



Fintech Focus: Leveraging Compliance as a Competitive Advantage

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Mitchel H. Kider
Jason W. McElroy

Kider@thewbkfirm.com
McElroy@thewbkfirm.com

Introduction

- The CFPB has made waves lately with moves and statements indicating its desire to regulate nonbank financial technology companies
- CFPB is concerned with prioritization of profits and customer acquisition over compliance with financial regulations
- Congress issued report in December 2022 accusing fintech companies of prioritizing profit over compliance with PPP program requirements
- Implosion of FTX has shone a bright light on failure to conduct proper risk management and compliance management due diligence
- Increased Enforcement Activity from regulators highlights importance of compliance as a competitive advantage

Director Chopra Speaks at Money 20/20

- On October 25, 2022, Director Chopra gave a speech at Money 20/20
 - Wants to shift US toward more open banking and open finance
 - More decentralized system will benefit consumers through competition
 - Push for procompetitive regulation to reduce costs of switching and barriers to entry, promote price transparency and shopping, and safeguards against firms exploiting control over critical networks

Director Chopra Speaks at Money 20/20

- Proposed three measures to accomplish the Bureau's procompetitive goals:
 - Requiring financial institutions offering accounts to set up secure methods for data sharing
 - Stopping the restriction of access to consumer's own data
 - Safeguards against excessive control or monopolization
- Much of the speech focused on antitrust-related concepts such as competition, market control
- CFPB looking to finalize rules in 2024

CFPB Digital Marketing Publication

- August 10, 2022, CFPB issued an interpretive rule outlining how it will determine whether digital marketing providers for financial firms are “service providers”
- Important because this will bring such “Service providers” into the regulatory ambit of the Bureau
 - Clarified what does not apply for “time and space” exception
 - Use of algorithmic targeting to consumer with specific characteristics
 - Targeting specific users at specific times to maximize engagement
 - Determining or suggesting the consumers who should receive ads

CFPB Revives Dormant Authority

- In April 2022, CFPB proposed process for establishing supervisory authority over nonbank covered persons
- Authorizes supervision of nonbanks that CFPB has reasonable cause to believe pose risks to consumers
- Aimed at fast-growing companies and markets outside the existing nonbank supervisory program

CFPB Proposes Contract Registry

- Registry of Supervised Nonbanks that Use Form Contracts to Impose Terms and Conditions that Seek to Waive or Limit Consumer Legal Protections
 - Proposed Rule 12 CFR Part 1092
- Form contracts – i.e., consumers have no ability to modify/negotiate
 - This encompasses virtually every consumer financial service contract
- Proposal excludes certain companies, including nonbanks with less than \$1 million in annual receipts from offering or providing consumer financial services of products
- Accessible to public as well as other regulators

Proposed Rule 12 CFR Part 1092

- Covered limitation on consumer legal protections (§ 1092.302(d))
 1. Limiting when a consumer can bring a legal action
 2. Specifying a forum/venue where a consumer must bring a legal action
 3. Limiting consumer's ability to bring/participate in collective legal actions
 4. Capping the amount of recovery or type of remedy
 5. Waiving a consumer's right to bring a legal action
 6. Limiting consumers from leaving reviews or making complaints
 7. Waiving a consumer's right to assert a right, defense, or protection
 8. Requiring arbitration

CFPB Nonbank Supervision Program

- “. . .the proposed registry can facilitate the ***Bureau’s prioritization of which entities to examine***, as well as, relatedly, its ***identification of entities eligible for examination***. The proposed registry also can facilitate ***the scoping of its examinations***.”
- “To ***facilitate*** public awareness and ***oversight by other regulators including the States***, the Bureau is proposing to publish information identifying registrants and their use of these terms and conditions.

