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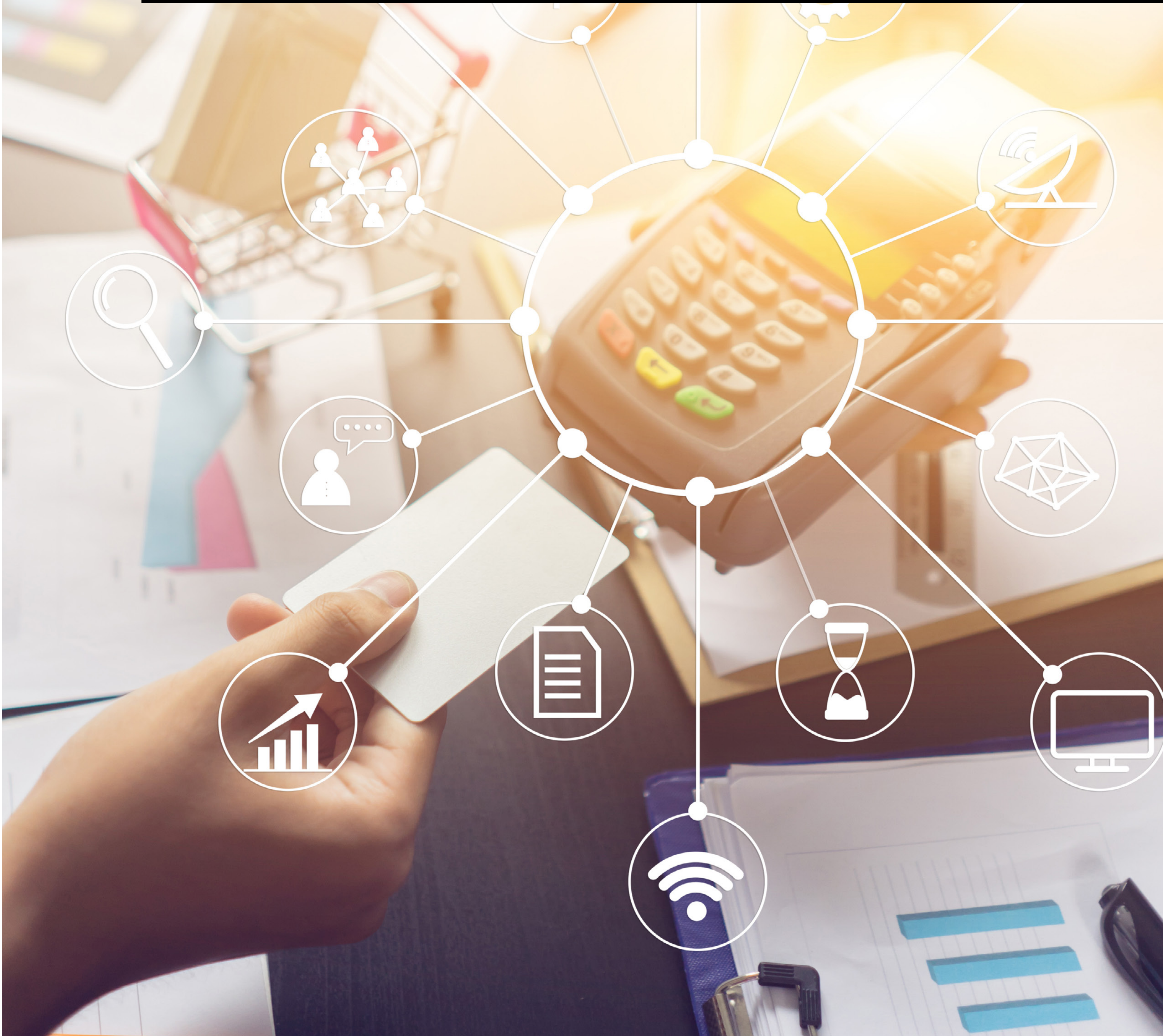

