



SETTLING FOR NOTHING: HOW KRANINGER'S CFPB LEAVES CONSUMERS HIGH AND DRY

**REPORT PREPARED BY THE MAJORITY STAFF OF THE
COMMITTEE ON FINANCIAL SERVICES, U.S. HOUSE OF REPRESENTATIVES**

**THE HONORABLE MAXINE WATERS, CHAIRWOMAN
116TH CONGRESS, FIRST SESSION
OCTOBER 2019**

*This report has not been officially adopted by the Committee on Financial Services
and may not necessarily reflect the views of its Members*

Table of Contents

Executive Summary	1
I. INTRODUCTION.....	4
A. History of Consumer Bureau Obtaining Restitution on Behalf of Consumers	4
B. Trump-appointed leadership declares, “ <i>The CFPB Has Pushed Its Last Envelope</i> ”	5
C. Enforcement Activity Declines Dramatically Under Trump-Appointed Leadership	7
D. The Committee’s Investigation	8
II. FINDINGS.....	9
A. A Political Appointee Overruled Career Staff’s Recommendation to Require Enova To Refund the Money It Had Illegally Taken from Consumers’ Accounts	9
B. Director Mulvaney Rejects Enforcement’s Recommendation to Provide Restitution to Consumers Harmed by Sterling Jewelers Inc’s (Sterling) Unlawful Conduct	15
C. The Trend of Limiting Redress for Consumers in Settlements Continued	20
III. CONCLUSIONS	21
APPENDIX A	22
APPENDIX B.....	24
APPENDIX C	67
APPENDIX D	71
APPENDIX E.....	79
APPENDIX F.....	83
APPENDIX G	89
APPENDIX H	129
APPENDIX I.....	131
APPENDIX J	138
APPENDIX K	148
APPENDIX L.....	190

APPENDIX M..... 193

APPENDIX N 201

APPENDIX O 209

APPENDIX P 213

APPENDIX Q 231

APPENDIX R 252

APPENDIX S 300

APPENDIX T..... 329



“Consumers want and need to have someone stand on their side to see that they are treated fairly. We seek to protect them against unfair surprises, frustrating runarounds, and bad deals that ruin their credit, cost them their homes, and saddle them with further problems. We stand with them, proudly and unapologetically.”¹

- **Richard Cordray**, Director of the Consumer Bureau from January 2012 to November 2017

“It’s fair to say that the bureau’s previous governing philosophy was to ‘push the envelope’ aggressively, under the assumption that we were the good guys and the financial-service industry was the bad guys.... The days of aggressively ‘pushing the envelope’ are over.”²

- **Mick Mulvaney**, Acting Director of the Consumer Bureau from November 2017 to December 2018

Executive Summary

In November 2017, political appointees of President Donald Trump assumed control of the Consumer Financial Protection Bureau (Consumer Bureau), the federal government’s watchdog dedicated solely to protecting American consumers from unfair, deceptive and abusive practices. Trump-appointed officials have since undermined the Consumer Bureau, including by weakening the Bureau’s previously robust policing of anti-consumer misconduct in the financial sector. As a result, Consumer Bureau leadership has denied consumers millions of dollars in relief, even in cases where returning cash to harmed consumers was an available and appropriate remedy.

Under Trump-appointed leadership, the Consumer Bureau’s enforcement actions have declined in volume and failed to compensate harmed consumers adequately. For example, during Director Kathleen Kraninger’s first six-months (December 11, 2018 to June 11, 2019), the Consumer Bureau obtained only \$12 million in consumer relief,³ a mere 6% of the \$200 million reported by the Obama-appointed Director, Richard Cordray, during the six months from October 1, 2016 to March 31, 2017.⁴

¹ Richard Cordray, *Prepared Remarks of CFPB Director Richard Cordray at the People and Places Conference*, Consumer Bureau (May 31, 2017), <https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-cfpb-director-richard-cordray-people-and-places-conference/>.

² Mick Mulvaney, *The CFPB Has Pushed Its Last Envelope*, Wall Street Journal (Jan. 23, 2018) <https://www.wsj.com/articles/the-cfpb-has-pushed-its-last-envelope-1516743561>.

³ *Highlights of Director Kraninger’s First Six Months*, Consumer Bureau (Jun. 11, 2019), <https://www.consumerfinance.gov/about-us/newsroom/highlights-director-kraningers-first-six-months/>.

⁴ *Semi-annual report of the Consumer Financial Protection Bureau*, Consumer Bureau (June 2017), https://files.consumerfinance.gov/f/documents/201706_cfpb_Semi-Annual-Report.pdf. This is the final Semi-Annual report to Congress submitted by Director Cordray including the amount of relief obtained through enforcement actions.

In February 2019, the Committee on Financial Services (Committee) opened an investigation to examine how and why the Consumer Bureau, under Trump-appointed leadership, failed to seek consumer relief in certain cases. Committee investigators reviewed thousands of pages of internal Consumer Bureau communications related to two recent enforcement actions against Enova International, Inc. (Enova) and Sterling Jewelers Inc. (Sterling). In both cases, contrary to Consumer Bureau precedent and in defiance of the recommendations of the Consumer Bureau's career enforcement attorneys, Trump's appointees failed to pursue remedies that would have returned money to the victims.

In an administrative settlement announced on January 25, 2019, the Consumer Bureau found that Enova International, Inc. (Enova), an online lender, illegally replaced the bank account information for 6,829 of its customers with bank account information obtained from internet loan applications. Enova never informed, or obtained authorization from, these customers prior to taking over \$2.6 million from their bank accounts. Enova's conduct was analogous to a friend agreeing to lend you a hundred dollars and then seeking to collect it by sneaking into your house and taking the money from your wallet. Eighteen months before the settlement, career attorneys in the Consumer Bureau's Office of Enforcement (Enforcement) had recommended, and Director Corday had approved, ordering Enova to refund consumers the money it took. In settlement negotiations that occurred before Director Corday's departure, Enova offered to return approximately \$1.4 million to consumers.

After President Trump appointed the director of the Office of Management and Budget, Mick Mulvaney, to serve as the Consumer Bureau's Acting Director, the Consumer Bureau abandoned its demand that Enova return the illegally-debited funds to consumers. At the direction of Trump's political appointees — and against the recommendation of career enforcement attorneys — the Consumer Bureau ultimately settled with Enova in January 2019 for \$3.2 million in civil penalties payable to the Consumer Bureau. The consumers harmed by Enova's egregious conduct received nothing.

In a separate civil action brought in January 2019 against Sterling Jewelers Inc. (Sterling), the Consumer Bureau alleged that Sterling employees at retail stores opened store credit-card accounts in customers' names without their consent; misrepresented credit-card terms and conditions; and enrolled unwitting customers in payment-protection insurance. The Consumer Bureau's career enforcement attorneys recommended that Sterling be required to refund certain consumers that were harmed when Sterling enrolled them in unwanted payment-protection insurance. Between 2014 and 2017, Sterling received over \$50 million in revenue annually from the sale of payment-protection insurance.

Despite career staff's recommendation and the Consumer Bureau's history of requiring redress in similar cases,⁵ Trump-appointed leadership again refused to seek refunds for consumers and settled with Sterling for penalties of \$10 million paid to the Consumer Bureau and \$1 million to the State of New York.

⁵ See, e.g., *CFPB Probe into Capital One Credit Card Marketing Results in \$140 Million Consumer Refund*, Consumer Bureau (Jul. 18, 2012), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-capital-one-probe/> (requiring Capital One Bank to pay \$140 million in refunds for deceptive marketing of credit card add-on products); *CFPB Orders American Express to Pay \$59.5 Million for Illegal Credit Card Practices*, Consumer Bureau (Dec. 23, 2013), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-american-express-to-pay-59-5-million-for-illegal-credit-card-practices/> (requiring American Express to pay \$59.5 million in refunds for illegal marketing and administration of credit card add-on products); *CFPB Orders Chase and JPMorgan Chase to Pay \$309 Million Refund for Illegal Credit Card Practices*, Consumer Bureau (Sept. 19, 2013), <https://www.consumerfinance.gov/about->

The Committee's investigation of these specific matters revealed that the politicization of the Consumer Bureau contributed to the decline in the Consumer Bureau's enforcement activity, leaving consumers holding the bag when entities violate federal consumer financial law. To ensure that the Consumer Bureau fulfills its mission as an independent agency tasked with enforcing federal consumer financial law and protecting consumers, Congress should pass the Consumers First Act (H.R. 1500), legislation introduced by chairwoman Waters that limits the number of political appointees at the Consumer Bureau. The Committee should also consider ways to strengthen the provisions in the CFPB authorizing the Consumer Bureau to seek relief for consumers through enforcement actions.

[us/newsroom/cfpb-orders-chase-and-jpmorgan-chase-to-pay-309-million-refund-for-illegal-credit-card-practices/](https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-chase-and-jpmorgan-chase-to-pay-309-million-refund-for-illegal-credit-card-practices/) (requiring Chase to pay an estimated \$309 million in refunds for illegal practices relate to the sale of credit card add-on products); *CFPB Orders First National Bank of Omaha to Pay \$32.25 Million for Illegal Credit Card Practices*, Consumer Bureau (Aug. 25, 2016), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-first-national-bank-omaha-pay-3225-million-illegal-credit-card-practices/> (requiring First National Bank of Omaha to pay \$27.75 million for illegal marketing and administration of credit card add-on products).

I. INTRODUCTION

A. History of Consumer Bureau Obtaining Restitution on Behalf of Consumers

In the wake of the 2008 financial crisis, Congress established the Consumer Financial Protection Bureau (Consumer Bureau) to protect consumers from the unlawful and predatory conduct that led to millions of Americans losing their savings and homes. The Consumer Financial Protection Act of 2010 (CFPA) authorized the Consumer Bureau to investigate potential violations of federal consumer financial law.⁶ The Consumer Bureau can initiate civil and administrative actions against entities that violate federal consumer financial law,⁷ including the CFPA's prohibition against unfair, deceptive, or abusive practices.⁸ The CFPA gives the Consumer Bureau broad powers to obtain relief for consumers harmed when a company violates federal consumer financial law, including requiring the company to pay compensation (also called "redress" or "restitution") to its victims.⁹ The Consumer Bureau has the authority to enter into settlements with financial institutions that require redress.¹⁰

In 2012, President Barack Obama appointed Richard Cordray as the Consumer Bureau's first director. Under Director Cordray's leadership, the Consumer Bureau brought numerous enforcement actions against providers of financial products or services who cheated consumers out of their hard-earned money. The Consumer Bureau announced its first public enforcement action on July 18, 2012, against Capital One Bank for deceiving consumers with low credit scores or low credit limits into purchasing credit card add-on products when they called to activate their new credit card.¹¹ As a result of the Consumer Bureau's enforcement action, Capital One Bank paid approximately \$140 million in restitution to two million harmed consumers.¹² In the ensuing years under Obama-appointed leadership, the Consumer Bureau held to account financial institutions when they broke the law and routinely returned money to the consumers they had ripped off.

In its first six years, the Consumer Bureau brought 201 enforcement actions that provided nearly \$12 billion in consumer relief.¹³ On November 24, 2017 – Director Cordray's last day at the Consumer Bureau – the

⁶ 12 U.S.C. § 5562 (2017).

⁷ 12 U.S.C. §§ 5563 - 5564 (2017).

⁸ 12 U.S.C. § 5531 (2017). The Consumer Bureau can initiate an enforcement action through the filing a notice of charges in an administrative action or by commencing a civil action in federal court. *See* 12 U.S.C. § 5563 - 5564 (2017); 12 C.F.R. § 1081.200 (2019).

⁹ The CFPA explicitly states that a court or the Consumer Bureau in an administrative action "shall have jurisdiction to grant any appropriate legal or equitable relief with respect to a violation of Federal consumer financial law . . . Relief under this section may include, without limitation . . . refund of moneys . . . restitution . . . payment of damages or other monetary relief." 12 U.S.C. § 5565(a) (2017).

¹⁰ The Consumer Bureau can enter into administrative settlements. 12 C.F.R. § 1081.200(d) (2017) ("where the parties agree to settlement before the filing of a notice of charges, a proceeding may be commenced by filing a stipulation and consent order"). The Consumer Bureau may also obtain relief on behalf of harmed consumer by filing a settlement agreement and accompanying complaint in federal court. 12 U.S.C. § 5564(c) (2017) (the Consumer Bureau "may compromise or settle any action if such compromise is approved by the court").

¹¹ *CFPB Probe into Capital One Credit Card Marketing Results in \$140 Million Consumer Refund*, Consumer Bureau (Jul. 18, 2012), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-capital-one-probe/>.

¹² *Id.*

¹³ Christopher L. Peterson, *Dormant: The Consumer Financial Protection Bureau's Law Enforcement Program in Decline* at 14, Consumer Federation of America (Mar. 12, 2019), <https://consumerfed.org/wp-content/uploads/2019/03/CFPB-Enforcement-in-Decline.pdf>.

Consumer Bureau’s website indicated that over 29 million consumers had received relief through its enforcement actions as of July 20, 2017.¹⁴

B. Trump-appointed leadership declares, “*The CFPB Has Pushed Its Last Envelope*”

To preserve the independence of the Consumer Bureau, Congress included provisions in the CFPA to prevent the politicization of the director position. Under the CFPA, the Consumer Bureau’s director serves for a five-year term and can only be removed from office for cause.¹⁵ Therefore, President Trump could not replace Director Cordray – except for inefficiency, neglect, malfeasance – until his term expired in July 2018 or he resigned voluntarily.

Director Cordray announced his resignation in November 2017, after which President Trump appointed the director of the Office of Management and Budget, Mick Mulvaney, to serve as acting director of the Consumer Bureau.¹⁶ From the outset, Acting Director Mulvaney communicated that the Trump administration intended to rein in the Consumer Bureau’s efforts to protect consumers. In an opinion piece for the Wall Street Journal titled *The CFPB Has Pushed Its Last Envelope*, Acting Director Mulvaney wrote: “It’s fair to say that the bureau’s previous governing philosophy was to ‘push the envelope’ aggressively, under the assumption that we were the good guys and the financial-service industry was the bad guys.... The days of aggressively ‘pushing the envelope’ are over.”¹⁷ With respect to enforcement, Acting Director Mulvaney stated, “we will focus on quantifiable and unavoidable harm to the consumer. If we find that it exists, you can count on us to pursue the appropriate remedies vigorously. If it doesn’t, we won’t go looking for excuses to bring lawsuits.”¹⁸ Mr. Mulvaney’s statements reflected his prior opposition to the very existence of the Consumer Bureau. As a member of Congress, he sponsored legislation to eliminate the agency.¹⁹ He also introduced legislation that would have allowed states to opt-out from any Consumer Bureau rules on payday loans for five years.²⁰

To accomplish its goal of reining in the Consumer Bureau, the Trump administration needed to increase the number of political appointees in Bureau leadership. Under the CFPA, the only political appointee within the Consumer Bureau is a director appointed by the President and confirmed by the Senate.²¹ Before Trump appointees assumed leadership of the Consumer Bureau, career officials with the title of associate director led each of the divisions within the Consumer Bureau, including the Division of Supervision, Enforcement, and Fair Lending (SEFL). Almost immediately upon taking control of the Consumer Bureau, Trump-appointed leadership

¹⁴ Consumer Bureau Homepage, Internet Archive Wayback Machine, <https://web.archive.org/web/20171123215352/https://www.consumerfinance.gov/> (last accessed Nov. 23, 2017).

¹⁵ 12 U.S.C. § 5491(c) (2017) (“The Director shall serve for a term of 5 years . . . Removal for Cause – The President may remove the Director for inefficiency, neglect of duty, or malfeasance in office”).

¹⁶ Tara Siegel Bernard, *Dueling Appointments Lead to Clash at Consumer Protection Bureau*, The New York Times (Nov. 24, 2017), <https://www.nytimes.com/2017/11/24/us/politics/consumer-financial-protection-bureau-cordray-leader-trump-mulvaney.html>.

¹⁷ Mick Mulvaney, *The CFPB Has Pushed Its Last Envelope*, Wall Street Journal (Jan. 23, 2018) <https://www.wsj.com/articles/the-cfpb-has-pushed-its-last-envelope-1516743561>.

¹⁸ *Id.*

¹⁹ Chris Arnold, *The Consumer Complaints Database That Could Disappear From View*, NPR (Apr. 25, 2018), <https://www.npr.org/2018/04/25/605835307/the-consumer-complaints-database-that-could-disappear-from-view>.

²⁰ Chico Harlan, *The pending crackdown on payday lending is causing the exact Washington argument you’d expect*, The Washington Post (Apr. 5, 2016), <https://www.washingtonpost.com/news/wonk/wp/2016/04/05/the-pending-crackdown-on-payday-lending-is-causing-the-exact-washington-argument-you-d-expect/>.

²¹ 12 U.S.C. § 5535(a).

announced its plan to hire political appointees to oversee each of the Consumer Bureau's divisions.²² Typically, federal financial regulators are staffed and led almost entirely by professional, career employees. Acting Director Mulvaney's decision to politicize the agency's top positions threatened to compromise the Consumer Bureau's independence.²³

In December 2017, Acting Director Mulvaney appointed Eric Blankenstein to oversee SEFL.²⁴ Mr. Blankenstein's professional background alone raised questions about his commitment to protecting consumers. Mr. Blankenstein had spent the majority of his legal career as an associate at Williams & Connolly where he "represent[ed] banks in regulatory investigations and litigation with the Office of the Comptroller of the Currency (OCC) and CFPB alleging violations of various consumer laws...."²⁵ While at Williams & Connolly, Mr. Blankenstein argued that the Consumer Bureau was unconstitutional in a motion filed on behalf of a bank seeking to dismiss a lawsuit filed by the Bureau.²⁶

Media outlets reported on the extent of Mr. Blankenstein's control over the day-to-day work of the Consumer Bureau's enforcement attorneys, including approving what documents they could demand from entities during their investigations.²⁷ It was also reported that Mr. Blankenstein reduced fines and consumer redress in certain cases. A December 2018 Washington Post article reported that in a case against a South Carolina lender and its affiliates, Mr. Blankenstein, "pushed to slash the fine" from \$11 million to ultimately \$5 million.²⁸ In a case against National Credit Adjusters, the Washington Post reported that Mr. Blankenstein "scrapped the recommendation" by career staff that would have provided \$60 million to consumers, instead only requiring an \$800,000 penalty.²⁹

On December 6, 2018, the United States Senate confirmed Trump-nominee Kathleen Kraninger as the new Director of the Consumer Bureau.³⁰ Director Kraninger continued the Trump administration's politicization of

²² Kevin Wack, *Mulvaney's plan to embed political staffers in CFPB sparks backlash*, American Banker (Dec. 05, 2017), <https://www.americanbanker.com/news/mulvaney-s-plan-to-embed-political-staffers-in-cfpb-sparks-backlash>; Nicholas Confessore, *Mick Mulvaney's Master Class in Destroying a Bureaucracy From Within*, The New York Times Magazine (Apr. 16, 2019), <https://www.nytimes.com/2019/04/16/magazine/consumer-financial-protection-bureau-trump.html>.

²³ *Id.*

²⁴ C. Ryan Barber, *Ex-Williams & Connolly Associate Snags Senior Adviser Post at Mulvaney's CFPB*, National Law Journal (Dec. 21, 2017), <https://www.law.com/nationallawjournal/sites/nationallawjournal/2017/12/21/ex-williams-connolly-associate-snags-senior-advisor-post-at-mulvaney-s-cfpb/>.

²⁵ Resume of Eric G. Blankenstein produced to American Oversight, <https://www.documentcloud.org/documents/6167433-AO-CFPB-Resumes-2.html#document/p3/a508877> (accessed Sept. 27, 2019).

²⁶ Memorandum of Law in Support of Defendant's Motion to Dismiss (Feb. 17, 2017), *Consumer Financial Protection Bureau v. TCF National Bank* (No. 0:17-cv-00166-RHK-KMM), https://www.chamberlitigation.com/sites/default/files/cases/files/17171717/Memo%20in%20Support%20of%20Defendant%27s%20MTD%20--%20CFPB%20v.%20TCF%20National%20Bank%20%28USDC%20-%20District%20of%20Minnesota%29_0.pdf.

²⁷ Nicholas Confessore, *Mick Mulvaney's Master Class in Destroying a Bureaucracy From Within*, The New York Times Magazine (Apr. 16, 2019), <https://www.nytimes.com/2019/04/16/magazine/consumer-financial-protection-bureau-trump.html>.

²⁸ Robert O' Harrow Jr. et al., *How Trump appointees curbed a consumer protection agency loathed by the GOP*, The Washington Post (Dec. 4, 2018), https://www.washingtonpost.com/investigations/how-trump-appointees-curbed-a-consumer-protection-agency-loathed-by-the-gop/2018/12/04/3cb6cd56-de20-11e8-aa33-53bad9a881e8_story.html?utm_term=.ce862709945b.

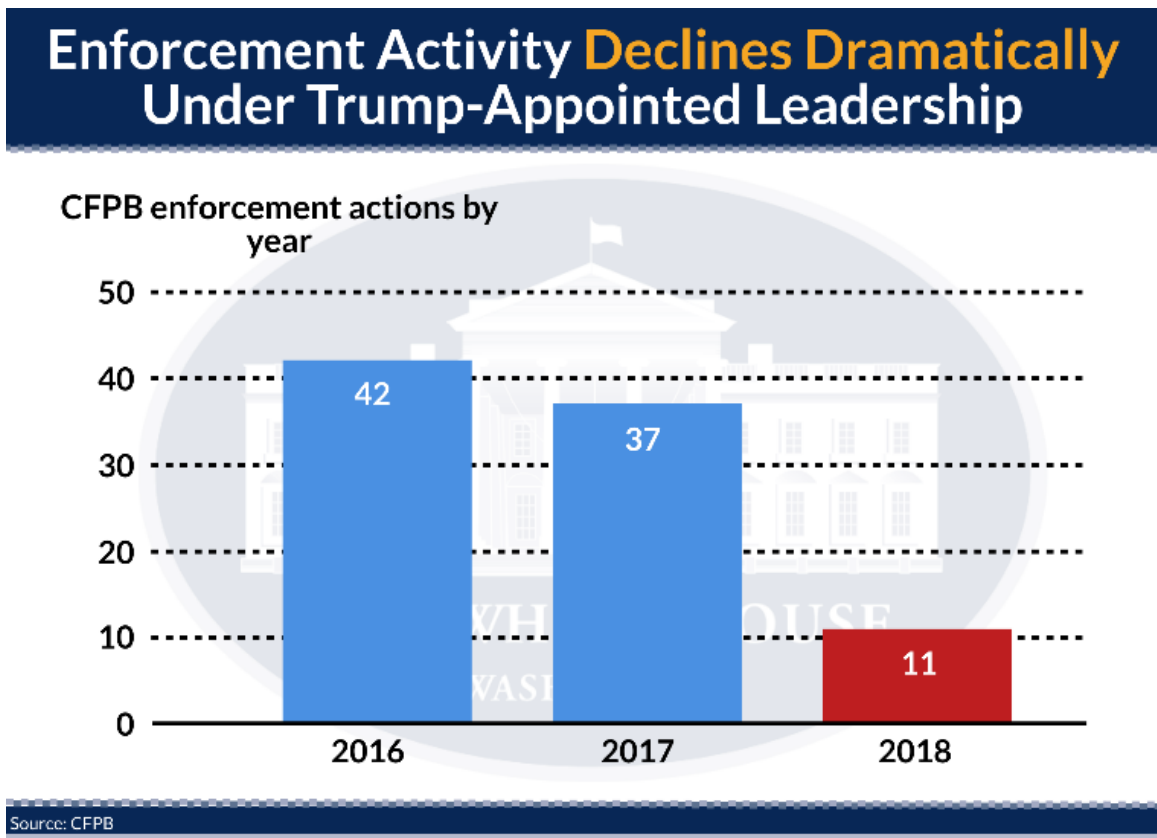
²⁹ *Id.*

³⁰ Jim Puzzanghera, *Senate confirms new consumer financial protection chief: Kathy Kraninger, protégé of industry-friendly Mick Mulvaney*, Los Angeles Times (Dec. 6, 2018), <https://www.latimes.com/business/la-fi-cfpb-kraninger-confirmation-20181206-story.html>.

the Consumer Bureau by maintaining the political positions created by Acting Director Mulvaney, including Mr. Blankenstein, who continued to oversee the Bureau’s enforcement activities until he resigned in May 2019.³¹

C. Enforcement Activity Declines Dramatically Under Trump-Appointed Leadership

The number of public enforcement actions taken by the Consumer Bureau declined dramatically under the Trump administration.³² During the twelve-month tenure of Acting Director Mulvaney, the Consumer Bureau announced only eleven public enforcement actions, as compared to thirty-seven in 2017 and forty-two in 2016 under Obama-appointed leadership.³³ The amount of consumer relief obtained by the Consumer Bureau in the public enforcement actions it did bring also declined. Under Obama-administration leadership, the average enforcement action by the Consumer Bureau returned \$59.6 million to consumers, as compared to an average \$31.4 million per action under Mulvaney.³⁴ However, even this average does not adequately portray the contrast between the two directors, as the Trump administration’s enforcement data is skewed by one particularly large settlement. Specifically, of the \$345 million in consumer relief obtained during Acting Director Mulvaney’s tenure, the Consumer Bureau obtained almost all the consumer relief from a \$335 million settlement with Citibank.³⁵



³¹ Renae Merle, *Trump appointee, whose past blogs on race sparked backlash, resigns*, The Washington Post (May 15, 2019), <https://www.washingtonpost.com/business/2019/05/15/trump-appointee-whose-past-blogs-race-sparked-backlash-resigns/>.

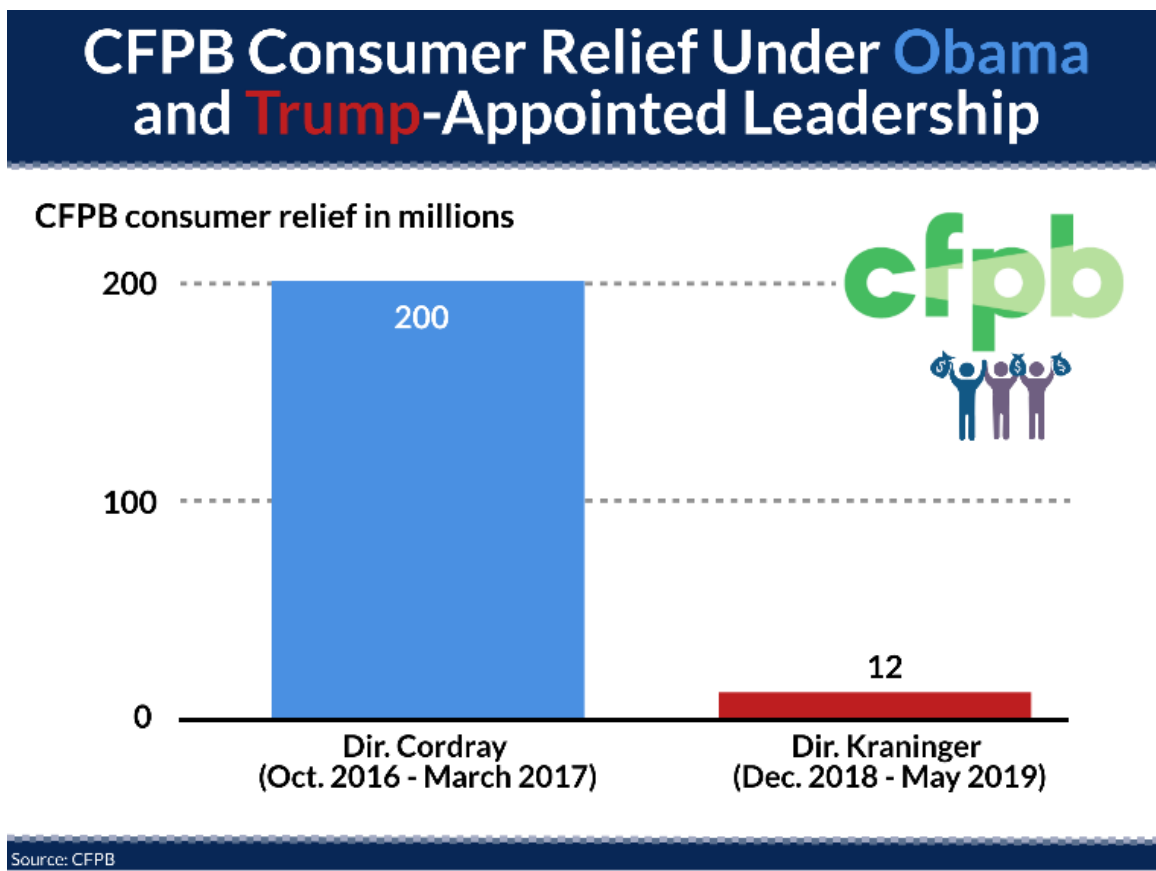
³² Christopher L. Peterson, *Dormant: The Consumer Financial Protection Bureau’s Law Enforcement Program in Decline*, Consumer Federation of America (Mar. 12, 2019), <https://consumerfed.org/wp-content/uploads/2019/03/CFPB-Enforcement-in-Decline.pdf>.

³³ *Id.* at 15.

³⁴ *Id.* at 16.

³⁵ *Id.*

While the pace of enforcement actions increased during Director Kraninger’s first six months as Director, the downward trend in the Consumer Bureau obtaining consumer relief under Trump-appointed leadership persisted. The Consumer Bureau announced eleven public enforcement actions during the first six months of Director Kraninger’s tenure but ordered only \$12 million in consumer relief.³⁶ This contrasts with the approximately \$200 million in consumer relief reported in the Consumer Bureau’s final semi-annual report to Congress submitted by an Obama-appointed director, covering the six months between October 1, 2016, and March 31, 2017.³⁷



The precipitous decline in the Consumer Bureau’s enforcement activity under the Trump administration resulted in less money being returned to American consumers harmed by bad actors in the financial services sector.

D. The Committee’s Investigation

The Committee initiated its investigation in response to the Consumer Bureau’s January 16, 2019 settlement with Sterling Jewelers Inc. (Sterling), January 25, 2019 settlement with Enova International, Inc. (Enova), and

³⁶ *Highlights of Director Kraninger’s First Six Months*, Consumer Bureau (June 11, 2019), <https://www.consumerfinance.gov/about-us/newsroom/highlights-director-kraningers-first-six-months/>. The number of enforcement actions was obtained through a search of the Consumer Bureau’s website. See *Enforcement actions*, Consumer Bureau, <https://www.consumerfinance.gov/policy-compliance/enforcement/actions/> (accessed Sept. 27, 2019).

³⁷ *Semi-annual report of the Consumer Financial Protection Bureau*, Consumer Bureau (June 2017), https://files.consumerfinance.gov/f/documents/201706_cfpb_Semi-Annual-Report.pdf.

February 1, 2019 settlement with NDG Financial Corporation and other Defendants (NDG Financial). These settlements authorized by Director Kraninger did not require the payment of redress to consumers harmed by the unlawful actions of the defendants in these matters.

The Committee sought to understand how the Consumer Bureau decided not to order consumer redress in these cases and, given prior media reports about the politicization of the Bureau, the role played by political appointees in enforcement decisions.³⁸ On February 7, 2019, Committee Chairwoman Maxine Waters and Subcommittee on Oversight and Investigations Chairman Al Green wrote to Director Kraninger requesting internal Consumer Bureau communications and documents related to the decision not to seek consumer redress in the aforementioned cases. Additionally, the Committee requested external communications between the Consumer Bureau and representatives of Sterling, Enova, and NDG Financial.³⁹

The Consumer Bureau produced the requested external communications with Sterling and Enova,⁴⁰ but the Committee encountered significant obstacles in obtaining internal documents from the Consumer Bureau regarding its decision not to seek consumer redress in these cases. Correspondence between Chairwoman Waters and Director Kraninger detail the Consumer Bureau's objections and the Committee's efforts to address them.⁴¹ The Consumer Bureau initially declined to produce any internal documents to the Committee.⁴² After extensive negotiations, the Consumer Bureau ultimately produced a self-selected subset of the internal documents requested by the Committee.

The Consumer Bureau generally refused to produce responsive emails, instead only permitting an *in-camera* review of certain emails. The Consumer Bureau withheld an untold number of documents, it only produced 1,974 pages of documents to the Committee. The Committee relied on these documents and the emails reviewed *in camera* to make the findings contained in this report.

II. FINDINGS

A. A Political Appointee Overruled Career Staff's Recommendation to Require Enova To Refund the Money It Had Illegally Taken from Consumers' Accounts

Acting Director Mulvaney appointed Eric Blankenstein as the political appointee responsible for overseeing the Consumer Bureau's Office of Enforcement (Enforcement). Following his appointment, the Washington Post reported that Mr. Blankenstein had previously authored racist blog posts that questioned "if using the n-word was

³⁸ Robert O' Harrow Jr. et al., *How Trump appointees curbed a consumer protection agency loathed by the GOP*, The Washington Post (Dec. 4, 2018), https://www.washingtonpost.com/investigations/how-trump-appointees-curbed-a-consumer-protection-agency-loathed-by-the-gop/2018/12/04/3cb6cd56-de20-11e8-aa33-53bad9a881e8_story.html?utm_term=.ce862709945b.

³⁹ Letter from Chairwoman Maxine Waters to Director Kathleen Kraninger (Feb. 7, 2019).

⁴⁰ Letter from Director Kathleen Kraninger to Chairwoman Maxine Waters (Mar. 5, 2019). Based on the representations in the March 5, 2019 letter, the Committee determined not to pursue further investigation of the NDG Financial settlement.

⁴¹ Letter from Chairwoman Maxine Waters to Director Kathleen Kraninger (Mar. 28, 2019); Letter from Chairwoman Maxine Waters to Director Kathleen Kraninger (June 20, 2019).

⁴² Letter from Director Kathleen Kraninger to Chairwoman Maxine Waters (Mar. 5, 2019).

inherently racist” and whether most hate crimes were hoaxes.⁴³ Mr. Blankenstein remained at the Consumer Bureau under Director Kraninger until he resigned in May of 2019.⁴⁴

Mr. Blankenstein overruled the recommendation of career attorneys and non-partisan senior management in Enforcement to order Enova to provide consumer redress. Before resigning, Director Cordray had approved Enforcement’s recommendation to require that Enova compensate consumers as a condition of settling the Consumer Bureau’s enforcement action. Nevertheless, Mr. Blankenstein explicitly directed Enforcement not to seek redress in the Consumer Bureau’s settlement with Enova. Director Kraninger ratified Mr. Blankenstein’s decision when she signed the Consumer Bureau’s consent order with Enova.

Mr. Blankenstein explicitly directed Enforcement not to seek redress in the Consumer Bureau’s settlement with Enova.

i. Director Cordray Approved Enforcement’s Recommendation to Require Enova to Refund the Money Illegally Debited from Consumers’ Accounts

Enforcement described Enova’s misconduct in a July 26, 2017 memo to Director Cordray seeking authority to settle the Consumer Bureau’s claims against the company.⁴⁵ Enova, an online lender that markets unsecured payday and installment loans and lines of credit, purchased loan applications from lead generators.⁴⁶ Lead generators collect relevant information from potential borrowers, including bank account information, and sell it to potential lenders like Enova.

Sometimes Enova purchased loan applications from lead generators for consumers who already had outstanding loans with the company, and Enova’s policy was to deny these applications.⁴⁷ However, without informing them or obtaining their authorization, Enova replaced the bank account information of 6,829 consumers with the bank account information contained in these loan applications.⁴⁸ Enova then attempted to unlawfully debit over \$5 million from consumers’ accounts, successfully withdrawing \$2,638,933 in payments.⁴⁹

Enova’s unauthorized attempts to debit consumers’ accounts — successful or not — could have resulted in insufficient fund (NSF) charges and other bank fees.⁵⁰ Enova engaged in additional unlawful practices, but its

⁴³ Robert O’Harrow Jr. et al., *Trump anti-discrimination official once called most hate crimes hoaxes*, The Washington Post (Sept. 26, 2018), https://www.washingtonpost.com/investigations/trump-anti-discrimination-official-once-called-most-hate-crimes-hoaxes/2018/09/26/05438bbe-c0fe-11e8-92f2-ac26fda68341_story.html.

⁴⁴ Renae Merle, *Trump appointee, whose past blogs on race sparked backlash, resigns*, The Washington Post (May 15, 2019), <https://www.washingtonpost.com/business/2019/05/15/trump-appointee-whose-past-blogs-race-sparked-backlash-resigns/>.

⁴⁵ Recommendation Memorandum for the Director (July 26, 2017), HFSC_CFPB_030519_00001824 - 43.

⁴⁶ *Id.* at 1826-1827.

⁴⁷ *Id.* at 1827.

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.*

practice of making unauthorized debits caused consumers the most harm.⁵¹ Enova had previously been the subject of an enforcement action by the Consumer Bureau.⁵²

On November 13, 2013, the Consumer Bureau entered into a consent order with Enova related to its unlawful conduct during a routine examination, including destroying documents and failing to provide requested information.⁵³

In the July 26, 2017 memo to Director Cordray, Enforcement recommended requiring Enova to refund consumers approximately \$2.16 million for successful unauthorized debits, and an “additional amount for all consumers affected by Enova’s unauthorized debiting, as a proxy amount for the consumer’s loss.”⁵⁴ Enforcement also recommended requiring redress of approximately \$30,840 for additional legal violations committed by Enova. Director Cordray approved Enforcement’s recommendation memo on the same day it was submitted.⁵⁵

Beginning in August 2017, the Consumer Bureau engaged in settlement negotiations with Enova. On November 7, 2017, Enova offered to provide \$1,367,567 in redress to consumers that included, “[f]ull refunds” for consumers with payday loans and “[r]efunds for up to four debits for installment loan and line-of-credit customers.”⁵⁶ This figure included redress related to NSF and other fees incurred as a result of Enova’s unauthorized debiting of accounts, regardless of whether the debit was successful.⁵⁷

ii. The Legal Division Affirms that the Consumer Bureau has the Authority to Seek Refunds of the Money Enova Took without Authorization.

On January 30, 2018, Enforcement submitted a memo to Mr. Blankenstein informing him that Enova had made a settlement offer of \$1,367,567 in redress on November 7, 2017 (prior to Director Cordray’s resignation), but on December 4, 2017 (after Mr. Mulvaney became Acting Director) Enova communicated that it was reassessing its settlement position.⁵⁸ On April 27, 2018, Mr. Blankenstein emailed his Senior Legal Advisor, a career employee, that he was “worried about restitution” in the Enova matter and requested that he call him “to discuss.”⁵⁹ Mr. Blankenstein requested that the Legal Division provide analysis on whether courts consider it

⁵¹ *Id.* at 1828-1831.

⁵² *Consumer Financial Protection Bureau Takes Action Against Payday Lender for Robo-Signing*, Consumer Bureau (Nov. 20, 2013), <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-takes-action-against-payday-lender-for-robo-signing/>.

⁵³ *Id.*

⁵⁴ Recommendation Memorandum for the Director at 1839 (July 26, 2017), HFSC_CFPB_030519_00001824 - 43. The difference between the \$2,638,933 successfully debited and the \$2.16 million in recommended redress was due to the fact that the enforcement attorneys recommended only seeking restitution for consumers whose bank accounts Enova unlawfully debited after the Consumer Bureau was established in 2011.

⁵⁵ Decision Memorandum from the Director (July 26, 2017), HFSC_CFPB_030519_00001906.

⁵⁶ Recommendation Memorandum for the SEFL Policy Director at 1959 - 60 (Oct. 3, 2018), HFSC_CFPB_030519_00001959 - 64.

⁵⁷ *Id.* Specifically Enova’s offer included

- \$35 per transaction for up to four debits for all consumers whose bank accounts Enova successfully debited without authorization;
- \$35 per transaction for up to four debits for all consumers whose bank accounts Enova attempted to debit without authorization; and
- \$35 per transaction for up to four debits for all consumers for whom Enova failed to honor loan extensions.

⁵⁸ Decision memo for Senior Advisor to the Acting Director (Jan. 30, 2018) (in-camera review).

⁵⁹ Email from Eric Blankenstein to Senior Legal Advisor (Apr. 27, 2018) (in-camera review).

appropriate to require a creditor to return money illegally collected from a borrower that actually owed the debt, as detailed in a May 2, 2018 email from the Senior Legal Advisor.⁶⁰

In two separate memos provided to Mr. Blankenstein, the Legal Division concluded that a legal basis existed for the Consumer Bureau to order Enova to refund consumers the money illegally debited from their

On May 6, 2018, the Senior Legal Advisor informed Mr. Blankenstein of the Legal Division’s conclusion that the law supported the Consumer Bureau seeking consumer redress against Enova.

accounts. While noting that their analysis was “preliminary,” the Legal Division concluded in a May 4, 2018 memo that the Consumer Bureau could indeed require Enova to refund consumers the “entire amount” illegally debited from consumers’ accounts, “notwithstanding that the consumer owed the debt.”⁶¹ On May 6, 2018, the Senior Legal Advisor informed Mr.

Blankenstein of the Legal Division’s conclusion that the law supported the Consumer Bureau seeking consumer redress against Enova.⁶²

On May 31, 2018, the Legal Division provided a more comprehensive thirty-nine-page memo addressing whether illegally debiting amounts actually owed could harm consumers.⁶³ The memo also addressed what was the “appropriate remedy” when a creditor illegally collects a debt actually owed.⁶⁴ Consistent with its initial analysis, the Legal Division concluded that consumers can suffer harm when creditors illegally collect debts actually owed.⁶⁵ The Legal Division also determined that it would be “legally appropriate,” although not required, for the Consumer Bureau to require Enova to refund consumers the money debited from their accounts without authorization.⁶⁶ Notably, the Legal Division asserted that there was no question that Enova caused harm when it “simply improperly t[ook] money from consumers.”⁶⁷

In analyzing these issues, the Legal Division referred to two prior occasions where the Consumer Bureau had ordered entities to provide redress to consumers for illegally collecting debt even where the debt was actually owed.⁶⁸ In 2012, the Consumer Bureau entered into a consent order with American Express⁶⁹ for illegal debt

⁶⁰ Email from Senior Legal Advisor to Cara Petersen et al. (May 4, 2018), HFSC_CFPB_030519_00001907.

⁶¹ Email from Legal Division attorney to Senior Legal Advisor et al. (May 4, 2018), HFSC_CFPB_030519_00001907; Attachment to email from Legal Division attorney to Senior Legal Advisor et al. (L&P Outline Regarding Debt Collection of Amounts that Consumers Actually Owe) at 1909 (May 4, 2018), HFSC_CFPB_030519_00001909 - 15.

⁶² Email from Senior Legal Advisor to Eric Blankenstein (May 6, 2018) (in-camera review) (“In essence, Legal’s view is that under the CFPB the Bureau could reasonably seek as damages the entire amount improperly taken from the consumer, leaving the collector to attempt to re-collect that amount using lawful means.”).

⁶³ Attachment to email from Eric Blankenstein to Senior Legal Advisor at 1918 (June 7, 2018), HFSC_CFPB_030519_00001916 - 56.
⁶⁴ *Id.*

⁶⁵ *Id.* at 1935 (“Based on our understanding of this precedent, we conclude that a consumer can be substantially injured when a creditor or debt collector improperly takes money from a consumer, even if the consumer owed a valid debt.”).

⁶⁶ *Id.* at 1954 (“From the relevant precedent, we are inclined to conclude that it would be legally appropriate for the Bureau to seek consumer redress in the full amount taken from consumers when a debt collector or creditor improperly takes money from consumers, notwithstanding that consumers owe a debt.”).

⁶⁷ *Id.* at 1955.

⁶⁸ *Id.* at 1920 - 21.

⁶⁹ American Express refers collectively to American Express Centurion Bank and American Express Bank, FSB.

collection practices that required the company to provide \$85 million in consumer redress.⁷⁰ In seeking such relief in the American Express matter, Enforcement attorneys reasoned, “[c]reditors and debt collectors have a right to collect debts that are owed. They do not, however, have a right to break the law when doing so ... in order to prevent consumers from receiving an improper windfall, we propose ... to allow the Bank to resume collection activities on the refunded debt....”⁷¹ Also, in a 2014 consent order with ACE Cash Express for using illegal tactics when collecting payday loan debt, the Consumer Bureau required the company to refund \$5 million to its consumers.⁷²

iii. Mr. Blankenstein Ordered Enforcement Management not to Require Redress and Eliminated Certain Claims Against Enova

On June 26, 2018, Mr. Blankenstein engaged in an email exchange with his Senior Legal Advisor about ordering Enforcement management not to seek refunds for consumers in the Enova matter. Mr. Blankenstein indicated that, irrespective of the Legal Division’s analysis, his position was that illegally debiting amounts actually owed did not harm consumers, and he thus did not want to require Enova to refund consumers the money withdrawn from their accounts.⁷³ In response, the Senior Legal Advisor noted that “a good argument” existed that the unauthorized debits did injure consumers, even if refunding the amount debited was not an available remedy.⁷⁴ Mr. Blankenstein, rejecting his Senior Legal Advisor’s advice, emailed Enforcement management later that day that he was “ok going forward” with the claim not because Enova’s unlawful debiting of accounts itself harmed consumers, but because the illegal debits resulted in consumers being charged NSF fees and overdraft charges as a result of “lower than expected account balances.”⁷⁵ Mr. Blankenstein appears to have adopted the argument made by Enova in their June 18, 2018 letter to Mr. Blankenstein and Kristen Donoghue, the Enforcement Director, that “[t]he only actual harm caused by the inadvertent account update would be any NSF or overdraft fees resulting from the debits to the incorrect account.”⁷⁶

Mr. Blankenstein, in that same email, explicitly directed Enforcement not to seek refunds of the amounts illegally debited:

I have reviewed Legal’s and Enforcement’s research on the question of whether the Bureau may seek as a remedy restitution of amounts that were validly owed but taken without authorization from a specific

⁷⁰ *CFPB Orders American Express to Pay \$85 Million Refund to Consumers Harmed by Illegal Credit Card Practices*, Consumer Financial Protection Bureau (Oct. 01, 2012), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-american-express-to-pay-85-million-refund-to-consumers-harmed-by-illegal-credit-card-practices/>.

