, up to a maximum of \$2,000.⁷ The loans must have a minimum term of one month and a maximum term of twelve months.⁸ A federal credit union is permitted to offer only one type of payday alternative loan at any given time.⁹ In addition, other requirements and restrictions apply, including prohibitions against rollovers, a limitation on the number of payday alternative loans that may be made to a single borrower in a given period, and a requirement that each loan fully amortize over its life.¹⁰ The PAL II Rule also prohibits federal credit unions from charging nonsufficient funds fees, including fees that could be assessed against the member for paying items that are presented for payment after the loan payment causes a negative balance in the member's account.¹¹ The PAL II Rule became effective on December 2, 2019.¹²

FEDERAL ENFORCEMENT ACTIONS

In addition to its rulemaking activities on small-dollar lending, the CFPB was also active on the enforcement front during the past year. On April 1, 2020, the CFPB issued a consent order against Cottonwood Financial, Ltd., d/b/a Cash Store ("Cash Store"), alleging violations of the Consumer Financial Protection Act ("CFPA"), the Fair Credit Reporting Act ("FCRA"), and the Truth in Lending Act ("TILA"), based on Cash Store's collections and marketing of consumer loans.¹³ The consent order states that Cash Store's television advertisements provided consumers could save 50 percent on finance charges. However, consumers actually paid all finance charges in full and only saved 50 percent on the first

4. Order at 2-3, *Cmty. Fin. Servs. Ass'n of Am. Ltd. v. Consumer Fin. Prot. Bureau*, No. 1:18-CV-0295-LY (W.D. Tex. Nov. 6, 2018), <https://www.cfsaa.com/files/files/rulestaynov2018.pdf>.

5. Payday Alternative Loans, 84 Fed. Reg. 51942 (Oct. 1, 2019).

6. *Id.*

7. *Id.* at 51944.

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.*

12. *Id.* at 51942.

13. Consent Order, Cottonwood Fin. Ltd., CFPB No. 2020-BCFP-0001 (Apr. 1, 2020), https://files.consumerfinance.gov/f/documents/cfpb_cottonwood-financial_consent-order_2020-04.pdf.

finance charge via a rebate.¹⁴ In addition, telemarketing calls promoting the 50 percent discount failed to explain the limitations of the discount.¹⁵ The CFPB found that the advertisements and associated telemarketing calls were deceptive.¹⁶

The CFPB also alleged that Cash Store made numerous collections calls, sometimes more than fifteen times in one day, to customers and their references (employers, family members, and other third parties).¹⁷ The CFPB claimed that Cash Store continued this practice even when customers and references asked them to stop and shared information about delinquent debts with third parties.¹⁸ The CFPB considered these actions to be unfair acts likely to cause substantial injury to consumers.¹⁹

The CFPB also alleged violations of the FCRA and Regulation V based on Cash Store's failure to maintain reasonable written policies and procedures concerning the consumer information furnished to credit reporting agencies and failure to provide the Annual Percentage Rate when discussing the costs of loans during telemarketing calls.²⁰ Along with conduct provisions and a compliance plan, the consent order required Cash Store to pay \$286,675.64 in consumer compensation and a civil penalty of \$1,100,000.²¹

In February 2020, the CFPB joined with the South Carolina Department of Consumer Affairs and the Arkansas Attorney General to sue Candy Kern-Fuller, Howard Sutter III, and Upstate Law Group LLC (collectively, "Upstate").²² Upstate worked with a series of companies brokering high-interest credit primarily to disabled veterans ("broker companies").²³ The broker companies purchased servicemembers' future pension and disability payments for a lump sum. The servicemembers were then required to repay a much larger amount.²⁴ Consumers were told that the product was not a loan, but the CFPB alleged that the substance of the transaction was an offer of credit because the servicemembers' creditworthiness was assessed and payments were due on a monthly basis.²⁵ According to the CFPB, this was a usurious and deceptive offer of credit and an unlawful assignment of federal servicemember benefits.²⁶

The CFPB alleged that Upstate repeatedly misrepresented to consumers that the contracts were valid and enforceable, even though they were not under federal law.²⁷ The CFPB claimed that Upstate knew or should have known that the

14. *Id.* at 7.