REGULATORY & ENFORCEMENT

CFPB Director Signals His Increased Focus on the Payments Industry

In a wide-ranging interview with *Law360*, Consumer Financial Protection Bureau (CFPB) Director Rohit Chopra recently discussed the bureau's increasing focus on the payments industry. According to Chopra, the "primary focus is really on the effect of real-time consumer payments," given the anticipated launch of FedNow (the Fed's real-time payment network) next year and the broader adoption of apps and other ways to transfer money in real time. The bureau is focused on the "attendant consumer protection issues that every developed country experiences when [real-time transfers] gain broader adoption," including errors, fraud, and scams. The CFPB is looking "closely" at how peer-to-peer payment apps are operating and addressing consumers who are allegedly defrauded or scammed through those services. Chopra acknowledged "a number of players in this space that have started to make changes" to address some of these customer-facing concerns, including "asking someone what the last four digits of the recipient's phone number are or going through a couple more steps to make sure that the sender-recipient transaction is a legitimate one."

Consistent with Chopra's concern about the payments industry, earlier this summer, the CFPB published an advance notice of proposed rulemaking seeking information about the Federal Reserve Board of Governors' 2010 immunity provision for excessive late fees on credit cards and data regarding "issuers' revenue and expenses, the potential deterrent effect of late fees, and the role late fees play in credit card companies' profitability." The comment period closed at the end of July.

The CFPB's focus is not limited to financial firms—it includes the Big Tech companies that pair with financial services companies. In prepared remarks at the 2022 National Association of Attorneys General Presidential Summit, Chopra highlighted the interconnectivity of Big Tech and financial services. His remarks reflect the position laid out by the CFPB in a recently issued interpretive rule. The rule explains that digital marketing providers for financial services firms are subject to federal consumer financial protection laws when they provide "material service" to financial firms. Specifically, digital marketing providers that are "involved in the development of content strategy" are providing a material service. The interpretative rule announces the CFPB's position on its authority to sue digital market providers for alleged violations of consumer financial protection laws.

FTC Settles Civil Enforcement Action Alleging Payment Processor's Merchant Clients Were "Consumers" Under Federal Law

Federal Trade Commission v. First American Payment Systems LP, et al., No. 4:22-cv-00654 (E.D. Tex.).

A recent settlement between the Federal Trade Commission (FTC) and payment processor First American Payment Systems indicates a potentially broad expansion of FTC enforcement activity against payment processors. First American primarily serves small businesses such as restaurants and nail salons. In late July, the FTC sued First American, alleging that First American and certain independent sales organizations misled merchants about First American's processing fees and falsely told the merchants they could cancel First American's processing services any time and without penalty. The truth, according to the FTC, was that First American's fees were higher than represented and that First American required its merchant customers to sign three-year agreements that could only be terminated upon payment of a $495 early termination fee. The FTC also alleged that First American unfairly debited customer settlement accounts for various fees and other amounts without customer authorization.

According to the FTC's complaint, First American's alleged misrepresentations violated Section 5 of the FTC Act, which generally prohibits unfair or deceptive trade practices. The FTC also alleged that First American's "unfair" debiting practices violated the federal Restore Online Shoppers' Confidence Act (ROSCA). Both of those statutes apply only to "consumers." The FTC therefore alleged that First American's merchant clients qualified as consumers for purposes of the FTC Act and ROSCA.

On the same day the FTC filed the complaint, the FTC and First American moved jointly for approval of a proposed settlement, in the form of a stipulated order for a permanent injunction and $4.9 million of monetary relief. The proposed settlement refers to First American's merchant customers as "consumers" and will, if approved, permanently enjoin First American and other related entities from engaging in the practices alleged by the FTC in its complaint. The proposed settlement also requires all defendants to establish compliance programs for the terms of the permanent injunction.

FinTech Company Agrees to Pay $2.7 Million Penalty

In the Matter of Hello Digit LLC, Admin. Proceeding File No. 2022-CFPB-0007.