⁷¹ Attachment to email from Eric Blankenstein to Senior Legal Advisor at 1920 (June 7, 2018), HFSC_CFPB_030519_00001916 - 56 (quoting July 26, 2012 Decision Memorandum for American Express approved by Director Cordray).

⁷² *Id.* at 1921; *CFPB Takes Action Against ACE Cash Express for Pushing Payday Borrowers Into Cycle of Debt*, Consumer Bureau (Jul. 10, 2014), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-ace-cash-express-for-pushing-payday-borrowers-into-cycle-of-debt/>.

⁷³ Email from Eric Blankenstein to Senior Legal Advisor (June 28, 2018) (in-camera review) (“Neither the unfairness liability nor restitution should be based on the actual amount of the unauthorized debit (where there is no dispute that it was for a valid debt actually due and owing).”).

⁷⁴ Email from Senior Legal Advisor to Eric Blankenstein (June 28, 2018) (in-camera review) (“I wouldn’t say in this email that the unfairness ‘liability’ theory should not be based on the amount of the debt validly owed. We have a good argument that the unauthorized taking of money from a consumer’s account is part of the ‘injury’ caused by the unfair practice here – even if restitution is not available for the aspect of the injury. . . .”).

⁷⁵ Email from Eric Blankenstein to Cara Petersen and Kristen Donoghue (June 28, 2018), HFSC_CFPB_030519_00001957 - 58.

⁷⁶ Letter from Matthew Previn to Kristen Donoghue at 1157 (June 18, 2018), HFSC_CFPB_030519_00001155 - 61.

bank account. Having considered the research, having discussed the issue with the Acting Director, based on the facts of this case the Bureau should not seek restitution of those amounts, and should instead impose only a civil penalty for this violation....⁷⁷

Cara Petersen, the Deputy Enforcement Director, then asked Mr. Blankenstein whether his decision to deny refunds to consumers would change if the Consumer Bureau “required Enova to return to consumers the funds it withdrew from their bank accounts without authorization, but also allowed it to recollect those amounts using lawful means?”⁷⁸ In prior negotiations with Enova, Enforcement had anticipated that any settlement would permit Enova to lawfully collect the debt in the future (even any amount refunded to consumers).⁷⁹ Mr. Blankenstein responded minutes later that he was not sure he “fully understood” her question, but that he “affirmatively d[id] not want the consent order to require repayment of debited funds when there is no dispute about the validity of the debt.”⁸⁰

Mr. Blankenstein also directed Enforcement not to seek refunds of the NSF and overdraft charges resulting from Enova’s unauthorized debits and other legal violations unless they could be “calculated with certainty for each affected consumer.”⁸¹ However, as the career enforcement attorneys explained, [t]he precise amount of fees incurred each affected consumer cannot be calculated with certainty because many of these transactions occurred over eight years ago and few, if any, consumers will have retained the relevant records for that length of time.”⁸²

Not only did Mr. Blankenstein direct Enforcement management not to seek redress for consumers, but he also directed them to drop three claims they intended to bring against Enova, including one concerning deceptive statements Enova made to consumers.⁸³ He also directed Enforcement not to pursue an additional claim if it became “an obstacle to settlement.”⁸⁴ The decision to drop claims took Enforcement management, and even the Senior Legal Advisor, by surprise. The Enforcement Director, Kristen Donoghue, had previously emailed Mr. Blankenstein that, “[o]ur understanding from [the Senior Legal Advisor] is that you are comfortable with liability and wanted to have further discussions just on remedies.”⁸⁵ After Mr. Blankenstein directed Enforcement to drop the three claims, Ms. Petersen emailed the Senior Legal Advisor that she “thought he was good on liability for all of the claims?”⁸⁶ The Senior Legal Advisor responded, “[s]o did I – I didn’t realize until today he hadn’t meant to include the various other claims. Apologies for the confusion.”⁸⁷

On October 3, 2018, Enforcement submitted a decision memo to Mr. Blankenstein seeking his authorization to enter into a settlement with Enova outside of the parameters previously authorized by Director Cordray and consistent with the directive contained in Mr. Blankenstein’s June 28, 2018 email to Enforcement

⁷⁷ Email from Eric Blankenstein to Cara Petersen and Kristen Donoghue (June 28, 2018), HFSC_CFPB_030519_00001957 - 58.

⁷⁸ Email from Cara Petersen to Eric Blankenstein and Kristen Donoghue at 1957 (June 28, 2018), HFSC_CFPB_030519_00001957 - 58.

⁷⁹ Recommendation Memorandum for the SEFL Policy Director at 1961 n.02 (Oct. 3, 2018), HFSC_CFPB_030519_00001959 - 64.

⁸⁰ Email from Eric Blankenstein to Cara Petersen and Kristen Donoghue at 1957 (June 28, 2018), HFSC_CFPB_030519_00001957 - 58.

⁸¹ Recommendation Memorandum for the SEFL Policy Director at 1961 (Oct. 3, 2018), HFSC_CFPB_030519_00001959 - 64.

⁸² *Id.*

⁸³ Email from Eric Blankenstein to Cara Petersen and Kristen Donoghue (June 28, 2018), HFSC_CFPB_030519_00001957 - 58.

⁸⁴ *Id.*

⁸⁵ Email from Kristen Donoghue to Eric Blankenstein (June 18, 2018) (in-camera review).

⁸⁶ Email from Cara Petersen to Senior Legal Advisor (June 28, 2018) (in-camera review).

⁸⁷ Email from Senior Legal Advisor to Cara Petersen (June 28, 2018) (in-camera review).

management.⁸⁸ Acting Director Mulvaney had delegated his authority to Mr. Blankenstein to approve settlement parameters for the Enova matter.⁸⁹ The October 3, 2018 decision memo chronicled the history of the matter: Director Cordray’s prior authorization to seek refunds of amounts illegally debited and Legal Division’s opinion that the Consumer Bureau could require a creditor to refund payments illegally collected but actually owed; Enova’s November 7, 2017 offer to pay \$1,367,567 in redress; Mr. Blankenstein’s directive that Enforcement should no longer seek redress for consumers; and Mr. Blankenstein’s directive to drop three claims previously authorized by Director Cordray.⁹⁰ Mr. Blankenstein approved the decision memo on October 3, 2018.⁹¹

iv. Director Kraninger Approved Mr. Blankenstein’s Decision to Overrule the Recommendation of Career Enforcement Attorneys

On January 22, 2019, Director Kraninger signed a consent order with Enova that lacked any redress for consumers whose accounts Enova illegally debited.⁹² Prior to her signing the consent order, Enforcement provided Director Kraninger with documentation describing how Mr. Blankenstein overruled Enforcement’s prior recommendation to require Enova to provide consumer redress. On January 18, 2019, Enforcement submitted a recommendation memo to Director Kraninger recommending that she sign a consent order resolving the Consumer Bureau’s investigation of Enova consistent with the revised settlement terms authorized by Mr. Blankenstein on October 3, 2018.⁹³ The memo to Director Kraninger informed her that, “under the delegation of authority from Acting Director Mulvaney for matters in which Director Cordray had previously authorized Enforcement to settle or sue, the SEFL Policy Director revised the parameters for settlement. Those revisions are memorialized in an October 3, 2018 memo from Enforcement to the SEFL Policy Director.”⁹⁴ Enforcement provided Director Kraninger with both the original July 27, 2017 memo to Director Cordray and the October 3, 2018 memo detailing Mr. Blankenstein’s directives to Enforcement on how to proceed in the matter.⁹⁵

On January 22, 2019, Director Kraninger signed a consent order with Enova that lacked any redress for consumers whose accounts Enova illegally debited.

B. Director Mulvaney Rejects Enforcement’s Recommendation to Provide Restitution to Consumers Harmed by Sterling Jewelers Inc’s (Sterling) Unlawful Conduct

Mr. Mulvaney rejected Enforcement’s recommendation to require Sterling to provide restitution to consumers that Sterling had unlawfully enrolled in payment protection insurance. Mr. Mulvaney’s decision represented a departure from the Consumer Bureau’s prior settlements involving similar misconduct that required entities to

⁸⁸ Recommendation Memorandum for the SEFL Policy Director (Oct. 3, 2018), HFSC_CFPB_030519_00001959 - 64. The memo also sought civil monetary penalties.

⁸⁹ *Id.* at 1960.

⁹⁰ Recommendation Memorandum for the SEFL Policy Director (Oct. 3, 2018), HFSC_CFPB_030519_00001959 - 64.

⁹¹ Decision Memorandum from the SEFL Policy Director (Oct. 3, 2018), HFSC_CFPB_030519_00001965.

⁹² Consent Order, *In the Matter of Enova International, Inc.*, 2019-BCFP-0003 (Jan. 25, 2019),

https://files.consumerfinance.gov/f/documents/cfpb_enova-international_consent-order_2019-01.pdf.

⁹³ Recommendation Memorandum for the Acting Director (Jan. 18, 2019), HFSC_CFPB_030519_00001972 - 73.

⁹⁴ *Id.*

⁹⁵ *Id.*

provide millions of dollars in redress. Director Kraninger, concurring with Mr. Mulvaney and rejecting Enforcement’s recommendation, announced a settlement providing no restitution for consumers.

i. Consistent with Prior Consumer Bureau Enforcement Settlements, Enforcement Recommends that Sterling Should Pay Redress to Consumers

Sterling operates approximately 1,500 jewelry stores across the United States under various names, including Kay Jewelers.⁹⁶ Sterling is a wholly-owned subsidiary of Signet Jewelers Limited (Signet) and generates approximately 60% of Signet’s total sales of approximately \$6.4 billion.⁹⁷ Until approximately June 2017, Sterling sold Payment Protection Plan (PPP) insurance to consumers financing their purchases.⁹⁸ PPP insurance is a credit card add-on product that assists consumers in making their monthly credit card payments in the event of certain events, such as death, loss of a job, or disability.⁹⁹ Although it varied by state and the type of coverage, PPP insurance typically cost 97 cents per \$100 purchase amount and was charged on the consumer’s monthly billing statement based on their account balance.¹⁰⁰

The Consumer Bureau alleged that Sterling, “enrolled some consumers in PPP insurance without their knowledge or consent. In many instances, consumers were asked to ‘sign here’ or select ‘Yes’ on an electronic ‘PIN-pad’ in order to hold an item, process an order, or verify their information when, in fact, their signature was used to enroll them in PPP.”¹⁰¹

On August 9, 2018, Enforcement submitted to Mr. Blankenstein a draft settlement recommendation memo for the Sterling investigation.¹⁰² Enforcement needed Mr. Blankenstein to approve their recommendation memo prior to submitting it to Mr. Mulvaney.¹⁰³ Enforcement recommended that Sterling, as part of any settlement with the Consumer Bureau, refund all PPP insurance fees paid by consumers enrolled at the point of sale (except fees paid by consumers who received a benefit from the insurance) from February 2013 through the date upon which Sterling entered into the consent order.¹⁰⁴ Between 2014 and 2017, Sterling earned over \$50 million in revenue annually from PPP insurance.¹⁰⁵ The recommendation was consistent with the relief ordered by the Consumer Bureau in similar credit card add-on matters.¹⁰⁶ Enforcement specifically cited the Consumer Bureau’s

⁹⁶ Complaint at ¶1 (Jan. 16, 2019), *Bureau of Consumer Financial Protection and the People of the State of New York, by Letitia James, Attorney General for the State of New York v. Sterling Jewelers Inc.*, S.D.N.Y. (No. 1:19-cv-00448), https://files.consumerfinance.gov/f/documents/bcfp_sterling-jewelers_complaint.pdf.

⁹⁷ *Id.* at ¶2.⁹⁸ *Id.* at ¶40.

⁹⁸ *Id.* at ¶40.

⁹⁹ *Id.* at ¶42.

¹⁰⁰ *Id.* at ¶47.

¹⁰¹ *Id.* at ¶45.

¹⁰² Recommendation Memorandum for the Acting Director (Aug. 24, 2018), HFSC_CFPB_030519_00001680-99. Unlike the Enova matter, Enforcement had not previously obtained settlement authority from Director Cordray.

¹⁰³ See Recommendation Memorandum for the Acting Director (Oct. 29, 2018), HFSC_CFPB_030519_00001728 - 58.

¹⁰⁴ Recommendation Memorandum for the Acting Director at 1696-97(Aug. 24, 2018) HFSC_CFPB_030519_00001680 - 99.

¹⁰⁵ *Id.*

¹⁰⁶ See, e.g., Consent Order, *In the Matter of Citibank, N.A.; Department Stores National Bank; and Citicorp Credit Services, Inc. (USA)*, 2015-CFPB-0015 (July 21, 2015), https://files.consumerfinance.gov/f/201507_cfpb_consent-order-citibank-na-department-stores-national-bank-and-citicorp-credit-services-inc-usa.pdf (requiring Citibank and related entities to pay \$700 million in redress related to the sale of credit card add-on products); Consent Order, *In the Matter of Bank of America, N.A.; and FIA Card Services, N.A.*, 2014-CFPB-0004 (Apr. 9, 2014), Consent Order, *In the Matter of Citibank, N.A.; Department Stores National Bank; and Citicorp Credit Services, Inc. (USA)*, 2015-CFPB-0015 (July 21, 2015), https://files.consumerfinance.gov/f/201507_cfpb_consent-order-citibank-na-department-stores-national-bank-and-citicorp-credit-services-inc-usa.pdf.

enforcement against Capital One providing \$140 million in redress to approximately two million consumers.¹⁰⁷ Referring to how the Consumer Bureau proceeded in its Enforcement action against Wells Fargo for opening unauthorized deposit and credit card accounts, Enforcement attorneys recommended that Sterling submit a plan for identifying consumers eligible for refunds for the Consumer Bureau’s approval because the company possessed the relevant data.¹⁰⁸

ii. Eric Blankenstein Opposed Requiring Sterling to Refund PPP Insurance Fees

Mr. Blankenstein’s initial reaction to the section of Enforcement’s August 9, 2018 memo recommending redress to consumers for PPP insurance was skepticism: “Given that we have two causation issues (whether the customer would have purchased the insurance anyway, and whether the customer actually was informed by the employee about the insurance options), I think disgorgement is the more appropriate remedy.”¹⁰⁹ Ms. Petersen, in a September 17, 2018 draft of the recommendation memo, reiterated Enforcement’s view on restitution:

“

“We believe a negotiated resolution that included relief for harmed borrowers is the best course of action.”

- Cara Petersen

We believe a negotiated resolution that included relief for harmed borrowers is the best course of action. We likely have sufficient evidence to convince a court to shift the burden to Signet to show that any particular consumer was not harmed by its widespread practices. Also, don’t these problems arise in a disgorgement analysis too? Calculating the disgorgement amount would rely on certain assumptions as well.¹¹⁰

The Senior Legal Advisor, responding to Cara Petersen’s comment, also proposed providing redress to consumers in an email to Mr. Blankenstein:

To the extent you’re uncomfortable seeking full redress for all customers, one middle ground position might involve seeking redress for only the first couple of bills to consumers.... That wouldn’t really address the causation connection flagged in your prior comment, but would be consistent with the burden-shifting case law discussed in Cara’s comment, and would be more fair to consumers than no redress at all.¹¹¹

¹⁰⁷ Recommendation Memorandum for the Acting Director at 1696-97(Aug. 24, 2018) HFSC_CFPB_030519_00001680 - 99.

¹⁰⁸ *Id.*

¹⁰⁹ *Id.* at 1696.

¹¹⁰ Sterling Settle or Sue Recommendation Memo ((Sept. 17, 2018) (in-camera review) (comment bubble of Cara Petersen).

¹¹¹ Email from Senior Legal Advisor to Eric Blankenstein (Sept. 17, 2018) (in-camera review).

Despite these arguments, Mr. Blankenstein’s opposition towards providing restitution for consumers persisted. In an October 26, 2018 draft of the memo, Mr. Blankenstein commented, “we probably should not even be suggesting that restitution would be appropriate here.”¹¹² The lead career attorney assigned to the Sterling matter responded to Mr. Blankenstein, writing, “[w]e would like to seek authority to discuss/negotiate redress as part of a settlement...”¹¹³

“... we probably should not even be suggesting that restitution would be appropriate here.”
- Eric Blankenstein

iii. Mr. Blankenstein Altered Enforcement’s Redress Recommendation

Mr. Blankenstein substantially changed Enforcement’s recommendation regarding providing redress to consumers for PPP insurance. The original August 9, 2018 version of the settlement recommendation memo submitted by Enforcement for Mr. Blankenstein’s review recommended that Sterling provide consumer redress for PPP insurance.¹¹⁴ This recommendation was consistent with numerous prior consent orders issued by the Consumer Bureau against entities for their fraudulent marketing of credit card add-on products.¹¹⁵ In reviewing Enforcement’s settlement recommendation memo, Mr. Blankenstein altered Enforcement’s initial recommendation to include alternatives to requiring consumer redress, explaining that, “[t]he idea behind this new section is to lay out the options, without a specific recommendation, and then adjust the recommendation memo to present the options (restitution, disgorgement, n/a).”¹¹⁶

Rather than expressly recommending that Sterling pay redress for enrolling consumers in PPP insurance without their consent, consistent with prior Consumer Bureau settlements in similar cases, Mr. Blankenstein included the options of Sterling paying disgorgement (which would not go to consumers) or only a civil penalty as alternatives to providing consumer redress. Mr. Blankenstein added the following language to the recommendation memo: “Alternatively, disgorgement of the PPP proceeds may be more appropriate. Or the Bureau could not order any specific monetary relief for this violation, but rather take it into account when

¹¹² Recommendation Memorandum for the Acting Director at 1723 (Oct. 26, 2018), HFSC_CFPB_030519_1700 - 26.

¹¹³ *Id.*

¹¹⁴ Recommendation Memorandum for the Acting Director at 1696-97 (Aug. 24, 2019), HFSC_CFPB_030519_00001680 - 99.

¹¹⁵ See, e.g., *CFPB Orders First National Bank of Omaha to Pay \$32.25 Million for Illegal Credit Card Practices*, Consumer Bureau (Aug. 25, 2016), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-first-national-bank-omaha-pay-3225-million-illegal-credit-card-practices/> (requiring First National Bank of Omaha to pay \$27.75 million for illegal marketing and administration of credit card add-on products); *CFPB Orders American Express to Pay \$59.5 Million for Illegal Credit Card Practices*, Consumer Bureau (Dec. 23, 2013), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-american-express-to-pay-59-5-million-for-illegal-credit-card-practices/> (requiring American Express to pay \$59.5 million in refunds for illegal marketing and administration of credit card add-on products); *CFPB Orders Chase and JPMorgan Chase to Pay \$309 Million Refund for Illegal Credit Card Practices*, Consumer Bureau (Sept. 19, 2013), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-chase-and-jpmorgan-chase-to-pay-309-million-refund-for-illegal-credit-card-practices/> (Requiring Chase to pay an estimated \$309 million in refunds for illegal practices relate to the sale of credit card add-on products); *CFPB Probe into Capital One Credit Card Marketing Results in \$140 Million Consumer Refund*, Consumer Bureau (Jul. 18, 2012), <https://www.consumerfinance.gov/about-us/newsroom/cfpb-capital-one-probe/> (requiring Capital One Bank to pay \$140 million in refunds for deceptive marketing of credit card add-on products).

¹¹⁶ Email from Eric Blankenstein to Jeff Ehrlich (Oct. 25, 2018) (in-camera review) (attaching his edits to the remediation section of the settlement memo).

determining the penalty amount.”¹¹⁷ Mr. Blankenstein also added a discussion of the potential “drawbacks” of providing redress to consumers:

Normally, when an institution is accused of inducing consumers to enter into transactions through unfair or deceptive means, restitution is appropriate. But, merely identifying the proper restitution population may be impossible given that there are likely no records of which consumers were subject to the specific practice of being misled about the PPP product or being enrolled without having provided affirmative consent. And, even though the Bureau need not prove causation in order to secure restitution, there is also the question of whether any specific customer would not have purchased insurance but for the unfair or deceptive conduct of a Sterling employee. As a result, blanket redress to all PPP consumers would potentially provide a windfall to those who were not proximately harmed by Sterling’s practices.¹¹⁸

While Mr. Blankenstein earlier had referenced that “[e]ach of the potential remedies for PPP claim has drawbacks,” he did not describe any drawbacks related to ordering disgorgement or only a civil penalty.¹¹⁹

After Mr. Blankenstein changed Enforcement’s recommendation regarding providing redress to harmed consumers, Enforcement wanted to inform Director Mulvaney that it favored the option of redress. A senior enforcement manager emailed Mr. Blankenstein a subsequent version of the memo that contained a sentence indicating that Enforcement favored the option of providing redress.¹²⁰ The final version of the recommendation memo submitted to Acting Director Mulvaney on October 29, 2018, reflected Mr. Blankenstein’s decision to include his alternatives to Enforcement’s initial recommendation of consumer redress, as well as the single sentence indicating that Enforcement favored requiring redress.¹²¹

Accompanying the final recommendation submitted to Acting Director Mulvaney was a one-page decision memo specifically laying out the three options of restitution, disgorgement, or “take the absence of other monetary relief into account when negotiating penalty amount.”¹²² Enforcement requested that the decision memo reflect that restitution was the “recommended action.”¹²³ With Mr. Blankenstein’s explicit approval, the version of the decision memo submitted to Acting Director Mulvaney did not reflect that restitution was the “favored” approach.¹²⁴ The decision memo provided Acting Director Mulvaney the ability to select which option he wanted to authorize.¹²⁵ The final decision memo signed by Acting Director Mulvaney on November 1, 2018, authorized

¹¹⁷ Recommendation Memorandum for the Acting Director at 1724 (Oct. 26, 2019), HFSC_CFPB_030519_00001700 - 27.

¹¹⁸ *Id.* at 1723.

¹¹⁹ *Id.* at 1723 - 24.

¹²⁰ Email from Jeff Ehrlich to Eric Blankenstein (Oct. 26, 2018) (in-camera review); Recommendation Memorandum for the Acting Director at 1723 (Oct. 26, 2018), HFSC_CFPB_030519_1700 - 27.

¹²¹ Recommendation Memorandum for the Acting Director (Oct. 29, 2019), HFSC_CFPB_030519_1728 - 58.

¹²² Decision Memorandum for the Acting Director (Oct. 29, 2019), HFSC_CFPB_030519_1759.

¹²³ Email from Senior Legal Advisor to Eric Blankenstein (Oct. 26, 2018) (in-camera review).

¹²⁴ Email from Eric Blankenstein to Senior Legal Advisor (Oct. 26, 2018) (in-camera review); Decision Memorandum for the Acting Director (Oct. 29, 2019), HFSC_CFPB_030519_1759.

¹²⁵ *Id.*

Enforcement to “take the absence of other monetary relief into account when negotiating penalty amount.”¹²⁶ On January 16, 2019, under the leadership of Director Kraninger, the Consumer Bureau announced a settlement with Sterling that provided no redress for consumers.¹²⁷ As previously indicated, this was inconsistent with numerous prior settlements involving similar misconduct.¹²⁸

On January 16, 2019, under the leadership of Director Kraninger, the Consumer Bureau announced a settlement with Sterling that provided no redress for consumers.

C. The Trend of Limiting Redress for Consumers in Settlements Continued

Since the Committee commenced its investigation in February 2019, Director Kraninger has approved additional settlements that appear to shortchange harmed consumers.

On August 28, 2019, the Consumer Bureau announced a settlement with the debt collector, Financial Credit Services, Inc., d/b/a Asset Recovery Associates (Asset Recovery).¹²⁹ According to the findings in the consent order signed by Director Kraninger, Asset Recovery unlawfully represented to consumers that the company would file lawsuits against them, file liens on their houses, garnish their wages or bank accounts, or cause them to be arrested – when the company had no intention of taking these actions.¹³⁰ Asset Recovery also misrepresented to consumers that it employed attorneys to collect debt.¹³¹ Under the terms of the Consumer Bureau’s consent order with Asset Recovery, only consumers who affirmatively complained would be eligible to receive redress.¹³² Thus, consumers subject to the illegal conduct but who did not complain will not receive any redress under the terms of the consent order.

Prior consent orders issued by the Consumer Bureau against debt collectors did not require consumers subject to illegal debt collection practices to have affirmatively complained in order to be eligible for redress. For example, in *In the Matter Encore Capital Group, Inc. Midland Funding LLC, Midland Credit Management, Inc. and Asset Acceptance Capital Corp. (Encore)*, No. 2015-CFPB-0022, the Consumer Bureau required Encore to provide redress to 12,000 consumers who made a payment within sixty days of Encore sending them a deceptive collection letter and to approximately 35,600 consumers who made a payment after Encore submitted a false affidavit in litigation.¹³³ In *In the Matter of Portfolio Recovery Associates, LLC, No. 2015-CFPB-0023 (PRA)*, the Consumer Bureau required PRA to provide redress to more than 34,000 consumers who made a payment

¹²⁶ Decision Memorandum from the Acting Director (Nov. 1, 2018), HFSC_CFPB_030519_1823.

¹²⁷ *Sterling Jewelers, Inc.*, Consumer Bureau (Jan. 16, 2019), <https://www.consumerfinance.gov/policy-compliance/enforcement/actions/sterling-jewelers-inc/>.

¹²⁸ See Footnote 116.

¹²⁹ *Consumer Financial Protection Bureau Settles with Asset Recovery Associates*, Consumer Bureau (Aug. 28, 2019), <https://www.consumerfinance.gov/about-us/newsroom/bureau-settles-asset-recovery-associates/>.

¹³⁰ Consent Order, *In the Matter of Financial Credit Service, Inc., d/b/a Asset Recovery Associates* at ¶7-13, 2019-BCFP-0009 (Aug. 28, 2019), https://files.consumerfinance.gov/f/documents/cfpb_asset-recovery-associates_consent-order_2019-08.pdf.

¹³¹ *Id.*

¹³² *Id.* at ¶3(a).

¹³³ Consent Order, *In the Matter of Encore Capital Group, Inc., Midland Funding, LLC, Midland Credit Management, Inc. and Asset Acceptance Capital Corp.* at ¶144 - 45, 2015-CFPB-0022 (Sept. 9, 2015), https://files.consumerfinance.gov/f/201509_cfpb_consent-order-encore-capital-group.pdf.

within sixty days of receiving a deceptive phone call from the company and to the 837 consumers who made payments after the company obtained a judgment on debt too old to sue on.¹³⁴ Neither the Encore or PRA consent orders denied restitution to harmed consumers simply because they did not affirmatively complain about the illegal conduct.

III. CONCLUSIONS

Congress enacted the CFPB to create a strong independent federal agency focused on enforcing federal consumer financial law, including returning money to consumers cheated by providers of financial services or products. Under Obama-appointed leadership, the Consumer Bureau held entities accountable when they violated the law and required them to provide redress to consumers when they did. Upon assuming leadership, the Trump-appointed Acting Director Mulvaney politicized the Consumer Bureau, installing political appointees to oversee the Consumer Bureau's career senior managers. The politicization of the Consumer Bureau included oversight of the Consumer Bureau's enforcement matters by a political appointee, Eric Blankenstein. Director Kraninger maintained the political oversight of the Consumer Bureau's work established under Acting Director Mulvaney.

A review of the public enforcement actions taken after the departure of Obama-appointed Director Cordray demonstrated the dramatic decline in the Consumer Bureau's enforcement activity, including the amount of relief it obtained for harmed consumers. The Committee's investigation of two specific matters revealed that Trump administration political appointees overruled career staff's recommendations to provide consumer relief. Political appointees inserted themselves between career staff and the director in the Consumer Bureau's enforcement process, impeding the ability of career staff to provide their unvarnished recommendations to the director. The significant role of political appointees, rather than career staff, in determining whether to provide redress to harmed consumers in these two cases suggests that the politicization of the Bureau contributed to the decline in the Consumer Bureau's enforcement activity under Trump-appointed leadership and the denial of millions of dollars in relief to consumers. The continued presence of political appointees at the Consumer Bureau raises significant, ongoing, concerns about its ability to obtain appropriate redress for consumers when entities violate the law. In addition, the decisions and actions made by these political appointees also raise questions about whether Consumer Bureau leadership requires further guidance about the importance of providing restitution to harmed consumers.

To ensure that the Consumer Bureau fulfills its mission as an independent agency tasked with enforcing federal consumer financial law and protecting consumers, Congress should take action to reverse the politicization of the Consumer Bureau. In May 2019, the House passed the Consumers First Act (H.R. 1500), legislation introduced by Chairwoman Waters to reverse past efforts of the Trump administration to undermine the mission of the Consumer Bureau. The Consumers First Act ensures that the number and duties of political appointees at the Consumer Bureau are consistent with other Federal financial regulators. The Committee should also consider ways to strengthen the provisions in the CFPB authorizing the Consumer Bureau to seek relief for consumers through enforcement actions.

¹³⁴ Consent Order, *In the Matter of Portfolio Recovery Associates, LLC* at ¶¶21, 137 – 38, 2015-CFPB-0023 (Sept. 9, 2015), https://files.consumerfinance.gov/f/201509_cfpb_consent-order-portfolio-recovery-associates-llc.pdf.

APPENDIX A

ERIC G. BLANKENSTEIN

(b)(6)

Experience

UNITED STATES TRADE REPRESENTATIVE, OFFICE OF GENERAL COUNSEL

Washington, D.C.

Assistant General Counsel

September 2017–Present

Represented United States in dispute settlement process before World Trade Organization; counseled US representatives in negotiation of various trade agreements; monitored US compliance with trade obligations.

WILLIAMS & CONNOLLY, LLP

Washington, D.C.

Associate

July 2009–September 2017

Engaged in all phases of litigation for both civil and criminal defendants encompassing: reviewing and analyzing applicable law and regulations, counseling clients on strategic decisions, conducting factual investigations, managing complex civil discovery, taking and defending depositions, assisting with the preparation of expert reports, drafting dispositive and non-dispositive briefing, making oral presentations to court, examining witnesses during trial, and negotiating and drafting settlement agreements.

Illustrative experience includes:

- Representing banks in regulatory investigations and litigation with OCC and CFPB alleging violations of various consumer laws, including the Consumer Financial Protection Act, Fair Credit Reporting Act and Electronic Fund Transfer Act
- Defending banks in securities litigation brought under the Securities Act and Securities Exchange Act, FIRREA, and state law, related to mortgage-backed securities, mortgage whole-loan sales, repurchase agreements, and other complex instruments and transactions
- Defending pharmaceutical and health care companies against alleged violations of federal and state False Claims Acts
- Representing a technology company in criminal investigation alleging contract and visa fraud, and export control violations
- Representing taxpayers protesting alleged federal tax liability related to status as Virgin Islands residents
- Defending oil field equipment manufacturer in suits related to the *Deepwater Horizon* incident
- Defending law firms accused of professional malpractice
- Representing pro bono clients in criminal cases, including co-first chair of three day jury trial and argument before Maryland Court of Special Appeals
- Representing an ex-wife against her ex-husband over property settlement that involved substantial undisclosed tax liability

UNITED STATES COURT OF APPEALS FOR THE ARMED FORCES

Washington, D.C.

Summer Clerk, Chambers of the Honorable Margaret A. Ryan

Summer 2007

Assisted with opinion editing, research, and review for various cases brought under UCMJ. Researched legal questions.

INFINITIVE, INC.

Ashburn, VA

Consultant

2005–2006

Managed several workstreams for College Board – SAT Scoring Operations directorate. Directly supported the Director of Scoring Operations in managing vendor performance, general scoring functions, system requirements development, and testing, and specific issue investigation.

IBM BUSINESS CONSULTING SERVICES (formerly PwC Consulting)

Arlington, VA

Consultant

2001–2005

Engaged in a number of Federal government related consulting projects, including supporting the Department of Agriculture, Department of Veterans Affairs, and the Department of Justice. Supported the leaders of the Department of Justice September 11th Victim Compensation Fund in various capacities, including the hearing and award appeals function.

Education

University of Virginia School of Law

Juris Doctor, May 2009

- Order of the Coif
- Federalist Society
- Managing Editor (2008–2009), Articles Review Committee (2007–2008), *Virginia Law and Business Review*

University of Virginia Graduate School of Arts and Sciences

Master of Arts, History, August 2009

University of Virginia, McIntire School of Commerce

Bachelor of Science in Commerce, *with distinction*, May 2001

Subject Concentrations: Finance and Management Information Systems

- Intermediate Honors, Fall 1999; Dean's List: Fall 1997, Fall 1998, Spring 1999, Spring 2000, Spring 2001;
- Member: Phi Eta Sigma, National Honor Fraternity; National Society of Collegiate Scholars; Golden Key Honor Society

APPENDIX B

UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

Consumer Financial Protection Bureau,

Case No. 17-cv-0166-RHK-KMM

Plaintiff,

vs.

**MEMORANDUM IN OF LAW
SUPPORT OF DEFENDANT’S
MOTION TO DISMISS**

TCF National Bank,

Defendant.

TCF National Bank (“TCF”) offers its customers an overdraft service that allows customers to withdraw funds or complete purchases—instead of having these transactions declined—if their account balance drops below zero. Enrolling is free and optional, but TCF charges a fee each time it extends this short-term, unsecured credit to customers. As one might expect in a heavily regulated industry, the Federal Reserve issued a regulation governing overdraft fees in 2009, called “Regulation E.” This regulation prohibits banks from charging overdraft fees for ATM and non-recurring *debit card transactions* unless the customer has consented to the service.

The regulation focuses on obtaining customer consent after providing written disclosures. TCF met each condition established by the regulation. It provided all required written disclosures to its customers, including (1) a separate notice called “*What You Need to Know About Overdrafts and Overdraft Fees*”

(“Notice”), and (2) a New Account Agreement (“Agreement”) that described TCF’s overdraft service and associated fees. These disclosures explained the voluntary nature of TCF’s overdraft service and the amount of the overdraft fee. TCF did not enroll any customers who did not affirmatively communicate to TCF their consent to enroll in overdraft service.

Plaintiff Consumer Financial Protection Bureau (“CFPB” or “Bureau”) acknowledges in its complaint that TCF provided these disclosures, but filed suit nonetheless, claiming that TCF used unlawful *methods* to obtain customers’ consent:

- For New Customers (defined by Regulation E as customers who opened accounts after July 1, 2010), the Bureau alleges that TCF engaged in deceptive and abusive conduct by sequencing the account opening process to separate the Notice from the enrollment decision and by giving “cursory,” “uninformative,” and “one-sided” oral explanations. Compl. ¶¶ 3, 105–18.
- For Existing Customers (defined as customers who already had TCF accounts before Regulation E’s effective date), the Bureau alleges that TCF violated Regulation E by asking an ice-breaker question that allegedly framed the decision in a way that turned overdraft service “into the default position.” Compl. ¶¶ 121–23.

These allegations are insufficient to state a claim. Failing to orally summarize terms and conditions already provided in unambiguous written disclosures is not deceptive or abusive conduct. Written disclosures are integral to consumer financial regulation. Consumers are presumed to read and understand documents provided by sellers as part of consumer transactions—particularly where, as here, there are no allegations that the documents themselves were confusing or misleading. This notion lies at the heart of the Federal Reserve’s approach to Regulation E, which focuses exclusively upon the adequacy of written disclosures and makes no mention of the substance or cadence of any oral description.

The CFPB attempts to sidestep this bedrock principle of consumer financial regulation by pleading only oral misconduct while ignoring the clear written disclosures that customers reviewed or signed, and asserting its belief that “consumers rarely read these disclosures.” *Id.* ¶ 76. But, this principle cannot be so easily dismissed. If the Bureau had sued a rental car company challenging its oral presentations at the rental counter, but downplayed the rental agreements in its complaint, this Court would not countenance the effort to leave out this crucial aspect of the story. Yet that is exactly what the Bureau seeks to do here.

The Bureau, moreover, does not claim TCF’s documentation can be ignored because TCF contradicted a writing with misleading oral statements. Instead, the

CFPB alleges that it has located a handful of former employees—out of thousands who worked at TCF over the years—who allegedly *perceived* pressure on employees to enroll customers and give cursory or “uninformative” answers to customer questions. Compl. ¶¶ 44, 70. But none of those employees claims to have engaged in misconduct, such as misrepresenting overdraft service or enrolling customers without their consent. Even if oral explanations were abbreviated or incomplete, no reasonable customer who read TCF’s disclosures could have failed to understand that they were making a voluntary decision to enroll in an overdraft service that authorized TCF to charge a fee if the customer overdrafted.

This enforcement action is an attempt to impose upon TCF a series of oral disclosure and sequencing requirements that are found nowhere in Regulation E. If the CFPB has regulatory concerns about the manner in which customers and bank employees orally interact, then it should give financial institutions advance notice and address those concerns through *prospective* rule-making, not by concocting novel interpretations and then applying them *retroactively* to conduct that occurred many years ago. It is not fair to change the rules after the game, and then penalize TCF for allegedly falling short of those new rules. *PHH Corp. v. Consumer Fin. Prot. Bureau*, 839 F.3d 1, 49 (D.C. Cir. 2016), *pet. for reh’g en banc granted* (Feb. 16, 2017) (No. 15-1177). While the judgment of the *PHH* panel was vacated upon grant of *en banc* review, and therefore has no legal effect, this Court can still look

to the panel opinion for its highly persuasive reasoning.¹ There are also a number of timeliness and retroactivity barriers to applying these new interpretations to conduct reaching back to 2010.

It is unfortunate that, in its effort to generate publicity (including a gratuitous reference to a boat owned by a now-deceased corporate officer), the CFPB brought this meritless lawsuit—as part of a fusillade of suits filed days before the change in administration²—against a consumer-oriented bank serving this community for nearly 100 years. Dismissal is required.

BACKGROUND

I. TCF’s Business Model Prioritizes Consumer Convenience and No-Minimum-Balance Checking.

TCF has a substantial retail presence—over 360 branches across seven states. Compl. ¶ 16. “Unlike many other banks its size, TCF does not generate substantial revenue from credit cards and home mortgage loans.” *Id.* ¶ 26.

Instead, TCF has a business model focused on a “limited portfolio of consumer banking products,” *id.* ¶ 26, such as no-minimum-balance checking. Its consumer-

¹ Per the rules of the D.C. Circuit, “[i]f rehearing *en banc* is granted, the panel’s judgment, but ordinarily not its opinion, will be vacated.” D.C. Cir. R. 35(d). The order granting rehearing *en banc* did exactly that, ordering that the “judgment . . . be vacated,” but remaining silent on the panel’s opinion.

² See Press Release, Navient, *Navient Rejects CFPB Ultimatum To Settle by Inauguration Day or Be Sued* (Jan. 18, 2017), <http://news.navient.com/releasedetail.cfm?ReleaseID=1008347>.

oriented business model—geared “primarily for personal, family, or household purposes,” *id.* ¶ 15—is focused on customer convenience.

Part of this convenience is giving customers the ability to complete their debit card purchases even when they do not have sufficient funds. Not all transactions that involve negative balances when they are approved result in a fee, though some do. Sometimes an account has sufficient funds when the transaction settles because of an intervening deposit. When this happens, TCF does not charge a fee. Many customers have never incurred an overdraft fee but nevertheless have enjoyed the benefit of this “swipe negative/settle positive” policy, which would only be available after the rule change if the customer opted in.

II. The Federal Reserve Issued a New Overdraft Regulation in 2009.

Before Regulation E became effective, TCF “provided overdraft coverage...as a standard feature on checking accounts.” *Id.* ¶ 19. Consistent with industry practice, it did not offer customers an opportunity to decline the service. In November 2009, the Federal Reserve decided customers ought to have a choice and “limit[ed] the ability of a financial institution to assess an overdraft fee for paying automated teller machine (ATM) and one-time debit card transactions that overdraw a consumer’s account, *unless the consumer affirmatively consents, or*

opts in, to the institution's payment of overdrafts for these transactions."³

Electronic Fund Transfers, 74 Fed. Reg. 59,033, 59,033 (Nov. 17, 2009) (emphasis added). The amended regulation, known as Regulation E, prohibits financial institutions from charging a fee for debit card transactions unless they had previously:

- 1) Provided the customer with a written notice that contained federally prescribed content about overdraft services;
- 2) Provided a reasonable opportunity for the customer to consent;
- 3) Actually obtained the customer's consent; and
- 4) Provided the customer written confirmation of the decision, which included a statement that the customer could revoke that consent.

See 12 C.F.R. § 205.17(b)(1)(i)–(iv).

The default under Regulation E is to opt out of overdraft service—i.e. unless a customer affirmatively consents to opt in, the Bank declines transactions when the balance is insufficient (which by definition includes declining what would otherwise be swipe negative/settle positive transactions). After July 2010, the only way customers could receive TCF overdraft service was to enroll. *Id.* § 205.17(c). The Federal Reserve considered the prevalence of swipe negative/settle positive transactions when finalizing the rule. 74 Fed. Reg. at 59,034.

³ The Federal Reserve excluded from this rule overdrafts caused by checks and ACH transactions. 74 Fed. Reg. at 59,034.

III. Opt-In Rates Vary Significantly.

Although the CFPB alleges that TCF’s 66% opt-in rate is higher than other banks, Compl. ¶ 5, there is no “proper” or “legal” enrollment rate. Indeed, the CFPB has acknowledged elsewhere⁴ that “opt in rates vary widely,”⁵ and that its comparison data “come from a small number of large banks” and “cannot be considered fully representative of the checking account market as a whole.”⁶ As a result, a “high” opt-in rate does not suggest misconduct.

(The complaint carefully avoids admitting that TCF’s enrollment rate for customers who opted in *online*—and who therefore could not have been subjected to any allegedly misleading oral presentations—is not materially different from the enrollment rate for TCF’s entire customer population. The Bureau learned this fact during its investigation, but chose not to mention it in the complaint.)

⁴ The Court may take judicial notice of the Bureau’s public statements. *See, e.g., Stahl v. U.S. Dep’t of Agric.*, 327 F.3d 697, 700 (8th Cir. 2003) (“The district court may take judicial notice of public records and may thus consider them on a motion to dismiss.”); *Hile v. Jimmy Johns Highway 55*, 899 F. Supp. 2d 843, 847 (D. Minn. 2012) (Kyle, J.) (“[W]hen ruling on a motion under Rule 12(b)(6), public records are not beyond the pleadings.”).

⁵ CFPB Fall 2015 Rulemaking Agenda, Nov. 20, 2015, at 2 (Declaration of Brian J. Hurd in Support of Defendant TCF National Bank’s Motion to Dismiss (“Hurd Decl.”) at Ex. 1). Indeed, the CFPB publicly reported that new-account opt-in rates at one bank were up to eight times higher than others, and that opt-in rates at some study banks “surpassed 50% in 2012.” *CFPB Study of Overdraft Programs* at 31–32 (June 2013) (Hurd Decl. Ex. 2).

⁶ *CFPB Data Point: Checking Account Overdraft* at 7 (July 2014) (Hurd Decl. Ex. 8).

IV. TCF Provided Disclosures Before, During, and After the Enrollment Decision.

A. TCF Provided All Customers with the Federally-Prescribed Notice Before an Enrollment Decision.

The complaint alleges that “[t]he Opt-In Rule requires depository institutions to provide consumers with a [written] notice describing the institution’s overdraft service, including, among other things, an explanation of the consumer’s Opt-In right and instructions for how to Opt In.” Compl. ¶54. The “first step” in TCF’s account opening process was to give customers “a copy of TCF’s version of the Notice.” *Id.* ¶ 59.

The Federal Reserve developed a model Notice, Form A-9, entitled, “*What You Need to Know About Overdrafts and Overdraft Fees.*” Hurd Decl. Ex. 3. Regulation E mandates that banks provide a notice to customers that is “substantially similar” to this model. 12 C.F.R. § 205.17(d). In particular, they must provide: (1) a description of the overdraft service; (2) a disclosure of the fees imposed; (3) a disclosure of the limits on the fees charged; (4) an explanation of the fact that the customer had the right to opt in; and (5) a description of any alternative plans that were available to cover overdrafts. *See id.* § 205.17(d)(1)–(5); 12 C.F.R. pt. 205 app. A (Hurd Decl. Ex. 4).