CFPB Tech Payment Info Requests

- In 2021, CFPB sent information requests to six of the largest tech platforms for information on their data collection practices
 - Amazon
 - Apple
 - Facebook
 - Google
 - PayPal
 - Square
- Followed up with additional requests in 2022

CFPB Report on Payments & Commerce

- CFPB is concerned that recent innovations bring increased risks that must be assessed, e.g.
 - Contactless transactions
 - Instant loans at time of purchase
 - Bank in an app and banking super apps
 - BNPL
 - Embedded commerce
- CFPB concerned about compilation of financial data information, monetization of a consumer's digital data and footprint
- Greater opportunities for fraud or accidental subscriptions that result in ongoing payments

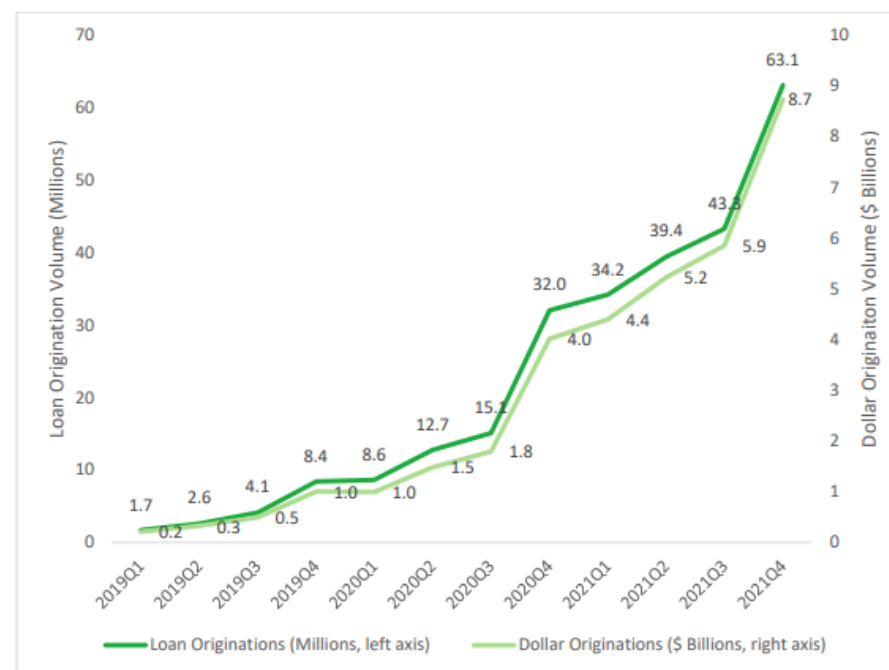
CFPB Report on BNPL

- September 2022 – Buy Now, Pay Later: Market Trends and Consumer Impacts
- CFPB is concerned with three potential harms:
 - Discrete consumer harms
 - Data harvesting
 - Overextension

TABLE 8: BNPL LOAN ORIGATION VOLUME AND AVERAGE LOAN SIZE, 2019-2021

	2019	2020	2021	19-21 CAGR
Loan Originations (Millions)	16.8	68.4	180.0	227%
Dollar Originations ⁵⁷ (\$ Billions)	2.0	8.3	24.2	245%
Average Loan Size (Dollar Originations / Loan Originations)	\$121	\$121	\$135	5.5%