On August 12, 2022, the CFPB entered a consent order with Hello Digit Inc., a FinTech company that offers consumers a personal finance management app. The app uses a proprietary algorithm to make automatic transfers from a consumer's checking account to an account held in Hello Digital's name to promote automated savings for vacations and rainy days. Consumers are charged a $5 monthly subscription fee for this service. The consent order stated that Hello Digit engaged in deceptive acts and practices by (1) falsely guaranteeing that it would not cause consumers' checking accounts to incur overdraft fees; (2) falsely promising it would reimburse customers for overdrafts and denying customer reimbursement requests; and (3) falsely promising it would not keep any interest earned on consumer funds.

In addition to ceasing any illegal activity, the order requires Hello Digit to pay (1) reimbursement requests for overdraft charges that it previously denied its customers (totaling at least $68,145); and (2) a $2.7 million penalty into a victims' relief fund.

Banking Industry Asks CFPB to Supervise Nonbank Data Users and Aggregators

In August, a group of banking trade associations headed by the American Bankers Association filed a petition for rulemaking with the CFPB. The petition asks the CFPB to issue rules that would allow it to supervise and examine nonbanks that are operating as data users and data aggregators of consumer financial data.

Currently, the CFPB is engaged in a rulemaking under Section 1033 of the Dodd–Frank Act to regulate how consumer financial data is collected and used. The CFPB has identified the main market participants other than consumers as data holders, data users, and data aggregators.

Banks and credit unions generally operate as data holders because they collect and retain consumer financial data in the ordinary course of their business. By contrast, data users and data aggregators are often nondepository institutions that, with consumer authorization, either use consumer financial data to offer products and services (data users) or support data holders and data users by aggregating and sharing consumer financial data (data aggregators). For example, companies like Credit Karma and PayPal might be considered data users while companies like Plaid and Fiserv might be considered data aggregators.

According to the petition, "data holders, such as banks and credit unions[,] are regularly supervised and examined by the CFPB, whereas non-depository institutions such as data aggregators and data users are not examined by the CFPB." The CFPB has authority to supervise nonbank covered persons that are "larger participant[s] of a market for other consumer financial products or services." Because of this, the petition asks for the CFPB to engage in a rulemaking to define "larger participants" as "data aggregators and data users that are larger participants in the aggregation services market," and to define the term "aggregation service" as a "financial product or service."

Together, these proposed definitions would place nonbank data users and data aggregators squarely under the CFPB's supervisory authority. The CFPB has stated it will post the petition online and consider next steps after reviewing public comments.

NEW LAWSUITS

Cryptocurrency Exchange Customers Allege That Algorithmic Stablecoin Is a Security

Lockhart v. BAM Trading Services Inc., et al., No. 3:22-cv-03461 (N.D. Cal.).

A class action filed in a California federal court alleges that the algorithmic stablecoin TerraUSD qualifies as a security under federal law and seeks to hold Binance, a cryptocurrency exchange, liable for losses allegedly suffered by TerraUSD owners. A stablecoin is a type of cryptocurrency whose value is tied to an underlying asset, such as gold, dollars, euros, or even other cryptocurrencies. Stablecoins seek to reduce price volatility, either by maintaining assets in reserve or through algorithms designed to automatically control the stablecoin's supply.

TerraUSD was created and is centrally controlled by Terraform Labs, a crypto-asset company based in Singapore. According to the complaint, TerraUSD had unique features, including that its price would be maintained by allowing owners to swap TerraUSD for another digital currency called Luna and the potential to earn interest on TerraUSD through an "Anchor Protocol" built into the currency. Binance is a cryptocurrency exchange where stablecoins like TerraUSD can be bought and sold.

A class of individuals who traded TerraUSD on the Binance exchange has alleged that TerraUSD is a security that Binance failed to register with the U.S. Securities and Exchange Commission (SEC). The plaintiffs label TerraUSD an "investment contract," and thus a security under federal securities laws, because TerraUSD owners allegedly invested money in TerraUSD relying on the TerraUSD ecosystem to not only maintain TerraUSD's price but to make profits. The plaintiffs further claim that TerraUSD is a derivative of Luna and a security for that reason as well.