The CFPB does not dispute that TCF’s version of the required Notice is substantially similar to the federal model. Among other things, it explains that

customers have a choice whether to enroll in overdraft service, and details (in **bold**) the fee TCF charges for an overdraft transaction.

What You Need to Know about Overdrafts and Overdraft Fees

We will **not** authorize and pay overdrafts for the following types of transactions unless you ask us to:

- ATM transactions
- Everyday debit card transactions

• We will charge you a fee of up to **\$35** each time we pay an overdraft.

What if I want TCF to authorize and pay overdrafts on my ATM and everyday debit card transactions?

If you also want us to authorize and pay overdrafts on ATM and everyday debit card transactions, call us at 1-800-TCFBANK (1-800-823-2265) or 612-823-2265 (if calling from the Minneapolis-St. Paul metropolitan area), stop by any TCF branch, or complete the **Opt-In election** in your Account Agreement. You may also send a written request, including your name, address, date of request, and account number(s), to us at:

What if I want to revoke my decision to have TCF authorize and pay overdrafts on my ATM and everyday debit card transactions?

If you opt-in and decide later that you want to revoke your decision to have TCF authorize and pay overdrafts on ATM and everyday debit card transactions, call us at 1-800-TCFBANK (1-800-823-2265) or 612-823-2265 (if calling from the Minneapolis-St. Paul metropolitan area), stop by any TCF branch, or send a written request, including your name, address, date of request, and account number(s), to us at:

The Federal Reserve also required that the Notice be a separate document “segregated from all other information.” 12 C.F.R. § 205.17(b)(1)(i). The complaint tacitly recognizes that TCF complied with this requirement too. Compl. ¶ 63 (“After the Notice was set aside, the employee printed out a New Account Agreement[.]”).

Regulation E required TCF to provide the Notice to all customers. 12 C.F.R. § 205.17(d). The CFPB alleges that TCF provided New Customers the Notice as the “first step in the [account opening] presentation” and informed them “in

substance: ‘This is the federally-prescribed notice describing our overdraft service.’” Compl. ¶ 59. The CFPB does not allege that TCF failed to deliver the Notice to Existing Customers before they were asked to enroll.

B. TCF’s New Account Agreement Disclosed Relevant Information.

After providing the Notice to New Customers, TCF employees then “printed out a New Account Agreement and placed it in front of the consumer.” *Id.* ¶ 63. The complaint references particular items in the Agreement, *id.* ¶¶ 64–67, and acknowledges that “the Opt-In section of the New Account Agreement included a written disclosure,” *id.* ¶ 76; *see also* Hurd Decl. Ex. 5.

The three-page Agreement included an Overdraft Fee Acknowledgement that explained TCF’s overdraft fee policy. Compl. ¶ 65; *see also* Hurd Decl. Ex. 5 at 3. The next section, entitled “ATM and Everyday Debit Card Overdrafts,” referenced the Notice and explained that TCF “does not charge overdraft fees...unless you have asked us to authorize and pay those transactions under the ‘Opt-In Election’ below.” Hurd Decl. Ex. 5 at 3. It then stated, in bold, “**You are not required to initial the ‘Opt-in Election’ below.**”⁷ *Id.*

⁷ While the content of the Agreement and Notice varied slightly over the years, the relevant disclosures were substantially similar throughout the alleged period.

Account Number(s) (the "Account") _____

OVERDRAFT FEE ACKNOWLEDGEMENT

All accounts, except Consumer Checking Accounts and Small Business Checking Accounts opened in Michigan: TCF charges a fee of \$35 each time an item is presented to us for payment from your Account and the item exceeds your Available Balance. "Items" include checks, ATM and debit card transactions, ACH transactions, in-person withdrawals, and other kinds of withdrawals and debits. We charge this fee regardless of whether we pay the item or decide not to pay it. There is no limit on the total fees we can charge.

OVERDRAFT FEE ACKNOWLEDGEMENT

TCF charges a fee of \$35 each time an item is presented to us for payment from your Account and the item exceeds your Available Balance.

All accounts: TCF may add to, increase, or modify the above fees in our sole discretion as provided in your Account Contract. You should avoid overdrafts whenever possible. To check your balance and recent transactions posted to your account you can contact TCF Customer Service at 1-800-TCF-BANK (823-2265) or use TCF Online Banking (www.tcfbank.com). Sign up for TCF Online Banking to get email and text alerts to help you avoid overdrafts.

ATM AND EVERYDAY DEBIT CARD OVERDRAFTS

TCF does not charge overdraft fees on ATM and everyday (that is, one-time or nonrecurring) debit card transactions unless you have asked us to authorize and pay those transactions under the "Opt-In Election" below. TCF has given you a notice called *What You Need to Know About Overdrafts and Overdraft Fees* that describes our policy. You are not required to initial the "Opt-In Election" below. You may opt-in for some accounts but not others. Whether or not you opt-in, TCF has the right to authorize, or not authorize, these transactions when they exceed your Available Balance. You have the right to revoke your election at any time. Check transactions, recurring electronic transactions, and other kinds of withdrawals and debits are not subject to opt-in.

Please read the entire TCF Privacy Policy. By signing, you agree to all the terms of your Account Contract as it may be amended from time to time. By signing below, you understand and agree to all the terms of your Account Contract as it may be amended from time to time. By signing below, you acknowledge that you have received the notice called *What You Need to Know About Overdrafts and Overdraft Fees*.

OPT-IN ELECTION (OPTIONAL)

I want TCF to authorize and pay overdrafts on my ATM and everyday debit card transactions for the checking account listed above.

1. Initial _____ 2. Initial _____ 3. Initial _____ 4. Initial _____

TO OPEN AN ACCOUNT, THIS AGREEMENT MUST BE SIGNED FOR INITIALED BY THE APPROPRIATE PERSON IN ALL PLACES WHERE INDICATED, EXCEPT THE OPT-IN ELECTION (WHICH IS OPTIONAL).

CFSA4036 (12/16/15) Page 2 of 3 Customer Authorized Signer

Even though the complaint acknowledges that the Agreement contained these written disclosures, it makes the astonishing allegation that “consumers rarely read these disclosures.” Compl. ¶ 76. There are no allegations that TCF employees told customers not to read the Notice or prevented customers from reading the Notice if they chose to.

According to the complaint, TCF employees presented the New Customer Opt-In decision by stating:

This next section covers the Opt-In / Not Opt-In Election. By initialing here, you are allowing TCF to authorize and pay overdrafts on your ATM and everyday debit card transactions for this account. Please note that your decision does NOT affect any other transactions such as checks, ACH, or recurring debit card transactions.

Id. ¶ 68. The Bureau contends that this explanation was so short and uninformative that customers “tended not to pay attention to the decision,” *id.* ¶ 70, and “did not understand the decision they had made,” *id.* ¶ 83. It alleges that “[t]he script...left consumers with the impression that opting in was mandatory,” *id.* ¶ 71, even though the place in the Agreement where customers would initial stated in bold that the decision was “**OPTIONAL.**”

The CFPB also contends that unspecified statements from TCF employees left the “net impression” with customers “that there was no cost to opting in,” *id.* ¶ 114, even though 1) there actually is no cost for opting in (as opposed to incurring an overdraft), and 2) the immediate preceding section of the Agreement, *which customers were required to acknowledge in writing*, explained that TCF charges fees for overdrafts.

The CFPB does not allege that TCF employees made any untruthful statements to New Customers.

C. TCF Used Scripts When Communicating with Existing Customers Over the Phone About their Opt-in Choices.

After TCF had sent Existing Customers the Notice, TCF employees contacted Existing Customers by phone and used scripts to guide those

conversations.⁸ The CFPB relies upon these scripts, Compl. ¶ 88, and quotes them on several occasions, *id.* ¶¶ 89, 92–94.

Prior to the August 15, 2010 effective date of Regulation E, TCF scripts opened with an ice-breaker question asking whether the customer wanted his debit card to “continue working as it does today,” *id.* ¶ 89, followed by a series of required disclosures,⁹ *id.* ¶ 94, and then the mandatory enrollment question, “do you want TCF to continue authorizing and paying overdrafts on your ATM and everyday debit card transactions for this account?” *Id.* ¶ 96; *see also* Hurd Decl. Ex. 6. Customers were not enrolled unless they answered “yes” to *that* question. *Id.*

⁸ The CFPB asserts that “TCF’s communication strategy for [] other channels more or less tracked the approach the Bank used in the call campaign.” Compl. ¶ 103.

⁹ The first script, in effect from March 22 to April 26, 2010, asked customers whether they wanted to hear some important regulatory disclosures, *id.* ¶ 98; subsequent scripts required TCF employees to recite the required disclosures without asking that question. *See* Hurd Decl. Ex. 6.

IMPORTANT: YOU MUST DISCLOSE TO THE CUSTOMER EVERYTHING THAT IS SHOWN IN BOLD TYPE BELOW.

Introduction:

- [Required] Hello, may I speak with (customer's name)? (Mr./Mrs./Ms. Customer's last name), this is _____ with TCF Bank. I am calling today regarding your TCF Check Card and some upcoming changes that would limit the usage of your card effective August 15, 2010. While reviewing your account activity I see you use your TCF Check Card often. **Would you like your TCF Check Card to continue to work as it does today?**
- [Required] Currently, TCF may, at its discretion, authorize your card transactions whether or not you have enough funds at the time of the transactions. There may be times when TCF would not authorize your purchases. For example, if your account was not in good standing.

[Optional] Customer Q: Can you give me an example of how this works?

- For instance, you are at the grocery store or a gas station and you want to use your card for a purchase but you don't have enough available funds in your account at the time of the transaction. Currently, TCF is able to authorize this transaction. After August 15, 2010, TCF will not authorize this purchase unless you have opted-in to TCF Overdraft Service.

[Optional] Customer Q: Is this free? or Customer Q: What does it cost?

- [Required] **You will pay nothing extra for TCF's Overdraft Service. However, you will be charged an overdraft fee, currently \$35 per item, if you overdraft your account. This includes overdrafts by check, teller withdrawals, ATM and card transactions, ACH and other electronic transactions. This fee may increase or change in the future.**
- [Required] TCF encourages you to avoid overdrafts whenever possible, However, if this does happen, you must pay any overdraft immediately.
- [Required] **TCF Q: So just to clarify, do you want TCF to continue authorizing and paying overdrafts on your ATM and everyday debit card transactions for this account?**
- [Required] Customer response: **Yes or No**
 - IF THE CUSTOMER SAYS "YES" ENTER "1" ON THE OPT-IN TCHG FIELD.
 - IF THE CUSTOMER SAYS "NO", YOU MUST ENTER "0" IN THE TCHG FIELD – **YOU CANNOT LEAVE THE OPT-IN FIELD BLANK.**

The CFPB contends that TCF considered a “yes” answer to the ice-breaker question as “an indication that the customer wanted to Opt In,” Compl. ¶ 90, and that asking the question in this way “changed the election from an Opt-In to an Opt-Out,” *id.* ¶ 122. The CFPB cites no facts to support the conclusion that the ice-breaker question somehow changed the default or undermined the customer’s consent to overdraft service after the other disclosures were provided. There is no allegation that answering “yes” to the ice-breaker question was relied on by TCF to enroll a customer in overdraft service without also confirming consent based on the final question in the script.

D. TCF Provided Written Confirmation After the Enrollment Decision.

Finally, financial institutions must provide customers with written confirmation of their enrollment decision, including a statement informing them of their right to revoke their consent. 12 C.F.R. § 205.17(b)(1)(iv). The complaint includes no allegations that TCF failed to provide written confirmation to every customer who enrolled in TCF's overdraft service.

LEGAL STANDARD

“To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face.”

Ashcroft v. Iqbal, 556 U.S. 662, 678 (2009) (internal quotation marks omitted).

The Court need not, however, accept factual assertions contradicted by the

complaint or documents upon which the complaint relies. *See, e.g., Cohen v.*

United States, 129 F.2d 733, 736 (8th Cir. 1942) (court need not accept “facts

which appear by a record or document included in the pleadings to be

unfounded”); *Montero v. Bank of Am., N.A.*, No. 13-cv-850 (SRN/JSM), 2014 WL

562506, at *5 (D. Minn. Feb. 13, 2014) (dismissing claim “[b]ecause the

documents attached to the Complaint directly contradict Plaintiff's assertions”).

The CFPB referenced or quoted certain documents but declined to attach them to the complaint. These documents are incorporated by reference and should be considered in their entirety for completeness. *See Silver v. H&R Block, Inc.*,

105 F.3d 394, 397 (8th Cir. 1997) (court dealing with claim of misleading statements could consider “the *complete statements* in granting the motion to dismiss”; plaintiff “cannot defeat a motion to dismiss by choosing not to attach the full statements to the complaint” (emphasis added)); *see also Dylla v. Aetna Life Ins.*, No. 07-3203 (RHK/JSM), 2007 WL 4118929, at *2 (D. Minn. Nov. 16, 2007) (Kyle, J.) (“[T]he Court may consider materials that are outside the pleadings if such materials are necessarily embraced by them. For example, materials are necessarily embraced by the complaint if they were mentioned or incorporated by reference in the complaint.” (citation and internal quotation marks omitted)).

ARGUMENT

I. TCF Did Not Engage in Deceptive or Abusive Acts or Practices.

Counts I and II assert claims as to New Customers, but the alleged violations are based on virtually identical facts. Both fail as a matter of law and should be dismissed.

A. TCF Did Not Deceive New Customers (Count II).

In light of the unchallenged written disclosures TCF provided to New Customers before, during, and after their enrollment decision, the CFPB cannot maintain a viable claim for consumer deception.

To state a claim for deceptive practices, the Bureau must show that there was a material “representation, omission, or practice that is *likely to mislead the*

consumer...acting reasonably [under] the circumstances.” Federal Trade Commission (FTC) Policy Statement on Deception (emphasis added), *appended to In re Cliffdale Assocs., Inc.*, 103 F.T.C. 110, 174–76 (1984).¹⁰ A representation or practice should not be viewed in isolation but instead “[t]he entire advertisement, transaction or course of dealing [should] be considered.” *Id.* Deception only occurs if the “net impression” of the transaction is materially misleading to a reasonable consumer. *See id.* at 176 n.7; *Kraft, Inc. v. FTC*, 970 F.2d 311, 314 (7th Cir. 1992).

The CFPB alleges that New Customers were deceived because TCF “created the net impression that initialing the Opt-In section of the Agreement was mandatory,” when in fact it was optional. Compl. ¶¶ 116–17. While the basis for the CFPB’s allegation of what an untold number of customers understood is never disclosed in the complaint, the substance of the disclosures referenced in the complaint undermines this astonishing assertion.

- The Notice that TCF employees handed customers as the “first step” in the account opening process specifically told customers that TCF

¹⁰ While the Consumer Financial Protection Act (“CFPA”) does not define a “deceptive” practice, the Bureau has stated that the definition is identical to Section 5 of the FTC Act, 15 U.S.C. § 45(a). *See Consumer Fin. Prot. Bureau v. Mortg. Law Grp., LLP*, No. 14-cv-513-bbc, -- F. Supp. 3d --, 2016 WL 3951226, at *12 (W.D. Wis. July 20, 2016).

“will not authorize and pay overdrafts for [certain] transactions unless you ask us to[.]” Hurd Decl. Ex. 4.

- The Agreement stated that enrollment was optional. It expressly referred customers back to the Notice, and told customers that TCF “does not charge overdraft fees...unless you have asked us to authorize and pay those transactions under the ‘Opt-In Election’ below” and that “**You are not required to initial the ‘Opt-In Election’ below.**” Hurd Decl. Ex. 5 at 3. If the customer chose to opt-in, he initialed the Agreement directly under a bold, upper-case heading, “**OPT-IN ELECTION (OPTIONAL).**” *Id.*

The CFPB also alleges that “the net impression left [on New Customers] by TCF’s process was that there was no cost to opting in” though overdraft fees could be charged to customers that opted in and used the service. Compl. ¶¶ 114–15.

TCF’s disclosures flatly contradict this contention:

- The Notice detailed (in **bold**) the fee TCF charged for an overdraft transaction. Hurd Decl. Ex. 4. Also, there was *no fee for enrolling in overdraft services*, only for incurring overdrafts.
- The Agreement required customers to acknowledge TCF’s overdraft fee policy under the heading, “**OVERDRAFT FEE ACKNOWLEDGEMENT.**” Hurd Decl. Ex. 5 at 3.

The deception claim cannot withstand these unambiguous disclosures. The law does not require that every material term found in a written disclosure be repeated orally at contract signing. Yet that is apparently the standard the CFPB seeks to impose on TCF. Compl. ¶ 59 (faulting TCF employees for not summarizing Notice); *id.* ¶ 74 (faulting oral script for failure to mention fees); *id.* ¶ 113(c) (oral script “did not adequately disclose other relevant terms and conditions, including fees”). And the Bureau cannot assert a “net impression” claim of consumer deception without presenting both the relevant oral statements *and* the documents the consumers reviewed or signed contemporaneous with hearing those oral statements.

Consumers are charged with acting “reasonably under the circumstances” and are presumed to be able to read and comprehend disclosure documents. *See Karakus v. Wells Fargo Bank, N.A.*, 941 F. Supp. 2d 318, 340 (E.D.N.Y. 2013) (“[A] reasonable consumer...is expected to read and be familiar with the terms of a document she signs.”).

Although the CFPB contends that bank customers “rarely read these disclosures,” Compl. ¶ 76, this assertion is legally irrelevant. Courts routinely reject unfair and deceptive practices claims when the customer received accurate and understandable written disclosures. *See, e.g., Davis v. HSBC Bank Nev., N.A.*, 691 F.3d 1152, 1161–62, 1168–69 (9th Cir. 2012) (affirming dismissal of claim

that advertisement was unfair and deceptive for failing to mention fees because disclaimer said “other restrictions may apply” and terms and conditions disclosed fees); *cf. FTC v. IFC Credit Corp.*, 543 F. Supp. 2d 925, 946 (N.D. Ill. 2008) (granting motion to dismiss unfair practices claim because consumer could reasonably avoid harm simply by reading the contract before signing).

This approach accords with bedrock legal principles. A party cannot claim ignorance of the terms of a written agreement of which he had notice and to which he assented. *See, e.g., Villines v. Gen. Motors Corp.*, 324 F.3d 948, 953 (8th Cir. 2003); *Gartner v. Eikill*, 319 N.W.2d 397, 398 (Minn. 1982) (en banc); Restatement (Second) of Contracts § 157 cmt. b (Am. Law. Inst. 1981) (“Generally, one who assents to a writing is presumed to know its contents and cannot escape being bound by its terms merely by contending that he did not read them; his assent is deemed to cover unknown as well as known terms.”).

Nor can parties avoid responsibility for signing a contract by later contending that they had insufficient time to review. *See, e.g., Karakus*, 941 F. Supp. 2d at 340 (rejecting deceptive practices claim based in part on allegation that defendant rushed plaintiff to sign loan documents; “This allegation is not nearly sufficient to overcome the principle that a reasonable consumer, at least in New York, is expected to read and be familiar with the terms of a document she

signs.”).¹¹ Unsurprisingly, courts—including this one—have uniformly upheld other terms of the Agreement against challenges from consumers who claimed not to have read them.¹²

The holding in *Rickher v. Home Depot, Inc.*, 2007 WL 2317188 (N.D. Ill. Jul. 18, 2007), *aff'd*, 535 F.3d 661 (7th. Cir. 2008) is particularly instructive. There, a customer brought a class action against Home Depot under the Illinois Consumer Fraud and Deceptive Business Practices Act (“CFA”),¹³ alleging that Home Depot deceived him into believing that an optional “damage waiver” for tool rentals was in fact mandatory. *Rickher*, 2007 WL 2317188, at *3. Like the CFPB, the customer alleged that Home Depot employees failed to make sufficient oral disclosures about the damage waiver. *Id.* at *4. The court rejected the claim

¹¹ The New York Deceptive Practices Act is modeled on the FTC Act and “New York State Courts have looked to FTC Act case law in interpreting” that law. *Assocs. Capital Servs. Corp. v. Fairway Private Cars, Inc.*, 590 F. Supp. 10, 15 (E.D.N.Y. 1982) (citing *Lefkowitz v. Colo. State Christian Coll.*, 346 N.Y.S.2d 482, 487–91 (Sup. Ct., N.Y. Cty. 1973)).

¹² See *Williams v. TCF Nat’l Bank*, No. 12 C 05115, 2013 WL 708123, at *1, *4 (N.D. Ill. Feb. 26, 2013) (arbitration agreement found in separate “Terms and Conditions” pamphlet enforceable because consumer “had actual possession of the Terms”); Order at 10, *Pellett v. TCF Bank, N.A.*, No. 10 C 3943 (D. Minn. Nov. 24, 2010) (Doty, J.) (“Plaintiffs may not avoid their signed agreements by claiming that they did not read or understand the contents of those agreements”); *Pivoris v. TCF Fin. Corp.*, No. 07 C 2673, 2007 WL 4355040, at *4 (N.D. Ill. Dec. 7, 2007) (arbitration agreement enforceable where “Account Agreement itself made mention of the arbitration provision in plain English and in bold print”).

¹³ That law, like the CFPA, defines deceptive acts or practices with reference to the FTC Act. 815 Ill. Comp. Stat. 505/2.

because 1) the rental agreement notified customers that the damage waiver was optional, and 2) the customer admitted he did not read that part of the contract. *Id.* at *4, *5. As the court explained, “failure to read the agreement dooms his CFA claim” because “Plaintiff simply chose not to read the agreement and discover...for himself” that the damage waiver was optional. *Id.* at *5–6.

While written disclosures may not always cure otherwise deceptive practices—such as when there are explicit misrepresentations,¹⁴ or where the written disclosure is buried in a lengthy document¹⁵ or located in an unusual place one would not think to look¹⁶—the complaint contains absolutely no allegations of that kind. No TCF customer acting reasonably under the circumstances could have been deceived. The Bureau’s apparent view that TCF customers should not be held to the clear disclosures they were provided breaks with longstanding principles of law. Count II should be dismissed.

B. TCF Did Not Abuse New Customers (Count I).

The CFPB likewise cannot maintain a viable claim for consumer abuse because the complaint has not plausibly alleged that TCF interfered with the

¹⁴ *See, e.g., FTC v. E.M.A. Nationwide, Inc.*, 767 F.3d 611, 632–33 (6th Cir. 2014) (disclosures contradicted by oral representations and only provided after consumer enrolled).

¹⁵ *Id.* at 633 (deceptive practice where “disclaimers and more accurate information were buried in written documents”).

¹⁶ *FTC v. Cyberspace.com, LLC*, 453 F.3d 1196, 1200–01 (9th Cir. 2006) (“fine print notices” on rear of check).

decision of customers to enroll; the complaint does not allege that TCF prevented New Customers from reading the disclosures or otherwise made oral statements that contradicted them.

To state a claim for abusive practices, the CFPB must allege that TCF “*materially interfere[d]* with the ability of a consumer to understand a term or condition of a consumer financial product or service.”¹⁷ 12 U.S.C. § 5531(d)(1) (emphasis added). Recycling almost all the allegations underlying the deception claim, the CFPB contends that TCF “materially interfered with its New Customers’ ability to understand” the terms and conditions governing overdraft service. Compl. ¶ 110. These allegations fall into three general categories, all of which fail as a matter of law.

First, the CFPB attacks TCF’s decision to give customers the Notice at the start of the account opening process and ask for an enrollment decision later, after a series of other disclosures and acknowledgments. But that allegation ignores the fact that separation is consistent with Regulation E, which required that the Notice be “segregated” from the Agreement. 12 C.F.R. § 205.17(b)(1)(i). And, there is nothing abusive about giving the required Notice at the outset. The Agreement referred customers back to the Notice, stating, “TCF has given you a notice called

¹⁷ The CFPA also prohibits as abusive an act or practice that “takes unreasonable advantage of” a consumer in various ways. 12 U.S.C. § 5531(d)(2). The Bureau relies only on the “material interference” aspect of an abusiveness claim. *See* Compl. ¶ 111.

What You Need to Know About Overdrafts and Overdraft Fees that describes our policy.” Hurd Decl. Ex. 5. If anything, providing the Notice first attributes greater prominence to the disclosure.

The CFPB’s newly-minted criticism also upends years of formal guidance from the Federal Reserve, which permits banks to provide the Notice “*prior to or at account-opening*” and includes no reminder requirement other than the written confirmation of enrollment provided afterwards. *See* 74 Fed. Reg. 59,033, 59,055 (Nov. 17, 2009), Official Staff Interpretations Comment 17(b)-5 (emphasis added). It is improper for the CFPB to attempt to impose liability based on its interpretation that contradicts official guidance in place at the time TCF enrolled New Customers. *See Christopher v. SmithKline Beecham Corp.*, 132 S. Ct. 2156, 2167 (2012) (refusing to apply new agency interpretation of “ambiguous regulations to impose potentially massive liability on respondent for conduct that occurred well before that interpretation was announced”); *PHH Corp.*, 839 F.3d at 49 (due process prevented the CFPB from retroactively applying different rules than predecessor regulator without fair notice).

Second, the CFPB contends that TCF materially interfered with New Customers’ ability to understand their enrollment decisions by instructing employees to give “uninformative” and “cursory” responses to questions and use “one-sided” hypotheticals. Compl. ¶¶ 3, 85–86, 110. Accepting the truth of these

allegations only for the purposes of this motion, they do not amount to “material interference” as a matter of law.

It cannot be that “uninformative” or “cursory” oral explanations (as the complaint’s totally conclusory allegations describe them) materially interfere with a customer’s decision where the law requires *no* explanation. Financial institutions throughout America can and do enroll millions of customers *online*. If the allegedly cursory summaries are not detailed enough, then online enrollment must be *per se* abusive. Yet the Federal Reserve’s guidance expressly permits online enrollment and does not require *any* oral disclosure. 74 Fed. Reg. at 59,055 (Official Staff Interpretation Comment 17(b)-4(iii)) (allowing customers to opt-in via “electronic means” including “at its Web site”).

The CFPB further alleges that many customers did not bother to read the Notice or the Agreement. But individual decisions to read or not read disclosures do not dictate whether TCF’s account-opening process was abusive. To properly allege abuse, the complaint must show that *TCF* took some action that “materially interfered” with a customer’s ability to understand the decision he was making.

The complaint only contains the conclusory allegation that TCF interfered with customer understanding through one-sided hypotheticals and cursory explanations. It does not explain how TCF’s alleged practices prevented New Customers from reading TCF’s clear, unambiguous disclosures, or how TCF

undermined customers' understanding that overdraft service was optional and a fee would be charged if the customer overdrafted. By providing customers with unambiguous written disclosures before, during, and after the enrollment decision, TCF gave New Customers the ability to understand the service it offered.

Third, the CFPB alleges that TCF deprived customers of the ability to understand overdraft service terms by incentivizing employees to reach unreasonably aggressive enrollment targets. Compl. ¶ 110. But employee incentives or goals are not *per se* abusive without a connection to actual improper conduct and resulting harm. Unlike other cases where the CFPB has alleged that improper conduct *actually resulted from* incentives,¹⁸ there are no allegations that *any* TCF employee engaged in any improper behavior, let alone improper behavior motivated by incentives. *See* Compl. ¶¶ 35–48.

Nothing in Regulation E or any other federal law prohibited the payment of financial incentives to employees, prohibited TCF from actively soliciting its customers to enroll in overdraft service, or required any particular oral statements to supplement the mandatory Notice and written confirmation. No matter how “uninformative” the Bureau says TCF’s scripts were, it has not pleaded facts sufficient to withstand dismissal of its abusiveness claim.

¹⁸ *See, e.g.*, Consent Order at 4–5, *In re Wells Fargo Bank, N.A.*, CFPB No. 2016-CFPB-0015 (Sept. 8, 2016) (incentives led employees to open accounts without consumer’s knowledge or consent).

C. The Bureau Cannot Retroactively Assert Claims that Pre-Date July 21, 2011.

“Elementary considerations of fairness dictate that individuals should have an opportunity to know what the law is and to conform their conduct accordingly; settled expectations should not be lightly disrupted.” *Landgraf v. USI Film Prods.*, 511 U.S. 244, 265 (1994). Thus, there is a “deeply rooted” presumption against retroactive application of legislation. *Id.*

In its zeal to address overdraft service, the CFPB is ignoring this bedrock principle by attempting to retroactively impose duties and penalties. The Court should reject this effort.

Counts I and II allege that TCF violated Sections 1031 and 1036 of the CFPA. Those provisions—and the Bureau’s authority to enforce them—did not become effective until July 21, 2011 (the “Effective Date”). Pub. L. No. 111-203, § 1037, 124 Stat. 1376 (July 21, 2010) (Sections 1031 and 1036 “shall take effect on the designated transfer date.”); 75 Fed. Reg. 57,252 (Sept. 20, 2010) (setting designated transfer date as July 21, 2011). Consequently, the CFPB cannot use these provisions to challenge conduct that occurred before the Effective Date.

Courts apply the two-part test from *Landgraf* to determine if a law may be applied retroactively. *See* 511 U.S. at 280; *In re ADC Telecomms., Inc. Sec. Litig.*, 409 F.3d 974, 976 (8th Cir. 2005) (applying *Landgraf* test). First, courts ascertain “whether Congress has expressly prescribed the statute’s proper reach.” *Landgraf*,

511 U.S. at 280. If so, ““there is no need to resort to judicial default rules.”” *ADC Telecommunications*, 409 F.3d at 976 (quoting *Landgraf*, 511 U.S. at 280). If not, “the court must determine whether the new statute would have retroactive effect, *i.e.*, whether it would impair rights a party possessed when he acted, increase a party’s liability for past conduct, or impose new duties with respect to transactions already completed.” *Landgraf*, 511 U.S. at 280. If it does, then the statute cannot be applied to past conduct. *Id.*

The CFPB cannot get past step one. Not only does the CFPA provide no express authorization of retroactivity, Congress’s intent was the opposite. Congress specifically set the Effective Date of the CFPA *in the future*. Pub. L. No. 111-203, § 1037, 124 Stat. at 2011. By contrast, Congress made the effective date of other provisions of Dodd Frank immediate. *See id.* § 4, 124 Stat. at 1390 (“Except as otherwise specifically provided...this Act and such amendments shall take effect 1 day after the date of enactment of this Act.”). Given Congress’s decision to make some provisions immediately effective and others effective at some future date, it necessarily follows that Congress intended the new provisions of the CFPA to apply only prospectively.

Even absent this clear expression of Congressional intent, the abusive and deceptive prohibitions still could not be applied retroactively under *Landgraf* step two. As to Count I’s allegations of abusive conduct, prior to passage of the CFPA

there was no law or regulation applicable to TCF that prohibited “abusive” conduct now covered by § 5531. Subjecting TCF to legal consequences for engaging in allegedly “abusive” behavior that pre-dates the Effective Date therefore would be the paradigmatic example of “impos[ing] new duties with respect to transactions already completed.” *Landgraf*, 511 U.S. at 280.

The CFPB also cannot enforce retroactively the deceptive prong of the CFPA. First, unlike with abusiveness, the FTC Act prohibited TCF from engaging in deceptive conduct before the Effective Date, but Congress nevertheless precluded the CFPB from enforcing the FTC Act. *See* 12 U.S.C. §§ 5481(14) (definition of Federal consumer financial law “does not include the Federal Trade Commission Act.”); 5481(12) (definition of enumerated consumer laws excludes FTC Act); 5581(b)(5)(B)(ii) (giving the CFPB authority to enforce *regulations* related to unfair and deceptive acts promulgated under the FTC Act, not authority to enforce violations of the FTC Act itself). To allow the Bureau to prosecute deceptive conduct that allegedly occurred before the Effective Date—ostensibly under the CFPA, but bootstrapped by reference to the FTC Act—would let in the backdoor that which is explicitly prohibited from entering through the front.

Second, the CFPA exposes TCF to greater potential penalties than TCF faced before its enactment. Before the Effective Date, only the Office of the Comptroller of the Currency (“OCC”), through 12 U.S.C. § 1818, could seek a

civil money penalty against TCF for deceptive practices under the FTC Act.

Under the CFPA, the CFPB can now also seek—and has sought in this case—civil money penalties under 12 U.S.C. § 5565.

Importantly, the CFPA did not displace the OCC’s authority to bring suit under the FTC Act, creating the possibility that TCF could now face *two* enforcement actions—and two separate penalties—for the same conduct, when before it could only face one. *See* 12 U.S.C. § 5581(b)(2)(A), (c)(2)(C)(ii) (partially transferring OCC authority to enforce Federal consumer financial laws (which exclude FTC Act), while maintaining the OCC’s authority to enforce 12 U.S.C. § 1818). This risk is not merely theoretical—in recent cases the CFPB and OCC have each sought (and received) civil money penalties for the same unfair or deceptive practices.¹⁹ Thus, if given retroactive effect the CFPA would impermissibly “attach[] new legal consequences to events completed before its enactment.” *Landgraf*, 511 U.S. at 270. The Court should therefore dismiss Counts I and II for conduct that pre-dates July 21, 2011.

¹⁹ *See, e.g.*, Consent Order at 13–15, 31, *In re First National Bank of Omaha*, CFPB No. 2016-CFPB-0014 (Aug. 25, 2016) (civil money penalty of \$4,500,000 to CFPB); Consent Order for a Civil Money Penalty at 2–3, *In re First National Bank of Omaha*, OCC No. 2016-076 (Aug. 18, 2016) (\$3,000,000 civil money penalty to OCC).

II. TCF Did Not Violate Regulation E (Count III).

Count III must be dismissed because the complaint does not plausibly contend TCF failed to comply with Regulation E in connection with its efforts to enroll Existing Customers in overdraft service.

Unlike New Customers, Existing Customers were accustomed to overdraft service, but were slated to default to opt-out status on August 15, 2010 if they did not affirmatively choose to enroll. The Bureau does not allege that TCF failed to provide the Notice to Existing Customers, nor does it contend that TCF failed to provide written confirmation of their enrollment decision. Instead, it claims that TCF violated Regulation E when it asked Existing Customers whether they wanted their card to “continue working as it does today.” *Id.* ¶ 121. According to the CFPB, this “fram[ed] the decision” in a way that “turned Overdraft Service...into the default position,” and, “[a]s a result, Existing Customers did not have a reasonable opportunity to consent nor did they affirmatively consent.” *Id.* ¶¶ 122–23. This conclusion is based on a demonstrable misreading of the “reasonable opportunity to consent” requirement.

A. TCF Gave Customers a Reasonable Opportunity To Consent.

Regulation E states that a “financial institution provides a consumer with a reasonable opportunity to provide affirmative consent when, among other things, it provides *reasonable methods* by which the consumer may affirmatively consent.”

74 Fed. Reg. at 59,042 (emphasis added). The regulation provides four examples, all of which focus on the *means* and *method* of obtaining affirmative consent, such as providing a mail-in form, a “readily available telephone number,” a web-based form, or a form that “the consumer can fill out and present in person...to provide affirmative consent.” *Id.*; *see also id.* at 59,055 (Official Staff Interpretations Comment 17(b)-4) (discussing “reasonable opportunity to provide affirmative consent”). The staff commentary for Regulation E makes clear that a “reasonable opportunity to consent” means that banks must provide “*reasonable methods*” to consent. *Id.*

The CFPB does not allege that TCF failed to provide reasonable enrollment options to Existing Customers. Indeed, the Bureau acknowledges that TCF gave customers the opportunity to enroll “through a number of [] communications channels[.]” Compl. ¶ 103. Nothing in the text of the regulation or the staff commentary suggests that the “reasonable opportunity” requirement has anything to do with the presentation or description of the customer’s opt-in choice. But that is exactly the meaning the CFPB asks the Court to give it here.

Allowing the CFPB to apply this novel (and incorrect) interpretation of Regulation E to TCF’s conduct from 2010 would violate TCF’s due process rights in the exact same way that the Bureau violated PHH’s rights by attempting to retroactively alter well established regulatory guidelines. *See PHH Corp.*, 839

F.3d at 44 (“But change becomes a problem—a fatal one—when the Government decides to turn around and *retroactively* apply that new interpretation to proscribe conduct that occurred *before* the new interpretation was issued.” (emphasis in original)); *see also Christopher*, 132 S. Ct. at 2167. If the CFPB wants to change the meaning of “reasonable opportunity” to require (or prohibit) oral disclosures, or specify the content of those disclosures, it must engage in a prospective rulemaking—which, interestingly, it is already doing.²⁰ A retroactive enforcement action seeking to establish new interpretations is improper.

B. The Complaint Fails To Allege Plausibly that Customers Did Not Provide Affirmative Consent.

The Regulation E claim also fails because the CFPB does not plausibly allege that TCF failed to obtain “affirmative consent” from customers. Count III asserts that TCF “changed the election from an Opt-In to an Opt-Out,” Compl. ¶ 122, by using call scripts that asked Existing Customers “something like” whether they would like their “TCF check card to continue to work as it does today” and then treating that “as *an indication* that the customer wanted to Opt In,” *id.* ¶¶ 89–90 (emphasis added).

²⁰ *See* CFPB Agency Rule List, Fall 2016 (Hurd Decl. Ex. 9) (listing “Overdraft” in the “Prerule Stage”); *see also* CFPB Fall 2016 Rulemaking Agenda, Dec. 2, 2016 (Hurd Decl. Ex. 10) at 3 (“The Bureau is continuing to engage in additional research and has begun consumer testing initiatives relating to the opt-in process.”); CFPB Fall 2015 Rulemaking Agenda, Nov. 20, 2015 (Hurd Decl. Ex. 1) at 2 (“The Bureau is preparing for a rulemaking concerning overdraft programs on checking accounts.”).

The CFPB does not allege that TCF actually enrolled customers based solely on the response to this ice-breaker question. To the contrary, it acknowledges—as it must—that TCF’s scripts called for additional disclosures about TCF’s overdraft service, *including fees*, *id.* ¶ 94, followed by a question asking whether the customer wanted to enroll in overdraft service. *Id.* ¶ 96; *see also* Hurd Decl. Ex. 6.

There is simply no allegation that TCF enrolled Existing Customers without their knowledge, or under false pretenses, or defaulted Existing Customers into Opt-In status. Instead, TCF only enrolled Existing Customers who answered “Yes” to the enrollment question *at the end of the script*. As a matter of law, this does not constitute a violation of Regulation E.

The CFPB’s “conversion” argument is also nonsensical. The Bureau alleges that TCF scripts led customers to believe that the default was to be opted into overdraft service because the script informed Existing Customers that “some upcoming regulatory changes...would limit the usage” of their TCF Check Cards, Compl. ¶ 89, and asked “whether they wanted their account ‘to continue working as it does today,’” *id.* ¶ 121. But there is nothing wrong or misleading about these statements, the Bureau’s *ipse dixit* assertion notwithstanding.

The challenged statements are factually accurate. At the time the calls were placed (i.e., before Regulation E became effective), Existing Customers were all enrolled in overdraft protection; if they did nothing, they automatically would have

been opted out of that service. If that happened, their cards would not have worked as they had—i.e., swipe negative/settle positive transactions would not have been approved and overdraft transactions would not have been honored. The CFPB cannot claim that TCF violated Regulation E by providing its customers with factually accurate information. Count III should be dismissed.

C. The CFPB Cannot Seek Restitution for Existing Customers Who Incurred Their First Overdraft Prior to March 6, 2014.

The CFPB contends that it can enforce alleged violations of Regulation E through the Electronic Funds Transfer Act (“EFTA”), 15 U.S.C. § 1693, and the CFPA, 12 U.S.C. § 5536(a)(1)(A). Claims under both statutes are time-barred to the extent the Bureau seeks restitution for customers who incurred an overdraft before *March 6, 2014*.²¹

The EFTA limits claims for “civil liability” to those brought “within one year from the date of the occurrence of the violation.” 15 U.S.C. § 1693m(g). Courts have interpreted this to mean that the one-year limitations period runs from the date of the first challenged transfer. *See, e.g., Harvey v. Google Inc.*, No. 15-cv-03590-EMC, 2015 WL 9268125, at *3 (N.D. Cal. Dec. 21, 2015); *Repay v. Bank of Am., N.A.*, No. 12 CV 10228, 2013 WL 6224641, at *5 (N.D. Ill. Nov. 27,

²¹ TCF entered into a series of tolling agreements with the CFPB beginning on February 11, 2015. Accounting for brief lapses between extensions (totaling 23 days), tolling runs from March 6, 2015. Hurd Decl. Ex. 7.

2013); *Pelletier v. Pac. WebWorks, Inc.*, No. CIV S-09-3503 KJM KJN, 2012 WL 43281 (E.D. Cal. Jan. 9, 2012).

Although a question of first impression, the EFTA's one-year limitations period for civil liability governs the Bureau's action here. Where Congress wishes to provide a longer limitations period for government action than private action, it can and does do so explicitly. *See, e.g.*, 12 U.S.C. § 2614 (requiring that suits to enforce §§ 2607 and 2608 be brought within one year, "except that actions brought by [various government agencies] may be brought within 3 years from the date of the occurrence of the violation."). Because there is no separate statute of limitations provision for actions by regulators, the one-year limitations period should apply. *Cf. Consumer Fin. Prot. Bureau v. ITT Educ. Servs., Inc.*, No. 1:14-CV-00292-SEB-TAB, -- F. Supp. 3d --, 2015 WL 1013508 at *32–33 (S.D. Ind. Mar. 6, 2015) (applying TILA's one-year civil liability limitations period to the Bureau's claims).

Nor does the CFPA's three-year limitations period apply because the CFPA claim is entirely derivative of the alleged EFTA violation. Section 1054 of the CFPA authorizes the CFPB to bring suits in federal court for alleged CFPA violations no later than "3 years after the date of discovery of the violation." 12 U.S.C. § 5564. This general rule, however, is subject to an important caveat: "any action arising solely under an enumerated consumer law," including the EFTA, is

not governed by the three-year limitations period, but instead is governed by “the requirements of that provision of law [i.e. the enumerated consumer financial law], as applicable.” *Id.* § 5564(g)(2)(A)–(B).

The Bureau alleges that TCF violated the CFPA, which makes it unlawful to “commit any act or omission in violation of a Federal consumer financial law.” 12 U.S.C. § 5536; *see also* 12 U.S.C. § 5481(14) (defining “Federal consumer financial law” to include “enumerated consumer laws”). This means that Count III’s CFPA claim is based solely on an alleged violation of an enumerated consumer law—the EFTA—and therefore subject to the one-year limitations period established by the same EFTA. Count III should be dismissed as time-barred for all Existing Customers who incurred their first overdraft fee before March 6, 2014.

III. The CFPB Is Unconstitutionally Structured Due to the Lack of Executive and Congressional Oversight.

The CFPB’s structure is unconstitutional. *See PHH Corp.*, 839 F.3d at 8. Its lack of oversight impermissibly interferes with the President’s ability to “‘take Care that the Laws be faithfully executed,’” *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 484 (2010) (quoting U.S. Const. art. II, § 1), and leaves the CFPB accountable only to itself. As a panel for the D.C. Circuit recently said, “when measured in terms of unilateral power, the Director of the

CFPB is the single most powerful official in the entire U.S. Government, other than the President.” *PHH Corp.*, 839 F.3d at 17.

The CFPB has several structural infirmities which, considered separately or together, make the Bureau unconstitutionally free from oversight by elected officials. First, unlike nearly all other independent agencies, the CFPB is led by a single Director, not a multi-member commission. 12 U.S.C. § 5491(b)(1). “As compared to a single-Director structure, a multi-member independent agency also helps to avoid arbitrary decisionmaking and to protect individual liberty because the multi-member structure—and its inherent requirement for compromise and consensus—will tend to lead to decisions that are not as extreme, idiosyncratic, or otherwise off the rails.” *PHH Corp.*, 839 F.3d at 27.

Second, the CFPB director does not serve at the pleasure of the President—he is appointed for a five-year term spanning across presidencies, and is subject only to for-cause removal. 12 U.S.C. § 5491(c)(1), (c)(3).

Third, the CFPB does not even answer to Congress for its budget—it independently funds itself through the Federal Reserve, and funds taken by the CFPB “shall not be subject to review by the Committees on Appropriations of the House of Representatives and the Senate.” *Id.* § 5497(a)(1), (a)(2)(C).

These structural infirmities create an agency “exceptional in our constitutional structure and unprecedented in our constitutional history.” *PHH*

Corp., 839 F.3d at 21. Without oversight from either elected branch of government, the CFPB is unconstitutional. And because it is unconstitutional, it lacks authority to bring this action. See *Noel Canning v. NLRB*, 705 F.3d 490, 493 (D.C. Cir. 2013) (NLRB action “void *ab initio*” when commissioners were unconstitutionally appointed), *aff’d on other grounds*, 134 S. Ct. 2550 (2014).