15. *Id.* at 8.

16. *Id.* at 8–9.

17. *Id.* at 5.

18. *Id.* at 5–6.

19. *Id.* at 6–7.

20. *Id.* at 10–11.

21. *Id.* at 11, 14, 16.

22. Complaint, CFPB v. Kern-Fuller, No. 6:20-cv-00786-DCC (D.S.C. Feb. 20, 2020), https://files.consumerfinance.gov/f/documents/cfpb_kern-fuller_stamped-complaint_2020-02.pdf.

23. *Id.* at 4.

24. *Id.*

25. *Id.* at 5–6.

26. *Id.* at 9, 13.

27. *Id.* at 9–10.

contracts were illegal and void from inception, that they were not sales but high-interest credit offers, and that they carried an interest rate, but that the broker companies did not disclose any interest rate to consumers.²⁸ The civil action was pending in federal district court at the time of this writing.

After more than two years of litigation and amidst a bankruptcy filing, the CFPB settled its case against Think Finance, Inc., and six subsidiaries (collectively, “Think Finance”).²⁹ The CFPB’s complaint alleged violations of the CFPA based largely on the illegal collection of void loans made in collaboration with tribal lenders.³⁰

The consent order, filed in February 2020, prohibited Think Finance from offering or collecting on loans if the loan violates state lending laws and from assisting others in engaging in that conduct.³¹ Interestingly, the consent order imposed only a \$1 fine per entity, for a total fine of \$7.³² However, under a consumer class action settlement, Think Finance must distribute consumer redress from a fund likely to have over \$39 million in it.³³ The Think Finance bankruptcy resolution incorporates the CFPB’s consent order, as well as a settlement with the Pennsylvania Attorney General discussed below and the consumer class action.³⁴

STATE ENFORCEMENT ACTIONS

In January 2020, LendingClub Corporation agreed to a \$1.25 million settlement with the Massachusetts Attorney General.³⁵ The attorney general alleged that LendingClub facilitated loans to Massachusetts residents with a “face amount” of more than \$6,000. However, because of an origination fee charged on the loans, the actual amount the borrowers received was \$6,000 or less.³⁶ Because the borrowers received \$6,000 or less from the loans, the attorney general asserted that the loans were subject to the Massachusetts Small Loan Statute.³⁷ As a result, the attorney general alleged that LendingClub facilitated small loans to Massachusetts residents without a license, and that, once LendingClub

28. *Id.* at 10–13.

29. Stipulated Final Consent Order, CFPB v. Think Fin., Inc., No. 4:17-cv-00127-BMM (D. Mont. Feb. 5, 2020), https://files.consumerfinance.gov/f/documents/cfpb_think-finance_stipulated-final-consent-order_2020-02.pdf.

30. *Id.*

31. *Id.* at 4–5.

32. *Id.* at 6.

33. See Settlement Agreement, Gibbs v. Plain Green, LLC, No. 3:17-cv-00495-MHL (E.D. Va. July 10, 2019), <https://www.thinkfinancesettlement.com/pdf/Settlement%20Agreement.pdf>.

34. See Findings of Fact and Conclusions of Law and Order Confirming the Second Modified First Amended Chapter 11 Plan of Reorganization of Think Finance, LLC and Its Subsidiary Debtors and Debtors in Possession, *In re* Think Fin., LLC, No. 3:17-bk-33964-hdh11 (Bankr. N.D. Tex. Dec. 5, 2019), <https://www.txnb.uscourts.gov/sites/txnb/files/opinions/17-33964%20Think%20Finance.pdf>.

35. Assurance of Discontinuance, *In re* LendingClub Corp., No. 20-0155C (Mass. Super. Ct. Jan. 17, 2020), <https://www.mass.gov/doc/lending-club-aod/download>.

36. *Id.* at 8.