The plaintiffs allege that in failing to register TerraUSD and disclose that TerraUSD and Luna were actually securities, Binance violated federal and state securities laws by misrepresenting the stability of TerraUSD's ecosystem and, therefore, the ability of that ecosystem to maintain TerraUSD's price. The plaintiffs further allege that they were damaged by these violations when the price of TerraUSD collapsed earlier this year. The class action complaint seeks declaratory and injunctive relief, damages, attorneys' fees, and a jury trial.

Antitrust Suit Against Credit Cards Settles Quickly

The Walt Disney Co. v. Visa Inc., et al., No. 1:22-cv-04489 (E.D.N.Y.).

Less than a week after filing its complaint, Disney settled its lawsuit against Visa and Mastercard alleging that their adoption of nearly identical rules eliminated competition and forced merchants like Disney to pay excessive interchange and network fees. Disney's stipulation and order of dismissal with prejudice did not include any details of the settlement.

Disney accepts Visa- and MasterCard-branded debit and credit cards from customers in all aspects of its businesses. According to Disney's complaint, Visa and Mastercard set "default" interchange fees for their member banks, which allegedly include nearly all card-issuing banks

in the United States. This, Disney contended, effectively fixes the price for the acceptance of cards at a "supracompetitive" level and precludes card-issuing banks from independently competing for merchant acceptance. Disney asserted that it has paid significantly higher costs to accept Visa- and Mastercard-branded debit and credit cards than it would if the banks using such cards competed for merchant acceptance.

Disney asserted four counts of violating Section 1 of the Sherman Act and was seeking relief in the form of compensatory and trebled damages as well as attorneys' fees and costs. Disney's claims are reminiscent of those made by merchants in a 2005 class action, *In re Payment Card Interchange Fee & Merchant Discount Antitrust Litigation*. In that case, the plaintiffs alleged that Visa and Mastercard conspired to fix interchange fees in violation of Section 1 of the Sherman Act.

Merchants Continue to Challenge Collection Tactics Employed by Merchant Cash Advance Companies

Peters Broadcast Engineering v. 24 Capital LLC, et al., No. 1:22-cv-00236 (N.D. Ind.).

Evexia Holdings Inc. v. Quick Funding Group LLC, No. 3:22-cv-00898 (D. Conn.).

The merchant cash advance (MCA) industry is generally known for issuing short-term cash advances to prospective small and medium-sized borrowers secured against those companies' accounts receivable. Merchants alleging to be aggrieved by certain MCA lenders' collection efforts—including, in many instances, the MCA lenders' use of confessions of judgment—have sought to expedite litigation as a means of challenging the alleged practices.

In *24 Capital*, the plaintiff—a merchant that was on the receiving end of a confession of judgment after going into default on a short-term MCA loan—filed federal racketeering (RICO) claims against the MCA lender, alleging that the company is engaged in an organizational enterprise to defraud cash-strapped small businesses. Later the very same day, the merchant then filed a motion for class certification, seeking to represent a class of "thousands" of borrowers "who received merchant cash advances and were advised the repayment would be against receivables only." The early class certification motion remains pending.

Like the merchant in *24 Capital*, the plaintiff in *Evexia Holdings* is a short-term borrower that was subject to a confession of judgment after defaulting on a $300,000 loan that was secured against its accounts receivable. Concurrent with the filing of its complaint for violation of its federal due process rights, the plaintiff also filed a motion for a temporary restraining order and a preliminary injunction, seeking to compel the MCA lender to release a freeze on the merchant's bank accounts and arguing that without immediate relief, it would be forced to close its doors and lay off its entire staff. The court denied the emergency motion sua sponte on evidentiary grounds the very next day. No further action of note has taken place since the court's swift ruling.