FIGURE 4: BNPL LOAN ORIGATION VOLUME BY QUARTER, 2019-2021



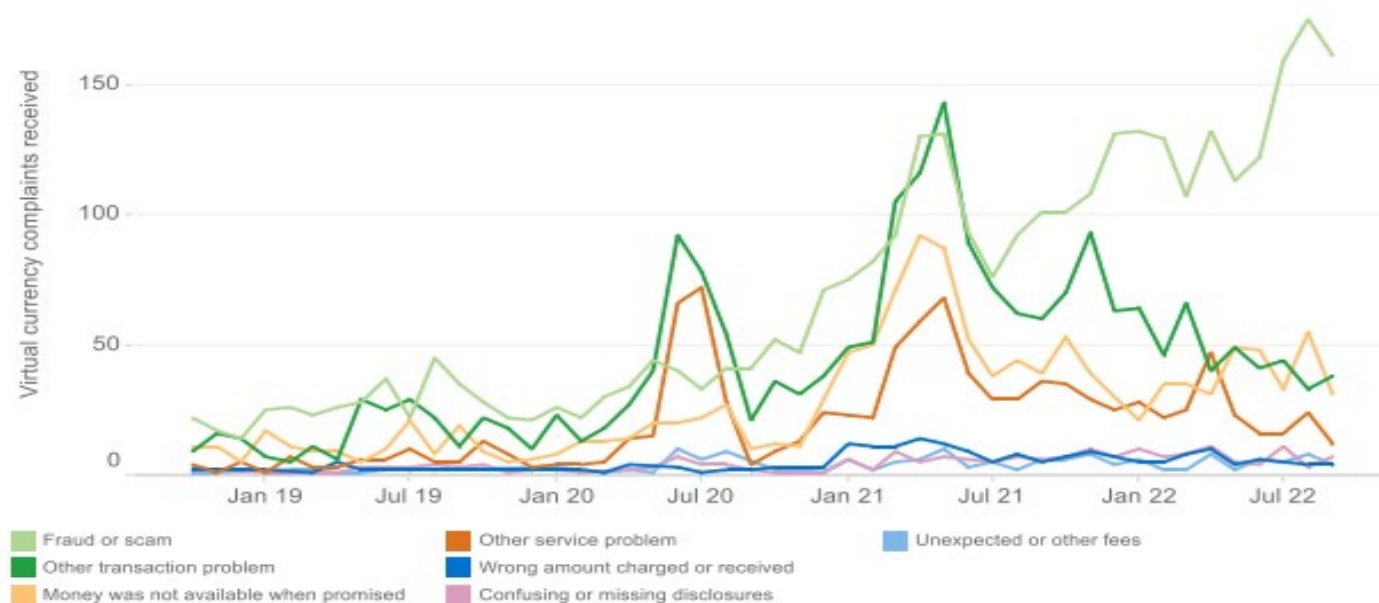
Congressional Report on PPP Fraud

- In December 2022, Congress issued a scathing report, alleging widespread fraud by certain fintech companies in processing of PPP loans
- Although fintechs originated almost a third of PPP loans, researchers found they were responsible for over 60% of all suspicious loans originated
- Companies allegedly spent exceedingly small amounts of money on fraud detection
- Report noted only a few companies displayed strong fraud detection efforts
- Recommended SBA and DOJ to investigate and prosecute PPP fraud

Crypto-related Interest Increases

- “Crypto Winter” related issues have piqued federal and state regulatory interest, underscored by FTX bankruptcy and allegations
- CFPB issued an analysis of consumer complaints related to crypto-assets in November 2022

FIGURE 5: VIRTUAL CURRENCY COMPLAINTS BY ISSUE BY MONTH, OCT. 2018 TO SEP. 2022



Crypto-related Interest Increases

- NY State Department of Financial Services issues Guidance on Custodial Structures for Customer Protection in the Event of Insolvency
- The guidance covers:
 - Segregation of and separate accounting for customer virtual currency
 - Custodian's limited interest in and use of customer virtual currency
 - Sub-custody arrangements
 - Customer disclosures

Greensky, LLC Consent Order

- Company provided point of sale financing technology
- Originated and serviced point of sale loans for participating merchants on behalf of participating banks
 - Retail, home improvement, and medical/health care
- Alleged that the company allowed contractors and merchants to take out loans on behalf of consumer without their authorization
- Order required company to refund or cancel up to \$9 million in loans to harmed consumers, pay civil money penalty of \$2.5 million

LendUp Loans Consent Order

- Settlement terminated all lending and servicing operations and pay a \$100K penalty.
- CFPB accused the company of “repeatedly lying and illegally cheating its customers.”
- The company allegedly had created a ladder system of credit, telling borrowers that if they performed well on low dollar, high-interest loans and took a credit class, they would qualify for larger loans with lower interest rates.
- However, CFPB alleged most customers never actually were given that opportunity.

Hello Digit, LLC Consent Order

- \$2.7 million civil money penalty and consumer redress.
- CFPB alleged UDAAP violations, alleging company misrepresented its services to consumers by saying its technology could save them the perfect amount of money automatically through regular transfers from the consumer checking account
- Company claimed that it did not make money by retaining interest on consumer's money, but they did as well as causing overdrafts

My Loan Doctor Settlement

- CFPB filed a lawsuit against company and its owner for UDAAP violations
- Alleged misrepresentations regarding deposits and a guaranteed rate of savings
- Misrepresented that funds would be used to originate loans for healthcare professionals, providing a high yield rate of return
- Deposits were not FDIC insured, and the company was not a bank
- \$19 million in consumer refunds, civil penalty of \$391,530
- Permanent injunction entered on all deposit taking activity

Questions?

(202) 628-2000

Kider@thewbkfirm.com

McElroy@thewbkfirm.com

www.thewbkfirm.com