The proper remedy in this case is to dismiss this action without prejudice to allow the Bureau to reconsider whether to bring an enforcement action *after* its structure conforms to the Constitution’s requirements. See *NLRB v. Whitesell Corp.*, 638 F.3d 883, 888–89 (8th Cir. 2011) (after prior decision held NLRB panel was not properly constituted for statutory reasons; “Our prior denial does not preclude the Board, *now properly constituted*, from considering this matter anew and issuing its first valid decision.” (emphasis added)); *Fed. Election Comm’n v. Legi-Tech, Inc.*, 75 F.3d 704, 708 (D.C. Cir. 1996) (properly reconstituted after *NRA Political Victory Fund, infra*, Federal Election Commission permissibly ratified past enforcement action); see also *Fed. Election Comm’n v. NRA Political Victory Fund*, 6 F.3d 821, 828 (D.C. Cir. 1993) (after severing unconstitutional structure; “appellants raise the constitutional challenge as a defense to an enforcement action, and we are aware of no theory that would permit us to declare the Commission’s structure unconstitutional without providing relief to the appellants in this case”).

This enforcement action has been entirely (and therefore unconstitutionally) shielded from executive oversight. Indeed, as noted earlier, the CFPB filed this suit on inauguration eve, likely in an effort to insulate this action from any Presidential review. Therefore, the case should be dismissed.

CONCLUSION

For the foregoing reasons the Complaint should be dismissed.

Dated: February 17, 2017

Respectfully submitted,

/s/ Timothy D. Kelly

Timothy D. Kelly (#54926)
Kristina Kaluza (#0390899)
DYKEMA GOSSETT PLLC
4000 Wells Fargo Center
90 South Seventh Street
Minneapolis, MN 55402
Telephone: 612.486.1900
Fax: 855.227.5097
tkelly@dykema.com
kkaluza@dykema.com

John. K. Villa (admitted *pro hac vice*)
Edward J. Bennett (admitted *pro hac vice*)
Ryan T. Scarborough (admitted *pro hac vice*)
Eric G. Blankenstein (*pro hac pending*)
WILLIAMS & CONNOLLY LLP
725 Twelfth Street, N.W.
Washington, DC 20005
Telephone: 202.434.5000
Fax: 202.434.5029

jvilla@wc.com
ebennett@wc.com
rscarborough@wc.com
eblankenstein@wc.com

Andrew L. Sandler (admitted *pro hac vice*)
Andrea K. Mitchell (admitted *pro hac vice*)

BUCKLEY SANDLER LLP

1250 24th Street, N.W.

Suite 700

Washington, DC 20037

Telephone: 202.349.8000

Fax: 202.349.8080

asandler@bucklesandler.com

amitchell@bucklesandler.com

*Attorneys for Defendant TCF National
Bank*

APPENDIX C

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

February 7, 2019

The Honorable Kathy Kraninger
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, D.C. 20552

Dear Director Kraninger:

The Consumer Financial Protection Bureau (“Consumer Bureau”) has recently announced several settlements against entities for engaging in unlawful practices without requiring the payment of redress to consumers harmed by the illegal conduct. This stands in stark contrast to the Consumer Bureau’s practice under the leadership of former Director Cordray. During Director Cordray’s tenure, the Consumer Bureau recovered nearly \$12 billion in relief for harmed consumers over its first six years.¹ American consumers deserve a Consumer Bureau that will fight to recover their hard-earned money when they are cheated.

On January 16, 2019, the Consumer Bureau announced it had reached a settlement with Sterling Jewelers Inc. (“Sterling”) for numerous claims, including that the company engaged in unfair practices by enrolling consumers who had a Sterling credit card in payment protection insurance without their consent.² Under the terms of the settlement, Sterling is required to pay a penalty to the Consumer Bureau of \$10 million, but does not have to refund consumers any of the money paid for payment protection insurance.³ According to the Consumer Bureau’s complaint against Sterling, payment protection insurance generated \$60 million in revenue in 2016 alone.⁴ The Consumer Bureau has previously required payments to consumers in similar cases where it found that consumers were enrolled in payment protection products without their consent.⁵ The Committee is deeply troubled that the Consumer Bureau would allow a company to keep the profits they made from their illegal sales practices.

On January 25, 2019, the Consumer Bureau announced a settlement with Enova International, Inc. (“Enova”), an online lender, for engaging in unfair practices by debiting consumers’ bank accounts without authorization.⁶ The settlement requires Enova to pay a \$3.2 million civil money penalty to the Consumer Bureau, but contains

¹ <https://www.consumerfinance.gov/about-us/blog/six-years-serving-you/>

² *Bureau of Consumer Financial Protection and the People of the State of New York, by Letitia James, Attorney General for the State of New York, v. Sterling Jewelers Inc.*, Case 1:19-cv-00448 (Jan. 16, 2019), available at <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-settles-claims-against-sterling-jewelers-inc/>.

³ *Id.*

⁴ Complaint at ¶41, available at https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/bcftp_sterling-jewelers_complaint.pdf

⁵ See e.g. . Consumer Financial Protection Bureau, Consent Order *In the Matter of Bank of America, N.A. and FIA Card Services, N.A.* 2014-CFPB-0004 (April 9, 2014) (providing approximately \$269 million in restitution to consumers for deceptively enrolling consumers in payment protection products) available at <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-bank-of-america-to-pay-727-million-in-consumer-relief-for-illegal-credit-card-practices/>; Consumer Financial Protection Bureau, Consent Order *In the Matter of Fifth Third Bank*, 2015-CFPB-0025 (Sept 28, 2015)(requiring approximately \$3 million in restitution to consumers for deceptively enrolling consumers in payment protection products) available at https://files.consumerfinance.gov/f/201509_cfpb_consent-order-fifth-third-bank-add-on.pdf;

⁶ Consumer Financial Protection Bureau, Consent Order *In the Matter of Enova International, Inc.*, 2019-CFPB-0003, (Jan25. 8, 2019), available at <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-reaches-settlement-enova-international-inc/>.

no provision for paying redress to consumers.⁷ The factual findings in the administrative consent order indicates that Enova debited payments on thousands of consumers' outstanding loans where it did not have authorization and "extracted millions of dollars in unauthorized debits from consumers' accounts."⁸

On February 1, 2019, the Consumer Bureau announced a settlement with NDG Financial Corporation and other Defendants ("NDG Financial") that did not require them to pay either a penalty or restitution to consumers.⁹ The Consumer Bureau initiated its action against NDG Financial when the agency was still led by former Director Cordray. In its December 2015 amended complaint, the Consumer Bureau alleged that NDG Financial engaged in unfair, deceptive, and abusive practices by collecting on payday loans that were made in violation of state law.¹⁰ The amended complaint specifically sought "damages and other monetary relief as the Court finds necessary to redress injury to consumers resulting from [NDG Financial's] violations of federal consumer protection laws including but not limited to restitution and the refund of monies paid."¹¹ Yet, the settlement agreement seeks no such relief for the wronged consumers.

Section 1055 of the Consumer Financial Protection Act of 2010 ("CFPA") explicitly authorizes the Consumer Bureau to obtain relief for consumers, including the refund of money, restitution, or the payment of damages or other monetary relief. 12 U.S.C. § 5565(a)(1)(2).

The Committee has serious concerns about how the Consumer Bureau is exercising its enforcement authority, especially how it is determining whether to require companies to pay redress to consumers that have been harmed. The fact that two of the three settlements involve online lending raises serious questions about the Consumer Bureau's commitment to protecting America's consumers from predatory online lending practices.

As part of the Committee's oversight over the Consumer Bureau,¹² please provide the following records by no later than March 5, 2019:

- (1) All documents and communications referring or related to the issue of restitution in the settlement in *Bureau of Consumer Financial Protection and the People of the State of New York, by Letitia James, Attorney General for the State of New York, v. Sterling Jewelers Inc.*, Case 1:19-cv-00448, including but not limited to, all memoranda (whether draft or final), any and all drafts of the proposed consent order, and all meeting minutes.
- (2) All communications between the Bureau and Sterling or its representatives referring or related to the issue of restitution in the settlement in *Bureau of Consumer Financial Protection and the People of the State of New York, by Letitia James, Attorney General for the State of New York, v. Sterling Jewelers Inc.*, Case 1:19-cv-00448, including but not limited to, any and all drafts of the proposed consent order.
- (3) All documents and communications referring or related to the issue of restitution in the settlement in *In the Matter of Enova International, Inc.*, 2019-CFPB-0003, including but not limited to, all

⁷ *Id.*

⁸ *Consent Order* at ¶¶ 14, 18, available at https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_enova-international-consent-order-2019-01.pdf.

⁹ *Consumer Financial Protection Bureau v. NDG Financial Corp. et al.*, Case 1:15-cv-05211-CM (February 1, 2019) available at <https://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-settles-ndg-financial-corp/>

¹⁰ Amended Complaint at ¶¶ 275-95 available at

https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/cfpb_northway_amended-complaint_122015.pdf

¹¹ *Id.* at ¶337(b).

¹² Rule X, Rules of the House of Representatives, 116th Congress 69

memoranda (whether draft or final), any and all drafts of the proposed consent order, and all meeting minutes.

- (4) All communications between the Bureau and Enova or its representatives referring or related to the issue of restitution in the settlement in *In the Matter of Enova International, Inc.*, 2019-CFPB-0003, including but not limited to, any and all drafts of the proposed consent order.
- (5) All documents and communications referring or related to the issue of restitution in the settlement in *Consumer Financial Protection Bureau v. NDG Financial Corp. et al.*, Case 1:15-cv-05211, including but not limited to, all memoranda (whether draft or final), any and all drafts of the proposed consent order, and all meeting minutes.
- (6) All communications between the Bureau and NDG (or any of the other Defendants named in the settlement) or their representatives referring or related to the issue of restitution in the settlement in *Consumer Financial Protection Bureau v. NDG Financial Corp. et al.*, Case 1:15-cv-05211, including but not limited to, any and all drafts of the proposed consent order.

Please address any questions regarding this request to Committee staff at (202) 225-4247.

Sincerely,



MAXINE WATERS
CHAIRWOMAN



AL GREEN
CHAIRMAN
Subcommittee on Oversight and Investigations

cc: The Honorable Patrick McHenry, Ranking Member

APPENDIX D

Bureau of Consumer Financial Protection
1700 G Street NW
Washington, D.C. 20552



March 5, 2019

The Honorable Maxine Waters
Chairwoman
Committee on Financial Services
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Al Green
Chairman
Subcommittee on Oversight and Investigations
Committee on Financial Services
U.S. House of Representatives
2129 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairwoman Waters and Chairman Green,

Thank you for your letter of February 7, 2019, regarding the terms of the Consumer Financial Protection Bureau's (Bureau's) recent settlements with Enova International, Sterling Jewelers, and NDG Financial Corporation. The Bureau is firmly committed to fulfilling its statutory mandate, which includes taking action against bad actors who violate Federal consumer financial laws.

Through these three settlements, the Bureau obtained more than \$13 million in civil money penalties, as well as injunctive relief to help ensure that these businesses refrain from engaging in illegal practices and that consumers are protected from future violations. Settlements allow the Bureau to avoid expending significant resources proving claims in court, mitigate trial risk, achieve speedier results for consumers, and provide certainty for companies. While the Bureau is committed to seeking all appropriate relief for consumers, not every case necessarily lends itself to restitution for affected consumers, particularly in the context of a negotiated settlement. Moreover, even when the Bureau does not obtain restitution through a negotiated settlement, in appropriate cases consumers may still be compensated for loss caused by violations of Federal

consumerfinance.gov

consumer financial law through payments from the Bureau's Civil Penalty Fund, relief obtained through private litigation, or payments made voluntarily by the responsible companies.

An initial production of documents responsive to your request is enclosed herein. This production includes communications responsive to items number 2 and 4 of your letter, which requested communications between the Bureau and Sterling Jewelers and its representatives, and between the Bureau and Enova International and its representatives, respectively, concerning whether any proposed settlement would include restitution for consumers. Per the conversation between Bureau staff and Committee staff on March 1, 2019, the Bureau continues to process your other requests.

Your letter also requests Bureau documents relating to the issue of restitution for each matter, including draft and final internal, pre-decisional memoranda. Many of these documents implicate longstanding Executive Branch confidentiality interests because they are law-enforcement sensitive and are protected by the Bureau's deliberative-process and attorney-client privileges. In order to accommodate the Committee's interest in this matter, I have attached a narrative summary describing the basis for the Bureau's decision not to require restitution as a condition for settling these three matters. As I have emphasized in our conversations, the Bureau is committed to accommodating the Committee's oversight interests and we look forward to working with you to determine a mutually agreeable path forward to satisfy your oversight needs while respecting the Bureau's legitimate confidentiality interests.

Today's production includes 1,679 pages bates labeled HFSC_CFPB_030519_00000001 - 00001679. The documents are being provided in PDF and TIFF formats. Minor redactions have been applied to protect personal privacy and system security interests. These documents contain confidential information of the Consumer Financial Protection Bureau. *See* 12 C.F.R. 1070.40 et seq. The documents may also be subject to disclosure restrictions set forth in other Federal laws, including but not limited to the Freedom of Information Act, 5 U.S.C. § 552, the Trade Secrets Act, 18 U.S.C. 1905, and the Privacy Act of 1974, 5 U.S.C. § 552a. The Bureau therefore requests that the Committee protect this information from any disclosure that would cause an unwarranted invasion of privacy or harm to any of the interests served by the law and policy prohibiting the public release of these documents or exempting them from disclosure.

Should you have any questions about this response, please contact me or have your staff contact Redacted by the Committee in the Bureau's Legal Division or Redacted by the Committee in the Bureau's Office of

Legislative Affairs. [Redacted by the Committee] can be reached at [Redacted by the Committee] and [Redacted by the Committee] can be reached at [Redacted by the Committee].

Sincerely,



Kathleen L. Kraninger
Director

Enclosure

cc: The Honorable Patrick McHenry, Ranking Member, Committee on Financial Services
The Honorable Andy Barr, Ranking Member, Subcommittee on Oversight and Investigations

Addendum

Sterling Jewelers

Signet Jewelers Limited and its wholly owned subsidiary, Sterling Jewelers, are specialty jewelry retailers that offer consumer-financing programs that extend credit directly to consumers. In coordination with the State of New York's Office of the Attorney General, the Bureau's and the State's parallel enforcement investigations concluded that there was a basis to allege that Sterling violated the Consumer Financial Protection Act, the Truth in Lending Act, and Regulation Z.

The investigations found that consumers who visited Sterling's stores were typically encouraged by Sterling's salespeople to finance their purchases, and that Sterling's company culture, reflected in its training materials and sales-performance standards, pressured employees to enroll consumers in company credit cards and to sell its financing plans and payment-protection insurance. In connection with offering these credit products, the investigation concluded that Sterling's salespeople at times misrepresented financing terms or omitted information necessary for consumers to understand the credit offer. Store employees often failed to inform consumers that they were applying for credit and misstated the reasons for requesting consumers' personal information. Many of Sterling's store managers and district managers encouraged deceptive tactics to induce consumers to apply for a credit card, and many turned a blind eye to such conduct. The investigations identified several illegal practices, including (1) submitting credit applications for consumers and causing credit cards to be issued without consumers' knowledge or consent; (2) misrepresenting credit-financing terms and conditions; and (3) enrolling consumers in payment-protection insurance without their knowledge or consent.

The Bureau and the State of New York reached a settlement with Sterling on January 16, 2019, which included injunctive relief, a \$10 million civil money penalty to the Bureau, and a \$1 million civil money penalty to the State of New York. The Bureau ultimately decided not to seek consumer restitution for its claims, but took the lack of restitution into account when negotiating the amount of its penalty. Among the factors the Bureau considered in deciding not to seek restitution was that it would be difficult to determine which consumers may have been impacted by Sterling's illegal sales practices. The improper practices recited in the consent order primarily relate to in-person interactions in the stores. Evidence documenting such interactions was not readily available in Sterling's records, and therefore identifying affected consumers would have required a consumer-by-consumer investigation and determination. The

decision to seek and approve a settlement on these terms was authorized by Acting Director Mulvaney.

Enova International, Inc.

Following an investigation into online payday and installment lender Enova International, Inc. (Enova), the Bureau concluded that it had a basis to allege that Enova violated the Consumer Financial Protection Act by debiting consumers' bank accounts without authorization and by failing to honor certain loan extensions it had granted to consumers. With respect to the unauthorized debits, while consumers authorized Enova to deduct payments from certain accounts, the company in many instances debited different accounts that the consumers had not authorized it to use. The Bureau reached a settlement with Enova on January 25, 2019, which enjoined Enova from making or initiating electronic fund transfers without valid authorization, and from failing to honor loan extensions. It also required Enova to pay a \$3.2 million civil money penalty.

The Bureau obtained civil money penalties and injunctive relief for the claim related to unauthorized debits, but did not require Enova to pay consumer redress for that claim. The amounts unlawfully debited by Enova were generally actually owed to Enova. As an exercise of its enforcement discretion, the Bureau decided not to require such refunds as a condition of settlement. In addition, consumers may have suffered collateral monetary harm to the extent that they may have incurred fees or been charged penalties by their account holder if, for example, the unauthorized debit caused the account to overdraw. However, the Bureau ultimately decided not to seek restitution for this claim because it would have been difficult for the Bureau to determine which consumers incurred such fees and penalties as a result of the unauthorized debits, and Enova had previously offered restitution to some consumers who incurred these fees. Similarly, while consumers may have been charged fees or penalties as a result of Enova's failure to honor loan extensions, the amount of fees and penalties for each consumer could not be calculated with certainty. The decision to seek and approve a settlement with Enova that did not include restitution was made by the Division of Supervision, Enforcement, and Fair Lending (SEFL) Policy Associate Director, in consultation with Acting Director Mulvaney, under delegated authority from Acting Director Mulvaney.

NDG Financial Corporation

The NDG Enterprise is a common enterprise consisting of a collection of interrelated companies that originate, service, and collect payday loans. Though these companies are owned and operated in Europe and Canada, certain NDG affiliates and subsidiaries did business in the United States, primarily through the marketing, origination, servicing, and collecting of payday loans to American consumers online. The Bureau's investigation concluded that the Bureau had a basis to allege that the NDG Enterprise offered loans to consumers that were void under certain states' licensing or usury laws, and routinely misrepresented to consumers that they were obligated to repay the void loans. In addition, NDG and its components misrepresented that loan agreements were not subject to United States federal or state laws and misrepresented that non-payment of the debts would result in lawsuits, arrests, imprisonment or wage garnishment. The Bureau's investigation found that there was a basis to allege these practices violated the Consumer Financial Protection Act. The Bureau also alleged that NDG and its components conditioned loan agreements upon irrevocable wage assignment clauses in violation of the Credit Practices Rule and the Consumer Financial Protection Act.

In light of this conduct, the Bureau filed a complaint against certain components of the NDG Enterprise ("Defendants") in the U.S. District Court for the Southern District of New York on July 31, 2015. Between 2015 and 2019, the Bureau engaged in a protracted legal battle with the Defendants, some of whom were ultimately sanctioned by the district court for refusal to comply with a court order requiring them to cooperate with the Bureau's discovery requests. At the Defendants' request, the matter was referred to a magistrate judge in October 2018 to facilitate a settlement.

The Bureau encountered substantial hurdles in trying to enforce its discovery demands, in part because the Defendants' companies and individuals are based overseas and Defendants refused to cooperate with Bureau discovery requests. The Defendants withheld consumer-level information required to establish the identities of consumers harmed by the alleged violations, as well as the full amount of that harm. Without these critical facts, the Bureau was not able to determine the amount of redress that might be owed to consumers, or the consumers to whom that redress could be paid. In addition, because the foreign Defendants did not have assets in the United States, the Bureau anticipated potential challenges in collecting on any penalties or remediation.

On February 1, 2019, the Bureau agreed to a settlement that included extensive injunctive relief permanently barring the Defendants from advertising, marketing, promoting, offering, originating, servicing, or collecting any consumer loan issued to any consumer residing in the United States, including assisting others and receiving remuneration from providing services to assist others in this conduct. The Defendants are also permanently barred from collecting on any of their existing loans to United States consumers, including any efforts to assign, sell or transfer such loans or any other action that would allow anyone to collect on such loans. Additionally, the Defendants are permanently barred from disclosing, using, or benefitting from customer information associated with their existing loans to consumers in the United States. The decision to seek and approve a settlement on these terms was authorized by Acting Director Mulvaney. The settlement order was approved by the district court on February 4, 2019.

APPENDIX E

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

March 28, 2019

The Honorable Kathy Kraninger
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, D.C. 20552

Dear Director Kraninger:

We write to express the House Financial Services Committee's (Committee) dissatisfaction with the Consumer Financial Protection Bureau's (Consumer Bureau) response to the Committee's document requests. As detailed below, the Consumer Bureau has produced an unacceptably small number of documents in response to the Committee's record requests made on February 7 and February 21. The Committee is further displeased that the Consumer Bureau has withheld responsive documents from the Committee without providing any assurances that it intends to fully comply with the Committee's requests.¹

The Committee continues to expect agencies under its jurisdiction to answer Committee document requests with all responsive documents. Withholding responsive documents denies the Committee information that is essential to its consideration of potential legislation.

February 7, 2019 Request

On February 7, 2019, the Committee transmitted a letter requesting that the Consumer Bureau provide, by March 5, 2019, documents regarding three recent enforcement actions that did not provide for consumer redress (Settlements Letter).² Specifically, the Committee sought "[a]ll documents and communications referring or related to the issue of restitution" in Consumer Bureau settlements with Sterling Jewelers Inc. (Sterling), with Enova International, Inc. (Enova), and with NDG Financial Corporation and other Defendants (NDG Financial).³ The Committee also requested "[a]ll communications between the Bureau" and these three entities or their representatives.⁴

On February 14, 2019, Committee staff hosted an initial, in-person meeting with Consumer Bureau staff to discuss the Settlements Letter and requested that the Consumer Bureau prioritize producing documents related to the Enova and Sterling settlements.

On February 15, 2019, Committee staff reiterated in an email its request to prioritize the Enova and Sterling documents.

On March 1, 2019, Committee and Consumer Bureau staff engaged in further discussions. The Consumer Bureau indicated that it would make an initial production of its communications with outside counsel for Enova and Sterling on March 5, 2019, but that it was unable to provide a date by which it would be able to produce internal documents and communications for those matters.

¹ This letter addresses only the first two document requests. The deadline for production for the third requests for documents was March 25, 2019, and Committee staff is still reviewing the Consumer Bureau's initial production.

² See 2/7/2019 Letter from Chairwoman Waters and Congressman Green to Director Kraninger.

³ *Id.*

⁴ *Id.*

On March 5, 2019, the Bureau produced 1,679 pages of external communications with Enova and Sterling. However, in its cover letter the Consumer Bureau did not commit to producing responsive internal documents, stating that these responsive documents “implicate long-standing Executive Branch confidentiality interests because they are law-enforcement sensitive and are protected by the Bureau’s deliberative process and attorney-client privileges.” Instead of producing these responsive documents, the Consumer Bureau included a “narrative summary describing the basis for the Bureau’s decision not to require restitution as a condition for settling these three matters.”

On March 8, 2019, Consumer Bureau staff disclosed during a call with Committee staff the existence of approximately 4,900 potentially responsive internal documents related to Enova, and approximately 6,800 potentially responsive internal documents related to Sterling. During the call, Committee staff requested that the Consumer Bureau provide a date for producing the responsive internal documents for Enova and Sterling.

On March 15, 2019, Committee staff spoke with Consumer Bureau staff and, again, inquired about a date for production of responsive internal Enova and Sterling documents. The Consumer Bureau estimated that it would be able to produce internal Enova and Sterling documents in three to four weeks, but that it had not yet decided whether it would withhold these documents due to attorney-client or deliberative process privilege.

Most recently, in a March 21, 2019 call, Consumer Bureau staff again communicated that “no decision” had been made regarding the assertion of privilege over the internal Enova and Sterling documents.

Thus, nearly a month after the deadline for producing responsive documents, the Consumer Bureau continues to withhold thousands of responsive documents without providing any commitment about when, or even if, it will produce them to the Committee.

February 21, 2019 Request

On February 21, 2019, the Committee requested that the Consumer Bureau provide, by March 21, 2019, documents regarding the decision to transfer the Office of Fair Lending and Equal Opportunity (OFLEO) to the Office of the Director (OFLEO Letter).⁵ The OFLEO Letter specifically sought communications and documents to and from various officials at the Consumer Bureau.⁶

On March 1, 2019, Committee and Consumer Bureau staff initially discussed these requests and agreed that the Bureau would prioritize producing documents responsive to Requests 1-4 from November 25, 2017 (when Mr. Mulvaney assumed leadership of the Bureau) to February 15, 2018 (a few weeks after the January 30, 2018 announcement regarding transferring OFLEO to the Office of the Director).

Committee and Consumer Bureau staff engaged in further discussion on March 8, 2019, during which Committee staff requested that the Consumer Bureau provide information on what responsive documents it would be able to produce by the March 21st deadline.

During a March 15, 2019 call, Consumer Bureau staff communicated that the Consumer Bureau intended to produce documents responsive to Requests 1-7, 10, and 12 in the OFLEO Letter.⁷

On March 21, the Consumer Bureau produced the following documents: (a) Mr. Mulvaney’s January 30, 2018 all-hands email announcing the planned reorganization that was widely quoted in press articles; (b) memoranda, including one that was completely redacted, approving implementation of the reorganization (months after the decision was made); (c) an April 27, 2018 presentation to the NTEU regarding the reorganization; (d) four Excel spreadsheets relating to the placement of current and former OFLEO staff throughout the Consumer Bureau before and after implementation of the reorganization; and (e) approximately 48 position descriptions related to OFLEO staff. In its cover letter, the Consumer Bureau stated that “a number of responsive documents implicate long-standing Executive Branch confidentiality interests as they are protected by the Bureau’s deliberative process and attorney-client privileges . . . a non-privileged document responsive to

⁵ See 2/21/2019 Letter from Chairwoman Waters and Congressman Green.

⁶ See e.g., Requests #1-6 in the OFLEO Letter.

⁷ There were a total of 12 separate documents requests in the OFLEO Letter.

request 1 is enclosed with this production; all other documents responsive to requests 1-6 reflect Bureau confidentiality interests.”

Committee staff learned in a March 21, 2019 conversation with Consumer Bureau staff that the Consumer Bureau was withholding approximately 600 documents that it had deemed potentially responsive to the OFLEO Letter.

In both your March 5th and March 21st letters, you expressed that the “Bureau is committed to accommodating the Committee’s oversight interests.” Your minimal production to date, however, belies that assertion. The Committee cannot exercise its oversight responsibility if the Consumer Bureau withholds thousands of potentially-responsive documents and provides a “written narrative” in lieu of underlying internal documents.

The Committee expects the Consumer Bureau to engage in a good faith effort to quickly produce the records sought. If the Consumer Bureau continues to deny the Committee the ability to review responsive documents without asserting a constitutionally-based privilege or providing a timeline for their delivery, we will be forced to begin considering the use of compulsory process.

Sincerely,



MAXINE WATERS
CHAIRWOMAN



AL GREEN
CHAIRMAN

Subcommittee on Oversight and Investigation

cc: The Honorable Patrick McHenry, Ranking Member

APPENDIX F

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

June 20, 2019

The Honorable Kathleen L. Kraninger
Director
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, D.C. 20552

Dear Director Kraninger:

As promised, I am writing to follow up on our conversation last week regarding the Consumer Financial Protection Bureau's (Consumer Bureau) inadequate response to House Financial Services Committee's (Committee) oversight requests. The Committee must ensure that the Consumer Bureau is fulfilling its statutory mandate to protect consumers.¹ In furtherance of that obligation, the Committee requested documents to determine whether the Consumer Bureau had (1) failed to obtain redress for harmed consumers where appropriate, (2) planned structural changes that weaken its ability to enforce fair lending laws, and (3) withdrawn a key provision from a rule issued to protect consumers from predatory payday lenders without adequate justification.² You asserted in your April 5, 2019 letter to Chairman Green and me that you "have a deep respect for the role that vigorous oversight from the Congress can play in promoting efficient, effective, and transparent government."³ The Consumer Bureau's continued stonewalling of this Committee by delaying the production of or withholding responsive documents belies that assertion.

February 7, 2019 Letter on Settlements

Committee staff worked diligently with Consumer Bureau staff to narrow what was already a very focused inquiry seeking documents on three settlements that did not require redress for consumers. On February 15, 2019, Committee staff further narrowed the scope of the request from three settlements to two – the Consumer Bureau's settlements with Sterling Jewelers Inc. (Sterling) and Enova International, Inc. (Enova). On March 5, 2019, the Consumer Bureau produced responsive documents and communications between the Consumer Bureau and outside counsel for Sterling and Enova.

The Committee also requested internal documents and communications related to restitution in the Sterling and Enova settlements. Consumer Bureau staff identified a set of responsive internal documents but initially refused to produce electronic copies of these documents. Instead, Consumer Bureau staff offered an *in camera* review of a smaller, Bureau staff-selected subset of the identified responsive documents. Committee staff reviewed the documents *in camera* on April 4, 2019, and immediately thereafter requested electronic copies of the same.

¹ 12 U.S.C. §5511.

² Letter from Chairwoman Maxine Waters to Director Kathy Kraninger (Feb. 7, 2019); Letter from Chairwoman Maxine Waters to Director Kathy Kraninger (Feb. 21, 2019); Letter from Chairwoman Maxine Waters to Director Kathy Kraninger (Apr. 5, 2019).

³ Letter from Director Kathy Kraninger to Chairwoman Maxine Waters (Apr. 5, 2019).

The Consumer Bureau ultimately produced these documents on May 6, 2019 – two months after the deadline for production.

Committee staff continued to narrow the scope of the February 7 letter. In Requests 1 and 3 of the letter, the Committee initially requested “[a]ll . . . communications referring or related to the issue of restitution”⁴ in the Sterling and Enova settlements. On May 14, 2019, Committee staff limited the scope of the communications in Requests 1 and 3 to correspondence related to restitution in the Sterling and Enova settlements from Eric Blankenstein, the political appointee overseeing the Consumer Bureau’s Division of Supervision, Enforcement & Fair Lending (SEFL), and his advisor. The production of all responsive emails from these two custodians is particularly important to the Committee because the Consumer Bureau has produced only a limited, Bureau staff-selected subset of responsive internal documents. Despite Committee staff’s modification of Requests 1 and 3, the Consumer Bureau’s response was to only provide Committee staff the opportunity to review these emails *in camera* on June 12, 2019. Based on Committee staff’s *in camera* review, these emails provide critical information on the dialogue between career staff and senior management on whether to provide restitution to consumers harmed by Sterling and Enova’s unlawful conduct. To date, the Consumer Bureau has refused to produce these emails. Thus, four months since the Committee requested documents on these settlements, the Consumer Bureau continues to withhold critical information.

February 21, 2019 Letter on the Reorganization of the Office of Fair Lending

Requests 1 through 6 of the Committee’s February 21, 2019 letter requested documents and communications from specific political appointees and senior managers regarding the reorganization of the Consumer Bureau’s Office of Fair Lending and Equal Opportunity (OFLEO). Before the initial production deadline, Committee staff modified these requests by limiting their scope to documents and communications made between November 25, 2017, and January 30, 2018. The Consumer Bureau produced one responsive email on March 21, 2019, the initial production deadline,⁵ with a cover letter informing the Committee that “all other documents responsive to requests 1 through 6 reflect Bureau confidentiality interests.”⁶ On May 6, 2019, the Consumer Bureau produced one additional email and an attached memo. The Consumer Bureau has continued to withhold responsive emails related to the decision to reorganize the OFLEO.

In Request 8 of the February 21 letter, the Committee initially requested “[a]ll documents and communications referring or related to a recommendation or decision made by the SEFL Policy Associate Director in a fair lending investigation or examination”⁷ In an effort to potentially narrow this request, Committee staff agreed to attend a May 13, 2019 briefing by the Consumer Bureau on the responsive fair lending investigations. On May 16, 2019, Committee staff reduced the number of fair lending investigations covered by the February 21, 2019 letter

⁴ Letter from Chairwoman Maxine Waters to Director Kathy Kraninger (Feb. 7, 2019).

⁵ On March 21, 2019, the Consumer Bureau also produced documents responsive to request 12 and “key documents regarding the reorganization that fall outside the timeframe of the initial decision, including documents related to the negotiations between the Bureau and NTEU and memoranda approving the implementation of the reorganization.” Letter from Director Kathy Kraninger to Chairwoman Maxine Waters (Mar. 21, 2019).

⁶ Letter from Director Kathy Kraninger to Chairwoman Maxine Waters (Mar. 21, 2019).

⁷ Letter from Chairwoman Maxine Waters to Director Kathy Kraninger (Feb. 21, 2019).

from twenty to six and limited email requests⁸ related to these six investigations to three individuals.⁹ Moreover, recognizing the sensitivity of ongoing enforcement actions, Committee staff selected six closed investigations. The Consumer Bureau produced internal memos on five of these investigations on June 5, 2019. Despite Committee staff's modifications, the Consumer Bureau has still not produced internal memos related to one of the closed investigations and responsive emails from Patrice Ficklin, Eric Blankenstein, and Redacted by the Committee

The Consumer Bureau's refusal to produce emails is particularly troubling. While Committee staff cannot determine the significance of documents that have yet to be produced, emails are a critical source of information in any congressional investigation or oversight matter.

April 5, 2019 Letter on the Consumer Bureau's Rescission of the Payday Rule

The Consumer Bureau produced by May 6, 2019, the initial production deadline, external communications requested by the Committee. The initial requests also sought a limited amount of internal communications and documents, and Committee staff has attempted to work with Consumer Bureau staff to further refine these requests. Requests 14 and 15 specifically sought drafts and final versions of memos related to the proposed payday rule circulated in the Director's briefing book or the current Deputy Director's briefing book. On May 10, 2019, Committee staff narrowed these requests to include only final versions of memos. Despite this accommodation, the Consumer Bureau has yet to produce all final versions of responsive memos. Especially concerning, the Consumer Bureau's production thus far has consisted primarily of informational memos from the Office of Legislative Affairs to Acting Director the attaching congressional correspondence, rather than substantive internal memos.

On May 10, 2019, Committee staff further narrowed the scope of Request 10 to emails and related briefing materials between Ron Borzekowski and the Director's Office or the political appointee overseeing rulemaking. The Committee had originally requested "all documents and communications"¹⁰ between Mr. Borzekowski and two additional individuals. To date, the Consumer Bureau has not produced a single email from Mr. Borzekowski. The Committee's letter also contained three additional requests (Requests 11-13) related to the Consumer Bureau's proposed payday rule. On June 3, 2019, Committee staff confirmed that the Consumer Bureau did not have to prioritize producing documents responsive to Requests 11-13.

No Justification Exists for the Consumer Bureau's Withholding of the Outstanding Responsive Documents

The Consumer Bureau has not challenged, because there is no legal basis for doing so, the legislative purpose of these requests. See *Eastland v. U.S. Servicemen's Fund*, 421 U.S. 491, 504 n.15 (1975); *McGrain v. Daugherty*, 273 U.S. 135, 177-78 (1927). This Committee and the U.S. House of Representatives recently passed H.R. 1500, the Consumers First Act, which specifically restores the supervisory and enforcement authorities of the Office of Fair Lending and Equal

⁸ Committee staff also requested memos, notes to file, or other documents authored by one of these individuals, Patrice Ficklin.

⁹ The Committee is also seeking "[a]ny memos, notes to file, or other documents," from one of these individuals, which have not been produced.

¹⁰ Letter from Chairwoman Maxine Waters to Director Kathy Kraninger (Apr. 5, 2019).

Opportunity and limits the number of political appointees – subjects specifically covered by the Committee’s requests.¹¹ Congress continues to engage in active consideration and debate related to these subjects.

Through staff, the Committee has engaged in lengthy negotiations with the Consumer Bureau and has significantly narrowed the scope of the Committee’s requests. Despite these efforts, the Consumer Bureau has continued to fail to satisfy the Committee’s narrowly targeted requests. Moreover, the Consumer Bureau has yet to produce whole categories of documents, particularly internal emails, critical to the Committee’s oversight interests.

I am enclosing with this letter copies of the three oversight letters at issue. I expect the Consumer Bureau to work with Committee staff to ensure the production of the following documents by the specified deadlines:¹²

February 7, 2019 Letter

By June 24, 2019

- All correspondence from Eric Blankenstein and [Redacted by the Committee] related to restitution concerning the Sterling and Enova settlements.

February 21, 2019 Letter

By July 8, 2019

- All documents and communications responsive to Requests 1 through 6 that have not been produced;
- Emails (including attachments) to and from Patrice Ficklin, Eric Blankenstein, and [Redacted by the Committee] regarding Matters 10, 12, 13, 16, and 17;
- Any memos, notes to file, or other documents authored by Patrice Ficklin regarding the decision not to pursue Matters 10, 12, 13, 16 and 17;
- The final settle or sue Enforcement Action Process (EAP) memo sent to the Director for Matter 7;
- Emails (including attachments) to and from Patrice Ficklin, Eric Blankenstein, and [Redacted by the Committee] regarding the ECOA claim in Matter 7;
- Any memos, notes to file, or other documents authored by Patrice Ficklin regarding the decision not to pursue the ECOA claim in Matter 7;
- All documents and communications related to the April 2018 presentation regarding Matters 9 through 16; and
- Any opinion or analysis received from the Department of Justice regarding disparate impact theory provided to the Division of Supervision, Enforcement & Fair Lending (SEFL) Policy Associate Director.

¹¹ <https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=403801>

¹² The Committee at this time is not seeking documents responsive to those requests it has not explicitly stated it wanted the Consumer Bureau to prioritize.

April 5, 2019 Letter

By July 26, 2019

- Documents responsive to Request 10 (specifically communications to and from Rob Borzekowski and the Office of the Director and Tom Pahl)
- All final versions of documents responsive to Requests 14 through 15.

If the Consumer Bureau fails to meet these deadlines, absent an agreed-upon extension, I will consider the use of compulsory process, including for the testimony of Consumer Bureau employees.

Sincerely,



MAXINE WATERS
CHAIRWOMAN

cc: The Honorable Al Green, Chairman, Subcommittee on Oversight and Investigation
The Honorable Patrick McHenry, Ranking Member

Enclosures

APPENDIX G



Consumer Financial Protection Bureau

1700 G Street NW, Washington, DC 20552

Very good sty!
PC

July 26, 2017

Recommendation Memorandum for the Director

FROM [Redacted by the Committee], Tony Alexis,
Office of Enforcement

SUBJECT Authority to Settle with Enova International, Inc. and to File Suit
– ENF Matter No. 2015-1636-02; Exam ID: 1961

Recommendation

We recommend that you authorize us: (1) to settle with online payday lender Enova International, Inc. (“Enova”), under the parameters described in Section IV below and the attached Term Sheet; and (2) if settlement negotiations are unsuccessful, to commence an enforcement action, either administratively or in federal court, consistent with the attached complaint.

I. Overview

a. The Company.

Enova International, Inc. (“Enova”) is an online lender that markets loans throughout the United States, United Kingdom, Australia, Canada, Brazil and China.¹ It is based in Chicago, Illinois. Enova’s business focuses on unsecured payday installment loans, line-of-credit loans, and short-term payday loans. In the United States, Enova

¹ Enova was a wholly-owned subsidiary of Cash America International, Inc. (“Cash America”), a publicly-traded financial services company that offers payday loans through retail stores. In November 20, 2013, the Bureau entered into a Consent Order with Cash America for various violations related to exam misconduct. These violations included unlawful conduct by Enova for failing to preserve materials responsive to the Bureau’s information requests, failing to provide examiners with requested information, and directing employees to mislead examiners. On November 13, 2014, Enova spun off from Cash America, and is now an independent, publicly-traded company.

offers online payday loans, payday installment loans, and lines of credit under the brand names CashNet USA and NetCredit America.

b. Exam Summary.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

c. Enforcement Investigation Summary.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

II. Factual Background

A. Enova's Unauthorized Debits.

Some consumers apply for payday and payday installment loans through a lead generator. The lead generator collects all the relevant application information, such as a consumer's name, address, social security number, and bank account information, and sends the loan request and application information to a network of lenders. The application is then sold to whichever lender offers the consumer a loan. Generally, consumers do not know which lenders will receive their application, and in some instances, may not even be aware at all that their loan application has been sold.⁴

Since 2008, Enova has used lead generators to find potential customers. Its stated policy is to deny a consumer's application if, after purchasing it from a lead

⁴ See *CFPB v. D and D Marketing, Inc.*, Case No. 2:15-cv-9692 (C.D. Ca.).

generator, Enova determines that the consumer already has an outstanding loan or line of credit with the company. But, in 2010, Enova began using the information obtained from lead generators to update consumers' existing loan files with any new or different information. For example, if an existing consumer with an outstanding loan applied for a new loan through a lead generator, Enova would deny the lead generator loan application, but overwrite the consumer's existing loan file with any new bank account information, and begin debiting payments for the outstanding loan from that new account. Enova did not inform consumers that it was debiting their new bank accounts, nor did Enova obtain authorization from consumers prior to doing so.

Enova represents that this issue arose as a result of a coding error which caused existing loan information to be overwritten. Enova fixed the coding error in June 2014, but admits that the new code only applied to the receipt of new applications. It did not correct the information it received and updated prior to this time, and in some instances, Enova continued to debit payments from some consumers' new bank accounts for nearly two years after it purported to have discovered the problem..

Enova overwrote bank account information for 6,829 consumers with outstanding loans using information obtained from lead generator loan applications. Enova then initiated close to 24,000 debit transactions representing over \$5 million in payments from these consumers' bank accounts. Enova was successful in extracting \$2,638,933 in payments from consumers' accounts in 13,688 transactions. The remainder of Enova's debit attempts was unsuccessful, and Enova states that the transactions were most likely returned due to insufficient funds or account closure.

Enova's debit attempts, whether or not successful, harmed consumers. Enova initiated these debits without consumers' authorization, resulting in unlawful debits, as well as consequential damages, such as NSF fees and other bank charges. Enova subsequently obtained authorization from a small fraction of these debit transactions to debit their updated bank accounts.⁵ However, for nearly 20,000 of the 24,000 debit transactions initiated by Enova, Enova acknowledges that it did not obtain subsequent authorizations. Further, some of those subsequent authorizations may have been obtained through deceptive means. As described in further detail below, the authorizations Enova obtained from consumers over the telephone failed to explain Enova's initial unauthorized debiting or the source of the consumers' updated bank account information. Based on our review of the telephone scripts and call recordings, we believe it is unlikely that consumers understood that they were providing

⁵ Enova obtained 270 authorizations from consumers online, 2,683 authorizations from consumers over the phone, and 949 authorizations from consumers in writing, totaling 3,902 authorizations.

authorization for Enova to debit the bank account Enova learned about through a lead generator.

After Enova self-disclosed this issue to the Bureau's exam team, it communicated with consumers about the overwritten bank account information, and offered consumers an opportunity to submit claims for damages associated with the unauthorized debits. Consumers made claims to Enova for over \$34,312 in NSF fees and late charges as a result of Enova's debits and debit attempts. However, the amount of harm suffered by consumers associated with these bank charges is likely much higher. Enova did not notify consumers that it had debited incorrect accounts without authorization until, in some instances, four years after the problem originated, and then only provided an opportunity for remediation through a claims process. It is unlikely that consumers recalled the transactions or retained the bank records necessary to make a substantiated claim for reimbursement, as required by Enova. Consumers made claims to Enova for NSF fees and late charges for only 1,700 of the over 24,000 unauthorized debit transactions or debit attempts, and of those claims, only a very small fraction met Enova's substantiation requirements. In fact, out of the \$34,312 in claims submitted by consumers, Enova has reimbursed only five consumers a total of \$654 for NSF fees and late charges.⁶

B. "Flash Cash" Extension Issue.

Enova offers certain consumers a same-day expedited funding option called "Flash Cash." Flash Cash is available only to consumers who have previously repaid two or more Enova loans, and who also have a debit card on file with Enova from a bank within an accepted network. In some instances, consumers who did not have a debit card on file from a participating bank applied for a loan, and requested Flash Cash funding. In those instances, Enova denied Flash Cash funding, but did fund the loan the following day within the normal time-frame.

Enova self-disclosed to the Bureau's exam team that from May 2013 until May 2014, Enova's computer systems erroneously coded loans to consumers who had been denied Flash Cash as "returned" and reflected a \$0 balance associated with the Flash Cash loan application. Enova then created a new, separate record associated with the loan that it funded within the normal next-day time frame. This created a problem when these consumers later requested and received a loan extension from Enova. Instead of processing the extension for the loan file associated with the actual funded loan, Enova processed the extension for the loan file with the \$0 balance. As a result, the consumer's bank account was debited for the full monthly loan payment instead of a \$20 extension

⁶ Enova provided actual refunds totaling \$170 to three consumers. The remaining two consumers received a credit on their outstanding loans.

fee. In some instances, consumers incurred overdraft and NSF fees as a result of these failed extensions.