37. *Id.*

obtained the small loan license, it facilitated loans with an annual percentage rate in excess of the state maximum rate.³⁸

In January 2020, Approved Financial, Inc., a Florida payday lender, settled with the North Carolina Attorney General.³⁹ The settlement resolved allegations that Approved made vehicle-title-secured consumer loans over the internet to North Carolina residents that exceeded the interest rates permitted by North Carolina law, violating the state's Consumer Finance Act.⁴⁰ Under the settlement, all loans made to North Carolina borrowers were deemed forgiven, Approved released all existing liens placed on North Carolina borrowers' vehicles, and Approved returned any vehicles repossessed but not yet sold.⁴¹ In addition, Approved agreed to pay over \$480,000 in consumer restitution and \$30,000 in attorney's fees and other costs to the state.⁴²

TitleMax of Nevada, Inc., a vehicle title lender, petitioned for judicial review of a disciplinary action from the Financial Institutions Division of the Nevada Department of Business and Industry.⁴³ Nevada law restricts the duration of title loans to either a thirty-day loan that may be extended up to six times in thirty-day increments, or to a 210-day loan.⁴⁴ A 210-day loan must be fully amortizing and cannot be extended, though a grace period with no additional interest is permitted in connection with such loans.⁴⁵ The Supreme Court of Nevada affirmed the administrative law judge's decision that TitleMax's Grace Period Payment Deferral Agreement, which the company marketed as an amendment and modification of its 210-day title loans, required borrowers to make unamortized and additional interest payments and extended the duration of the borrowers' loans in violation of Nevada law.⁴⁶ However, the court also held that TitleMax's violations were not "willful" because its interpretation of the state's title lending statutes was reasonable. TitleMax was therefore not subject to statutory penalties that would have provided that it was prohibited from recovering principal, interest, or other fees in connection with the loans.⁴⁷

In August 2019, the New York Department of Financial Services announced a multistate investigation of the payroll advance industry, alleging potential violations by the industry of state usury limits, licensing laws, consumer protection laws, and other state laws regulating payday lending.⁴⁸ The investigation focused

38. *Id.* at 9.

39. Consent Judgment, North Carolina *ex rel.* Stein v. Approved Fin., Inc., No. 19CVS006382 (Wake Cnty. Super. Ct. Jan. 24, 2020), <https://ncdoj.gov/wp-content/uploads/2020/01/ApprovedFinancialConsentJudgment.pdf>.

40. *Id.* at 2.

41. *Id.* at 4–5.

42. *Id.* at 6–7.

43. Nev. Dep't of Bus. & Indus. v. TitleMax of Nev., Inc., 449 P.3d 835, 836 (Nev. 2019).

44. *Id.*

45. *Id.*

46. *Id.*

47. *Id.* at 841–43.

48. Press Release, N.Y. State Dep't of Fin. Servs., Superintendent of Financial Services Linda A. Lacewell Leads Multistate Investigation of the Payroll Advance Industry (Aug. 6, 2019), https://www.dfs.ny.gov/reports_and_publications/press_releases/pr1908061.

on providers who offer consumers access to earned wages prior to the payroll and, in particular, those who collect “tips,” monthly membership fees, or other fees from such consumers, or who charge overdraft charges in connection with such transactions.⁴⁹ Eleven other jurisdictions joined New York in the investigation.⁵⁰

In July 2019, the Pennsylvania Attorney General entered into a settlement with payday lender Think Finance, LLC.⁵¹ The settlement stemmed from allegations that Think Finance solicited, arranged, funded, purchased, serviced, and/or collected unlicensed loans or cash advances made to Pennsylvania citizens over the internet that exceeded the state’s usury cap, and engaged in other types of unfair, deceptive, and abusive conduct related to the loans.⁵² The Pennsylvania Attorney General further asserted that to evade licensure, Think Finance affiliated with Native American tribes and banks.⁵³ The state alleged that Think Finance’s actions violated Pennsylvania’s Corrupt Organizations Act, its Unfair Trade Practices and Consumer Protection Law, its Fair Credit Extension Uniformity Act, and the CFPA.⁵⁴ Among the relief provided in the settlement, Think Finance, which declared bankruptcy during the proceedings, agreed to repay Pennsylvania consumers for a portion of the interest paid on loans with Think Finance, to void loans to Pennsylvania borrowers, and not to conduct further business in Pennsylvania.⁵⁵

