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When CFPB Finds Deception Regardless Of A Lender's Intent

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There is a tendency to think of consumer fraud and misrepresentation as intentional acts that deceive consumers into engaging in transactions that they would not otherwise engage in. A recent case demonstrates that the Consumer Financial Protection Bureau, and at least one federal district court, take a much different view — that misrepresentation exists simply because statements later turn out to be incorrect, regardless of whether the person making the representation may have had a reasonable belief and good faith legal basis for the belief before making the representation.

In 2014, the CFPB filed a suit against CashCall Inc., alleging that CashCall engaged in unfair, deceptive, and abusive acts and practices (UDAAP). On June 30, 2016, the CFPB filed a motion for partial summary judgment in the case. On Aug. 31, 2016, a U.S. district court granted the CFPB's motion for partial summary judgment and found that CashCall's actions were deceptive.

For the CFPB to use the deception prong of its UDAAP authority against a provider of financial services is by no means new, but this time it's different. In this case, the CFPB applied the deception standard to a disputed issue of law. Further, the application of the law to the facts at issue was not established by prior statute, rule or even a pre-existing order. Rather, the law is a conclusion of law asserted in the CFPB's suit and found by the court in the instant case.

Moreover, the legal finding itself involves a complex, fact-specific and evolving legal doctrine about who is the "true lender" in loan arrangements that presumably was not understood by CashCall or it is unlikely that CashCall would have made the loans in the first place.

The facts in the CashCall case are that a member of the Cheyenne River Sioux Tribe (CRST) created a financial institution, Western Sky Financial, licensed by the CRST to do business on the CRST reservation in South Dakota. Western Sky built facilities on the reservation, including a call center, and employed over 100 individuals.

Consumers applied to Western Sky for loans and Western Sky originated loans. The loan agreements between Western Sky and consumers provided that the loans were subject solely to the laws of the CRST, and not subject to any state's law.

CashCall entered into agreements with Western Sky to purchase loans made by Western Sky and Western Sky agreed to sell loans to CashCall. CashCall also established an account for Western Sky to fund loans made by Western Sky. Per their agreement, shortly after origination, Western Sky sold the loans to CashCall. Consumers made payments to CashCall, and CashCall contacted consumers when payments were not made, seeking to collect such payments.

The CFPB alleged that CashCall engaged in a deceptive practice by collecting payments on the Western Sky loans because CashCall created the "impression in consumers that they [CashCall] were servicing loans that were subject to CRST law and payable." The CFPB further stated that "this impression was likely to mislead consumers ... because it was false." The district court accepted the assertion made by the CFPB, holding that CashCall engaged in a deceptive practice.

The CFPB's assertion of deception in this case is that deception took place because CashCall could not legally rely upon tribal sovereignty in determining that state law did not apply to the transactions. In other words, the CFPB asserted that because CashCall was not legally entitled to rely on tribal sovereign immunity, CashCall engaged in a deceptive practice by giving consumers the "impression that [CashCall] loans were subject to CRST law."

The CFPB does not address, and the court does not inquire, whether CashCall reasonably believed it could rely on CRST law. It is possible that CashCall might extend credit that it believed to be illegal based on the assumptions that the issue would never arise, that the issue would only come up in so few cases, that the loan program would remain profitable, or that the program would otherwise remain profitable after any legal action. But those possibilities, which are relevant in evaluating whether CashCall intended to deceive consumers in seeking to collect on its loans, were never alleged by the CFPB or examined by the court.

The CFPB simply asserted that because consumers believed that they had to repay their loans, it was deceptive for CashCall to seek to collect payments. The court agreed, stating that a "mistake of law" is not typically a defense to liability, no matter how reasonable that belief may be.

The theory of deception in this case risks turning every contract dispute between a consumer and a provider of consumer financial services into a deception case because by seeking to enforce a contract the provider could be deemed to have engaged in a deceptive practice unless it ultimately prevails on other legal claims in the case. This bootstrap approach used by the CFPB to assert a practice is deceptive is a broad expansion of the legal basis for establishing deception.

This approach raises potentially significant risks for lenders. For example, going forward, will consumers be able to routinely challenge collection actions by asserting that an action is deceptive, by pointing to the CFPB's innovative theory and/or by asking the CFPB to intervene? Only time will tell.

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