Consumers first called Enova about dishonoring its extensions in September 2013. In November 2013, Enova identified a coding error as the source of the problem. It implemented a coding fix in January 2014. However, ten days later, the fix failed, and was manually disabled. Enova did not run daily checks to ensure the Flash Cash extension issue was permanently resolved, and did not catch that the fix had been disabled until May 2014. Only then did Enova re-enable the fix.

Enova did not inform consumers that it had deducted the full payment amount, instead of the extension fee, until April 2015. The issue impacted 333 consumers. Prior to this time, Enova processed refunds and credits to consumers who affirmatively called the company to complain about the issue. On April 14, 2015, Enova sent impacted consumers an email notifying them of the issue, and providing them an opportunity to seek reimbursement. Of the 333 impacted consumers, 75 consumers made claims to Enova regarding fees incurred as a result of the Flash Cash issue. Enova provided either loan credits or refunds to these consumers in an amount equal to \$5,794. This number may under-represent the number of consumers actually affected by the Flash Cash Issue. In some instances, consumers did not receive Enova's notice about the issue until more than a year had passed since the improper deduction of the full payment amount instead of the \$20 fee. Some consumers may not have remembered whether they had incurred additional charges such as NSF or overdraft fees as a result of Enova's error.

C. Duplicate Debit Issue.

During the exam, Enova disclosed to the Bureau's exam team that there were two instances in early 2014 where Enova erroneously debited numerous consumers' accounts twice for the same monthly payment. In January 2014, the error occurred due to a system failure that resulted in Enova initiating an ACH debit request to some consumers' accounts before a previous request had cleared. In other words, Enova debited some consumers' accounts, and before those debits cleared, initiated a second debit for the same monthly payment. Enova discovered the error almost immediately, and reversed the debits the same day. It is unlikely that consumers suffered any harm as a result of the January 2014 error because the transactions were reversed the same day before the debit transactions cleared consumers' accounts.

In February 2014, a second, similar error occurred when Enova failed to appropriately reconcile payments made by consumers prior to their due date. Notwithstanding the early payment, Enova still debited consumers' accounts by ACH on the due date, causing consumers to be charged twice for that month. Enova discovered the error promptly and immediately reversed the ACH debit requests. However, because the error occurred on a Friday, consumers did not receive the refunds until Monday,

depriving them of the use of those funds over the weekend and resulting in NSF fees and overdraft charges for some consumers. In all, 78 consumers were improperly debited a total of \$15,744.46, and Enova reimbursed four consumers who made claims for NSF fees or overdraft charges.

D. ACH Authorization Contract Language.

Some of Enova's consumer contracts do not comply with EFTA and Regulation E requirements for preauthorized EFT (PEFT) authorizations. Pursuant to Section 1005.10(d)(1) of Regulation E, financial institutions and payees must provide consumers with a notice of when PEFTs will vary in amount from the previous transfer under the same authorization. There is an exception to this requirement in section 1005.10(d)(2), under which financial institutions and payees can give consumers the option of receiving notice only when the PEFT falls outside a specified range. It appears that Enova intended to use this exception, but our investigation found that many of Enova's contracts do not define terms necessary to determine the parameters of the range, including the "returned payment charges" or "late charges" that Enova may debit and that are included in the range stated in the authorization. The Commentary to section 10(d)(2) states that an entity must provide an acceptable range that could be anticipated by the consumer when providing an opt-out option. Here, by using terms in the opt-out range that are undefined, consumers cannot reasonably anticipate what their payment amounts would be should they opt out of the notice requirements of section 10(d)(1).⁷

Based on our review of a sample of Enova's contracts, this violative language appears in many installment loan contracts used in a variety of states under Enova's NetCredit and Cashnet USA brands.⁸ Enova uses or has used many different iterations of installment contracts throughout the United States for these brands since 2011 and it is likely that the contract language at issue appears in many more contracts. Based on our review of the sampled data, we concluded that over 8,400 consumers executed contracts in eight different states with this problematic language. Enforcement is not

⁷ Enova disclosed in an investigational hearing that a state regulatory authority had previously brought this contract language to Enova's attention and that it was working to remediate the language in future contracts, but had not done so at the time of the hearing.

⁸ This language is found in NetCredit Installment Loan Agreements used in Alabama, California, Delaware, Georgia, Idaho, Missouri, North Dakota, New Mexico, South Carolina, South Dakota, Utah, Virginia and Wisconsin. This language also appears in CashnetUSA installment contracts used in California, Delaware, Missouri, New Mexico, South Carolina, South Dakota, and Wisconsin. The Bureau is only pursuing claims for those installment loan contracts that fail to define terms.

pursuing claims for Enova's line of credit contracts that contain similar language and terms due to the fact that lines of credit customers receive period billing statements that may satisfy the notice requirements of 10(d)(1).

III. Legal Analysis

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

IV. Recommendation to Settle or Sue

A. Summary

As detailed below, we seek authority to negotiate a consent order that would include (1) injunctive relief; (2) restitution; and (3) civil money penalties.

B. Discussion

1. Injunctive Relief

We propose seeking injunctive relief prohibiting Enova from violating the Bureau’s prohibition against the commission of unfair and deceptive acts in the future, as well as certain specific injunctive relief regarding Enova’s processes for prioritizing coding error fixes, enjoining it from collecting any further payments from consumers’ bank accounts without authorization, requiring it to retain an independent consultant to review all telephone authorizations for validity, requiring it to amend any contract language that violates Regulation E, and for any existing contract that violates Regulation E, requiring Enova to notify consumers of the amount of any new transfer that will vary from the amount of the previous transfer or from the preauthorized amount before initiating the new transfer.

²² Check City; FAMI Tosh, Inc.; QC Holdings.

2. Monetary Relief

(a) Redress

i. Unauthorized Debits Issue.

We propose seeking restitution on behalf of consumers from whom Enova successfully debited payments from the new bank account, and from whom Enova did not obtain a valid updated authorization, an amount equal to approximately \$2.16 million, plus an additional amount for each consumer affected by Enova's unauthorized debiting, as a proxy amount for the consumer's loss.²³

ii. Flash Cash Extension Issue.

Enova's error affected 333 consumers. We propose seeking restitution on behalf of each consumer in an amount equal to the average NSF and late fees experienced by consumers related to the Flash Cash Issue (e.g. consumers experienced on average \$95 in fees associated with the transaction). This amount would be offset by those consumers already refunded or credited by Enova for these fees. We expect that this methodology will result in Enova paying additional restitution of approximately \$24,600.

iii. Duplicate Debit Issue.

We propose seeking damages on behalf of each consumer in an amount equal to the average NSF and late fees experienced by consumers. (e.g. \$80). This amount would be offset for any consumers already refunded or credited by Enova for these fees. We expect that this methodology will result in Enova paying additional restitution of approximately \$6,240.

iv. EFTA Violation.

It is not feasible to accurately calculate restitution for Enova's Regulation E violation because it would require the Bureau to undertake an analysis of millions of contracts, review the payment histories for each contract, and interview each consumer who executed the contract. As an alternative, we propose using the EFTA civil liability provisions as a proxy for administrative enforcement of this violation. The civil liability provisions of EFTA allow for a range of damages between \$100 to \$1,000.²⁴ Factors

²³ We are only seeking restitution for those consumers whose bank accounts were unlawfully debited post-transfer date. This restitution would not affect the validity of the underlying loan.

²⁴ 15 U.S.C. § 1693m(a)(2)(A).

considered for civil liability under EFTA include (1) the frequency and persistence of noncompliance, (2) the nature of such noncompliance, and (3) the extent to which the noncompliance was intentional.²⁵

Based on the sample data provided, Enova executed contracts which contained opt-out range provision language with undefined terms with 8,417 consumers in eight different states. We propose asking Enova to retain an independent consultant to identify the remaining number of contracts executed with this type of language, and imposing a penalty of \$100 for each contract identified. At a minimum, the penalty would be \$841,700. This figure is included in the civil penalty recommendation of \$1-3 million below.

(b) Civil Money Penalties

The CFPB provides for three tiers of penalties, escalating based on the degree of intent behind the conduct. 12 U.S.C. § 5565(c). In this matter, we believe Enova's conduct warrants a penalty at the Second tier level for recklessly violating Federal consumer financial law, and potentially even the Third tier level for knowingly violating Federal consumer financial law related to its unauthorized debiting of consumers' accounts. At the Second tier level, the penalty for Enova's conduct would amount to \$28 million. However, based on our analysis below, we recommend reducing that amount to a range of \$1 million to \$3 million based on the statutory factors set forth in 12 U.S.C. § 5565(c)(3), keeping in account the policy goals of specific and general deterrence, and incorporating the elements of responsible business conduct where applicable, *see* CFPB Bulletin 2013-06 (June 25, 2013) (Responsible Business Conduct).

When considering the statutory factors required by 12 U.S.C. § 5565(c)(3), particularly relevant to this matter were the (1) severity of the risks or losses to consumers, (2) the size of Enova's financial resources, and (3) such other matters as justice may require.²⁶ First, the "Flash Cash" and "Double Debit" issues impacted a small number of consumers relative to the total number of loans Enova makes on an annual basis, and the damages associated with these claims are less than \$100 on average for each consumer. Additionally, while the unauthorized debiting issue impacted a larger number of consumers over a longer period of time, it is not disputed that the affected consumers did in fact owe a debt to Enova, and Enova's debiting may have mitigated the severity of net losses to consumers over the lifecycle of their loan. Second, while Enova is one of the largest and most profitable online lenders in the industry, it is unlikely that it could withstand a \$28 million penalty without significant

²⁵ 15 U.S.C. § 1693m(b)(1).

²⁶ 12 U.S.C. § 5562(c)(3)(A), (C), and (E).

impact on its operations and offerings to consumers. Third, we believe the amount of restitution sought in this matter – approximately \$2 million – warrants consideration as a mitigating factor under subparagraph (E) of section 5565(c)(3) and the total penalty amount should relatively reflect the restitution sought in this matter.

Also relevant to our penalty analysis is Enova’s recidivism. Enova was the subject of a 2013 consent order that resulted from misrepresentations it made to the Bureau exam staff and its efforts to conceal information from Bureau exam staff during an exam. Similarly, we believe that Enova has misrepresented when it became aware of its unauthorized debiting to Bureau exam and enforcement staff. This recidivism in making misrepresentations to the Bureau plays an important factor in our penalty recommendation.

We also considered Enova’s responsible business conduct. While Enova did self-disclose its unauthorized debiting to the Bureau’s exam team, it misrepresented when it became aware of the issue on multiple occasions to both Supervision and Enforcement teams. While self-disclosure may in some instances constitute responsible business conduct meriting consideration in an Enforcement action, any credit that could be given in this particular instance is negated by Enova’s misleading statements to Bureau personnel.

We believe imposing a penalty in the \$1 million to \$3 million range is appropriate, properly incorporates the required statutory facts, including consideration of responsible conduct, and will also serve to accomplish the goals of specific deterrence and general deterrence. Based on the severity of the conduct, the size of the institution, and its history of recidivism, a penalty in this range will be recognized by the institution and the market as conveying a meaningful message.

V. Assessment of Risks of the Recommended Approach

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



VI. Conclusion

We recommend that you authorize us to settle this matter under the parameters described in Section IV and the attached Term Sheet. If settlement negotiations are unsuccessful, we recommend that you authorize us to file suit.

Attachment(s)

Tab 1: Draft Decision Memorandum from the Director

Tab 2: Proposed Term Sheet.

Tab 3: Draft Complaint.

Tab 4: Enova's NORA Response.



1700 G Street NW, Washington, DC 20552

Decision Memorandum from the Director

FROM Richard Cordray, Director

TO Tony Alexis, Assistant Director for Enforcement

SUBJECT Authority to Settle with Enova International, Inc. and to File Suit
– ENF Matter No. 2015-1636-02; Exam ID: 1961

I authorize the Office of Enforcement to enter into a settlement with and file a lawsuit against Enova International, Inc. under the parameters recommended by the Office of Enforcement on July 26, 2017.

Richard Cordray
Director
Consumer Financial Protection Bureau

Date

TERM SHEET
(Summary of Proposed Settlement Parameters)

As detailed in the foregoing memorandum, Enforcement seeks authority to negotiate a settlement with Enova International, Inc. (Enova) in this matter within the following parameters:

A. Core terms

1. Civil money penalties in a range of \$1 million to \$3 million;
2. Damages of at least \$2.1 million, consistent with the framework set forth in the foregoing memorandum; and
3. Injunctive relief as follows:
 - a. Prohibiting Enova from violating the Bureau's prohibition against the commission of unfair and deceptive acts;
 - b. Requiring Enova to retain an independent consultant to review and revise its processes for prioritizing and resolving software coding errors;
 - c. Enjoining Enova from collecting any further payments from consumers' bank accounts without authorization;
 - d. Requiring Enova to retain an independent consultant to review all ACH payment plan telephone authorizations associated with its unauthorized debiting for validity, and to the extent any of the authorization are invalid, requiring Enova to refund each of those consumers the total amount debited, plus some punitive amount;
 - e. Requiring Enova to amend any contract language that violates Regulation E; and
 - f. For outstanding contracts with language that violates Regulation E, requiring Enova to notify consumers of the amount of any new transfer that will vary from the amount of the previous transfer or from the preauthorized amount before initiating the new transfer.

**IN THE UNITED STATES DISTRICT COURT
FOR THE _____**

Consumer Financial Protection Bureau,
Plaintiff,
v.
Enova International, Inc.
Defendant.

Case No. _____

COMPLAINT FOR INJUNCTIVE AND OTHER EQUITABLE RELIEF

The Consumer Financial Protection Bureau (the “Bureau” or “Plaintiff”) brings this action against Enova International, Inc. (“Enova” or “Defendant”) under: (1) Sections 1054 and 1055 of the Consumer Financial Protection Act of 2010 (“CFPA”), 12 U.S.C. §§ 5564 and 5565 to obtain permanent injunctive relief, civil money penalties, damages, and other relief as set forth below.

Jurisdiction and Venue

1. This Court has subject-matter jurisdiction over this action because it is brought under Federal consumer financial law, 12 U.S.C. § 5565(a)(1); presents a federal question, 28 U.S.C. § 1331; and is brought by an agency of the United States, 28 U.S.C. § 1345.

2. Venue is proper pursuant to 28 U.S.C. § 1391(b) and 12 U.S.C. § 5564(f) because Enova does business in this District and the events giving rise to this Complaint substantially took place in this District.

3. Enova’s headquarters, collections, and support teams are located in Chicago, Illinois. Additional support teams are located in Gurnee, Illinois. Enova makes and receives calls to and from consumers regarding its loan products and applications out of both of these locations.

Parties

4. The Bureau is an independent agency of the United States charged with regulating the offering and provision of consumer financial products or services under Federal consumer financial laws. 12 U.S.C. § 5491(a). The Bureau also enforces the Electronic Funds Transfer Act (EFTA) pursuant to its authority under EFTA and subtitle E of the CFPA. 15 U.S.C. § 16930(a)(5).

5. The Bureau has independent litigating authority to enforce Federal consumer financial laws. 12 U.S.C. §§ 5481(14), 5564(a) and (b).

6. Enova is a corporation which maintains its principal place of business in Chicago, Illinois. At all times relevant to this complaint, Enova has done business in this District and throughout the United States.

7. Enova is a covered person subject to the Bureau's authority because it offers or provides consumer financial products or services as defined by the CFPA. First, Enova extends credit and services loans offered or provided for use by consumers primarily for personal, family, or household purposes. 12 U.S.C. § 5481(15)(A)(i). Second, Enova collects debt related to the loans it extends. 12 U.S.C. § 5481(15)(A)(x). Third, Enova is a "person" as that term is defined in section 1005.2(j) of Regulation E, implementing the Electronic Funds Transfer Act. 12 C.F.R. § 1005.2(j).

Factual Background

8. Enova is a publicly-traded, online lender that markets and makes loans throughout the United States, the United Kingdom, Australia, Canada, Brazil, and China.

9. Enova is one of the largest and most profitable online lenders in the world. In 2016, it reported a gross profit margin of 56% and net income of \$34.6 million.

10. Enova extends unsecured payday and payday installment loans to individual consumers for personal, family, or household purposes in every state in the United States.

11. Typically, Enova deposits the loan proceeds as a lump sum into borrowers' bank accounts. Under the terms of Enova's payday loan agreements, consumers must repay the loan in full on their next payday, plus interest and loan fees, unless a loan extension is granted. Enova's installment loan product allows consumers to pay back the loan in regular installments, along with interest and loan fees.

12. In the United States, Enova offers online payday and installment loans under the brand names Cashnet USA and NetCredit America.

Unauthorized Debiting of Consumers Accounts

13. Some consumers apply for payday or installment loans through a lead generator.

14. A lead generator collects relevant application or underwriting information from the consumer, such as name, address, social security number, and bank routing and account numbers and makes this information available to a network of lenders. Any lender may then purchase that information and extend the consumer a loan offer.

15. Generally, consumers do not know which lender will receive and purchase their application. In some instances, consumers may not even be aware that their loan application has been sold.

16. Since 2008, Enova has used lead generators as a source for potential new customers.

17. It has been Enova's policy to extend only one loan at a time to any consumer. Therefore, if Enova purchased a lead generator loan application and subsequently learned that the consumer had an outstanding loan with Enova, it would deny the application.

18. In 2010, Enova began overwriting consumers' existing loan files with any new, different, or additional information contained in the leads it purchased from lead generators.

19. For example, if an existing customer with an outstanding loan applied for a new loan through a lead generator, and Enova purchased the lead, Enova would deny the lead generator loan application, but overwrite the consumer's existing loan file with any new bank account information obtained from the lead generator, and begin debiting payments for the outstanding loan from that new account.

20. Enova did not inform consumers that it was debiting their new bank account, nor did Enova obtain authorization from consumers prior to doing so.

21. Enova updated the bank account information of 6,829 consumers using data obtained from lead generator loan applications.

22. Enova then initiated approximately 24,000 debits from consumers' new accounts, and attempted to debit over \$5 million dollars in payments without consumers' authorization. Enova successfully debited approximately \$2.16 million from consumers without authorization.

23. Enova contends that its other attempts to debit consumers' bank accounts without authorization were unsuccessful because some consumers did not have adequate funds to cover the payment or they had closed the account.

24. In some instances where consumers did not have adequate funds to cover the payment, consumers incurred NSF or overdraft charges because they did not anticipate Enova debiting that particular account or had designated funds in that account for other bills or obligations.

25. Enova claims that it obtained subsequent authorizations from some consumers to debit their new bank account. However, those authorizations represent only a small fraction of Enova's attempted debits. For nearly 20,000 debit attempts, Enova failed to get any consumer authorizations at all.

26. Enova became aware that it was debiting consumers' bank accounts without authorization in 2010, but continued doing so until June 2014 and failed to notify consumers of the issue until late October 2014.

27. When it did notify consumers, Enova described its actions as follows: “While conducting a standard review of our accounts, it has come to our attention that there may have been an error involving certain debits from your bank account in conjunction with your loan . . . Our records indicate that your bank account on file was likely updated based upon information you provided in a subsequent application while your loan was outstanding and we may have debited the updated account in error.”

28. Enova’s written correspondence failed to inform consumers that the source of the new bank account information was an application made to a lead generator, not Enova.

29. Enova’s written correspondence also implies, incorrectly, that Enova did not know whether or not it debited a bank account without authorization.

30. Additionally, Enova’s communication to consumers implied that if their account was improperly debited, they were only entitled to reimbursement of bank fees, and had no right to dispute the underlying debits.

31. A consumer acting reasonably under the circumstances could interpret Enova’s actions and communications to mean:

- (1) Information supplied to Enova – not a lead generator – was involved;
- (2) Enova was not sure if it did or did not improperly debit the consumer’s account;
- (3) Enova lawfully debited the consumer’s new bank account; and
- (4) Consumers were only entitled to reimbursement of any fees that may have resulted from the debit.

32. These representations were material as a consumer could be discouraged from disputing the illegal withdrawals if they believed they were in fact lawful, or they were only entitled to the reimbursement of fees.

33. Enova’s telephone scripts and conversations with consumers reinforced these misleading representations. In calls with consumers impacted by Enova’s

unauthorized debiting, Enova representatives would merely confirm the last four digits of the updated bank account and confirm that the consumer would like payments debited from that account.

34. The representatives never revealed that the bank account information had been obtained from a lead generator source or that Enova did not have authorization to debit the account in previous transactions. Representatives presented the account information to consumers without indicating that it had been initially improperly used.

35. Enova first notified consumers of its unlawful debiting four years after the problem originated. And although Enova then provided consumers an opportunity for remediation through a claims process; it also erected significant barriers to obtaining redress.

36. For example, Enova required consumers to submit detailed documentation about the debits and the fees they incurred, even though these events may have occurred several years earlier. To date, 1,700 consumers have claimed that they incurred over 34,000 in NSF and other bank fees as a result of Enova's unauthorized debits and debit attempts. Enova has reimbursed five of these consumers a total of \$654.

Flash Cash

37. Enova offers certain consumers a same-day expedited funding option called "Flash Cash."

38. Flash Cash is available only to consumers who have previously repaid two or more Enova loans, and who also have a debit card on file with Enova from a bank within an accepted network.

39. In some instances, consumers who did not have a debit card on file from a participating bank applied for a loan, and requested Flash Cash funding.

40. In those instances, Enova denied Flash Cash funding, but did fund the loan the following day within the normal funding time-frame.

41. Enova's computer systems erroneously coded loans to consumers who had been denied Flash Cash as "returned" and reflected a \$0 balance associated with the Flash Cash loan application.

42. Enova then created a new, separate record associated with the loan that it funded within the normal next-day time frame.

43. This created a problem when these consumers later requested and received a loan extension from Enova.

44. Instead of processing the extension for the loan file associated with the actual funded loan, Enova processed the extension for the loan file with the \$0 balance.

45. As a result, the consumer's bank account was debited for the full monthly loan payment, instead of a \$20 extension fee.

46. In some instances, consumers incurred overdraft and NSF fees, as a result of these failed extensions.

47. In September 2013, consumers began calling Enova to complain about the dishonored extensions.

48. Two months later in November 2013, Enova identified a coding error as the source of the problem. Enova took another two months to correct the coding error.

49. Ten days later, due to additional software problems, Enova disabled the corrective code, causing the error to recur.

50. Enova did not run daily checks to ensure that it had resolved the Flash Cash extension issues. As a result, Enova failed to detect that it disabled the corrective code and the error persisted until May 2014. In May 2014, Enova again corrected the error.

51. Enova's Flash Cash coding error caused it to overcharge 333 consumers.

52. Enova did not inform consumers that it had erroneously deducted the full payment amount, instead of the extension fee, until April 2015 – approximately

eighteen months after learning of the issue and more than a year after correcting the error.

Enova's Double Debiting

53. In two instances in 2014, Enova erroneously debited numerous consumers' accounts twice for the same monthly payment.

54. In January 2014, Enova erroneously initiated an ACH debit request to some consumers' accounts before a previous request had cleared.

55. In other words, Enova debited some consumers' accounts, and before those debits cleared, initiated a second debit for the same monthly payment.

56. Enova discovered the error almost immediately, and reversed the debits the same day.

57. In February 2014, Enova again erroneously debited numerous consumers' accounts twice for the same monthly payment. This error was caused by Enova's failure to appropriately reconcile payments made by certain consumers prior to their due date.

58. Notwithstanding the consumers' early payments, Enova still debited their account by ACH on their due dates. Enova thus double-charged consumers for the relevant month.

59. In all, Enova charged 78 consumers twice, and thus overdebited consumers' account in an amount equal to \$15,744.46

60. Enova discovered the error and reversed the ACH debit requests.

61. However, because the error occurred on a Friday, consumers did not receive the refunds until Monday, and thus were deprived of the use of those funds over the weekend. Some consumers incurred NSF fees and overdraft charges as a result of Enova's double ACH debit requests.

ACH Authorization Contract Language

62. Regulation E implements the Electronic Funds Transfer Act (EFTA)..

63. With respect to preauthorized transfers, such as monthly loan debits by ACH, section 1005.10(d)(1) of Regulation E provides that financial institutions or payees (such as Enova) must provide consumers with a notice of transfers varying in amount. Under the range exception in section 1005.10(d)(2), the financial institution or payee may give consumers the option of receiving notice only when a transfer falls outside a specified range or amounts or only when a transfer differs from the most recent transfer by more than an agreed-upon amount specified by contract.

64. Some of Enova's consumer contracts do not comply with this requirement of Regulation E.

65. Pursuant to Section 1005.10(d)(2), Enova must adequately define the range of charges that a consumer could reasonably expect to be charged in connection with preauthorized ACH debits.

66. The Commentary to this section provides that the payee "must provide an acceptable range that could be anticipated by the consumer. For example, if the transfer is for payment of a gas bill, an appropriate range might be based on the highest bill in winter and the lowest bill in summer." Commentary to Regulation E, Section 1005.10(d)(2) -1(1996)

67. A number of Enova's contract fail to adequately define the range of charges that a consumer could reasonable expect to be charged in connection with ACH debits.

68. Some of these NetCredit contracts provide that Enova can debit either (1) the minimum amount specified in the Payment Schedule set forth in the consumer's contract, or (2) an amount equal to the total outstanding balance on the consumer's loan, plus "returned payment charges" and "late charges" – which are undefined.

69. But, many of its NetCredit contracts do not define the “returned payment charges” or “late charges” that Enova states in its contracts it may debit as a part of consumers’ monthly payment debits.

70. A consumer could not reasonably anticipate what the upper limit of the range that Enova might debit from his or her account without those terms being defined in the contract.

71. The following language appears in certain of Enova’s consumer contracts:

Authorization for Repayment by ACH – Range of Varying Amounts. Please note that you have the right to receive notice of all transfers varying in amount, and that by signing this ACH Authorization you acknowledge that we have elected to offer you a specified range of amounts for debiting (in lieu of providing the notice of transfers in varying amounts). The amount of any ACH debit will range from (i) the payment amount provided in the Payment Schedule (which may be less than a scheduled payment if partial prepayments have been made), to (ii) an amount equal to the total outstanding balance (which may be greater than or less than a payment based upon your actual payments), plus as applicable, any returned payment charges and/or any late charges you may owe under the Agreement. For any debit outside of this specified range, we will send you a notice. Therefore, by agreeing to the terms of this ACH Authorization you are choosing to only receive notice when a transfer amount exceeds the range specified above.

72. By failing to define key terms, Enova’s contracts make consumers’ monthly payments in practice unknowable.

VIOLATIONS OF THE CONSUMER FINANCIAL PROTECTION ACT

Unfair, Deceptive, or Abusive Acts of Practices

73. Sections 1031 and 1036 of the CFPA, 12 U.S.C. §§ 5531(a) and 5536(a)(1) prohibit a “covered person” or “service provider” from engaging in “any unfair, deceptive or abusive act or practice.” 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

74. An act or practice is unfair if it causes or is likely to cause substantial injury to consumers, which is not reasonably avoidable by consumers, and such substantial injury is not outweighed by countervailing benefits to consumers or competition. 12 U.S.C. § 5531(c).

75. An act or practice is deceptive if the act or practice misleads or is likely to mislead a consumer, the consumer's interpretation is reasonable under the circumstances and the misleading act or practice is material.

76. Section 1054(a) of the CFPB grants the Bureau authority to commence a civil action against any person who violates a federal consumer financial law. 12 U.S.C. § 5554(a). The CFPB is a federal consumer financial law. 12 U.S.C. § 5481(14).

Count I

Enova's Act of Debiting Consumers' Bank Accounts Without Authorization Was Unfair.

77. The Bureau incorporates by reference the allegations contained in paragraphs 1 through [REDACTED], herein by reference.

78. Enova debited or attempted to debit consumers' bank accounts nearly 20,000 times for payments totaling of \$5 million without their authorization.

79. Enova caused or was likely to cause substantial injury to consumers because it successfully withdrew \$2,1583.36 in funds from consumers' bank accounts without their authorization. Enova's actions also caused consumers to incur NSF fees and overdraft charges, even where it was unsuccessful in withdrawing funds from their accounts.

80. Consumers could not reasonably avoid these injurious NSF fees and overdraft charges. When applying for a loan with a lead generator, consumers could not know that their application would be eventually be purchased by Enova, nor could they predict that Enova would debit their bank accounts without their authorization.

81. Enova did not notify consumers or otherwise disclose to them that it would use the bank account information they supplied to a lead generator to debit payments on an unrelated loan.

82. The injury consumers suffered was not outweighed by countervailing benefits to consumers or to competition. There is no discernable cost-savings passed on to consumers by Enova debiting their accounts without authorization.

83. By and through the acts and practices described in paragraphs 1 through [REDACTED] above, Enova's acts and practices therefore, constitute unfair acts or practices in violation of the CFPA, 12 U.S.C. §§ 5531(a) and (c)(1), and 5536(a)(1)(B).

Count II

Enova's Representations to Consumers Regarding its Unauthorized Debiting of Their Bank Accounts Were Deceptive.

84. The Bureau incorporates by reference the allegations in paragraphs 1 through [REDACTED], herein by reference.

85. In numerous instances, in connection with offering, providing, and collecting on payday and installment loans, Enova represented to consumers directly or indirectly, expressly or by implication, that:

- (a) Enova was legally authorized to debit a consumer's new bank account;
- (b) the source of the new bank account information was an application made to Enova, as opposed to a lead generator;
- (c) Enova was not sure if it improperly debited the consumer's account; and
- (d) affected consumers were only entitled to reimbursement of bank fees, and had no right to dispute the underlying debits.

86. These representations were material; as a consumer could be discouraged from disputing the illegal withdrawals if they believed they were in fact lawful, or they were only entitled to the reimbursement of fees.

87. In truth and in fact, as Enova knew when it made the representations described in paragraphs [REDACTED] to [REDACTED], Enova had been debiting consumers' new bank accounts without authorization using account information the consumers provided to

lead generators and consumers were entitled to dispute the underlying unauthorized debits.

88. Therefore, Enova's representations as set forth in paragraphs 1 through [REDACTED], were false and misleading and constitute deceptive acts in violation of the CFPA, 12 U.S.C. § 5536(a)(1)(A) and 5536(a)(1)(B).

Count III

Enova's Failure to Honor Loan Extensions Was Unfair.

89. The Bureau incorporates by reference the allegations in paragraphs 1 through [REDACTED], herein by reference.

90. In numerous instances, in connection with offering, providing, and collecting on payday loans and installment loans, Enova failed to honor loan extensions that offered to consumers. Enova's actions caused it to overcharge consumers by debiting their full monthly payment amount, instead of an extension fee.

91. Enova's actions caused or were likely to cause substantial injury to consumers by charging them for amounts that they did not owe, depriving consumers of the use of those funds, and causing them to incur bank fees for insufficient funds.

92. Consumers could not reasonably avoid these injuries because they could not know or predict that Enova would fail to honor their loan extension and improperly debit their accounts for the full amount due.

93. The injuries that Enova caused are not outweighed by countervailing benefits to consumers or competition.

94. Therefore Defendants' representations set forth in Paragraphs [REDACTED] to [REDACTED] constitute unfair acts or practices in violation of the CFPA, 12 U.S.C. § 5531(a)(1)(B) and 5536(a)(1)(B).

Count IV

Enova's Representations to Consumers Regarding its Failure to Honor Loan Extensions Were Deceptive.

95. The Bureau incorporates by reference the allegations in paragraphs 1 through [REDACTED], herein by reference.

96. In numerous instances, in connection with offering, providing, and collecting on payday and installment loans, Enova represented to consumers directly or indirectly, expressly or by implication, that:

- (a) Consumers could receive a loan extension for a fee of \$20;
- (b) That paying the fee would delay their monthly payment obligation; and
- (c) When Enova granted a loan extension, it would debit the extension fee of \$20, instead of the full monthly payment amount, from the consumers' accounts.

97. In truth and in fact, despite granting consumers' requests for a loan extension, Enova debited the full payment amount from consumers' accounts.

98. Fees such as loan extension fees are material to a consumer's decision to obtain credit and the manner in which to use the credit.

99. Therefore, Enova's representations as set forth in paragraphs 1 through [REDACTED], were false and misleading and constitute deceptive acts in violation of the CFPA, 12 U.S.C. § 5536(a)(1)(A) and 5536(a)(1)(B).

Count V

Enova's Act of Double-Charging Consumers Was Unfair

100. The Bureau incorporates by reference the allegations in paragraphs 1 through [REDACTED], herein by reference.

101. In numerous instances, in connection with offering, providing, and collecting on payday loans and installment loans, debiting consumers accounts twice for the same monthly payment.

102. Enova's actions caused or were likely to cause substantial injury to consumers by charging them for amounts that they did not owe, depriving consumers of the use of those funds, and causing them to incur bank fees for insufficient funds.

103. Consumers could not reasonably avoid these injuries because they could not know or predict that Enova would fail to properly account for their early payments.

104. The injuries that Enova caused are not outweighed by countervailing benefits to consumers or competition.

105. Therefore Defendants' representations set forth in Paragraph _____ to _____ constitute unfair acts or practices in violation of the CFPA, 12 U.S.C. § 5531(a)(1)(B) and 5536(a)(1)(B).

Count VI

Violation of Regulation E

106. The Bureau incorporates by reference the allegations in paragraphs 1 through _____, herein by reference.

107. Regulation E, implements the Electronic Funds Transfer Act (EFTA).

108. Section 1005.10(d) of Regulation E requires that payees must inform consumers of their right to receive notice of all varying transfers, but may give a consumer the option of receiving notice only when a transfer falls outside a specified range of amounts or only when a transfer differs from the most recent transfer by more than an agreed-upon amount. Regulation E further requires that this range of amounts must be reasonably anticipated by consumers.

109. Enova is a payee for purposes of EFTA and Regulation E.

110. As described in paragraphs _____ to _____, Enova made loans using loan contracts that failed to define certain terms related to charges that may be debited by Enova from consumers and by defining the range of payments as the minimum amount due all the way up to the entire outstanding loan balance, plus the undefined charges. As

a result, consumers could not reasonably anticipate the range of amounts set forth in Enova's loan contracts.

111. Enova's loan contracts therefore violate Section 1005.10(d) of Regulation E, 12 C.F.R. § 205.10(d).

Prayer for Relief

The Bureau requests that the Court:

- a. Permanently enjoin Defendants from committing future violations of the CFPB and Regulation E and enter such other injunctive relief as appropriate;
- b. Award such relief as the Court finds necessary to redress injury to consumers resulting from Defendants' violations of the CFPB and Regulation E, including but not limited to damages;
- c. Award civil money penalties against the Defendants;
- d. Award costs against the Defendants; and
- e. Award additional relief as the Court may deem just and proper.

Dated: [xx], 2017

Respectfully submitted,

Attorneys for Plaintiff
Consumer Financial Protection Bureau

ANTHONY ALEXIS
Enforcement Director

Redacted by the Committee
Acting Litigation Deputy

Redacted by the Committee
Acting Assistant Litigation Deputy

/s/ _____

Redacted by the Committee

Redacted by the Committee

APPENDIX H



1700 G Street NW, Washington, DC 20552


Decision Memorandum from the Director

FROM Richard Cordray, Director

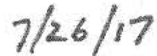
TO Tony Alexis, Assistant Director for Enforcement

SUBJECT Authority to Settle with Enova International, Inc. and to File Suit
– ENF Matter No. 2015-1636-02; Exam ID: 1961

I authorize the Office of Enforcement to enter into a settlement with and file a lawsuit against Enova International, Inc. under the parameters recommended by the Office of Enforcement on July 26, 2017.



Richard Cordray
Director
Consumer Financial Protection Bureau



Date

APPENDIX I



October 3, 2018

Recommendation Memorandum for the SEFL Policy Director

FROM	Redacted by the Committee Cara Petersen, and Kristen Donoghue, Office of Enforcement
THROUGH	Chris D'Angelo, SEFL Associate Director
SUBJECT	Authorization to Enter into Settlement with Enova International, Inc. Outside of Previously Authorized Parameters, or to File Suit

Recommendation

The Office of Enforcement recommends that you authorize a settlement in this matter under the parameters described below.

I. Overview

Based on the SEFL Policy Director's modification of the settle-or-sue authority in this matter described below, the Bureau should seek to settle with Enova International, Inc. (Enova) outside of previously authorized parameters.

Former Director Cordray authorized the Bureau to settle or sue on its potential claims against Enova on July 27, 2017. The Bureau and Enova began settlement negotiations in August 2017. On November 7, Enova offered to settle the matter for \$1,367,567 in redress to consumers and a \$1.2 million penalty. The redress portion of Enova's offer consisted of the following:

- Full refunds for payday customers whose bank accounts Enova debited without authorization;
- Refunds for up to four debits for installment loan and line-of-credit customers whose bank accounts Enova debited without authorization;

- \$35 per transaction for up to four debits for all consumers whose bank accounts Enova successfully debited without authorization;
- \$35 per transaction for all consumers whose bank accounts Enova attempted to debit without authorization; and
- \$35 per transaction for consumers for whom Enova failed to honor loan extensions.

On December 4, Enova indicated that it was reassessing its settlement position and has provided no further counter-offer since that time. On June 28, 2018, pursuant to the Acting Director's delegation of his authority, the SEFL Policy Director modified the settle-or-sue authority, eliminating several claims and modifying the relief to be sought, as described below.¹

This memorandum includes only facts relevant to the revised parameters. A copy of the previously approved recommendation memorandum with a more complete discussion of the facts is attached. The count numbers referenced in this memorandum correspond to the previously approved draft complaint against Enova, which is also attached.

II. Claims

The SEFL Policy Director declined to reauthorize three claims previously authorized by Director Cordray. The SEFL Policy Director directed Enforcement to eliminate deception claims relating to Enova's unauthorized debiting of consumers' bank accounts and its failure to honor loan extensions to consumers (Counts II and IV). The SEFL Policy Director also directed Enforcement to eliminate the Regulation E claim (Count VI). Further, the SEFL Policy Director directed Enforcement to drop the unfairness claim with respect to Enova's debiting consumers' accounts twice for the same monthly payment (Count V), if the claim proves to be a bar to settlement.

At the direction of the SEFL Policy Director, Enforcement will no longer pursue Counts II, IV and VI.

¹ The SEFL Policy Director's instructions are set forth in an e-mail to the Enforcement Director dated June 28, 2018.

III. Restitution

After discussion with the Office of Enforcement, the Legal Division, and the Acting Director, the SEFL Policy Director directed Enforcement not to seek restitution of loan principal or fees in connection with Count I. The loan principal and fees in question were legally owed, but unlawfully collected.²

The SEFL Policy Director also directed Enforcement not to seek restitution for any incidental NSF fees or overdraft charges incurred by consumers as a result of Enova's unauthorized debiting, given the impossibility of calculating restitution with certainty for each affected consumer. The precise amount of fees incurred by each affected consumer cannot be calculated with certainty because many of these transactions occurred over eight years ago and few, if any, consumers will have retained the relevant records for that length of time.

The SEFL Policy Director also directed Enforcement to seek restitution based on fees and penalties incurred as a result of erroneous charges (addressed in Counts III and V) only to the extent they can be calculated with certainty for each consumer. For the same reasons described above, these amounts cannot be calculated with certainty.

Thus, Enforcement will no longer seek consumer restitution for Counts I, III, or V.

IV. Penalties

Based on the facts developed during this investigation, since at least July 21, 2011, Enova acted recklessly by initiating over 14,000 debits from consumers' bank accounts without authorization, using account information obtained from lead generators. Further, a Missouri regulator notified Enova of the illegal debiting on

² Enforcement previously recommended, and received authorization to require as part of a settlement, refunds of amounts Enova unlawfully collected notwithstanding that consumers owed those amounts. The Legal Division subsequently prepared a memorandum addressing whether consumers may suffer "substantial injury" when a creditor (or debt collector) unlawfully collects debt that the consumer actually owes, and whether the Bureau has legal basis to require a creditor under those circumstances to return to consumers the funds that the creditor unlawfully collected. That memorandum concludes that consumers may suffer substantial injury under those circumstances, and that the Bureau could properly require the creditor to provide refunds for debts that were legally owed, but unlawfully collected, but that the Bureau would not be compelled to seek that remedy. Enforcement's previous negotiations with Enova contemplated that the company would retain the ability to collect amounts refunded to consumers to the extent permitted by law.

April 15, 2014, yet Enova knowingly continued to initiate an additional 5,600 debit payments from consumers' bank accounts without authorization after that notification. Accordingly, the facts would support a civil money penalty of nearly \$500 million from Enova before consideration of the statutory mitigating factors.

When considering the statutory factors required by 12 U.S.C. § 5565(c)(3), particularly relevant to this matter are the (1) severity of the risks or losses to consumers, (2) the size of Enova's financial resources, and (3) such other matters as justice may require. For the reasons discussed below, a civil money penalty of between \$3 million and \$5 million properly takes into account the required statutory factors.

i. The size of financial resources and good faith of the person charged.

While Enova is one of the largest and most profitable online lenders, generating over \$840 million in revenue in 2017, it likely does not have sufficient resources to pay a penalty in the range of \$500 million without significant negative impacts on its operations and offerings to consumers. Accordingly, some mitigation is warranted based on the size of Enova's financial resources.

ii. The gravity of the violation or failure to pay.

Here, the gravity of the violation does not serve as a mitigating factor on the recommended penalty range. Enova acted recklessly and at times, knowingly, and its misconduct involved unlawfully debiting millions of dollars from consumers' bank accounts without authorization. Failing to impose a significant civil penalty for the violations described above would not promote the goals of specific and general deterrence.

iii. The severity of the risks to or losses of the consumer, which may take into account the number of products or services sold or provided.

The "Flash Cash" and "Double Debit" issues impacted a small number of consumers relative to the total number of loans Enova makes on an annual basis, and the damages associated with these claims are less than \$100 on average for each consumer. The size of these claims may serve as a mitigating factor. With respect to Enova's unlawful debits, while consumers owed the amounts Enova unlawfully debited, as described above, consumers were nevertheless substantially injured by this unlawful conduct. It is therefore not, in Enforcement's view,

appropriate to consider the fact that the amounts debited were owed by consumers a significant mitigating factor here.

iv. The history of previous violations.

Enova is a recidivist. It was the subject of a 2013 consent order that resulted from misrepresentations it made to the Bureau exam staff and its efforts to conceal information from Bureau exam staff during an exam. Similarly, there is evidence suggesting that Enova has misrepresented to the Bureau when it became aware of its unauthorized debiting. Enova's history of similar violations and its misrepresentations to the Bureau thus do not provide a basis for mitigation.

v. Such other matters as justice may require.

As described in the previously approved recommendation memorandum, Enforcement previously recommended prioritizing obtaining redress for consumers over obtaining the maximum justifiable civil penalty. Now that the Bureau is no longer authorized to seek restitution for consumers, that consideration does not warrant further mitigation.

In addition to the statutory mitigating factors, the Bureau is authorized to "compromise, remit, or modify" the penalty in an enforcement action,³ including in the interest of obtaining a negotiated settlement. Enforcement recommends doing so here. We previously recommended a penalty in the range of \$1 million to \$3 million and restitution of \$2.1 million, prioritizing restitution over the penalty to be imposed. In light of the revisions to the claims and relief described herein, we believe a penalty of between \$3 million and \$5 million is appropriate as the monetary component of a settlement. Enova unlawfully collected approximately \$2.6 million from consumers' accounts (even leaving aside its other violations). Absent consumer redress, a penalty in an amount substantially less than \$3 million is likely insufficient to force the company to internalize the impact of its misconduct. The company likely will perceive its litigation risk to have decreased with the elimination of several claims and withdrawal of the Bureau's request that it provide redress to consumers, and may not be willing to settle, short of litigation, for an amount it might previously have been willing to pay. That said, we believe there is a realistic chance that it will agree to settle within these monetary parameters.

³ 12 U.S.C. § 5565(c)(4).

V. Injunctive Relief

The Bureau should seek appropriate injunctive relief that would, among other things, prohibit Enova from engaging in the conduct described in the revised draft complaint. Relevant injunctive terms should include a bar on debiting consumers' accounts without authorization, failing to honor loan extensions, and debiting consumers' bank accounts twice for the same monthly payment.

Attachments:

Tab 1: Draft Decision Memo from the SEFL Policy Director.

Tab 2: July 26, 2017 Recommendation Memorandum.

Tab 2a: July 26, 2017 Decision Memo

APPENDIX J

To: [Redacted by the Committee] (CFPB); [Redacted by the Committee] Petersen, Cara (CFPB); [Redacted by the Committee]; [Redacted by the Committee]
(CFPB); [Redacted by the Committee] [Redacted by the Committee] (CFPB); [Redacted by the Committee]
(CFPB); [Redacted by the Committee] [Redacted by the Committee] (CFPB); [Redacted by the Committee]; [Redacted by the Committee]
(CFPB); [Redacted by the Committee]
From: [Redacted by the Committee] (CFPB)
Sent: Fri 5/4/2018 9:06:03 PM
Subject: RE: Restitution Research
Damages and Restitution Outline LP 5.4.18 final.doc

Hi [Redacted],

Here's an outline with Legal's research and thoughts.