Consumers File Additional Complaints Against P2P Transfer Providers

Hope v. Early Warning Services LLC d/b/a Zelle, No. 2:22-cv-04639 (C.D. Cal.).

Al-Ramahi v. PayPal Inc., No. 5:22-cv-03632 (N.D. Cal.).

Last edition, we covered a number of new class actions filed against banks and related companies for their alleged failures to protect their customers from scams aimed at users of Zelle. And while additional cases have since been filed against Zelle, recent litigation has also targeted Venmo, which is owned and operated by PayPal.

The plaintiff in *Hope v. Early Warning Services LLC d/b/a Zelle* alleges that he voluntarily transferred $395 via Zelle to a company purporting to offer investment trading through the foreign exchange market, only to later find out that the company was a fraud. The plaintiff then sought reimbursement from his bank for the lost funds, but the bank refused. Asserting that Zelle knowingly misrepresents and conceals the risks of using its quick-pay service, the plaintiff filed a class action complaint seeking to represent both a California and a nationwide class of similarly situated Zelle users, asserting claims under California's Unfair Competition Law and False Advertising Law.

The second class action complaint contains similar allegations. In *Al-Ramahi v. PayPal Inc.*, the plaintiff alleges that he fell victim to a scheme whereby an individual posing as his boss sent him a check for $4,950 and then instructed him to disburse those funds—including by sending an outgoing transfer of $2,450 via quick-pay app Venmo. When the scheme quickly unraveled, the plaintiff was out not just the funds he sent via Venmo, but also the original funds, which were clawed back by the bank when it discovered that the check was fraudulent. Asserting that Venmo fails to disclose that "users are at extreme and undisclosed risk of fraud when using" the app, the plaintiff filed suit, alleging claims under the Electronic Fund Transfer Act, as well as numerous California state-law and statutory claims.

Class Action Challenging "Buy Now Pay Later" Payments Plans Refiled in California State Court

Sliwa v. Sezzle Inc., No. 22STCV24110 (Los Angeles Superior Court, Cal.).

Last edition, we reported on several class actions challenging "buy now pay later" (BNPL) programs, which give retail consumers the option to spread payments over several installments, usually interest-free. One of those suits—a May 2022 suit against Sezzle—has since been voluntarily dismissed by the plaintiff and refiled in the Superior Court of California, Los Angeles County. The refiled suit asserts the same allegations as the initial federal case, but drops the claim for violation of Minnesota's Consumer Fraud Act.

The plaintiff again alleges that he incurred overdraft fees when Sezzle attempted to draw an installment payment from his account and there were insufficient funds to cover it. The plaintiff claims that Sezzle markets its service as one that allows purchasers to buy now, pay later with "no interest," but fails to warn users of the risk that they may become liable for

insufficient funds or overdraft fees. The plaintiff also alleges that Sezzle knows that its BNPL service specifically targets low-income consumers who are more likely to incur large bank fees if they are unable to timely pay the installments. The plaintiff's new class action complaint asserts claims for violations of California's Unfair Competition Law and False Advertising Law.

Tap and Pay Generates $1 Billion Per Year via Alleged Anticompetitive Use

Affinity Credit Union v. Apple Inc., 4:22-cv-04174 (N.D. Cal.).

Apple was hit with a class action complaint alleging that it engaged in anticompetitive behavior with its proprietary Apple Pay mobile wallet. The class complaint, which was brought on behalf of all banks, credit unions, and other card issuers that "(a) issued any Payment Card enabled for Apple Pay and (b) paid Apple a fee for any Apple Pay transaction on that Payment Card," alleges that Apple wrongfully generated more than $1 billion in 2019 via its allegedly anticompetitive conduct—a number that will purportedly quadruple by 2024.