OTHER CONSUMER LITIGATION

The U.S. Bankruptcy Court for the Middle District of Alabama tackled the issue of sufficient possession in an Alabama pawn transaction.⁵⁶ Two individuals entered into pawn transactions with TitleMax, providing TitleMax with certificates of title to their cars and identifying TitleMax as the only lienholder.⁵⁷ The individuals filed bankruptcy petitions and TitleMax objected to confirmation of the plans.⁵⁸ Among other defenses, the individuals argued that the pawn transactions were invalid because TitleMax failed to take possession of endorsed certificates of title and keys to the vehicles.⁵⁹ The court disagreed and

49. *Id.*

50. *Id.* The other jurisdictions joining the investigation are Connecticut, Illinois, Maryland, New Jersey, North Carolina, North Dakota, Oklahoma, Puerto Rico, South Carolina, South Dakota, and Texas.

51. Notice of Settlement, *Pennsylvania v. Think Fin., Inc.*, No. 2:14-cv-07139-JCJ (E.D. Pa. July 23, 2020).

52. First Amended Complaint at 1, *Pennsylvania v. Think Fin., Inc.*, No. 2:14-cv-07139-JCJ (E.D. Pa. July 6, 2015).

53. *Id.* at 2.

54. *Id.* at 5.

55. Stipulation of Settlement Between the Plaintiff Commonwealth of Pennsylvania and the Think Finance Defendants at 7, *Pennsylvania v. Think Fin., Inc.*, No. 2:14-cv-07139-JCJ (E.D. Pa. Feb. 6, 2020).

56. *In re Thompson*, No. 2:18-bk-32609, 2019 Bankr. LEXIS 3328 (Bankr. M.D. Ala. Oct. 24, 2019).

57. *Id.* at *2, *5.

58. *Id.*

59. *Id.* at *7.

found that TitleMax's possession of the vehicles' certificates of title naming it as lienholder was sufficient to create a transaction under the Pawnshop Act.⁶⁰

Unconscionability again made headlines in a California court case.⁶¹ In *In re Donahue*, a California consumer obtained a \$4,000 line of credit with an interest rate of 240 percent per annum and the right to rescind advances from Gaia Finance, LLC.⁶² After consummation of the agreement, Gaia wired Donohue the full \$4,000, allegedly without Donohue's direction.⁶³ Donohue later filed bankruptcy and Gaia filed a proof of claim for the \$4,000 advance as well as accrued interest.⁶⁴ Donohue objected, alleging that the 240 percent interest rate was unconscionable.⁶⁵ The U.S. Bankruptcy Court for the Northern District of California agreed, finding that the loan was procedurally unconscionable because Gaia took advantage of Donohue's severe financial distress by wiring Donohue the full \$4,000 without asking.⁶⁶ The court also found that the 240 percent interest rate was substantively unconscionable.⁶⁷ The court ordered Gaia to file an amended proof of claim with an interest rate of 100 percent or less.⁶⁸

STATE LEGISLATIVE AND REGULATORY ACTIVITY

Two states on opposite sides of the country passed legislation and introduced regulations in the past year that affected each state's small-dollar lending landscape. In Virginia, the Virginia Fairness in Lending Act⁶⁹ significantly altered the consumer lending landscape in the Commonwealth. Most notably, the Act imposed a 36 percent annual interest rate cap on consumer loans of \$300 to \$35,000, short-term loans, formerly known as "payday loans," and motor vehicle title loans.⁷⁰ In addition to the name change and the interest rate cap, the Act increased the maximum amount of short-term loans from \$200 to \$2,500, and required lenders to make a reasonable ability-to-repay determination.⁷¹ The Act also increased the maximum amount cap for motor vehicle title loans.⁷² The Act became effective on January 1, 2021.

California legislation also imposed a rate cap on certain types of loans. The Fair Access to Credit Act⁷³ capped charges on loans of \$2,500 to \$10,000

60. *Id.* at *12–13.

61. See *In re Donohue*, No. 4:19-bk-41271, 2020 Bankr. LEXIS 196 (Bankr. N.D. Cal. Jan. 27, 2020); see also Justin B. Hosie, K. Dailey Wilson, Erica A.N. Kramer & Christopher J. Capurso, *Small-Dollar Lending Regulation in 2019*, 75 BUS. LAW. 2025, 2029–30 (2020) (in the 2020 Annual Survey).