Thanks,

[Redacted]

-----Original Appointment-----

From: [Redacted by the Committee] (CFPB)
Sent: Wednesday, May 02, 2018 9:22 AM
To: Petersen, Cara (CFPB); [Redacted by the Committee] (CFPB); [Redacted by the Committee] (CFPB); [Redacted by the Committee] (CFPB); [Redacted by the Committee] (CFPB); [Redacted by the Committee] (CFPB); [Redacted by the Committee] (CFPB); [Redacted by the Committee] (CFPB)
Subject: Restitution Research
When: Wednesday, May 02, 2018 12:30 PM-1:00 PM (UTC-05:00) Eastern Time (US & Canada).
Where: 8122

Hi all,

With apologies for the short notice, I was hoping to have a quick conversation tomorrow about the status of the efforts in Legal and Enforcement to research a question I've discussed with [Redacted] and Cara: namely, whether courts consider restitution an appropriate remedy where an illegal practice (such as a violation of the FDCPA or an unfair act under the CFPA or FTC Act) results in a consumer paying a debt that is validly owed, and if so, whether the creditor may be barred from further attempts to recollect the same debt. Eric asked me to get him whatever research I could on that issue by this Friday.

Thanks,

[Redacted]

L&P Outline Regarding Debt Collection of Amounts that Consumers Actually Owe

Points of Contact: Redacted by the Committee, Redacted by the Committee

Summary:

When the Bureau determines that a debt collector improperly takes money from a consumer that the consumer actually owes, Legal is of the preliminary view that the Bureau reasonably could, under the Consumer Financial Protection Act, seek as damages the remedy of the entire amount that was taken from the consumer, notwithstanding that the consumer owes the debt. FDCPA case law awarding “actual damages” supports this theory of relief, as does the common law principle reflected in the Restatement (Second) of Torts that the consumer has the right to choose how to allocate payments to creditors. Notably, under this theory, the underlying debt would not be extinguished (unless the Bureau sought that as an additional remedy, which we do not consider here). So the collector could still thereafter pursue the consumer for the debt using lawful means. That said, we do not think that the Bureau would be required to seek the entire amount that was taken from the consumer, and the FTC does not seem to generally have done so. We do not know the reasons for the FTC’s approach. One hypothesis may be that the FTC, under its remedy provisions, can generally only get injunctive relief in UDAP actions, which could be a more limited remedy in this context. But there may also be other explanations.

We note that because of the short time frame, Legal has not completed a full-fledged analysis of this issue with full management review, and this outline represents preliminary research and analysis of the issue.

Statutory Overview:

CFPA:

- “The court (or the Bureau, as the case may be) in an action or adjudication proceeding brought under Federal consumer financial law, shall have jurisdiction to grant any appropriate legal or equitable relief with respect to a violation of Federal consumer financial law.” 12 U.S.C. 5565(a)(1).
- Relief “may include, without limitation”:
 - (A) rescission or reformation of contracts;
 - (B) refund of moneys or return of real property;
 - (C) restitution;
 - (D) disgorgement or compensation for unjust enrichment;
 - (E) payment of damages or other monetary relief;
 - (F) public notification regarding the violation, including the costs of notification;
 - (G) limits on the activities or functions of the person;
 - and
 - (H) civil money penalties....

12 U.S.C. 5565(a)(2) (emphasis added).

- But “[n]othing in this subsection shall be construed as authorizing the imposition of exemplary or punitive damages.” 12 U.S.C. 5565(a)(3).

FDCPA:

- “[A]ny debt collector who fails to comply with any provision of [the FDCPA] with respect to any person is liable to such person” for both “any actual damage sustained by such person as a result of such failure” and so-called statutory damages, i.e., “such additional damages as the court may allow, but not exceeding \$1,000.” 15 U.S.C. 1692k(a) (emphasis added).

FTC Act:

- “In the early and mid-1980s, the Commission began to make widespread use of the permanent injunction proviso of Section 13(b) in its consumer protection program to challenge cases of basic consumer fraud and deception. . . . T[he] Commission [may] obtain an order not only permanently barring deceptive practices, but also imposing various kinds of monetary equitable relief (i.e., restitution and rescission of contracts) to remedy past violations.” <https://www.ftc.gov/about-ftc/what-we-do/enforcement-authority> (emphasis added)
- Note that the Bureau’s remedy provision (CFPA section 1055) appears not to be modeled after this provision, but instead after section 19 of the FTC Act, 15 U.S.C. 57b, which applies to violations of FTC cease-and-desist orders. *See id.*
 - In other words, the FTC is limited in its UDAP actions to injunctive (including monetary equitable) relief, but can seek a fuller range of remedies in response to violations of cease-and-desist orders. By contrast, under the CFPA, the Bureau can get the full range of remedies in its UDAAP actions.

FDCPA Caselaw:

- District court cases (with some affirmances by the Circuits without discussion of this issue) appear to uniformly hold that an amount that a consumer paid as a result of illegal debt collection conduct can be recovered by the consumer as a remedy for an FDCPA violation even if the consumer owes the debt. Since under the FDCPA remedy provision this recovery is for “actual damages,” these cases arguably bear on the meaning of the term “damages” in the Bureau’s remedy provision, 12 U.S.C. 5565(a)(2)(E).
 - *FTC v. Check Enft*, 2005 WL 1677480, at *10 (D.N.J. July 18, 2005), *aff’d sub nom. FTC v. Check Inv’rs, Inc.*, 502 F.3d 159 (3d Cir. 2007) (“[T]he FTC has established that \$10,204,445.00 in payments were procured by the defendants using the improper purposes addressed in this Opinion. For the reasons discussed in the FTC’s Memorandum in Support of its summary judgment motion, this sum is recoverable from the defendants, jointly and severally, as restitution in this matter.”).
 - *Abby v. Paige*, 2013 WL 141145, at *9 (S.D. Fla. Jan. 11, 2013), *aff’d*, 553 Fed. Appx. 970 (11th Cir. 2014) (“[B]ecause the FDCPA permits a plaintiff to recover

- for violations of the law even when he defaulted on a debt, it follows that debtors may recover the amount paid to settle a debt if the debt collector violated the FDCPA in connection with collecting that debt.”) (quotation marks omitted).
- *Hamid v. Stock & Grimes, L.L.P.*, 876 F. Supp. 2d 500, 503 (E.D. Pa. 2012) (“If her payment was not a proper element of actual damages under the FDCPA, a debt collector could harass a debtor in violation of the FDCPA, as a result of that harassment collect the debt, and thereafter retain what it collected. We do not believe that Congress intended this result.”).
 - *Alonso v. Blackstone Fin. Group LLC*, 962 F. Supp. 2d 1188, 1198 (E.D. Cal. 2013) (“Allowing debt collectors to retain money that was collected by violating the FDCPA would encourage misconduct, especially in cases where large amounts of debt are owed.”).
- Also, to get damages for the amounts paid to the debt collector, the consumer must show that the FDCPA violation actually caused the payment. (The CFPA unfairness provision expressly contains the similar requirement that the act or practice “causes or is likely to cause substantial injury.” 12 U.S.C. 5531(c)(1)(A).)
 - *McMahon v. LVNV Funding, LLC*, 12 C 1410, 2018 WL 1316736, at *12 (N.D. Ill. Mar. 14, 2018) (“The Court agrees with plaintiff that the amount class members paid as a result of receiving deceptive dunning letters is at least a permissible measure of damages under the FDCPA, and it may well be a proper measure of damages in this case...[But] it does not follow that the class members need not bother proving that defendants' failure to comply with the FDCPA caused them to make payments.”).
 - On the other hand, the consumer should not be able to recover FDCPA damages for payments on debts actually owed simply because the debt collector violated state law. This is consistent with other FDCPA precedent indicating that violations of state law do not necessarily constitute FDCPA violations.
 - *Moritz v. Daniel N. Gordon, P.C.*, 895 F. Supp. 2d 1097, 1116–17 (W.D. Wash. 2012) (“Other courts have found that plaintiffs are not injured in the amount collected when the plaintiff owed the debt even where the debt collector violated state law in doing so. . . .Based on these cases, the court concludes that Ms. Moritz cannot recover the amounts she paid to [the collector] because those amounts were less than the total amount she owed to [the creditor] on a valid debt.”).
 - *Carlson v. First Revenue Assurance*, 359 F.3d 1015, 1018 (8th Cir. 2004) (“The FDCPA was designed to provide basic, overarching rules for debt collection activities; it was not meant to convert every violation of a state debt collection law into a federal violation.”); *see also Wade v. Regional Credit Association*, 87 F.3d 1098, 1100 (9th Cir. 1996); *Belser v. Blatt, Hasenmiller, Leibsker & Moore, LLC*, 480 F.3d 470, 473 (7th Cir. 2007).
 - FDCPA cases also hold that an FDCPA violation does not extinguish the underlying debt. We do not believe this case law is in tension with the cases holding that the debt collector can be required to return payments improperly procured even if the consumer

owes the money. Instead, we believe this holding means that the debt collector remains free after returning the money collected unlawfully to pursue lawful collection of the amount owed. The fact that the underlying debt is not extinguished also arguably suggests that the remedy of returning money unlawfully collected but owed would not be punitive in contravention of the proviso to the Bureau's remedy provision, 12 U.S.C. 5565(a)(3).

- *Vitullo v. Mancini*, 684 F. Supp. 2d 760, 764 (E.D. Va. 2010) (“The statute's remedial scheme does not envision, and indeed does not permit, courts to cancel or extinguish debts as a remedy for FDCPA violations.”).
 - *United States v. Iwanski*, 805 F. Supp. 2d 1355, 1359 (S.D. Fla. 2011) (“Nothing in the FDCPA suggests that a borrower can have his debt extinguished or cancelled in lieu of recovering damages.”).
 - *Midland Funding, LLC v. Pipkin*, 283 P.3d 541, 542 (Utah Ct. App. 2012) (“While Midland's alleged failure to comply with the FDCPA may subject it to liability under the act, such failure is not a defense to liability for the underlying debt.”)
- Notwithstanding that the debt would not be extinguished, the federal court will typically not, in a consumer's FDCPA action, hear a counterclaim from the debt collector on the debt:
 - *Leatherwood v. Universal Bus. Serv. Co.*, 115 F.R.D. 48, 50 (W.D.N.Y. 1987) (“To allow a debt collector defendant to seek to collect the debt in the federal action to enforce the FDCPA might well have a chilling effect on persons who otherwise might and should bring suits such as this. Moreover, it would involve this Court in questions of no federal significance.”)
 - *Ayres v. Natl. Credit Mgt. Corp.*, 1991 WL 66845, at *4 (E.D. Pa. Apr. 25, 1991) (“The act does not explicitly address federal jurisdiction over actions by debt collectors to collect on debts.... By thus addressing creditors' actions, without providing for federal jurisdiction over these actions, Congress implicitly renounced the bringing of such actions in federal court, ancillary to FDCPA claims.”).

Restatement (Second) of Torts:

- Although not directly on point, the theory that a consumer can receive his or her payment on the debt in damages for unlawful collection draws some support from the common law principles that a debtor is allowed to allocate payment of his debts as he sees fit and that a tortfeasor may not limit a plaintiff's recovery by paying a debt of the injured person. For example, the Restatement indicates:
 - “A tortfeasor cannot diminish the amount of recovery by paying a debt of the injured person without the latter's consent, unless (a) the damages recoverable against the tortfeasor would include the amount of the debt, or (b) the payment of the debt was made unofficiously from the proceeds of the property of the injured person for the value of which suit is brought.

...

“Comment on Clause (b): The rule stated in this Clause is particularly applicable to a sheriff or other officer who, by mistake of law or fact, has made an improper levy upon goods of a debtor and who before he has discovered the mistake, pays some or all of the debt from the proceeds of the sale made under the levy. (See Illustration 4). It applies also to a person who, without authority, takes the goods of a deceased person and without administration, pays his debts. (See Illustration 5). The rule does not apply when the payment was made in bad faith nor when it would defeat some policy of the law. (See Illustration 6). Nor does the rule permit a creditor who has improperly seized his debtor's goods to have the damages for the conversion diminished by the amount of the debt.”

Restatement (Second) of Torts § 923 (emphasis added).

- We have found this elaboration in the caselaw:
 - “Mitigation of damages in tort cases is restricted by principles of equity, and in conversion cases, a defendant generally cannot diminish the amount of damages by paying a debt of the injured party without the latter's consent. [See] Restatement of Torts, § 923 To allow mitigation by application of the converted property to the benefit of the injured party would result in the converter dictating to the owner how the owner's property is to be used. Such a result would seriously weaken the concept of property ownership because a defendant would not be penalized for interfering with another person's possessions if the ultimate offset of the interference resulted in a benefit to that person.
“The language of the Michigan Supreme Court asserted over 100 years ago is still viable today. That court said in *Northrup v. McGill*, 27 Mich. 234, 240 [(1873)]:
In general, when there is no fraud, and when the law does not forbid, a man may dispose of his own property according to his own ideas of propriety. If he is indebted by note to different parties, he may apply his property to the payment of one, and refuse to apply it to the payment of another, and he may lawfully discriminate in this way, though in doing so he ignores the stronger moral claim resting upon him. This results from the supreme dominion which is involved in the absolute ownership of property.
“A contrary view would result in gross abuses and allow officious intermeddlers to determine payment priorities which are best left to debtors.
“The exceptions to the rule involve cases where the application of the property is compelled by legal duty, such as liens or security interests . . . or when the converter causes the plaintiff to owe a debt and then satisfies it himself (Restatement of Torts 923, Comment (a)).”

FTC Caselaw:

- In the FTC cases that we have identified that appear to present similar circumstances, the FTC sought only disgorgement of profits – in this context, return to consumers only of interest and fees paid on the loan, not the principal. We do not know the reasons for the FTC’s approach. One hypothesis may be that the FTC, under its remedy provisions for

FTC Act section 13(b) UDAP actions, can generally only get injunctive relief, which could be a more limited remedy in this context. But there may also be other explanations.

- *FTC v. LoanPointe, LLC*, 2011 WL 4348304, at *12 (D. Utah Sept. 16, 2011), *aff'd*, 525 Fed. Appx. 696 (10th Cir. 2013) (“In this case, Defendants argue that they did not collect any money that was not owed, and they were not unjustly enriched by deceptive practices that induced a consumer to act to its detriment. Defendants assert that requiring them to disgorge amounts paid for repayment of loans would amount to a penalty, not simply a prevention of unjust enrichment, and, therefore, it is beyond the scope of fair equitable relief.... While the garnishment letter violated federal law, the court does not believe that Defendants should be required to disgorge the principal loan amounts. To the extent that disgorgement applies to ‘ill-gotten gains,’ a return of the loan principal lent to the consumer is not actually a ‘gain’ to Defendants. The court, therefore, concludes that the only amounts that can be considered to be ‘ill-gotten gains’ or ‘gains flowing from the illegal activities’ are the interest amounts received through the inappropriate garnishments. Technically, Defendants may have been entitled to the interest payments under the terms of the loans. But, requiring Defendants to disgorge the interest they received through garnishment fulfills one of the purposes of disgorgement, which is to make violations unprofitable.” (citations omitted)).
- *FTC v. PayDay Fin. LLC*, 989 F. Supp. 2d 799, 820 (D.S.D. 2013) (“The FTC's request for disgorgement of \$417,740 stems from the amount of finance charges, interest, and fees collected by certain of the Defendants through garnishment. The garnishment practices of the Defendants doing collections were violative of § 5 of the FTCA and stemmed in part from clauses violative of the Credit Practices Rule. The Defendants argue, however, that they were collecting moneys owed under the loan agreements by consumers through garnishment. That is, Defendants argue they were not receiving ill-gotten gains, but rather collecting what amounts were owed.... This Court agrees with the rationale in *LoanPointe*, and finds that disgorgement of the \$417,740 Defendants PayDay Financial LLC and Financial Solutions LLC collected through their illegal garnishment practices is appropriate. Those two Defendants profited from the illegal garnishment in violation of § 5, the profits—which came in the form of astoundingly high interest rates and fees—were in fact collected through illegal garnishment in the amount of \$417,740, and that figure reasonably approximates the amount of unjust enrichment.”).

Restatement (Third) of Restitution and Unjust Enrichment:

- The Restatement may support this principle of more limited recovery under the injunctive remedy of disgorgement, although further research into the caselaw would be helpful:
 - “Even if the claimant has conferred a benefit that results in the unjust enrichment of the recipient when viewed in isolation, the recipient may defend by showing that some or all of the benefit conferred did not unjustly enrich the recipient when the challenged transaction is viewed in the context of the parties' further obligations to each other.

“Comment.... *The baseline of unjust enrichment.* The standard application of § 62 is to a case in which a payment by the claimant, viewed in isolation, creates unjust enrichment of the recipient and a prima facie right to recovery in restitution. Examples include payments by mistake, payments under duress, and payments under illegal contracts. The defendant answers that the question of unjust enrichment between the parties can only be judged in light of the further relations between them. The baseline from which unjust enrichment is measured, in other words, is not the moment before the challenged payment but a point preceding other transactions between them....

“[Illustration 2:] A owes B \$5000. Intending to pay C, another creditor, A sends \$5000 to B who accepts the payment despite notice of A's mistake. (B's notice of A's mistake means that B is not entitled to defend as a bona fide payee by the rule of § 67.) A has a prima facie claim to restitution of the mistaken payment (§ 6), but B is not unjustly enriched by A's unintended payment of a valid debt. B is not liable to A in restitution.”

Restatement (Third) of Restitution and Unjust Enrichment § 62

APPENDIX K

To: Blankenstein, Eric (CFPB) [Redacted by the Committee]
From: [Redacted by the Committee] (CFPB)
Sent: Thur 6/7/2018 5:46:51 PM
Subject: RE: Legal Memo re Valid Debt Issues
Valid Debt Memo -- Rev'd 06.07.18 -- Redline.docx

Hi Eric,
Here's the redline showing the revisions to the valid debt memo. Happy to look into any of this further if you'd like.
Thanks,

[Redacted]

Confidentiality Notice: If you received this email by mistake, you should notify the sender of the mistake and delete the e-mail and any attachments. An inadvertent disclosure is not intended to waive any privileges.

From: [Redacted by the Committee] (CFPB)
Sent: Thursday, May 31, 2018 3:51 PM
To: Blankenstein, Eric (CFPB)
Subject: Legal Memo re Valid Debt Issues

Hi Eric,

I've attached the memo Legal prepared addressing the questions coming out of the Enova investigation concerning substantial injury and remediation. The memo also reflects a couple comments from Enforcement.

It's fairly long, and I'd be happy to discuss or arrange a meeting with Legal and/or Enforcement for a broader discussion once you've had a chance to review it.

Thanks,

[Redacted by the Committee]

[Redacted by the Committee]

Acting Counsel to the SEEL Policy Director
[Redacted by the Committee]

Bureau of Consumer Financial Protection
consumerfinance.gov

Confidentiality Notice: If you received this email by mistake, you should notify the sender of the mistake and delete the e-mail and any attachments. An inadvertent disclosure is not intended to waive any privileges.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

TO: SEFL
FROM: [Redacted], Senior Counsel, Legal Division²
THROUGH: [Redacted by the Committee], Assistant General Counsel
[Redacted by the Committee], Deputy General Counsel
DATE: ~~May 31~~ June 7, 2018
RE: Injury and Remedy for Illegal Debt Collection of Amounts Actually Owed

Formatted: Section start: Continuous

QUESTIONS PRESENTED

- (1) Can a consumer be substantially injured when a creditor or debt collector illegally collects debt that the consumer actually owes?
- (2) What is the appropriate remedy when a creditor or debt collector illegally collects debt that a consumer actually owes?

STATEMENT OF THE ISSUE

The Bureau has frequently brought claims against creditors and debt collectors under the Consumer Financial Protection Act (CFPA) and against debt collectors under the Fair Debt Collection Practices Act (FDCPA). In many of these instances, it is not disputed that the consumer does indeed owe the money that the creditor or collector is trying to collect. Nonetheless, the Bureau may allege that the means by which the creditor/collector has collected the debt violates the CFPA or the FDCPA or both. To take the example that the Bureau is currently considering, a creditor may simply take the money from the consumer's bank account without authorization from the consumer to do so. Is a consumer substantially injured by this practice, if the creditor has only collected money that the consumer actually owes?

Further, assuming the creditor/collector's conduct violates the CFPA or the FDCPA, what is the appropriate remedy for such a violation? For instance, is it appropriate for the Bureau to require the creditor or collector to return to consumers any money improperly collected – notwithstanding that the consumer does indeed owe that money? And if the Bureau does receive that remedy, may the creditor or collector thereafter again seek payment from the consumer on the debt?

This memorandum addresses these issues.

A related issue, not squarely addressed by this memorandum, is the situation in which a creditor or debt collector behaves improperly in some way toward the consumer and the consumer then subsequently repays the debt. For example, the creditor/collector may lie to the consumer, improperly threaten the consumer, or

² [Redacted by the Committee] and [Redacted by the Commi] in Legal also provided significant contributions.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

improperly humiliate the consumer, and the consumer may then pay the debt. How should the Bureau consider the injury and/or remedy in that context? This memorandum may be preliminarily helpful in informing the answers to those questions, but further thinking would probably need to be done to fully analyze that situation. We would be happy to do further work on that issue, which we acknowledge the Bureau may confront more frequently than the present situation in which a creditor simply improperly took money from a consumer's bank account.

SUMMARY

(1) *Substantial injury:* At common law, a creditor who took a debtor's property without having a security interest in that property was liable to the consumer for the tort of conversion, notwithstanding that the property was taken to satisfy a valid debt. Further, FTC Act caselaw in the debt collection context suggests that there is indeed substantial injury in these circumstances. And FDCPA caselaw suggests that "actual damages" in the amount that the debt collector improperly collected is appropriate in these circumstances. Accordingly, this memorandum concludes that substantial injury under the CFPA may occur in these circumstances.

(2) *Remedy:* At common law, a creditor who took a debtor's property without having a security interest in that property would generally owe the debtor *damages* for the tort of conversion. Unlike the remedy of restitution (which includes disgorgement of unjust enrichment), the remedy of damages is not subject to equitable defenses. Indeed, relevant precedent suggests that the creditor in these circumstances would owe the debtor the full value of the property taken, with no setoff or reduction for the amount owed. That said, the debtor would still owe the creditor the amount owed, and the creditor could continue to pursue the debtor for that amount using legal means.

The Bureau, unlike the FTC in direct litigation enforcing violations of the FTC Act, is able to recover damages in UDAAP cases. Under the FDCPA, which has been called a "federal tort action," "actual damages" in this situation has been found to be the full amount that the consumer paid. And in a relatively rare situation in which the FTC was statutorily entitled to get damages as consumer redress for an unfair practice, using the statutory provision that most resembles the CFPA remedy provision, the Ninth Circuit found that the FTC could get damages as redress in the full amount of consumer loss, even if this exceeded the defendant's unjust gains.

In all these cases, in order to collect damages commensurate with consumer loss, it must be shown that the collector's conduct *caused* the consumer loss. At least in the factual circumstance directly being addressed here (in which the creditor or collector simply improperly takes money from the consumer), we do not think that is a difficult showing.

It is generally the plaintiff's choice which remedy to seek, and plaintiffs may even seek multiple remedies, so long as they do not "double collect" the same amount.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

Accordingly, this memorandum concludes that it would be legally appropriate for the Bureau to seek redress in the full amount taken from consumers in this situation. On the other hand, we do not believe that the Bureau would be legally compelled to seek this remedy, since it is the plaintiff's choice which remedy to seek.

The memorandum ends by offering some very preliminary thoughts on the situation in which a creditor or debt collector behaves improperly in some way toward the consumer and the consumer then subsequently repays the debt.

EARLY HISTORY OF THE ISSUE AT THE BUREAU

The idea that the Bureau would seek the refund of payments (including principal) that consumers made on debts that they owed as relief for consumers subject to illegal debt collection practices appears to have originated within the Bureau in the Office of Enforcement. The first time the Legal Division became aware of the desire of the Office of Enforcement to seek such relief in the debt collection context appears to have been in 2012, in a group of enforcement actions the Bureau worked on in coordination with the FDIC, OCC, and FRB against American Express. The Bureau and other Federal regulators believed American Express was using deceptive debt collection tactics in violation of sections 1031 and 1036 of the CFPB and section 5 of the Federal Trade Commission Act to persuade consumers to repay loans they owed to the bank.

The July 26, 2012 Decision Memorandum approved by the Director for this matter explained on pages 29-30:

We note that, to our knowledge, this would be the first time a federal regulator has provided complete restitution to consumers who were deceived into paying debts that were owed (although the FTC has in the past sought and obtained disgorgement of unlawfully collected debt). However, given the age of the debt, the nature of the deception, and American Express's willingness to provide the relief, we believe restitution is appropriate here. Creditors and debt collectors have a right to collect debts that are owed. They do not, however, have a right to break the law when doing so.

In order to prevent consumers from receiving an improper windfall, we propose structuring the proposed redress to allow the Bank to resume collection activities on the refunded debt, while notifying consumers if appropriate that the debt is [time-]barred for litigation and credit reporting purposes.

(footnotes omitted).

Further, as far as the Legal Division is aware, the Bureau has never had a hard and fast policy or practice to always seek such relief. For example, in 2013, the

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

Bureau brought an enforcement action against ACE Cash Express, Inc. (ACE) because it believed this payday lender was using unfair, deceptive, and abusive debt collection tactics in violation of sections 1031 and 1036 of the CFPA to persuade consumers to repay loans they owed to the lender. The Decision Memorandum approved by the Director on November 12, 2013, authorized the Office of Enforcement to settle the matter on terms that included, as “restitution,” any amounts paid by consumers subject to the illegal collection practices, but also authorized the Office of Enforcement, “[i]f necessary to settle the case,” to settle the matter on terms including only partial restitution consisting of the interest and fees paid by consumers subject to the illegal collection practices. Decision Memorandum for the Director, Authorization to Enter into Settlement with Specified Parameters with ACE Cash Express, Inc., at 16.

Ultimately, the ACE action resulted in a Consent Order approved by the Director on July 8, 2014. The Order required a Redress Plan that included the following: “Provide that all Restitution Eligible Consumers [*i.e.*, consumers subject to the illegal practices]] who submit a timely claim form shall receive a refund of all payments to ACE during the Relevant Period plus 1.3% [(presumably for interest)], unless the total of such payments would exceed \$5,000,000, in which case the amount paid to each Restitution Eligible Consumer shall be reduced pro rata by the Administrator.” In the Matter of ACE Cash Express, Inc., Consent Order, Administrative Proceeding File No. 2014-CFPB-0008, ¶ 42(d). The Order also required ACE to notify eligible consumers that “claiming a refund will not subject the consumer to any new debt collection activity.” *Id.* ¶44(e). The Order further provided that ACE “shall not be entitled to a set-off, or any other reduction, of the amount of payments to Restitution Eligible Consumers because of any debts owed by the Restitution Eligible Consumers” and that the redress provided by ACE “shall not limit consumers’ rights except for double recovery.” *Id.* ¶ 46.

LEGAL FRAMEWORK

a. Bureau’s Authority with Respect to Debt Collection

The Bureau may bring claims against debt collectors under the CFPA or the FDCPA or both. The Dodd-Frank Act indicates that both the CFPA and the FDCPA are “Federal consumer financial laws.” *See* 12 U.S.C. 5481(12)(H), (14). And the Bureau has authority, subject to certain exceptions, to bring claims against “any person [who] violates a Federal consumer financial law,” 12 U.S.C. 5564(a), and to supervise certain persons, such as payday lenders, for the purpose of “assessing compliance with the requirements of Federal consumer financial law,” *see* 12 U.S.C. 5514.

Under the CFPA, “collecting debt related to any consumer financial product or service” is a “financial product or service.” 12 U.S.C. 5481(15)(A)(x). The Bureau has frequently brought claims under the CFPA for unfair, deceptive, or abusive acts or practices (UDAAPs) involving debt collection conduct by creditors such as payday lenders. *See* 12 U.S.C. 5531(a).

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

As is explained by other memoranda, the CFPA's UDAAP provision is modeled after (or "borrowed from") FTC Act section 5's "UDAP" provision, which "declare[s] unlawful" "unfair or deceptive acts or practices in or affecting commerce." 15 U.S.C. 45(a)(1). Specifically, the CFPA UDAAP provision borrows the FTC Act language on unfairness, that is, that the Commission has no authority "to declare unlawful an act or practice on the grounds that such act or practice is unfair unless the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition." 15 U.S.C. 45(n); *see also id.* (describing "public policy considerations").

The Bureau and FTC both have authority to bring claims against debt collectors under the FDCPA. *See* 15 U.S.C. 1692l(a) and (b)(6). The FDCPA also creates a private cause of action. *See* 15 U.S.C. 1692k(a), (d). The FDCPA defines "debt collector" as "any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another." 15 U.S.C. 1692a(6). Generally and roughly speaking, the FDCPA applies to anyone who collects debts owed to someone else (i.e., "third-party debt collectors") or whose "principal purpose" is debt collection, but the FDCPA does not apply to creditors to whom debts are originally owed (so-called "first-party creditors").

b. CFPA Relief Provision

The CFPA "relief" section, CFPA 1055, contains three parts/provisions about "relief," which are located in subsection (a) of 1055. (The remainder of 1055 concerns recovery of costs and additional details on civil money penalties.) As described below, at least the second and third parts of the CFPA relief section (CFPA 1055) appear to have been modeled on section 19 of the FTC Act (with some additions from the Federal Deposit Insurance Act).

The first part of the CFPA relief section indicates that "[t]he court (or the Bureau, as the case may be) in an action or adjudication proceeding brought under Federal consumer financial law, shall have jurisdiction to grant any appropriate legal or equitable relief with respect to a violation of Federal consumer financial law." 12 U.S.C. 5565(a)(1).

The second part of the CFPA relief section indicates that relief "may include, without limitation":

- (A) rescission or reformation of contracts;
- (B) refund of moneys or return of real property;
- (C) restitution;
- (D) disgorgement or compensation for unjust enrichment;
- (E) payment of damages or other monetary relief;
- (F) public notification regarding the violation, including

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

- the costs of notification;
- (G) limits on the activities or functions of the person;
- and
- (H) civil money penalties....

12 U.S.C. 5565(a)(2).

The third part of the CFPA relief section indicates that nothing in subsection (a) “shall be construed as authorizing the imposition of exemplary or punitive damages.” 12 U.S.C. 5565(a)(3).

c. FTC Act Remedies: Sections 5, 13(b), and 19

The FTC has authority to enforce against violations of FTC Act section 5 (i.e. UDAPs) either administratively or directly in court. *See generally* A Brief Overview of the Federal Trade Commission’s Investigative and Law Enforcement Authority, <https://www.ftc.gov/about-ftc/what-we-do/enforcement-authority> (“FTC Overview”). As explained below, when the FTC enforces UDAP violations administratively, it then also has the authority to seek consumer redress in court if the conduct was such that “a reasonable man would have known under the circumstances was dishonest or fraudulent.” *See* 15 U.S.C. 57b(b).

The FTC enforces UDAP violations directly in court under section 13(b) of the FTC Act. Section 13(b) authorizes the FTC to seek a “permanent injunction” if it has “reason to believe” that any person “is violating, or is about to violate, any provision of law enforced by the Federal Trade Commission.” 15 U.S.C. 53(b). Section 13 was added to the FTC Act in 1973. *See FTC v. H. N. Singer, Inc.*, 668 F.2d 1107, 1110 (9th Cir. 1982); *FTC v. World Travel Vacation Brokers, Inc.*, 861 F.2d 1020, 1027 (7th Cir. 1988).

As the FTC has summarized: “In the early and mid-1980s, the Commission began to make widespread use of the permanent injunction proviso of Section 13(b) in its consumer protection program to challenge cases of basic consumer fraud and deception.” FTC Overview. Although section 13(b) refers only to permanent injunctions, all the Circuits to have considered the question have nonetheless determined that the Commission may under section 13 “obtain an order not only permanently barring deceptive practices, but also imposing various kinds of monetary equitable relief (i.e., restitution and rescission of contracts) to remedy past violations.” *Id.*; *see FTC v. Verity Intern., Ltd.*, 443 F.3d 48, 66 (2d Cir. 2006) (summarizing precedent). The contours of the equitable relief available to the FTC under section 13 (and the distinction between legal and equitable relief) are described in detail below.

The FTC enforces UDAP violations administratively under section 5(b) of the FTC Act. Section 5(b) authorizes the FTC, when it has “reason to believe” that any person “is using any ... unfair or deceptive act or practice in or affecting commerce,”

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

to conduct an administrative proceeding and then to issue an order requiring such person "to cease and desist... from the act or practice." 15 U.S.C. 45(b).

After issuing such an administrative order, the FTC may then, under section 19 of the FTC Act, seek redress in federal court for consumer injury caused by the conduct that was at issue in the administrative proceeding. *See* FTC Overview. Section 19(a) authorizes the FTC to bring lawsuits against any person "with respect to which the Commission has issued a final cease and desist order" if the Commission shows that the act or practice "is one which a reasonable man would have known under the circumstances was dishonest or fraudulent, the court may grant relief under [FTC Act section 19(b)]." 15 U.S.C. 57b(a). (The FTC can also file suit under Section 19(a) where a person, partnership, or corporation violates an FTC rule regarding unfair or deceptive acts or practices.) In turn, section 19(b) provides in relevant part:

The court in [a UDAP action] shall have jurisdiction to grant such relief as the court finds necessary to redress injury to consumers ... resulting from ... the unfair or deceptive act or practice, as the case may be. Such relief may include, but shall not be limited to, rescission or reformation of contracts, the refund of money or return of property, the payment of damages, and public notification respecting the rule violation or the unfair or deceptive act or practice, as the case may be; except that nothing in this subsection is intended to authorize the imposition of any exemplary or punitive damages.

15 U.S.C. 57b(b). This provision (section 19) was added to the FTC Act in 1975. *See* PL 93-637, 88 Stat 2183 (Jan. 4, 1975).

For what it is worth, the legislative history – including the Conference Report and the Senate Commerce Report -- for these provisions has been cited by dozens of courts. *See, e.g., FTC v. S.W. Sunsites, Inc.*, 665 F.2d 711, 720 (5th Cir. 1982) (quoting the Conference report); *FTC v. World Travel Vacation Brokers, Inc.*, 861 F.2d 1020, 1027 (7th Cir. 1988) (quoting the Commerce report). As relevant here, the Conference Report emphasizes that section 19's list of remedies is non-exhaustive: "While this section enumerates several types of relief which may be granted, the nature of the relief authorized is limited only by the nature of the injury done and the remedial powers of the court. The enumeration of specific types of relief available are not exclusive and do not limit the Commission in pleading, or the court in fashioning, other appropriate remedies." S. Rep. No. 93-1408 (1974) (conference report), 1974 U.S.C.C.A.N. 7755, 7773.

Further, the Senate Commerce Report elaborates on the role that the Commission plays in standing in the shoes of consumers in section 19 cases:

After a cease-and-desist order is made final, the Commission may seek remedial relief on behalf of consumers injured by the specific unfair or deceptive act or practice which was the subject of the cease-and-

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

desist proceeding in an action initiated in Federal district court. This provision would enable the Commission to more adequately protect consumers by affording them specific redress for their injuries. At the present time, cease-and-desist orders have prospective application only and afford no specific consumer redress to consumers who have been injured.

S. Rep. No. 93-151 (1973) (report of the Senate Committee on Commerce).

d. Relationship Between CFPA Remedy Provision and Other Statutes

The third part of the CFPA relief provision, CFPA 1055(a)(3), appears to have been borrowed essentially verbatim from the second sentence of FTC Act section 19(b).

The second part of the CFPA relief provision, CFPA 1055(a)(2), appears to have borrowed much of its language from the second sentence of FTC Act section 19(b). CFPA 1055(a)(2) lists word-for-word all the remedies that appear in FTC Act Section 19(b). CFPA 1055(a)(2) also lists two remedies that are not in 19(b): “limits on the activities or functions of the person” and “civil money penalties.” 12 U.S.C. 5565(a)(2). These two remedies appear to have been borrowed word-for-word from remedies available to the prudential banking regulators under the Federal Deposit Insurance Act. See 12 U.S.C 1818(b)(7) and (i).

The first part of the CFPA relief provision, CFPA 1055(a)(1), is roughly similar to the first sentence of FTC Act section 19(b), but the relief listed is distinct. To reiterate, CFPA 1055(a)(3)(1) states: “The court (or the Bureau, as the case may be) in an action or adjudication proceeding brought under Federal consumer financial law, shall have jurisdiction to grant *any appropriate legal or equitable relief* with respect to a violation of Federal consumer financial law.” 12 U.S.C. 5565(a)(1) (emphasis added). The first sentence of FTC Act section 19(b) states in relevant part: “The court in an action under subsection (a) shall have jurisdiction to grant *such relief as the court finds necessary to redress injury to consumers ...* resulting from the ... the unfair or deceptive act or practice, as the case may be.” 15 U.S.C. 57b(b) (emphasis added).

As a preliminary matter, it seems fair to conclude that the CFPA relief provision appears to provide the Bureau with authority to receive at least the remedies that the FTC may receive in cases brought under section 13(b) (the direct-litigation provision) and the remedies that the FTC may receive in cases brought under section 19 (the provision involving cease-and-desist orders with dishonesty or fraud). As described above, under FTC Act section 13(b), the FTC may receive a permanent injunction and therefore so-called “equitable relief.” Since the first part of the CFPA remedy provision provides that the Bureau may receive “any appropriate legal or equitable relief,” 12 U.S.C. 5565(a)(1), the Bureau should at least be able to receive equitable relief akin to what the FTC received under section 13(b) (as well as additional “legal” relief). Further, the second part of the CFPA relief

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

provision provides that the Bureau may receive all the remedies listed in FTC Act section 19.

That said, the Bureau is prohibited from receiving “exemplary or punitive” damages as the FTC is in FTC Act section 19.

e. FDCPA Remedies

The FDCPA remedy provision provides that “any debt collector who fails to comply with any provision of [the FDCPA] with respect to any person is liable to such person” for both “any actual damage sustained by such person as a result of such failure” and so-called statutory damages, i.e., “such additional damages as the court may allow, but not exceeding \$1,000.” 15 U.S.C. 1692k(a). (The statute has other rules for class actions. See 15 U.S.C. 1692k(a)(2)(B).) The FDCPA also provides that “in the case of any successful action to enforce the [FDCPA],” the court shall award “the costs of the action, together with a reasonable attorney’s fee as determined by the court.” 15 U.S.C. 1692k(a)(3).

ANALYSIS

This memorandum begins with the substantial injury question and then proceeds to the remedy question.

I. Substantial Injury

As a matter of common law, a creditor who did not have a security interest or other right of repossession of property could be sued for conversion if the creditor seized property to repay a defaulted debt. Consistent with this precedent, FTC Act caselaw indicates that consumers can be substantially injured by creditor conduct even if the consumer owes the debt. Similarly, consumers can bring claims (and receive damages) under the FDCPA notwithstanding that the consumer owes the debt.

a. Common law

At common law as codified in the Uniform Commercial Code, the mechanism by which a creditor ensures he can lawfully seize property upon a debtor’s default is the creation of a security interest in a contractual agreement. If the creditor seizes a consumer’s property upon default without such a valid security interest, the creditor would be liable to the debtor for the tort of conversion, notwithstanding that the debt is owed.

i. Conversion Generally

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

“Actions involving collection abuses . . . have traditionally been viewed as sounding in tort.” *Sibley v. Fulton DeKalb Collection Serv.*, 677 F.2d 830, 834 n.4 (11th Cir. 1982). In particular, “[c]onversion is the wrongful possession or disposition of another’s property as if it were one’s own.” 18 Am. Jur. 2d Conversion § 1; see also, e.g., C.J.S. Trover and Conversion § 1.

As relevant here, where the property taken was money, not physical property, the leading remedies treatise indicates:

As a result of purely formal considerations no longer of any great consequence, some of the common law courts took the position an action of trover [i.e. to recover damages] for conversion of money would not lie unless there was an obligation to return some specific pieces of gold or the like.

The common law rule is still occasionally repeated, though usually with substantial qualification. For the most part it is ignored altogether, and suits for “conversion” of money, and sometimes for conversion of even less tangible values, are entertained in the courts. Even where the conversion action was not entertained, plaintiff was not necessarily out of court; the ‘conversion’ label could be disregarded and the claim treated as a claim in assumpsit for money had and received. This means that in some jurisdictions plaintiff can simply recover on a conversion theory when money is improperly taken, while in others he can recover, but must do so on an assumpsit theory.

Dan B. Dobbs and Caprice L. Roberts, Law of Remedies § 6.1 (3rd ed. 2018) (footnotes omitted); see also 90 C.J.S. Trover and Conversion § 2 (“Trover is the technical name of the action to recover damages...”).³

Similarly, Corpus Juris Secundum indicates that “[m]oney may be the subject of conversion” but an action may not be brought “to enforce a mere obligation to pay money.” 90 C.J.S. Trover and Conversion § 16. This treatise indicates that in some courts, a conversion claim may generally be brought for money, whereas in other courts, a conversion claim may only be brought “where the money is specific and capable of identification.” *Id.*; see *id.* (“Although there is authority to the contrary [i.e., indicating that a money conversion claim can generally be brought], the general rule is that money is an intangible and therefore not subject to a claim for conversion. However, there is an exception where the money is specific and capable of identification....”) (footnotes omitted).

Specifically relevant to the facts at issue in the present matter, in which money was taken from a bank account without consumer authorization, under this

³ We have not researched recovery of money under the alternative assumpsit theory discussed in the Dobbs treatise, but could look into that further if that would be helpful.

doctrine, courts have found that “[m]oney in a bank account can properly be the subject of a conversion action when the account and amount are separate and ascertainable.” *Republic of Haiti v. Crown Charters, Inc.*, 667 F. Supp. 839, 845 (S.D. Fla. 1987). For example, in a case from an intermediate appellate court in Florida, the court considered an appeal of a finding of conversion where one owner of two jointly owned bank accounts withdrew money from the accounts without the other owner’s permission. *Allen v. Gordon*, 429 So. 2d 369, 370–71 (Fla. 1st Dist. App. 1983). The court rejected the argument that “the money in question could not be the subject of conversion,” finding that “[t]he two accounts involved here were separate ascertainable amounts and accounts,” so “[t]he money was, therefore, specific and identifiable.” *Id.* at 371.

In another example (from a higher court, albeit with less similar facts), the Supreme Court of South Carolina considered a conversion suit by a corporation against its former employee. *SSI Med. Services, Inc. v. Cox*, 392 S.E.2d 789, 791 (S.C. 1990). The employee had been responsible for disposing of leased cars used by the corporation at the end of the lease term. *Id.* Rather than returning the cars to the leasing companies, the employee had been selling the cars to third-parties, depositing the proceeds in his personal bank account, and paying the leasing companies what was owed to them for the cars, thereby pocketing the difference between the sale price and what was owed to the leasing companies. *Id.* When the corporation found out, it terminated the employee and sued him for conversion of the amount pocketed. *Id.* The Court affirmed a lower court’s grant of summary judgment to the corporation and expressly rejected the employee’s argument that “money may not be the subject of a conversion action.” *Id.* at 792. In so ruling, the court noted that the corporation “established a determinate amount of money that was converted” and “can also identify into which account these sums were deposited.” *Id.* at 792-93.⁴

ii. Seizure of Property to Pay Debts Without a Security Interest

Under the Uniform Commercial Code and at common law, a “secured party” is “a person in whose favor a security interest is created or provided for under a security agreement.” Unif. Commercial Code § 9-102(72). And “[a]fter default, a secured party” may “take possession of the collateral” either with or without “judicial process.” Unif. Commercial Code § 9-609. That is, if a consumer defaults on a debt and the creditor has a security interest in the consumer’s property, the creditor or his agent (e.g. a “repo man”) can lawfully seize the property to satisfy the defaulted debt, without going to court. See 68A Am. Jur. 2d Secured Transactions § 440 (describing that “a secured party” may “proceed first against the collateral by

⁴That said, it should be noted that, for the FTC Act “disgorgement does not require the district court to apply equitable tracing rules to identify specific funds in the defendant’s possession that are subject to return.” *F.T.C. v. Bronson Partners, LLC*, 654 F.3d 359, 373 (2d Cir. 2011).

Formatted: Normal, Indent: First line: 0"

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

repossessing it by self-help”) (footnotes omitted). The FTC’s Credit Practices Rule puts some limitations that are not relevant here on what security interests can be obtained in “household goods.” See 16 C.F.R. 444.2(a)(4).