Specifically, the plaintiff alleges that Apple has violated the Sherman Act in two ways: (1) by unlawfully "tying" its mobile devices and its mobile wallet together; and (2) by monopolizing the market for "tap and pay" mobile wallets in its iOS operating system. Through this conduct, the plaintiff asserts that Apple has forced card issuers to pay fees they would not have incurred in a competitive mobile wallet market, including a 0.15% fee on all credit card transactions and a flat 0.5 cent ($0.005) fee on all debit card transactions consummated through Apple Pay. The plaintiff seeks broad classwide relief, including monetary damages, an injunction, and "other relief available to stop Apple's ongoing exclusionary practices and redress the harm they have caused."

Digital Payments Company Faces Derivative Lawsuit over Compliance Issues

Jefferson v. Schulman, et al., No. 2022-0684 (Court of Chancery, Del.).

On August 3, 2022, a PayPal shareholder brought a derivative suit against PayPal's CEO, CFO, and board of directors alleging false and misleading statements surrounding PayPal's compliance infrastructure. The complaint alleges that PayPal made multiple public statements about actions taken to ensure compliance with consumer protection laws and financial regulations when, in fact, the company's compliance controls were deficient and resulted in investigations by the CFPB and SEC. The complaint further alleges that when PayPal disclosed these investigations in a financial report, its stock price dropped $18.81 per share.

At the heart of the complaint are allegations that PayPal failed to comply with a 2015 consent order with the CFPB that resolved various allegations against PayPal and instituted a compliance plan. The complaint alleges PayPal repeatedly violated this compliance plan and made false and misleading statements about its compliance, which "put the Company on the radar of regulators." Jefferson asserts claims for breach of fiduciary duty, gross mismanagement, abuse of control, and unjust enrichment and seeks the damages sustained by the company and an order directing the company to reform and improve its corporate governance and internal procedures.

Payment Processor for Fast-Food App Sued for Double Charging

Dodd v. Adyen Inc. and Karavites Management Inc., 2022-CH-07507 (Cook County Circuit Court, Ill.).

On August 2, 2022, Adyen Inc.—the payment processor for the McDonald's mobile app—was sued for an alleged design defect that caused customers to be billed twice for their fast-food orders.

The class action claims that customers ordering through the McDonald's app would pay using a credit card and that Adyen would process that payment. The plaintiff alleges that "there is a design defect" that "results in payment verification not being advanced to the physical McDonald's location" where customers pick up their food. Consequently, "[w]hen customers arrive at the physical McDonald's restaurant of their choice[,] they are informed when they attempt to pick-up their order that the McDonald's location has not received their payment [so they] are then forced to provide a second payment to receive their food."

Based on these allegations, the plaintiff seeks to certify a class of "all persons who, within the applicable statute of limitations, provided payment through the McDonald's mobile application for a food order but had to provide payment a second time when picking up their order." On behalf of this class, plaintiff brings claims for breach of implied contract, breach of contract, violations of the Illinois Consumer Fraud and Business Deceptive Practices Act, and unjust enrichment.

NOTEWORTHY DECISIONS

Court Dismisses Investor's Complaint Alleging Chinese FinTech Company Misrepresented Its Compliance with Chinese Cybersecurity Laws

In re 360 DigiTech Inc. Securities Litigation, No. 1:21-cv-06013 (S.D.N.Y.).

On July 28, 2022, the Southern District of New York dismissed a securities fraud class action brought against 360 DigiTech Inc., a Chinese company that trades in the United States and provides financial services to borrowers through its downloadable app. The lawsuit was brought by an individual who accused the company and its executives of misleading investors about 360 DigiTech's compliance with Chinese regulations governing the collection of user data.

According to the plaintiff, the company represented that it complied with Chinese data privacy regulations, but after a new Chinese privacy law was introduced in May 2021, 360 DigiTech was forced to temporarily remove its app from major app stores in China to rectify privacy issues. That disruption allegedly caused 360 DigiTech's stock price to fall.

The court found that the plaintiff failed to allege any material misrepresentation by 360 DigiTech because the company adequately disclosed China's evolving regulatory landscape and the attendant risks to investors. The court also found the complaint to be insufficiently specific to meet heightened pleading standards that apply to securities class actions. Moreover, the plaintiff did not sufficiently allege that the company's alleged failure to comply with Chinese data regulations caused the stock price to drop, rather than general market fluctuations. The court dismissed the complaint without prejudice, permitting the plaintiff to amend the complaint to cure the pleading deficiencies.