62. *In re Donohue*, 2020 Bankr. LEXIS 196, at *1–2.

63. *Id.*

64. *Id.* at *1.

65. *Id.* at *3.

66. *Id.* at *7.

67. *Id.* at *8.

68. *Id.* at *9.

69. H.B. 789, 2020 Leg., Reg. Sess. (Va. 2020).

70. Act of Apr. 22, 2020, ch. 1215, 2020 Va. Laws 1215.

71. *Id.*

72. *Id.*

73. A.B. 539, 2019 Leg., Reg. Sess. (Cal. 2019).

made by Consumer Finance Act licensees at an annual interest rate of 36 percent, plus the Federal Funds Rate.⁷⁴

State legislators and regulators in other parts of the country were also active over the past year. The Kentucky Department of Financial Institutions finalized regulations concerning the use of the state's deferred deposit database by deferred deposit service business licensees.⁷⁵ The regulations require licensees to, among other things, maintain a record of all current transactions and to check the record of current transactions so as not to have more than two deferred deposit transactions with any one consumer at any one time in violation of Kentucky law.⁷⁶

In Oregon, legislation⁷⁷ permitted pawnbrokers to store large items off-premises from the business location if the parties agree in writing to such storage and if the off-premises storage site complies with the requirements for pawnbroker business locations.⁷⁸ The Oregon Department of Consumer and Business Services defined a "large item" to mean boats, snowmobiles, trailers, all-terrain vehicles, or an item that a pawnshop would normally prefer to store off-premises due to its size, shape, or weight.⁷⁹

In June 2020, the Georgia legislature passed significant changes to what was previously known as the Georgia Industrial Loan Act, which became effective on July 1, 2020.⁸⁰ Prior to this legislation, those making loans of \$3,000 or less with interest rates of 8 percent or less were exempt from the Act.⁸¹ With these changes, lenders making installment loans of \$3,000 or less are required to obtain a license and comply with the substantive provisions of the Act, regardless of the interest rate charged. In addition, the legislation also removed the exemption for businesses organized or operating under the authority of any law of the State of Georgia or the United States relating to real estate loans or mortgage companies.⁸²

The Texas Finance Commission amended several of its rules in response to the passage of H.B. 1442, which became effective September 5, 2019.⁸³ These amendments included changes related to the term of licenses, the renewal process, and expiration dates for regulated lenders and credit access businesses.⁸⁴ Other amendments to the rules included revisions to implement the optional pawnshop employee licensing program, changes to the pawnshop

74. CAL. FIN. CODE § 22304.5(a) (West 2020).

75. 808 KY. ADMIN. REGS. 9:010 (2020).

76. *Id.*; see also KY. REV. STAT. ANN. § 286.9-100(9) (West 2020).

77. H.B. 2463, 80th Leg., Reg. Sess. (Or. 2019).

78. OR. REV. STAT. ANN. § 726.380 (West 2020).

79. OR. ADMIN. R. 441-740-0000 (2020).

80. S.B. 462, 2020 Leg., Reg. Sess. (Ga. 2020).

81. See GA. CODE ANN. § 7-3-6 (2019).

82. GA. CODE ANN. § 7-3-4(b) (2020).

83. H.B. 1442, 2019 Leg., Reg. Sess. (Tex. 2019).

84. 7 TEX. ADMIN. CODE §§ 83.403, 83.3009, 83.4002 (2020).

employee licensing fees, and clarifications related to license terms, renewals, and expirations.⁸⁵

The Texas Finance Commission also finalized amendments to its rules effective July 9, 2020, relating to the plain language contract provisions under Chapter 342 of the Texas Finance Code.⁸⁶ These amendments included changes to the review procedures for non-standard contracts, adding model language for a credit reporting clause, and revisions to model clauses.⁸⁷

85. *Id.* §§ 85.102, 85.104, 85.202, 85.306.

86. 45 Tex. Reg. 2790, 2790–93 (May 1, 2020).

87. 7 TEX. ADMIN. CODE §§ 90.104, 90.202–204 (2020).