At common law, “[a] creditor is liable for wrongful repossession upon the debtor’s default where the creditor takes possession of property that is not subject to its security interest.” 68A Am. Jur. 2d Secured Transactions § 490. And “a security interest cannot exist in the absence of a security agreement.” *Barnes v. N.W. Repossession, LLC*, 210 F. Supp. 3d 954, 962 (N.D. Ill. 2016) (quoting *Allis-Chalmers Corp. v. Staggs*, 453 N.E.2d 145, 148 (Ill. App. 1983)); see also, e.g., *Matter of Martin Grinding & Mach. Works, Inc.*, 793 F.2d 592, 594 (7th Cir. 1986) (relying on *Allis-Chalmers*). Accordingly, if a creditor has not obtained a security interest in a consumer’s property via a security agreement and yet nonetheless takes possession of a consumer’s property, that creditor would be liable for the tort of conversion.

Further, and importantly for present purposes, “indebtedness of the plaintiff to the defendant or the latter’s claim of such indebtedness is not a defense, or ground for mitigation of the damages, in a civil action for conversion of the plaintiff’s property by the defendant.” 100 A.L.R. 1376; see also 18 Am. Jur. 2d Conversion § 106 (“[T]he indebtedness of the plaintiff to the defendant, or the defendant’s claim of such indebtedness, is not a defense [to an action for conversion].”)

For example, in *Caldwell v. Carpenter*, 234 P. 767, 768 (Okla. 1925), the Supreme Court of Oklahoma considered the conversion claim of a blacksmith whose tools had been seized from his home during his absence. The Court noted that “there was no lien or mortgage against the property, although the plaintiff was indebted to the bank of which the defendant was cashier” and affirmed a jury’s award of damages for the value of the tools. *Id.* The same Court later specifically cited *Caldwell v. Carpenter* for the proposition that “the fact that owner was indebted to wrongdoer is no defense” to the “illegal taking or wrongful assuming of right to personal property[, which] constitutes conversion.” *Murrell v. Griswold*, 338 P.2d 150, 153 (Okla. 1959) (citing *Carpenter*).

Similarly, in *Caldwell v. Ryan*, 108 S.W. 533, 534 (Mo. 1908), the Supreme Court of Missouri considered a conversion claim by Robert Caldwell (not to be confused with the Oklahoman Jesse Caldwell from *Caldwell v. Carpenter*). Caldwell alleged his two mules had been improperly seized and sold by Ryan to satisfy a debt. *Id.* Caldwell conceded that he owed a debt to Ryan, but successfully contended that his mules were exempt from seizure “because he was the head of a family and had no other property.” *Id.* at 535. When Caldwell sued for conversion for the value of the mules, Ryan argued that Caldwell’s claim should be “offset” by the amount that Caldwell owed Ryan. *Id.* at 535 (“The defendant was insisting on having his debts, for which he already had two judgments, set off against whatever judgment the plaintiff might obtain against him....”). The Court rejected this contention, finding that “a debt could not be set off against a demand for damages arising in a tort.” *Id.* at 536. Accordingly, the Court ordered judgment for Caldwell in the amount of the cash value of the two mules. As discussed below in the remedy section, the Court nonetheless suggested that Ryan could thereafter proceed with recovery on his suit for the underlying debt.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

A related line of cases comes to a similar conclusion in the bankruptcy context. Many bankruptcy cases deal with the situation in which a debtor defaults on a debt and then a creditor “seizes [the] insolvent’s property without process or claim of lien and then claims right of setoff when sued by the [bankruptcy] trustee for conversion.” *In re Natl. Hydro-Vac Indus. Services, L.L.C.*, 314 B.R. 753, 766 (Bankr. E.D. Ark. 2004). In that context, “there is a line of cases which hold that a setoff should not be allowed” against the bankruptcy trustee’s conversion claim. *Brunswick Corp. v. Clements*, 424 F.2d 673, 676 (6th Cir. 1970); *see also id.* (collecting cases). These courts reason that the creditor who seizes the property in these circumstances “has attempted to convert its claim into a fully secured claim to the prejudice of other unsecured creditors in the case.” *In re Natl. Hydro-Vac*, 314 B.R. at 766. For present purposes, the interesting point raised by these cases is that when a creditor or debt collector illegally seizes a consumer’s property to pay a debt, the creditor/collector may be harming the consumer’s other creditors.

Further, though not exactly the subject of this memorandum, it may be helpful to note that courts historically held debt collectors liable on a tort theory of “invasion of privacy” for harassing consumers about debts. As one court stated: “[A] creditor has a right to take reasonable action to pursue his debtor and persuade payment, although the steps taken may result to a certain degree in the invasion of the debtor’s right of privacy, but that the debtor has a cause of action for injurious conduct on the part of the creditor which exceeds the bounds of reasonableness.” *Dawson v. Associates Fin. Services Co. of Kansas, Inc.*, 529 P.2d 104, 110 (Kan. 1974) (quotation marks omitted); *see also id.* (summarizing cases “sufficient to create this cause of action,” including a case involving “letters to employers coupled with frequent telephone calls” and a case involving “calls to the debtor’s neighbors calculated to annoy, embarrass and humiliate the debtor”). *See generally* Liability for improper collection methods, 15 A.L.R.2d 108 § 28. *But see* *Gouldman-Taber Pontiac, Inc. v. Zerbst*, 100 S.E.2d 881, 882–83 (Ga. 1957) (holding that “a letter written by a creditor to an employer notifying him that his employee is indebted to the creditor and seeking the employer’s aid in the collection of the debt . . . did not violate [the debtor’s] right of privacy”).

Likewise, the Restatement (Second) of Torts specifically notes that “collecting creditors have been held liable for extreme abuse of their position” but “have not been held liable for mere insults, indignities, or annoyances that are not extreme or outrageous.” Restatement (Second) of Torts § 46 (1965). It also provides a few examples involving harassing debt collection conduct.

b. FTC Act Caselaw

In perhaps the most relevant precedent, the FTC recently brought two cases against payday lenders for improperly taking consumer’s money to satisfy debts. In both cases, the lenders took the money by improperly garnishing consumers’ wages. These cases were both authorized by the FTC commissioners by a vote of 4-0, brought directly to litigation under FTC Act section 13, and litigated to decision in federal court. *See* FTC Charges Payday Lender with Deceiving Employers in Scheme

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

to Collect Debts (April 7, 2010), <https://www.ftc.gov/news-events/press-releases/2010/04/ftc-charges-payday-lender-deceiving-employers-scheme-collect>; FTC Charges Payday Lending Scheme with Piling Inflated Fees on Borrowers and Making Unlawful Threats when Collecting, <https://www.ftc.gov/news-events/press-releases/2012/04/ftc-charges-payday-lending-scheme-piling-inflated-fees-borrowers> (April 2, 2012). In both matters, the courts expressly rejected the defendants' argument that they did not injure consumers because they were only garnishing amounts that the consumers owed.

In *FTC v. LoanPointe*, the court considered FTC claims against a short-term, small dollar lender. *FTC v. LoanPointe, LLC*, 2011 WL 4348304, at *1 (D. Utah Sept. 16, 2011), *aff'd*, 525 Fed. Appx. 696 (10th Cir. 2013). LoanPointe's contracts with consumers indicated that the consumer "agree[d] to have my wages garnished to pay any delinquent amount on this loan." *Id.* Upon delinquency, LoanPointe "would inform consumers that their continued failure and refusal to repay loans would result in garnishment of their wages." *Id.* at *3. If consumers still failed to repay, LoanPointe would send a "garnishment package" to the consumer's employer, which stated: "One of your employees has been identified as owing a delinquent debt to [LoanPointe]. The Debt Collection Improvement Act of 1996 (DCIA) permits agencies to garnish the pay of individuals who owe such debt without first obtaining a court order. Enclosed is a Wage Garnishment Assignment directing you to withhold a portion of the employee's pay each period and to forward those amounts to [LoanPointe]." *Id.* at *2. About 20% of employers receiving the notice did indeed garnish consumers' wages and remit them to LoanPointe. *Id.* at *5.

The FTC sued LoanPointe under section 13 of the FTC Act, alleging that LoanPointe "violated the FTC Act by engaging in the following unfair or deceptive practices: misrepresenting to consumers' employers that they were authorized to garnish wages under the DCIA without a court order; misrepresenting to consumers' employers that they had notified consumers and given consumers an opportunity to dispute the debt prior to sending the garnishment request; and communicating with and disclosing the existence and amount of consumers' loans to consumers' employers without consumers' knowledge or consent." *Id.* at *3-4. (The FTC also alleged FDCPA and TSR claims.)

On summary judgment, the district court ruled for the FTC on each of the FTC Act claims. With respect to deception, the court noted that LoanPointe conceded that both the statement about its right to garnish funds without a court order and the statement about giving consumers a chance to dispute the debt were false. *Id.* at *4. The court rejected LoanPointe's contention that these statements could not be deceptive because they were directed to employers, rather than consumers themselves. *See id.* at *5. With respect to unfairness, the court relied on *American Financial Services Association v. FTC*, 767 F.2d 957, 974 (D.C. Cir. 1985) and related FTC findings that "wage assignment clauses and wage garnishment procedures cause substantial harm to consumers." 2011 WL 4348304, at *6. Noting the FTC's findings about "severe, substantial disruption of employment, the pressure that results from threats to file wage assignments, and the disruption of family finances," the court "conclude[d] that [LoanPointe's] practice of disclosing debts and the

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

amount of the debts to consumers' employers qualifies as an unfair practice under the FTC Act." *Id.* at *6.

Importantly for present purposes, the court noted the following argument from LoanPointe:

[LoanPointe] argue[s] that borrowers suffered no injury because any moneys they paid to Defendants were due and owing. Consumers who applied for payday loans with Defendants agreed to pay back the loan amount and interest at rates identified in the terms of repayment. Although the portion of the terms of repayment allowing Defendant to garnish the consumers' wages was inappropriate, there is no argument in this case that the other terms of repayment were misleading, deceptive, or inappropriate.

Id. at *11. The court rejected this argument, finding that "the garnishment letter violated federal law" and that LoanPointe's "violations should not allow [it] to profit more than other similar businesses who have complied with the law." *Id.* at *12. (The details of the remedy are discussed in the remedy section of this memorandum below.)

On appeal, LoanPointe argued, as relevant here, both that the district court's order was "improper due to the lack of evidence that any borrowers were actually misled by the violation" and that "the profit earned by means of the deceptive letters was not ill gotten because appellants did not collect any more tha[t] was not owed." 525 Fed. Appx. at 701 (quotation marks omitted).

With respect to the argument that consumers were not harmed because they owed the money collected, the Tenth Circuit stated that "[t]his rationale could be used to justify essentially any method of collecting debt since it ignores the harm that can flow from the act of collection itself." *Id.* The court also approvingly quoted this language from *Floersheim v. FTC*, 411 F.2d 874, 878 (9th Cir. 1969): "Petitioner contends there is no deception because deception requires injury, and here there is no injury because all the debtors owe the money. There is no merit in this contention. Deception itself is the evil the statute is designed to prevent." 525 Fed. Appx. at 700 n.2.

With respect to the argument about the lack of evidence of deception, the Tenth Circuit found that LoanPointe "misconstrue[d] the standard for liability under § 5 of the FTC Act." *Id.* The court indicated that "[t]he FTC does not need to prove actual deception, only the likelihood that a consumer (here, employers), acting reasonably under the circumstances, *would be* deceived." *Id.* The court held that the district court "properly applied this standard in reasoning that the letters were deceptive because an employer would likely be unfamiliar with the law governing debt collection and unable to verify the facts," so "[n]o further evidentiary basis was required." *Id.*

Similarly, in *FTC v. PayDay Financial, LLC*, a district court considered a variety of FTC claims, some of which were alleged FTC Act violations for improperly taking consumers' money to pay debts. 989 F. Supp. 2d 799 (D.S.D. 2013). As in *LoanPointe*,

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

"[w]hen a borrower whose loan agreement contained a wage assignment clause defaulted on the loan agreement and failed to work toward paying off the loan, [PayDay] on occasion sent a garnishment packet to the borrower's employer. *Id.* at 816. The packets indicated that Indian law "permit[s] agencies to garnish the pay of individuals who owe such debt without first obtaining a court order." *Id.* On summary judgment, the court held that these statements were deceptive because such garnishments were not actually lawful, noting that PayDay collected more than \$1 million from employers using the procedure. *Id.* at 817.

On the other hand, the court denied the FTC summary judgment on a related § 5 claim involving "communicat[ions] with borrowers' employers via written correspondence or over the telephone" that "concerned garnishment of the borrowers' wages ... after [PayDay] had sent the employers a garnishment packet." *Id.* at 817-18. The FTC alleged that these communications were unfair as "these communications took place without consumers' knowledge or consent and ... disclosed the existence and occasionally the amount of the consumers' debt." *Id.* at 818. The court denied summary judgment on the grounds that that there was insufficient evidence in the record about "what was said during the telephone conversations" and "a question of fact concerning whether the borrowers were aware that [PayDay] would be communicating with their employers or that the communications ... caused or were likely to cause substantial injury." *Id.*

We acknowledge that the FTC alleged in these cases that the improper garnishment of funds was a deceptive, rather than an unfair, act or practice, whereas the FTC alleged that the disclosure of the debt to consumers' employers by the garnishment was unfair. We nonetheless believe these decisions are instructive on the question of whether the unauthorized taking of money from the account of a consumer who owes a valid debt can constitute substantial injury.

Both the district court and the Tenth Circuit in *LoanPointe* specifically rejected the argument that "there is no injury because all the debtors owe the money." 525 Fed. Appx. at 700 n.2 (quoting *Floersheim*); see also 2011 WL 4348304, at *11 (rejecting argument that "borrowers suffered no injury because any moneys they paid to Defendants were due and owing"). Just as a textual matter, it is difficult to see how these statements about *injury* would not apply to the "substantial injury" component of an unfairness claim involving the improper seizure of consumers' funds by a creditor, notwithstanding that they were made in the context of deception in the seizure of consumers' funds by a creditor. That is particularly so because monetary harm is the paradigmatic form of "substantial injury." See FTC Policy Statement on Unfairness (Dec. 17, 1980) (noting that "[i]n most cases a substantial injury involves monetary harm").

And as explained further below, the courts made these statements in the context of awarding (and affirming an award of) disgorgement of the profit procured from consumers by the deceptive garnishments. The *LoanPointe* district court stated that its "equitable power may only be exercised over property that is causally related to the illegal actions of the defendant." 2011 WL 4348304, at *12. And the court found that the profit deceptively collected met this criterion – it was injury causally related to the deception. Notably, the courts did not suggest that the

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

deception created some separate compensable injury. Therefore, it is difficult for us to conclude that the deception creates a harm in itself that is somehow separate or independent from the money improperly taken from consumers.

c. *FDCPA caselaw*

Several Circuits have indicated that it is possible for a debt collector to violate the FDCPA – and for consumers to be awarded damages -- even when collecting an amount that the consumer owes. These courts have rejected the argument that an admission by the consumer that he or she owes the debt somehow undermines FDCPA liability. *See, e.g., Sykes v. Mel Harris and Associates, LLC*, 285 F.R.D. 279, 292 (S.D.N.Y. 2012) (“The various claims of the named plaintiffs as to the validity or existence of the underlying debts are not at issue here. Liability under the FDCPA can be established irrespective of whether the presumed debtor owes the debt in question.”); *Sykes v. Mel S. Harris and Associates LLC*, 780 F.3d 70, 83 (2d Cir. 2015) (affirming this specific conclusion and quoting *Baker v. G.C. Svcs. Corp.*, 677 F.2d 775, 777 (9th Cir. 1982) for the proposition that the FDCPA “is designed to protect consumers who have been victimized by unscrupulous debt collectors, regardless of whether a valid debt actually exists”).

That said, courts have found that consumers should not be able to recover FDCPA damages for payments on debts actually owed simply because the debt collector violated state law. *See, e.g., Moritz v. Daniel N. Gordon, P.C.*, 895 F. Supp. 2d 1097, 1116–17 (W.D. Wash. 2012) (“Other courts have found that plaintiffs are not injured in the amount collected when the plaintiff owed the debt even where the debt collector violated state law in doing so. . . . Based on these cases, the court concludes that Ms. Moritz cannot recover the amounts she paid to [the collector] because those amounts were less than the total amount she owed to [the creditor] on a valid debt.”). This is consistent with other FDCPA precedent indicating that violations of state law do not necessarily constitute FDCPA violations. *See Carlson v. First Revenue Assurance*, 359 F.3d 1015, 1018 (8th Cir. 2004); *Wade v. Regional Credit Association*, 87 F.3d 1098, 1100 (9th Cir. 1996); *Belser v. Blatt, Hasenmiller, Leibsker & Moore, LLC*, 480 F.3d 470, 473 (7th Cir. 2007).

~~The amount of recovery under the FDCPA for debt collection of amounts actually owed—and the related issue that the collector’s illegal conduct must cause the collector to make a payment for the consumer to recover that payment—is discussed below in the discussion of remedies because that is where it is discussed in the caselaw.~~

An argument might be made that the FDCPA is unhelpful in understanding the concept of “substantial injury” here because the FDCPA is focused on the “injury” caused by the illegal collection practices themselves (e.g., deceptive statements or harassing phone calls), rather than on the “injury” of having money go toward a valid debt. But such an argument would be difficult to reconcile with how courts have approached awarding “actual damages” under the FDCPA. As addressed further below in the remedies section, FDCPA caselaw suggests that “actual damages” are recoverable by the consumer for “monetary damage, emotional

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

distress or other injury that the debtor can prove the debt collector caused.” *Johnson v. Eaton*, 80 F.3d 148, 152 (5th Cir. 1996). In turn, courts have found that the amount that the debt collector improperly collected is appropriate as “actual damages,” even if those amounts are owed. This indicates that such amounts are injury. Consistent with that, FDCPA plaintiffs may recover both damages for the amount improperly collected and damages for other harm caused by the defendant’s conduct, as well as statutory damages for the violation itself. *See Hamid v. Stock & Grimes, LLP*, 876 F. Supp. 2d 500, 502-03 (E.D. Pa. 2012) (plaintiff could recover the amount paid to debt collector as damages and could also recover various other damages, including damages for mental distress and for “\$110 for two lost days of work as a result of her mental distress”). The ability of plaintiffs to recover money paid toward a valid debt, and not merely statutory damages or other forms of damages such as emotional distress or lost wages, indicates that payment of a valid debt can itself constitute an injury under the FDCPA.

d. Analysis and Conclusions

Based on our understanding of this precedent, we conclude that a consumer can be substantially injured when a creditor or debt collector improperly takes money from a consumer, even if the consumer owes a valid debt. At common law, a creditor who took a debtor’s property in these circumstances would be liable for the tort of conversion; FTC Act caselaw in the debt collection context suggests that there is substantial injury; and FDCPA caselaw suggests that there is compensable injury due to the finding that actual damages are warranted. We see little reason to believe that a different conclusion would be warranted under the CFPA. In particular, because the FTC Act standard for unfairness and deception is so similar to the CFPA standard, we find little basis for concluding that this conduct would be a UDAP but not a UDAAP. Further, the common law and FDCPA precedent suggests that this would be a relatively ordinary conclusion for a court to draw in the tort context. Indeed, it seems that the contrary conclusion would find little basis in precedent.

II. Remedy

At common law, if a creditor without a security interest in the consumer’s property seized that property to satisfy a debt, the consumer would be able to recover the full value of the seized property as damages in a conversion suit, without “set-off” of the amount of the debt. That said, the consumer would still owe the debt, and the creditor could collect on the debt using lawful means.

The FTC at least theoretically has different remedies available depending on whether a case is brought under section 13 (the direct liability provision) or section 19 (the cease-and-desist with dishonesty and fraud provision). There also appear to be differences in different Circuits as to what remedy the FTC may receive under section 13. Under section 13, the FTC can at least get the equitable remedy of disgorgement, and in some Circuits, can get full restitution for consumer harm. Under section 19, the FTC can get consumer redress in the form of damages paid to

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

consumers. As noted above, the CFPB gives the Bureau the ability to get at least the remedies that the FTC can get under either section 13 or section 19. The caselaw under either provision requires a causal link between the defendant's actions and the remedy.

In the two recent debt collection cases referenced above that the FTC brought under FTC Act section 13, the FTC sought and received the equitable remedy of restitution (specifically, disgorgement), which in these cases meant interest and fees but not principal were paid by the defendants to the FTC, which it could then distribute to consumers as redress to the extent harmed consumers could be identified, with any remainder going to the Treasury.

The voluminous FDCPA caselaw includes many cases in which actual damages were awarded to consumers. This caselaw includes precedent that specifically addresses the fact that consumers did owe the debts in question, and indicates that damages can be awarded to return amounts that consumers actually owed so long as the consumer shows causation between the collector's illegal conduct and the payment. But the FDCPA violation does not extinguish the underlying debt.

It is generally up to the plaintiff to elect which of the available remedies is sought.

a. Overview of Remedies Doctrine and the Common Law

1. Relevant Overview on Remedies

The leading treatise on remedies describes "four major categories" of remedies: "(1) damages remedies, (2) restitutionary remedies, (3) coercive remedies such as injunctions, [and] (4) declaratory remedies." Dan B. Dobbs and Caprice L. Roberts, *Law of Remedies* § 1.1 (3rd ed. 2018). The treatise indicates that "[d]amages was historically a legal remedy," the injunction was "equitable," and restitution and declaratory relief could be either legal or equitable. *See* *Law of Remedies* § 1.2; *see also* *Great-W. Life & Annuity Ins. Co. v. Knudson*, 534 U.S. 204, 215 (2002) (describing distinctions).

It should be noted at the outset – as both the treatise and the Supreme Court have noted – that courts may not be particularly careful about using the correct label for a particular type of remedy in contexts in which the distinctions between types of remedies would not affect the outcome. As the treatise indicates: "The reader of restitutionary material is always challenged by its archaic terminology and by loose usage to analyze cases by their content rather than their terms." *Law of Remedies* § 1.1; *see also* *Great-W. Life*, 534 U.S. at 214-15 ("Admittedly, our cases have not previously drawn this fine distinction between restitution at law and restitution in equity, but neither have they involved an issue to which the distinction was relevant.").

The treatise indicates that, in addition to the availability of a jury trial, the only modern significance to the distinction between law and equity is that "when a plaintiff asserts an equitable remedy, equitable defenses can be invoked even if they

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

could not be invoked against a 'legal' claim." Law of Remedies § 2.1. This difference is discussed below.

"[Restitutionary] remedies include, for example, monetary restitution, constructive trust, equitable lien, and disgorgement." *Id.* § 4.1. Confusingly, as this statement suggests, the word "restitution" includes both "disgorgement" and "monetary restitution." *See also Kokesh v. SEC*, 137 S. Ct. 1635, 1640 (2017) ("Generally, disgorgement is a form of restitution." (quotation marks omitted)). As discussed further below, "monetary restitution" (or "redress") in this context typically means returning money to consumers, while "disgorgement" in this context generally means turning over money to the government, regardless of where that money ultimately ends up going. *See* Law of Remedies § 1.1 ("Although an award of restitution may in fact provide compensation for plaintiff in some cases, the restitutionary goal is distinct. The restitutionary goal is to prevent unjust enrichment of defendant by making him give up what he wrongfully obtained from plaintiff.").

One notable difference between damages and restitution is that "damages is measured by plaintiff's loss; restitution is measured by defendant's unjust gains." Law of Remedies § 3.1; *see also id.* § 1.1. Accordingly, "[r]estitution measures the remedy by defendant's gain and seeks to force disgorgement of that gain. It differs in its goal or principle from damages, which measures the remedy by plaintiff's loss and seeks to provide compensation for that loss." Law of Remedies § 4.1.

It should be noted that this memorandum assumes that the claims the Bureau might bring against a creditor or debt collector could ultimately be brought in a forum in which the defendant could request a jury trial, such as federal district court. We have checked with Enforcement about the present matter that the Bureau is considering, and it would indeed likely be litigated in federal district court (if it is not settled). This also seems like a reasonable assumption generally, since the Bureau can typically bring UDAAP claims in federal court. *See* 12. U.S.C. 5564(a) ("If any person violates a Federal consumer financial law, the Bureau may, subject to [the restrictions for banks of certain sizes], commence a civil action against such person to impose a civil penalty or to seek all appropriate legal and equitable relief...."). Of course, the Bureau will as a practical matter often be settling claims or handling them in Supervision. So a jury trial is not actually going to happen on many of these claims. But the point is that a jury trial would typically be available were these claims ultimately to end up in litigation. If, by contrast, for some reason the Bureau would only be able to bring a claim in a forum without a jury trial (such as an administrative adjudication), it is possible that the remedy in that situation would be restricted to equitable remedies, which might not include "damages." Since that situation would not be the norm, this memorandum does not consider it further, and more thinking would need to be done about that issue if it were to arise.

2. *Common Law Remedies Involving Debt Collection*

i. *Conversion and Damages*

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

As noted above, when a creditor seizes a consumer's property without a security interest, even to satisfy a valid debt, the consumer would likely have a claim under the common law tort of conversion. "Conversion damages are intended to compensate the wronged party for a loss sustained because property was wrongfully taken. Thus, the primary principle to be applied in awarding damages for loss of property through conversion is that the owner should be compensated for the actual loss sustained." 18 Am. Jur. 2d Conversion § 116 (footnotes omitted).

Equitable defenses would not be available in a suit for conversion, since "[a]lthough in some respects an action for conversion has been regarded as partaking of the nature of a suit in equity, or as an action in which the court is competent to investigate and determine the equity of the case, it has been stated to be strictly a legal action." 18 Am. Jur. 2d Conversion § 64 (footnotes omitted). Especially relevant here, "[i]t is a general rule that the mere fact that the defendant has credited the value of the property to an indebtedness of the plaintiff to the defendant is not ground for mitigation of damages in an action for conversion . . ." 18 Am. Jur. 2d Conversion § 138.

The two cases cited above, *Caldwell v. Ryan* and *Caldwell v. Carpenter*, both demonstrate this principle. In *Caldwell v. Carpenter*, 234 P. 767, 768 (Okla. 1925), the Supreme Court of Oklahoma awarded the blacksmith the full value of his converted tools, without any set-off for the amount that the smith owed to the employer of the person who stole the tools. Similarly, in *Caldwell v. Ryan*, the Supreme Court of Missouri affirmed an award of damages in the full amount of the value of the two converted mules and expressly rejected the argument that the damages award should be set-off against existing debts. 108 S.W. 533, 536 (Mo. 1908) ("[A] debt could not be set off against a demand for damages arising in a tort."); see also *id.* at 538 (Lamm, J., dissenting) ("I agree [with the majority] that... [i]f A. sues B. for damages for assault and battery, B. may not by answer set off a promissory note or a judgment debt against A.'s claim for the tort.").

The Court in *Ryan* distinguished this situation, when the debtor has a tort claim and the creditor has a countervailing contract claim, from situations in which the plaintiff and the defendant each have contract claims against each other. The Court indicated that setting off a contract claim against another contract claim would be appropriate, but setting off a contract claim against a tort claim is not. See *id.* at 535-36 "[W]hen the parties are mutually indebted, one debt may be set off against the other, ... but the demands must come under the classification of debts A demand of damages for a tort is not a debt, and is not embraced in the statute of set-off.). Courts have ruled similarly in the bankruptcy context: when evaluating conversion claims. See, e.g., *Brunswick Corp. v. Clements*, 424 F.2d 673, 676 (6th Cir. 1970) ("[L]iability for willful conversion may not be setoff against monies owing the converter by the bankrupt."). But see id. (noting "a split of authority" on set off of other types of tort claims against contract claims)."; see also *Collier on Bankruptcy*

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

¶ 553.04 (“If the creditor’s liability to the debtor is based upon the willful conversion of the debtor’s property, courts have also denied setoff.”)⁵.

The Court in *Caldwell v. Ryan* also specifically indicated that the creditor’s unlawful conversion of the debtor’s property did not extinguish the debtor’s existing debt, and so the creditor could still proceed to enforce a judgment against the debtor on that existing debt. Indeed, the Court partially reversed the lower court on these grounds. The Court found that the judgment below would have been proper if the lower court “would have left the plaintiff with his judgment, and the defendant with his, and each entitled to sue out execution.” 108 S.W. at 536. However, the lower court instead seemed to indicate that the debtor could collect on his judgment without the creditor being able to sue on the underlying debt, “leav[ing] the defendant without recourse for the debt due him.” *Id.* To the contrary, the Court held that the debtor “may sue out execution on his judgment, and the [creditor] may likewise have execution on his.” *Id.*

In a case with more complicated facts, a California appellate court similarly found that “in conversion cases, a defendant generally cannot diminish the amount of damages by paying a debt of the injured party without the latter’s consent.” *Dakota Gardens Apt. Inv’rs B v. Pudwill*, 142 Cal. Rptr. 126, 129 (Cal. App. 5th Dist. 1977). That court stated:

To allow mitigation by application of the converted property to the benefit of the injured party would result in the converter dictating to the owner how the owner’s property is to be used. Such a result would seriously weaken the concept of property ownership because a defendant would not be penalized for interfering with another person’s possessions if the ultimate offset of the interference resulted in a benefit to that person.

The language of the Michigan Supreme Court asserted over 100 years ago is still viable today. That court said in *Northrup v. McGill*, [27 Mich. 234, 240 (1873)]: “In general, when there is no fraud, and when the law does not forbid, a man may dispose of his own property according to his own ideas of propriety. If he is indebted by note to different parties, he may apply his property to the payment of one, and refuse to apply it to the payment of another, and he may lawfully discriminate in this way, though in doing so he ignores the stronger moral claim resting upon him. This results from the supreme dominion which is involved in the absolute ownership of property.”

⁵ Collier notes that under the current Bankruptcy Code, eligibility for set-off generally does not turn on the character of the obligation (e.g., contract or tort). That general rule is subject to several exceptions, including the exception for conversion claims. See Collier on Bankruptcy ¶ 553.04 (“[U]nder [11 U.S.C. § 553(a)], a contract claim may be offset against a tort claim, and a statutory claim may be offset against an obligation arising in equity. There are several exceptions to this rule: penalty claims; certain claims for intentional misconduct; and exempt debts are not subject to setoff against other types of claims under section 553(a).”).

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

A contrary view would result in gross abuses and allow officious intermeddlers to determine payment priorities which are best left to debtors.

Id.

The court also cited to the Restatement (Second) of Torts. That Restatement states in relevant part:

A tortfeasor cannot diminish the amount of recovery by paying a debt of the injured person without the latter's consent, unless (a) the damages recoverable against the tortfeasor would include the amount of the debt, or (b) the payment of the debt was made unofficiously from the proceeds of the property of the injured person for the value of which suit is brought....

Comment on Clause (a): When the defendant's tort causes the plaintiff to be liable to a third person (see § 871A), the tortfeasor can terminate all but consequential damages by payment of the claim....

Comment on Clause (b): The rule stated in this Clause is particularly applicable to a sheriff or other officer who, by mistake of law or fact, has made an improper levy upon goods of a debtor and who before he has discovered the mistake, pays some or all of the debt from the proceeds of the sale made under the levy. (See Illustration 4). It applies also to a person who, without authority, takes the goods of a deceased person and without administration, pays his debts. (See Illustration 5). The rule does not apply when the payment was made in bad faith nor when it would defeat some policy of the law. (See Illustration 6). *Nor does the rule permit a creditor who has improperly seized his debtor's goods to have the damages for the conversion diminished by the amount of the debt.*"

Restatement (Second) of Torts § 923 (emphasis added).

It should be noted that the Comment on Clause (a), as well as its illustrations, clarify that the situation being contemplated by Clause (a) is when the *tort itself* causes the creation of a debt to a third party. It is that situation in which the "damages recoverable against the tortfeasor would include the amount of the debt." *Id.*; see also Restatement (Second) of Torts § 871A (describing tort liability for creation of debt to a third party). Clause (a) indicates that the tortfeasor in that situation can just pay off the debt, rather than paying the amount of the debt in damages. For example, one of the illustrations is: "A negligently injures B, who is treated by C, a physician. A pays C's charges. B's damages against A are diminished." *Id.* (illustration 3). That is not the situation considered in this memorandum; here, there is an existing debt owed to the creditor/collector before the collection activity, not a new debt created by the collection activity itself. That this is true is confirmed by the Comment on Clause (b), which clearly indicates that the rule does not "permit a creditor who has improperly seized his debtor's

goods to have the damages for the conversion diminished by the amount of the debt." *Id.*

ii. *Restitution*

By contrast, as noted above, one feature of equitable restitution is that equitable defenses may be available. For example, the Restatement (Third) of Restitution and Unjust Enrichment ("Third Restatement") states that "[e]ven if the claimant has conferred a benefit that results in the unjust enrichment of the recipient when viewed in isolation, the recipient may defend by showing that some or all of the benefit conferred did not unjustly enrich the recipient when the challenged transaction is viewed in the context of the parties' further obligations to each other." Third Restatement (Third) of Restitution and Unjust Enrichment § 62. The Third Restatement continues:

Comment.... *The baseline of unjust enrichment.* The standard application of § 62 is to a case in which a payment by the claimant, viewed in isolation, creates unjust enrichment of the recipient and a prima facie right to recovery in restitution. Examples include payments by mistake, payments under duress, and payments under illegal contracts. The defendant answers that the question of unjust enrichment between the parties can only be judged in light of the further relations between them. The baseline from which unjust enrichment is measured, in other words, is not the moment before the challenged payment but a point preceding other transactions between them....

[Illustration 2:] A owes B \$5000. Intending to pay C, another creditor, A sends \$5000 to B who accepts the payment despite notice of A's mistake. (B's notice of A's mistake means that B is not entitled to defend as a bona fide payee by the rule of § 67.) A has a prima facie claim to restitution of the mistaken payment (§ 6), but B is not unjustly enriched by A's unintended payment of a valid debt. B is not liable to A in restitution.

Id. Another provision of the Third Restatement notes that the remedy of restitution does not displace remedies that may be available in tort:

Conscious interference with property rights of any kind, with contractual expectations, or with other interests to which the law of torts extends a similar protection, will support the claim in restitution described in this section. Because defendants in such cases are alternatively liable for damages in tort, restitution is significant in those cases where the benefits wrongfully obtained exceed the provable injury to the claimant.

Third Restatement § 44 comment b.

Formatted: Font: Not Italic, Font color: Black

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

The Third Restatement was published in 2011, and Section 62 does not appear to have been cited in any case available on Westlaw. Section 62 is based on Sections 60 and 61 in the Restatement (First) of Restitution (1937) ("First Restatement"), and Illustration 2 cited above was based on Illustration 4 in Section 60 in the First Restatement.⁶ Section 60 provides that "[a] person who has performed a duty owed to another, enforceable at law or in equity, is not entitled to restitution from the other for such performance, although the performance was induced by mistake or by the fraud of the other." First Restatement § 60. Like the Third Restatement, the First Restatement notes that the remedy of restitution does not displace tort remedies:

The rule stated in this Section gives only the result with reference to restitution. This Section does not deal with the procedure by which the transferee is entitled to make the defense; nor does it deal with the liability in tort which may arise from acts improperly done in obtaining performance.

Id. § 60 comment a.

In the debt collection context, a similar-sounding doctrine that is sometimes mentioned is the so-called "voluntary payment doctrine." The essence of this doctrine is that if a person voluntarily makes a payment on an alleged debt knowing that it is possible that he does not actually owe the money, the person cannot later bring a claim to recover the payment if it turns out that indeed he did not owe the debt. See Third Restatement (Third) of Restitution and Unjust Enrichment § 6 (describing voluntary payment rule as "money voluntarily paid in the face of a recognized uncertainty as to the existence or extent of the payor's obligation to the recipient may not be recovered"). Because this doctrine is about circumstances in which money is not actually owed, it is not relevant to this memorandum, which is about circumstances in which a creditor or collector improperly collects money that is owed. See *id.* (describing doctrine as being about "[m]istaken payment of money not due" or "a payment in excess of an underlying liability").

To wit, in the debt collection context, courts have rejected the voluntary payment doctrine's application to amounts improperly collected but actually owed. The case of *Hamid v. Stock & Grimes, LLP*, 876 F. Supp. 2d 502 (E.D. Pa. 2012) is one example and is discussed below.

b. Choice Among Remedies

The leading remedies treatise indicates that the plaintiff will generally be able to choose among available remedies, subject to some constraints, and can receive multiple remedies. The treatise states:

⁶The Second Restatement was drafted but abandoned.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

Availability of specific remedies depends much on the facts of the case. Plaintiff who suffers personal injury will have little use for an injunction. In many instances, however, plaintiff will be given a choice among remedies, for instance, a choice between rescission and damages. At other times, courts may limit plaintiff's remedy to damages even if plaintiff would benefit by and would prefer a coercive remedy such as specific performance. This reflects a general preference in the courts for the damages remedy, but in spite of that preference, coercive remedies are widely available. In some instances, plaintiffs can have more than one remedy so long as the total does not provide more than one complete compensation or one complete restitution. In the same way, plaintiff can have more than one measure of damages so long as the elements do not duplicate one another.... Frequently, plaintiff will have a choice between damages or restitution....

Law of Remedies § 1.1. The treatise continues:

Plaintiff's choice of remedy is of course governed by her own interests in maximum recovery or in strategy for trial and settlement. The public interest, however, is not necessarily to maximize plaintiff's recovery or her strategic position. How should a judge choose between two or more potential remedies, each of which provides an acceptable match for plaintiff's right? Where all the available remedies are approximately equivalent in effect upon both to plaintiff and to defendant, and none imposes special costs upon the court or the public, plaintiff's choice of remedy should be respected. This is not to say that all remedies should be equally available. Policy or traditions may dictate a rule against specific performance of many contracts, and when it does, plaintiff is left only to her damages remedy. When specific performance is an available option, however, plaintiff's preference for or against that remedy should be and usually is respected if it imposes no special costs upon the court, the public, or defendant. Very difficult remedial decisions must be made when two or more remedies will each provide appropriate redress of plaintiff's entitlement, but one of them will entail onerous costs to defendant or economic waste. In general, we wish to fully redress plaintiff's rights, but at the same time we wish to count the costs.

Law of Remedies *Id.* § 1.7 (footnotes omitted).

Finally, as on the point about how the costs to the defendant are typically evaluated where two remedies are available, the treatise further elaborates:

To impose a remedy is to impose costs and to create benefits. Any remedy, including injunctive and other non-money remedies, will impose costs upon defendant. Any effective remedy will also create

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

benefits for plaintiff. Remedies may also impose costs upon or provide benefits for third persons or the public. In choosing between two remedies (or two measures of a single remedy), courts usually attempt to choose a remedy that will approximately vindicate plaintiff's right. But costs and benefits of a remedy must also be considered. A remedy that costs more than the benefit it provides may be an inefficient means of vindicating plaintiff's right. Because rights are more important than efficiencies in some cases, a costly, inefficient remedy is not necessarily "wrong." But judges will want to consider the alternatives before inflicting a remedy that costs more to defendant than it is worth to plaintiff. So counting costs and benefits of remedies is worthwhile.

Id. § 1.9 (footnotes omitted). For example, the Restatement (Second) of Contracts states:

[I]f the performance is defective as distinguished from incomplete, ... [the plaintiff] can usually recover damages based on the cost to remedy the defects. Even if this gives him a recovery somewhat in excess of the loss in value to him, it is better that he receive a small windfall than that he be undercompensated by being limited to the resulting diminution in the market price of his property. Sometimes, however, such a large part of the cost to remedy the defects consists of the cost to undo what has been improperly done that the cost to remedy the defects will be clearly disproportionate to the probable loss in value to the injured party. Damages based on the cost to remedy the defects would then give the injured party a recovery greatly in excess of the loss in value to him and result in a substantial windfall. Such an award will not be made. It is sometimes said that the award would involve "economic waste," but this is a misleading expression since an injured party will not, even if awarded an excessive amount of damages, usually pay to have the defects remedied if to do so will cost him more than the resulting increase in value to him. If an award based on the cost to remedy the defects would clearly be excessive and the injured party does not prove the actual loss in value to him, damages will be based instead on the difference between the market price that the property would have had without the defects and the market price of the property with the defects. This diminution in market price is the least possible loss in value to the injured party, since he could always sell the property on the market even if it had no special value to him.

Restatement (Second) of Contracts § 348 (1981); see also, e.g., Measure of contractor's recovery, 24 Williston on Contracts § 66:14 (4th ed.) (similar).

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

As specifically relevant here, the treatise indicates that with respect to conversion, “[t]he option is with plaintiff: he may sue for ordinary tort damages if that suits him, but he may obtain restitution of the proceeds if he prefers, as he presumably would when the tortfeasor’s gain exceeds plaintiff’s loss.” *Id.* § 5.17.

We are not aware of any application by courts of these “cost” principles to damages in the debt collection context. We nonetheless think these remedy principles support the monetary relief contemplated in the Enforcement action under consideration—which, as noted above, would involve the return of money taken without authorization from consumers’ accounts, but would not bar the creditor from seeking to collect that amount using legal means. The amounts that consumers would receive would “approximately vindicate plaintiff’s right”—because they would be equivalent to the amounts improperly taken. Law of Remedies § 1.7. By contrast, the alternative choice—providing no monetary relief to consumers—would not provide those consumers any benefit.⁷ Further, the amounts provided to consumers would not constitute a windfall, since the creditor could still seek to collect the amount using legal means. And while we aren’t very familiar with the facts in the case, it is hard to imagine that would be excessively costly to implement a plan to return the funds that were improperly taken.

c. *FTC Act*

1. *FTC Act Remedies Overview*

As described above, the FTC Act authorizes the FTC to bring direct litigation cases under FTC Act section 13 and in those cases to receive injunctions, which courts have found to include other forms of equitable relief. By contrast, FTC Act section 19 authorizes, among other things, damages.

Consistent with the distinction between law and equity described above and the textual differences between section 13 and section 19, FTC Act caselaw involving section 13 refers to “restitution” (the equitable remedy), whereas the caselaw involving section 19 refers to “damages.” *See, e.g., FTC v. Verity Int’l, Ltd.*, 443 F.3d 48 (2d Cir. 2006) (restitution under section 13); *FTC v. Publishers Bus. Services, Inc.*, 540 Fed. Appx. 555, 556–57 (9th Cir. 2013) (same); *FTC v. Security Rare Coin & Bullion Corp.*, 931 F.2d 1312, 1316 (8th Cir. 1991) (same); *FTC v. Figgie Int’l, Inc.*, 994 F.2d 595 (9th Cir. 1993) (per curiam) (damages under section 19). And indeed, the FTC Act caselaw described below sometimes relies on the distinction between damages and restitution.

Consistent with the legislative history cited above, courts often state that the FTC Act allows the FTC to seek redress “on behalf of” consumers. Relevant for present purposes, courts have sometimes specifically suggested that the FTC should be able to get the remedies that would be available to consumers. For example, in

⁷ Of course, the Bureau could still seek other forms of relief that may provide other benefits, such as injunctive relief and civil money penalties.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

FTC v. Kuykendall, the en banc Tenth Circuit considered whether the FTC is “authorized to seek sanctions on behalf of consumers in a compensatory civil contempt proceeding.” 371 F.3d 745, 763-64 (10th Cir. 2004) (en banc). The court cited section 13 for the proposition that “[t]he FTC Act explicitly authorizes the Commission to seek injunctions.” *Id.* at 764 (citing 15 U.S.C. 53). Then the court reasoned: “Violation of a permanent injunction has traditionally sounded in contempt, and no reason exists to believe Congress intended to withhold the traditional remedy of compensation to those consumers victimized by the defendants’ violations of the Permanent Injunction. Accordingly, after proving a violation of the Permanent Injunction, the FTC was allowed to seek sanctions on behalf of injured consumers.” *Id.* at 764 (citations omitted).

2. *Restitution Under Section 13*

FTC Act case law under section 13 reflects the distinction between equitable restitution and damages, though there is a related split among the Circuits.

In *FTC v. Verity*, the Second Circuit reversed a district court’s restitution award in a case brought by the FTC under section 13. The court noted that the defendants there had not received all the money unlawfully paid by consumers; in that case, third parties “received some fraction of the money paid by consumers before any payments were made to the defendants.” 443 F.3d at 67. The court held that the appropriate amount of restitution was only the amount that the defendants had actually taken in -- “the benefit unjustly received by the defendants.” *Id.* Yet the district court instead had “measured the appropriate amount of restitution as the full amount lost by consumers,” which was more than the defendants had received (because the third parties first took some of the money). *Id.* The Second Circuit found this to be “error.” 443 F.3d at 67.

By contrast, at least the Ninth Circuit has disagreed with *Verity* and found that “[e]quity may require a defendant to restore his victims to the status quo where the loss suffered is greater than the defendant’s unjust enrichment.” *FTC v. Stefanichik*, 559 F.3d 924, 931 (9th Cir. 2009); see *FTC v. Publishers Bus. Services, Inc.*, 540 Fed. Appx. 555, 556–57 (9th Cir. 2013) (noting disagreement with *Verity*). Accordingly, the Ninth Circuit has, in a section 13 case, “held that the FTC Act permits restitution measured by the loss to consumers.” *Publishers Bus. Services, Inc.*, 540 Fed. Appx. at 556–57. In these Circuits, it appears that a defendant can be required to make consumers whole for the full amount that consumers lost, even if the defendant never received that amount of money.