Challenge to Bank's Administration of Credit Card Program Settles for $2.25 Million

Campagna, et al. v. TD Bank NA, No. 1:20-cv-18533 (D.N.J.).

On August 29, 2022, a New Jersey federal judge gave her preliminary approval of a $2.25 million settlement of a proposed class of TD Bank customers' lawsuit challenging TD Bank's administration of its cash-secured credit card program. The plaintiffs were also seeking approval of a nationwide class for settlement purposes only, which the judge conditionally certified. The final approval hearing is set for February 23, 2023.

The complaint, which was filed over two years ago, alleges that TD Bank failed to follow through on its promise to timely upgrade the plaintiffs to an unsecured TD Bank credit card after maintaining their accounts for seven consecutive billing cycles without defaulting. In August 2021, the court denied TD Bank's motion to dismiss. The judge found that the plaintiffs' allegation that TD Bank did not keep its word to automatically review whether customers with secured cards can transition to unsecured credit cards after seven consecutive billing cycles in good standing was sufficient to state a claim. However, the judge rejected the plaintiffs' assertion that TD Bank promised to automatically upgrade accounts if customers did not default for seven consecutive months.

If the settlement is approved, participating class members will receive a portion of the annual fee they would have paid on their credit card plus an additional amount if the net settlement fund is sufficient following the deduction of service awards, attorneys' fees, and other litigation and administrative costs. The plaintiffs assert that this settlement provides a good result for the class given the court's rejection of their automatic-graduation theories at the pleading stage.

Unfair and Deceptive Fees Suit Moves On

Bruin v. Bank of America NA, No. 3:22-cv-00140 (W.D.N.C.).

On August 31, 2022, a North Carolina federal judge denied Bank of America's motion to dismiss a proposed class action asserting it misled the plaintiffs and other reasonable consumers into believing that they had to pay transfer fees in order to make electronic transfers through the National Automated Clearinghouse (NACHA) system, which is a nationwide network through which depository institutions send each other batches of electronic credit and debit transfers.

The plaintiff alleges NACHA is increasingly used for small-dollar consumer payments such as utility bills, gym memberships, and insurance payments. The plaintiff claims that a payment can either be "pushed" from an account to a recipient or it can be, with proper authorization, "pulled" by a recipient from that same account. According to the plaintiff, recipients "pulling" funds from an account do not charge fees for doing so, nor does the NACHA system assess any fees on recipients for transfers. The plaintiff complains that Bank of America assesses fees on its accountholders for initiating transfers that are ultimately processed over the NACHA network—in other words, for starting the process that leads to pushing funds to a recipient.

Therefore, the plaintiff alleges that Bank of America has an incentive to encourage its customers to initiate pushes to recipients so it can collect the $3 to $10 fee each time it convinces an accountholder to do so. The plaintiff claims that Bank of America misled its customers "into believing that they had to pay these fees in order to make those transfers" even though other banks don't charge such fees. Further, the plaintiff asserts that she could effectuate the same transaction for free by asking the financial institution on the other end of the transfer to initiate the transaction.

The plaintiff asserts two claims against Bank of America on her own behalf and on behalf of a nationwide class for violation of North Carolina's Unfair and Deceptive Trade Practices Act and unjust enrichment under North Carolina common law.

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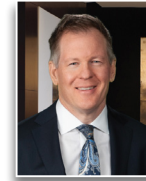

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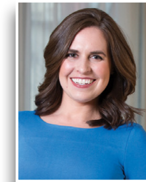

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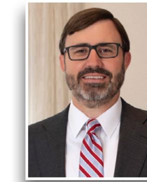

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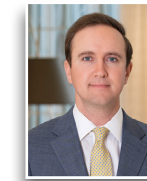

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