That said, the disagreement between the Circuits may not be as great as it seems because of an important distinction with respect to restitution -- between a defendant’s gains (also known as “revenue”) and a defendant’s profits. The defendant’s gains/revenue is the total amount of money that the defendant takes in, whereas the defendant’s profits is the total amount taken in minus costs. The Circuits agree that, in a section 13 case, the proper measure of restitution is gains, not profits – that is, “it is well established that defendants in a disgorgement action

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

are not entitled to deduct costs associated with committing their illegal acts.” *FTC v. Bronson Partners, LLC*, 654 F.3d 359, 375 (2d Cir. 2011).

Accordingly, for example, in the *Verity* case, the defendants were not required to disgorge money “that never reached them,” but with respect to the money they did receive, the defendants were not allowed to deduct expenses. *Bronson*, 654 F.3d at 375 (describing *Verity*); see also, e.g., *FTC v. Washington Data Resources, Inc.*, 704 F.3d 1323, 1327 (11th Cir. 2013) (citing *FTC v. Direct Mkg. Concepts Inc.*, 624 F.3d 1, 14–16 (1st Cir. 2010); *FTC v. Febre*, 128 F.3d 530, 536 (7th Cir. 1997)). So, while the Circuits may have some disagreement about what happens with respect to money that the defendant never touches but that consumers lost, the Circuits agree that all the money that the defendant touches is fair game for restitution, even if that amount of money is more than the defendant actually profited from the scheme, once costs are considered.

In so ruling in *Verity*, the Second Circuit drew a distinction that could conceivably be relevant for the present situation faced by the Bureau. The court stated: “Undeniably, in many cases in which the FTC seeks restitution, the defendant’s gain will be equal to the consumer’s loss because the consumer buys goods or services directly from the defendant. Thus, in these cases it is not inaccurate to say that restitution is measured by the consumer’s loss. But it is incorrect to generalize this shorthand and apply it as a principle in cases where the two amounts differ.” 443 F.3d at 67. In the present case faced by the Bureau, the alleged misconduct is not with respect to the initial sale of goods or services, but rather with respect to later collection conduct. In this situation, there could, arguably, be reason to conclude that the consumer’s loss is the full amount improperly taken during collection, but that this differs from the amount of the creditor’s unjust enrichment, since the creditor did provide an initial legitimate service to the consumer for which he is owed a debt. This idea is discussed further below.

Courts have approved of restitution in section 13 in the form of both “monetary restitution” (returning money to consumers, also known as “redress”) and “disgorgement” (turning money over to the government). In *FTC v. Gem Merchandising Corp.*, 87 F.3d 466, 467 (11th Cir. 1996), the court upheld a district court’s order to reimburse 5,000 consumers approximately \$100 each “and, to the extent repayment is not feasible, [to] pay the remainder to the United States Treasury.” *Id.*; see also *id.* n.1. The court found that disgorgement, “the purpose of which is not to compensate the victims of fraud, but to deprive the wrongdoer of his ill-gotten gain, is appropriate” under the court’s equitable powers. *Id.* at 470 (quotation marks omitted). Other Circuits have ruled similarly where “it would be impossible or impracticable to locate and reimburse all of the consumers who have been injured.” *FTC v. Pantron I Corp.*, 33 F.3d 1088, 1103 n. 34 (9th Cir. 1994).

3. Remedies Under Section 19

There are many fewer cases under FTC Act section 19, with the leading case on remedies being *FTC v. Figgie Intern., Inc.*, 994 F.2d 595 (9th Cir. 1993). This

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

memorandum will discuss *Figgie* and one other case, *FTC v. AMREP Corp.*, 705 F. Supp. 119 (S.D.N.Y. 1988). The other cases litigated to decision under FTC Act section 19 do not appear to address the issue of remedy. See *FTC v. S.W. Sunsites, Inc.*, 1988 WL 94519 (C.D. Cal. Apr. 5, 1988) (addressing dispute among defendants about indemnification and related issues); *FTC v. Macmillan, Inc.*, 1983 WL 1858, at *6 (N.D. Ill. July 29, 1983) (holding that the FTC failed to establish “dishonesty or fraud”); *FTC v. Turner*, 1982 WL 1947, at *3 (M.D. Fla. Dec. 29, 1982) (finding liability but reserving decision on “the amount and type of redress appropriate”).

In *Figgie*, the FTC entered a cease-and-desist order against a seller of fire safety devices that misled consumers about the effectiveness of the devices, and then went to district court for redress under section 19, alleging that “the defendant’s practices were dishonest or fraudulent,” as required for section 19 remedies. *Figgie*, 994 F.2d at 603-604. The court agreed and ordered the defendant to pay consumer redress – a minimum of \$7,590,000, “the amount of its profits,” and up to \$49,950,000, “the amount spent by consumers.” *Id.* at 605. Between these amounts, the exact amount the defendant would ultimately be required to pay would depend on claims made by consumers, who could claim the total amount that they paid for the device plus interest. *Id.*

On appeal, the defendant challenged the district court’s order on various grounds that may be relevant for present purposes. First, the defendant argued that “only those consumers that can prove that they purchased [the] heat detector in reliance on [deceptive] statements should be entitled to redress.” *Id.* at 606. The court rejected this argument as a matter of fact and law. With respect to the law, the court found that “[a] presumption of actual reliance arises once the Commission has proved that the defendant made material misrepresentations, that they were widely disseminated, and that consumers purchased the defendant’s product.” *Id.* Accordingly, because the defendant “presented no evidence to rebut the presumption of reliance, injury to consumers has been established.” *Id.*; see also, e.g., *Kuykendall*, 371 F.3d 745, 765 (10th Cir. 2004) (en banc) (“[G]ross receipts are an appropriate measure of actual loss because a presumption of consumer reliance arises when the FTC shows that the misrepresentations or omissions were of a kind usually relied upon by reasonable and prudent persons, that they were widely disseminated, and that the injured consumers actually purchased the defendants’ products.” (quotation marks omitted)).

Second, the defendant argued that consumers should not receive the full amount that they paid for the devices because, the defendant argued, “th[e] heat detectors have some value.” *Id.* The court rejected this argument as well because “[t]he seller’s misrepresentations tainted the customers’ purchasing decisions.” *Id.*

Third, the defendant argued that the remedy forced it “to pay for losses beyond its gains.” *Id.* at 606. The defendant noted that it sells heat detectors for cash to distributors who set their own mark-ups, so “[m]any consumer dollars therefore go into the distributors’ pockets, not Figgie’s.” *Id.* The court rejected this argument on two notable grounds. The court first stated: “Section 19(b) does not limit its remedies to the amount of the unjust enrichment. Statutory remedies include ‘the payment of damages.’ There is no question but that *Figgie*, which designed,

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

authorized and supervised the dishonest sales presentations, was the proximate cause of consumers' loss. It may be held responsible for the damages it caused." *Id.* The court then also stated that "familiar principles of restitution support the district court's order" because "[w]hile ordinarily the proper measure of restitution is the amount of enrichment received, if the loss suffered by the victim is greater than the unjust benefit received by the defendant, the proper measure of restitution may be to restore the status quo." *Id.* (quotation marks omitted). (Note that this ruling may implicate the Circuit split described above – that is, it appears consistent with the Ninth Circuit's rulings on restitution under section 13, but may be inconsistent with the decisions of other Circuits.)

Fourth and finally, the defendant argued, and the court agreed, that making it pay a minimum amount even if that amount exceeded redress to customers improperly violated section 19's prohibition on "exemplary or punitive damages." 12 U.S.C. 5565(a)(3). The court held that "[i]f disgorgement of Figgie's receipts would exceed redress to consumers, then in the circumstances of this case requiring Figgie to pay the Commission the excess would be for purposes of punishing Figgie, not making redress to the consumers who bought heat detectors." *See also Kokesh v. SEC*, 137 S. Ct. at 1639 (finding that disgorgement "in the securities-enforcement context" constituted a "penalty").

In the other litigated FTC Act section 19 case addressing remedies, *AMREP*, the court (S.D.N.Y.) declined to grant consumer redress to the Commission at summary judgment because of concerns about causation. The court indicated that "the court may grant relief only as to those individuals who sustained injury as a result of the defendant's deceptive acts and practices." 705 F. Supp. at 128. And the court noted that the FTC's allegations were of "false representations [that] were contained in a variety of written and filmed sales materials, as well as in oral presentations at dinner parties that varied from instance to instance." *Id.* Accordingly, "[a]s to any particular purchaser on whose behalf the Section 19 action is brought," it was unclear at summary judgment if "he or she was the recipient of false representations." *Id.* (The court distinguished that situation from "a case where liability is premised on the utilization of a false newspaper ad or prospectus," where "each and every purchaser who responded to the ad or the prospectus would have been a recipient of the same false representation." *Id.*) Given this uncertainty about which consumers had been subject to deceptive statements, the court found that there were "genuine issues of fact with respect to AMREP's practices during the redress period" and denied summary judgment to the Commission. *Id.*

4. *Recent FTC Act Debt Collection Cases*

As described above, in the recent *LoanPointe* and *PayDay Financial* cases, both brought under FTC section 13(b), the FTC prevailed on summary judgment on FTC Act § 5 debt collection claims, notwithstanding that consumers actually owed the money. In each of these cases, the FTC was awarded disgorgement of the "ill-gotten gains" caused by the improper debt collection practices, which was

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

understood to be only the interest or fees that could be traced to the practice and not the loan principal.

In *LoanPointe*, LoanPointe argued that, because it “did not collect any money that was not owed,” requiring it “to disgorge amounts paid for repayment of loans would amount to a penalty, not simply a prevention of unjust enrichment.” 2011 WL 4348304, at *11. The court rejected this argument, finding that if LoanPointe “were subject to only an injunction, the resulting message would be that improper wage assignment clauses can be included in loan applications until discovered, at which point, the only consequence would be to stop violations of the law in the future.” *Id.* at *12.

However, the court did conclude that, “[w]hile the garnishment letter violated federal law, the court does not believe that [LoanPointe] should be required to disgorge the principal loan amounts. To the extent that disgorgement applies to ‘ill-gotten gains,’ a return of the loan principal lent to the consumer is not actually a ‘gain’ to [LoanPointe].” *Id.*

Further, relying on the principle that “equitable power may only be exercised over property that is causally related to the illegal action of the defendant,” the court declined to require LoanPointe to repay money from other “consumers who repaid their loans according to the terms of repayment [that] were not impacted by the inappropriate garnishment.” *Id.* at *12. The court noted that these other consumers did have loan agreements with the garnishment clause, but found that “[t]here is no basis for concluding that the garnishment clause had anything to do with their repayment of the loans.” *Id.*

As noted above, LoanPointe (but not the FTC) appealed. The Tenth Circuit upheld the district court’s reasoning on remedy in full, finding that the district court “deliberately fashioned a remedy that serves the two purposes of disgorgement, stripping the wrongdoer of ill-gotten gains and deterring improper conduct, without penalizing appellants” and noting that the award only included funds that “had a strong causal connection to the relevant violations.” 525 Fed. Appx. at 702.

It may be noteworthy that in its motion for summary judgment in *LoanPointe*, the FTC first argued that LoanPointe should be ordered to disgorge the full amount that LoanPointe “took in” via the improper garnishments or the full amount that LoanPointe collected in any manner on loans with a loan agreement containing the improper garnishment clause. Pl.’s Mem. in Sup. of Its Mot. for S.J., at 40-41 (February 16, 2011). In opposition, the defendant argued solely that it should not disgorge any money because it was all owed. Opp. of Defs. to Mot. for S.J., at 42-44 (April 18, 2011). Yet in its reply brief, the FTC nonetheless apparently conceded, without explanation, that only interest and fees and not principal “represents Defendants['] gains flowing from their illegal activities.” Pl.’s Reply in Support of Its Mot. for S.J., at 9-10 (May 5, 2011) (quotation marks omitted).

Similarly, in *PayDay Financial*, the FTC sought disgorgement of “the amount of finance charges, interest, and fees collected by certain of the Defendants through garnishment” that the court had determined “were violative of § 5 of the FTC[Act].” 989 F. Supp. 2d at 820. Here, the FTC appeared to concede in its initial summary judgment motion that the principal should not be disgorged. *See* Pl.’s Mem. in Sup. of

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

Its Mot. for S.J., at 28 (January 31, 2013). And the defendants again “disput[ed] the appropriateness” of any disgorgement on the grounds that “they were not receiving ill-gotten gains, but rather collecting what amounts were owed.” 989 F. Supp. 2d at 820. The FTC reiterated in its reply brief that “the FTC is not seeking to disgorge ‘money that borrowers agreed to repay,’ but money that Defendants unlawfully obtained,” and noted that “the FTC does not seek to disgorge the entire \$1.5 million, which includes principal owed on the debt, but rather seeks a disgorgement judgment of \$417,740 in fees, interest, finance charges, and other miscellaneous items collected.” Pl.’s Reply in Support of Its Mot. for S.J., at 29-30 (Mar. 26, 2013).

Relying on *LoanPointe*, the *PayDay* court rejected the defendant’s argument, finding that “the profits – which came in the form of astoundingly high interest rates and fees -- ... reasonably approximates the amount of unjust enrichment.” *Id.* at 821. The court noted that “the FTC does not seek, nor would this Court award, disgorgement of the loan principal balances” because “return of the principal that the Defendants lent to consumers was not actually a ‘gain’ to the Defendants.” *Id.*

These courts’ reasoning that disgorgement does not require the return of the principal seems to be consistent with the fact that these were FTC Act cases brought under section 13 and that therefore the remedy was disgorgement, which as explained above is a form of equitable restitution that is subject to equitable defenses. As noted above, the Restatement on Unjust Enrichment indicates that “the recipient [of facially unjust enrichment] may defend by showing that some or all of the benefit conferred did not unjustly enrich the recipient when the challenged transaction is viewed in the context of the parties’ further obligations to each other.”

It may also perhaps be notable that *LoanPointe* and *PayDay Financial* were litigated in courts in the Tenth and Eight Circuits, respectively, which do not appear to have weighed-in on the Circuit split described above about the scope of restitution under FTC Act section 13.

5. FDCPA

As described above, the FDCPA provides that consumers may receive as a remedy both statutory damages (up to \$1000) and actual damages. ~~Courts~~ These actual damages are intended to “compensate the debtor fully for any monetary damage, emotional distress or other injury that the debtor can prove the debt collector caused.” *Johnson v. Eaton*, 80 F.3d 148, 152 (5th Cir. 1996). Further, courts have specifically connected these FDCPA damages to the remedies available to consumers in tort. For example, the Eleventh Circuit stated: “[The FDCPA] clearly falls into a traditional tort area analogous to a number of traditional torts. The relief sought is money damages -- the traditional form of relief offered in the courts of law. Indeed, equitable relief is not available to an individual under the civil liability section of the Act.” *Sibley v. Fulton DeKalb Collection Serv.*, 677 F.2d 830, 834 (11th Cir. 1982).

Several courts have concluded that consumers should receive as actual damages payments that the consumers made, so long as they were caused by the debt collector conduct violating the FDCPA, even if these payments were on debts

Formatted: Font: Not Italic

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

actually owed. We have not been able to locate any FDCPA precedent that differs from this conclusion.

The leading case in this regard (in terms of citations) seems to be *Hamid v. Stock & Grimes, LLP*, 876 F. Supp. 2d 500 (E.D. Pa. 2012). In that case, a debt collector brought a state court lawsuit against a consumer on a debt for which the statute of limitations had run; the consumer nonetheless paid money to settle the suit. *Id.* at 501-02. The consumer then sued the debt collector under the FDCPA, prevailed, and sought actual damages in “the amount of money she paid to [the creditor] in settlement of the state court collection action,” lost wages and emotional damages “as a result of her mental distress sustained due to the collection action,” and “mileage and parking expenses.” *Id.* The debt collector argued that the “state law voluntary payment doctrine precludes [the consumer] from recovering the amount she paid in settlement of the underlying state action at trial in this case.” *Id.* at 502.

The court rejected this argument. First, as noted briefly above, the court rejected that the state law voluntary payment doctrine, if it applied, indeed prevented recovery. *See id.* at 502 n.2. The court found that “the voluntary payment doctrine only applies where the payment is made because of a mistake of law.” *Hamid*, Civ. No. 11-2349, Mem. Accompanying Order Denying S.J. to Def. and Granting S.J. in Part to Pl., at 6 (E.D. Pa. June 12, 2012) (quotation marks omitted). And the court found that, here, the consumer “made no mistake of law, but rather paid [the creditor] ‘to buy her peace.’” *Id.*

Second, the court found that the doctrine did not apply to claims under the FDCPA. The court stated:

It is clear from its underlying purpose that debtors may recover for violations of the FDCPA even if they have defaulted on a debt. It follows that debtors may recover the amount paid to settle a debt, if the debt collector violated the FDCPA in making the collection, as occurred here. [The consumer] paid some or all of the money she owed to [the creditor] only as a result of the untimely lawsuit filed by [the debt collector] on behalf of the [creditor]. If her payment was not a proper element of actual damages under the FDCPA, a debt collector could harass a debtor in violation of the FDCPA, as a result of that harassment collect the debt, and thereafter retain what it collected. We do not believe that Congress intended this result.

876 F. Supp. 2d at 503.

This reasoning from *Hamid* has been cited and relied on by other district courts. *See McMahon v. LVNV Funding, LLC*, 12 C 1410, 2018 WL 1316736, at *12 (N.D. Ill. Mar. 14, 2018); *Alonso v. Blackstone Fin. Grp. LLC*, 962 F.Supp.2d 1188, 1197–98 (E.D. Cal. 2013); *Abby v. Paige*, 2013 WL 141145, at *9 (S.D. Fla. Jan. 11, 2013), *aff’d*, 553 Fed. Appx. 970 (11th Cir. 2014) (no opinion).

It should be noted that one of these decisions, *McMahon*, describes the *Moritz* case described above with a “but see.” *See McMahon*, 2018 WL 1316736, at *12. As

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

explained above, in *Moritz* the court found that “plaintiffs are not injured in the amount collected when the plaintiff owed the debt even where the debt collector violated state law in doing so.” 895 F. Supp. 2d 1097, 1116–17 (W.D. Wash. 2012). The “but see” in *McMahon* about *Moritz* seems to suggest that *Moritz* is contrary to the reasoning in *Hamid*. However, on close reading, *Moritz* is not actually contrary to the principle that consumers can collect as damages money that is actually owed. Rather, as noted above, *Moritz* is best understood as part of the larger caselaw indicating that mere violations of state law are not necessarily FDCPA violations.

In a similar but slightly different situation, the FTC brought FDCPA claims against a debt collector in *FTC v. Check Enforcement*, 2005 WL 1677480 (D.N.J. July 18, 2005), *aff’d sub nom. FTC v. Check Investors, Inc.*, 502 F.3d 159 (3d Cir. 2007). The collector there had collected money from consumers who had bounced checks. The collector collected both amounts that the consumers actually owed – the amounts of the checks that had been bounced – and additional fees, which the district court determined consumers did not owe. *See* 2005 WL 1677480, at *9 (“In dunning letters, defendants represented to consumers that their alleged debts were greater than the debt owed....”). The court found that the collector had violated the FDCPA both by falsely representing to consumers that these amounts were owed and by committing a variety of harassing collection practices, such as falsely threatening consumers with arrest. *See id.* at *8-*10. The court granted “restitution” in the full amount that the collector had recovered, notwithstanding that some of this amount represented valid debts. *Id.* at *10. On appeal, the collector does not appear to have challenged the appropriateness of this relief but instead argued “that the FDCPA and the FTC Act do not apply to them,” which the Third Circuit rejected in affirming the district court. *See* 502 F.3d at 167-76.

Consistent with the FTC Act caselaw described above about causation, courts have found that, even though payments made may be an acceptable measure of “actual damages,” the consumer must “prov[e] that defendants’ failure to comply with the FDCPA caused them to make [the] payments.” *McMahon v. LVNV Funding, LLC*, 12 C 1410, 2018 WL 1316736, at *12 (N.D. Ill. Mar. 14, 2018); *see also Bartlett v. Heibl*, 128 F.3d 497, 499 (7th Cir. 1997) (indicating that a consumer can’t sue for actual damages based on a deceptive letter that he did not read). In *McMahon*, this showing was that “the deceptive letters actually caused them to make these payments.” 2018 WL 1316736, at *11-12. *McMahon* does not suggest that, to prove causation of actual damages under the FDCPA, consumers must present evidence that in a hypothetical world in which the violation did not occur they would not under any circumstances have voluntarily made the payment. Nor have we identified any other FDCPA case suggesting that proof of causation of actual damages under the FDCPA requires such evidence. Rather, as noted, it is sufficient for a plaintiff to present evidence that the alleged violation “actually caused them to make these payments.” *Id.*

Finally, the FDCPA caselaw indicates that an FDCPA violation does not extinguish the underlying debt. *See Vitullo v. Mancini*, 684 F. Supp. 2d 760, 764 (E.D.

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

Va. 2010) (“The statute’s remedial scheme does not envision, and indeed does not permit, courts to cancel or extinguish debts as a remedy for FDCPA violations.”); *United States v. Iwanski*, 805 F. Supp. 2d 1355, 1359 (S.D. Fla. 2011) (“Nothing in the FDCPA suggests that a borrower can have his debt extinguished or cancelled in lieu of recovering damages.”); *Midland Funding, LLC v. Pipkin*, 283 P.3d 541, 542 (Utah Ct. App. 2012) (“While Midland’s alleged failure to comply with the FDCPA may subject it to liability under the act, such failure is not a defense to liability for the underlying debt.”).

That said, however, the federal court will typically not, in a consumer’s FDCPA action, hear a counterclaim from the debt collector on the debt. *See Leatherwood v. Universal Bus. Serv. Co.*, 115 F.R.D. 48, 50 (W.D.N.Y. 1987); *Ayres v. Natl. Credit Mgt. Corp.*, 1991 WL 66845, at *4 (E.D. Pa. Apr. 25, 1991).

6. *Analysis and Conclusions*

i. *The present situation*

From the relevant precedent, we are inclined to conclude that it would be legally appropriate for the Bureau to seek consumer redress in the full amount taken from consumers when a debt collector or creditor improperly takes money from consumers, notwithstanding that consumers owe a debt. The debt would still be owed, and the creditor/collector could continue to collect the debt using legal means. On the other hand, we do not believe the Bureau would be legally required to take this approach.

The precedent suggests to us that consumers would, in these circumstances, themselves be able to recover the full amount taken from them as “damages” either in a common law conversion suit or in an FDCPA suit (depending on whether the person who took the money is a creditor or an FDCPA debt collector). Since the Bureau under the CFPA remedy provision (CFPA 1055) can also receive the remedy of “damages,” it seems reasonable to conclude that the Bureau’s recovery of this same amount as consumer redress is appropriate. (It might also be possible that the Bureau could alternatively recover this amount as equitable restitution. Since the analysis is more straightforward as to damages, this memorandum does not consider the equitable restitution issue further.)

We are not aware of any precedent suggesting that the same word, “damages,” should be construed differently for the CFPA in the same circumstances than with respect to common law conversion and the FDCPA. (If anything, the FDCPA’s use of the modifier “actual” suggests a more limited view of what can be recovered as damages under that statute.) So the grant of authority to the Bureau in CFPA 1055 to seek damages seems to suggest that recovery of these amounts would be legally appropriate.

Further, we note that the FTC Act legislative history and judicial precedent suggest that the FTC, when it seeks consumer redress for a UDAP violation, is doing so “on behalf of” consumers. This suggests that the remedy that a consumer might be able to get by bringing a case him or herself in a particular factual circumstance is

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

at least a relevant consideration for what the FTC should be able to recover *on behalf of* consumers in that situation. Indeed, in the *Kuykendall* case described above, the en banc Tenth Circuit reasoned in this way. *See* 371 F.3d at 763-64. Presumably, the Bureau is also acting “on behalf of” consumers when it gets redress under its similar UDAAP provision. Accordingly, since consumers could get the remedy of damages in the full amount paid in these circumstances, it makes sense that the Bureau could recover the same for consumers.

We also do not believe that questions of causation are seriously present when, as here, the collector or creditor simply improperly takes money from consumers. That said, as discussed below, this could be a more significant issue for other factual scenarios.

It does appear that, in analogous situations, the FTC under section 13 of the FTC Act has chosen only to seek a creditor’s “profit,” which was understood to be interest and fees but not principal, as “disgorgement” of “unjust enrichment.” However, it seems clear to us that Congress chose not to limit the Bureau to equitable remedies, as the FTC is limited under section 13. That’s because the CFPB remedy provision includes both “equitable relief” (i.e. what the FTC gets under section 13) and the full set of remedies available to the FTC under section 19. To wit, in the *Figgie* case involving FTC Act section 19, the Ninth Circuit recognized that the express statutory grant of authority to recover “damages” under section 19 meant that the remedy is “not limit[ed] ... to unjust enrichment.” *Figgie*, 994 F.2d at 606. Even putting that case aside, this conclusion seems to flow from the plain text of the CFPB, which includes both the section 13 and section 19 remedies.

We also note that, in some Circuits, even under the section 13 equitable relief provision, the FTC can get restitution for the full amount of consumer loss, not just the amount of a defendant’s unjust gains (though this is the source of the Circuit split). Additionally, we note that it is possible that redress in the full amount taken from the consumer might also fall into a category of remedy available to the Bureau other than “damages,” such as “refund.” Because we believe that analyzing the issue from the perspective of “damages” largely answers the question (and that this may be the most persuasive way of viewing the issue, given the common law analogy of conversion and its remedy of damages), we do not consider those other remedies here.

Finally, because it appears that the choice of remedy is largely up to the plaintiff (subject to reasonable constraints), we believe that it would be the Bureau’s option to seek damages in the full amount taken in these circumstances. Conversely, we do not believe the Bureau would be required to seek this or any other particular remedy.

ii. Related situations

It seems to us that more difficult issues could be presented in the related situations that are not the direct subject of this memorandum. One such situation is when a creditor or debt collector behaves improperly in some way toward the consumer and the consumer then subsequently repays the debt. Most obviously,

PRIVILEGED AND CONFIDENTIAL ATTORNEY WORK PRODUCT

issues of causation may come up here, as it may not be clear that the bad behavior caused the consumer to pay the debt. It also may be helpful to research what the appropriate remedy at common law would be (if any) for such conduct. Accordingly, we will offer only some preliminary thoughts here, as more thinking would seem to need to be done to analyze this situation carefully.

Under FTC Act precedent, it does seem fair to say that there would be something like a rebuttable presumption under certain circumstances that the payment was caused by the inappropriate conduct. For instance, in *Figgie*, the Ninth Circuit rejected the argument that “only those consumers that can prove that they purchased [the] heat detector in reliance on [deceptive] statements should be entitled to redress,” finding instead that “[a] presumption of actual reliance arises once the Commission has proved that the defendant made material misrepresentations, that they were widely disseminated, and that consumers purchased the defendant’s product.” *Figgie*, 994 F.2d at 606; see also, e.g., *Kuykendall*, 371 F.3d at 765 (similar statement).

Similarly, in *LoanPointe*, the Tenth Circuit found that the FTC could collect any funds paid by a consumer’s employer who received a letter that deceptively instructed the employer to garnish funds. The court rejected *LoanPointe*’s argument that there was a “lack of evidence that any borrowers were actually misled by the violation,” finding instead that “[t]he FTC does not need to prove actual deception, only the likelihood that a consumer (here, employers), acting reasonably under the circumstances, would be deceived.” 525 Fed. Appx. at 701 (quotation marks omitted). On the other hand, the *LoanPointe* district court did reject the FTC’s argument that any consumer with a *loan contract* containing a deceptive garnishment statement who then later made a payment on the debt should receive redress for the payments made.

Likewise, although the FDCPA precedent does require a causal connection between the collector’s conduct and the damages recovered, the bar for showing that causation seems to be relatively low; consumers are barred from recovery if they, for example, did not even read a deceptive statement, but it does not seem consumers need to make a vigorous showing that reading the statement “really” caused them to make the payment.

Perhaps the proper way to consider this question might be to consider how closely linked the improper conduct was with the consumer’s payment. A deceptive statement that a consumer never read can’t really be said to have caused the consumer to do much of anything. But if a consumer received a deceptive statement in a collection letter that could be highly relevant to the consumer’s decision to pay the debt, it may fairly be presumed that the deception caused the payment, at least until the collector offers evidence otherwise.

APPENDIX L

From: Blankenstein, Eric (CFPB)
Sent: Thursday, June 28, 2018 9:27 PM
To: Petersen, Cara (CFPB); Donoghue, Kristen (CFPB)
Cc: D'Angelo, Chris (CFPB); Bleicken, David (CFPB); Redacted by the Committee (CFPB)
Subject: RE: Enova

Not sure I fully understand your question, but I affirmatively do not want the consent order to require repayment of debited funds where there is no dispute about the validity of the debt.

Thanks,
Eric

From: Petersen, Cara (CFPB) Redacted by the Committee
Date: June 28, 2018 at 9:16:07 PM EDT
To: Blankenstein, Eric (CFPB) Redacted by the Committee, Donoghue, Kristen (CFPB)
Redacted by the Committee
Cc: D'Angelo, Chris (CFPB) Redacted by the Committee, Bleicken, David (CFPB)
Redacted by the Committee Redacted by the Committee Redacted by the Committee
Subject: RE: Enova

OK, I'll share with the team, and let you know if we have questions. I have an initial question about your second paragraph on Count I. Does your view hold if the order required Enova to return to consumers the funds it withdrew from their bank accounts without authorization, but also allowed it to recollect these amounts using lawful means?

From: Blankenstein, Eric (CFPB)
Sent: Thursday, June 28, 2018 4:46 PM
To: Donoghue, Kristen (CFPB); Petersen, Cara (CFPB)
Cc: D'Angelo, Chris (CFPB); Bleicken, David (CFPB); Redacted by the Committee (CFPB)
Subject: Enova

With apologies for the delay, here is my guidance on how to proceed in Enova. For clarity, I've used the counts in the Bureau's draft complaint to refer to the potential claims against Enova.

Count I. I am okay going forward with the unauthorized debiting claim on a theory of unfairness based on injury from the NSF fees and overdraft charges incurred by borrowers that resulted from lower-than-expected account balances. My understanding is that, because of the difficulty of gathering relevant information, it will be exceedingly difficult to determine which consumers did or didn't incur NSF fees or overdraft charges, and (for those who did) what the amounts were beyond those that Enova has already remediated. As a result, we should not seek restitution of those fees and charges, unless the team can determine a way to identify in a reliable way additional restitution owed (either to previously unremediated customers or additional amounts owed customers who have already received some restitution).

Also, I have reviewed Legal's and Enforcement's research on the question of whether the Bureau may seek as a remedy restitution of amounts that were validly owed but taken without authorization from a specific bank account. Having considered that research, having discussed the issue with the Acting Director, based on the facts of this case the Bureau

should not seek restitution of those amounts, and should instead impose only a civil penalty for this violation, as well as appropriate injunctive relief.

Count III. I am also okay going forward with the extension issue on a theory of unfairness. Restitution should be based on fees and penalties incurred as a result of the erroneous charges, to the extent they can be quantified for each affected consumer in a reliable way.

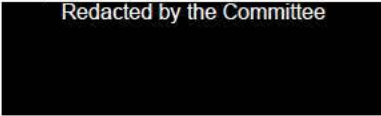
Counts II, IV, and VI. I do not want to proceed on the two claims related to allegedly deceptive communications about the company's payment processing errors. Both claims seem somewhat weak on the merits, and could be viewed as derivative of the unfairness claims. To the extent any of those communications are relevant to establishing the facts necessary to allege unfairness claims, the consent order can include findings about them. Nor do I believe that the evidence and argument presented in support of Count VI amounts to a Reg E violation.

Count V. Given the technical nature of the violation and the small number of affected consumers, I do not think it worth pursuing the "Duplicate Debit Issue" if it is going to be an obstacle to settlement, so please make that an optional settlement term when preparing a revised settlement recommendation memo. My understanding is that Enova provided restitution of the "double" payments already. For reasons similar to those above, we can seek additional restitution based on fees and penalties incurred as a result of the erroneous charges, to the extent they can be quantified for each affected consumers in a reliable way. Also, this claim should not factor significantly into the CMP we seek.

Thanks,
Eric

Eric Blankenstein
Policy Director
Supervision, Enforcement, and Fair Lending

Redacted by the Committee

A large black rectangular redaction box covering several lines of text.

APPENDIX M

FOIA CONFIDENTIAL TREATMENT REQUESTED

June 18, 2018

VIA EMAIL

Kristen Donoghue, Enforcement Director
Eric Blankenstein, Policy Director
Division of Supervision, Enforcement & Fair Lending
Consumer Financial Protection Bureau
1625 Eye St., N.W.
Washington, D.C. 20006

RE: Enova International, Inc.

Dear Ms. Donoghue and Mr. Blankenstein:

We understand that new CFPB leadership is reviewing all active enforcement matters and that Bureau enforcement is focusing on “quantifiable and unavoidable harm to the consumer.”¹ We thought, therefore, it would be helpful to reiterate the position of Enova International, Inc. (“the Company” or “Enova”) with respect to the issues the Bureau has been reviewing.²

For the reasons explained below and in prior submissions by the Company,³ Enova submits that no enforcement action is necessary or appropriate here. This matter is, unfortunately, an example of former Bureau leadership’s attempt to set new precedent through enforcement. A fair reading of the relevant facts indicates that the Company did not violate the Bureau’s prohibition on unfair and deceptive acts and practices (“UDAAP”), the sole theory of liability alleged here by the CFPB.⁴ The issues identified by the CFPB resulted from inadvertent

¹ See Mulvaney, M. (Jan. 23, 2018). *To Everybody from the Acting Director* [Memorandum].

² Enova uses technology to develop innovative financial products and services for consumers and businesses. Enova offers its financial products online through several different brands in the United States, United Kingdom, and Brazil. Enova is a publicly traded company listed on the NYSE. As an independent public company, Enova has developed a rigorous compliance program that significantly enhanced the Company’s identification of and response to operational and compliance issues. See Enova’s NORA submission dated May 31, 2017 for additional details on the compliance enhancements.

³ See Enova’s NORA submission dated May 31, 2017, and letters dated September 15, 2017, and October 13, 2017.

⁴ The Bureau raised one additional issue as part of its investigation. The Bureau has asserted that Enova’s varying transfer disclosures violate Regulation E, but that is a misinterpretation of the regulation. The CFPB asserts that because some of Enova’s loan contracts do not specify how much Enova charges for “returned payment charges” or “late charges,” a consumer cannot anticipate the full range of potential debit amounts. But Enova’s varying transfer disclosure is clear that Enova will assess these charges only where “applicable,” and in all instances where such

technology coding errors affecting a limited number of customers of the Company's CashNetUSA brand. The Company self-reported the issues to the CFPB, and the Company has proactively acted to provide remediation to the small number of potentially impacted consumers for any speculative harm they may have sustained.

If the Bureau believes Enova has not made all impacted consumers financially whole, Enova reiterates that it stands ready to provide additional restitution for quantifiable harm to consumers. But any restitution should do no more than make consumers whole and should not be an unjustified windfall based on speculative damages. The CFPB's prior settlement demands have been, unfortunately, grossly disproportionate to any conceivable harm caused. We respectfully urge the CFPB to reconsider its aggressive settlement posture and decline to bring an unnecessary and punitive enforcement action that contradicts the mission of the Bureau and exceeds its statutory authority.

I. The Leads ACH Issue

The most significant portion of the Bureau's settlement demands relates to the Leads ACH issue. The Leads ACH issue refers to a coding error in place from approximately July 2010 through June 2014 that affected customers with active Enova loans who submitted subsequent applications for additional loans through lead generators. In the very small percentage of instances where a customer provided a different bank account in connection with a new loan application than he or she had previously provided Enova, a coding error inadvertently replaced the bank account on file with the updated bank account. Enova subsequently used the updated bank account to process future credits and debits in connection with the existing Enova loan.

This coding error updated the accounts of approximately 6,398 CashNetUSA customers from July 21, 2011 until it was fixed in June 2014, although not all of those customers were impacted because Enova did not attempt to debit all updated accounts. During this same timeframe, Enova processed over 1.4 million CashNetUSA applications from lead generators. That means that **less than 0.46% of applications** from lead generators were affected by this inadvertent coding issue. Moreover, many of the customers impacted by the issue subsequently authorized Enova to debit the updated bank account when later scheduling a one-time payment online or setting up a payment plan with a customer service representative.

In 2014, after the coding error was fixed and the issue was disclosed to the Bureau, Enova sent emails and follow-up letters to potentially impacted customers advising them that Enova may have debited the updated bank account in error, and offered to reimburse any damages, such as bank NSF or overdraft fees, incurred as a result. Enova, of course, could not then, and cannot now, know which, if any, customers incurred a bank fee as a result of these debits. Some of the debits from the updated bank account may have triggered a bank fee, but most almost certainly did not.

charges are applicable, Enova clearly disclosed the amount of these charges. Enova's varying transfer disclosures, therefore, comply with Regulation E. Regardless, this is the type of issue that should be resolved through discussions between Enova and its CFPB examiners, not through an enforcement action.

Approximately 90% of the debits Enova ultimately made to the updated bank accounts were payments for lines of credit and installment loans, and only 10% of the debits were for payday loans. A significant majority (76%) of the impacted line of credit customers took new draws on the credit lines after their bank account information was updated, frequently before a debit was attempted on that account, which caused Enova to deposit funds into the updated bank account and then make debits from that account according to the payment schedule. Many of the line of credit customers used their lines actively, making multiple subsequent draws into the updated bank account. Indeed, some customers took tens of thousands of dollars in draws into the updated accounts over several years, thereby generating tens of thousands of dollars in debits.⁵ At the high end, some customers used their accounts so frequently after the bank account update that they generated more than 90 debits to the updated bank account over several years. There is no conceivable way these customers were unaware of the bank account being used by Enova, and they had ample opportunity to stop the debits to their accounts.

The Bureau has pointed to absolutely no legal authority supporting its demand to refund the debits themselves, an outcome that would place the consumer in an exponentially *better* position than he or she was in prior to taking out their loans. Indeed, the remedy demanded by the Bureau would mean that some consumers would have the benefit not just of an interest-free loan, but entirely free money from Enova. Under the CFPB's proposed consent order, Enova would be required to refund the debits at issue and would then be barred from attempting to recollect either principal or interest on the newly created debts the consumers would then owe Enova as a result of the refunded loan payments. Such a result would be tremendously unfair to Enova, which self-disclosed and attempted to remediate this issue, and is unsupported in any case law or legal precedent.

The CFPB's demand that Enova make refunds for the full amount of all of these debits, in addition to completely speculative damages the customer *may* have incurred, is extreme and punitive. Enova should not be required to pay a customer thousands of dollars (in some instances tens of thousands of dollars) because it inadvertently debited the bank account provided by the customer in connection with a different loan application. As noted above, a substantial number of the line of credit customers, who account for almost three quarters of the debits at issue, continued to use their credit lines by drawing new funds into the updated bank account *after* the Leads ACH update, and could easily have instructed Enova (either online or by telephone) to switch bank accounts if that had been their preference. Indeed, approximately 2/3 of all the "Class A" debits⁶ at issue were taken *after* the impacted customer took a draw into the updated bank account. A reasonable customer would surely have known which bank account Enova was using for debits and credits as soon as the funds from a draw were deposited into the updated bank account as well as after one or more debits to the account.

The only actual harm caused by the inadvertent account update would be any NSF or overdraft fees resulting from the debits to the incorrect account. Enova long ago contacted potentially impacted customers whose bank accounts had been debited following the update and offered to reimburse them for any bank fees that were assessed as a result of the updated bank account being debited. Enova even provided a draft copy of the customer communication to

⁵ The data in this paragraph are based on the debit information provided in Written Report 5.

⁶ See Written Report 5.

examiner Michael Ramsden during the last CFPB examination prior to sending it. All customers who submitted claims in response to the final communication were promptly reimbursed. To the extent that the CFPB believes some customers have not been made whole through the remediation process Enova implemented in 2014, Enova is willing to discuss additional potential remediation to reimburse customers for any bank fees they were assessed.

But Enova should not be compelled to provide an extravagant windfall to consumers by refunding the debits themselves. The Bureau is seeking to set new precedent by demanding these payment refunds. These were valid loans, and there is no dispute that the affected consumers were legally obligated to pay Enova the sums Enova in fact debited from their accounts in accordance with the loan terms, albeit from a different bank account than originally authorized by the consumer as a result of the inadvertent coding error. Because the consumers were legally obligated to pay the amounts debited, the debits at issue did not result in any unjust gains to Enova. Enova regrets the coding error that caused the bank account updates, but the appropriate remediation is to make consumers whole, not to extract a punitive settlement ungrounded in law or principle that would place consumers in a materially better position than before taking out the loan by entirely refunding the loan payments and awarding additional speculative damages.

The Bureau has suggested that Enova should refund these debits because they were “unauthorized” transactions under Regulation E. Putting aside whether or not the debits were, in fact, “unauthorized” under Regulation E, the CFPB does not, and cannot, allege that the debits at issue violated Regulation E because that regulation has a one-year statute of limitations, which renders almost all the debits at issue beyond its scope. And, in any event, Regulation E notably does not provide for refunding of unauthorized charges in these circumstances. This presumably explains why the CFPB alleges liability solely under a UDAAP theory, suggesting that the debits were “unfair” and that the Company’s communications to consumers inviting them to submit claims if they were damaged were “deceptive.” Enova disagrees that its practices violated UDAAP’s prohibition on unfair and deceptive practices for the reasons stated in its NORA response,⁷ and maintains that the Bureau’s UDAAP authority should not be invoked to circumvent the statute of limitations and restitution framework set forth in the federal regulation governing debit transactions like the ones at issue here.

But even if one considers the debits in the context of UDAAP, the proper remedy for a UDAAP violation is to make consumers whole by remediating any *actual* harm to the consumer.⁸ Here, that means refunding any damages incurred by the consumer as a result of a different bank account being debited. As noted above, Enova cannot know which, if any, consumers incurred possible bank fees as a result of the debits, but it has already made a good-faith effort to provide such remediation through proactive and voluntary communications with potentially impacted borrowers. Enova self-disclosed the coding error to the CFPB and shared a draft of its communication to borrowers regarding the issue prior to finalizing the

⁷ See NORA Response at 5-17.

⁸ The CFPB’s Supervision and Examination Manual states that consumer injury resulting from a UDAAP violation “typically takes the form of monetary harm, such as fees or costs paid by consumers because of the unfair act or practice.” CFPB Bulletin 2013-07, Prohibition of Unfair, Deceptive, or Abusive Acts or Practices in the Collection of Consumer Debts (Jul. 10, 2013) at 2.

communication. To bring an enforcement action under such circumstances would contravene the Bureau's own guidance on exercising its enforcement discretion.⁹

II. The Flash Cash Issue

Flash Cash was a CashNetUSA product feature (no longer offered by Enova) that provided eligible customers the ability to receive same-day funding through a debit card. The Flash Cash issue refers to a coding error, described more fully in the Company's NORA Response (at p. 17), that impacted a tiny percentage of customers seeking loan extensions from April 2013 through May 2014. As a result of a technical glitch, Enova inadvertently debited the loan amount due on the original due date, rather than just the finance charge that would be debited with an extension. This issue impacted 333 loan extension requests, which represents less than 0.044% of the 770,491 successful CashNetUSA extensions processed during this same time period.

For the reasons stated more fully in the Company's NORA response (at pp. 17-22), the Flash Cash issue was not an "unfair" practice. It was an inadvertent technical issue that impacted a miniscule percentage of loan extension requests. Customers did not pay any improper or extra fees; they simply did not receive the benefit of a loan extension. Any consumer harm is entirely speculative, and the Company responsibly sought to offer appropriate remediation. Enova sent an email to the 308 impacted customers explaining the extension error and inviting them to contact the Company if they incurred any bank fees as a result of the failed loan extension.

Enova's communications to consumers about the issue, moreover, were not "deceptive." The Bureau suggests that the Company's initial communications regarding the loan extensions were deceptive because the communications indicated that consumers would receive a loan extension when, in fact, 308 customers ultimately did not receive extensions as a result of the coding error. But the Bureau's argument is flawed. Enova's communication was accurate as to more than 99.9% of the recipients. The fact that a tiny percentage (0.044%) of the loan extensions ultimately failed as a result of a technical issue after the communication was made does not convert the underlying communication from accurate to unlawfully deceptive. To maintain otherwise would render any inadvertent breach of contract a *per se* UDAAP violation, which would dramatically expand the proper scope of UDAAP.

Enova regrets that these loan extensions failed for these 308 consumers, but the coding error at issue should not be deemed an unfair or deceptive practice.

III. The February Debit Issue

The February Debit issue refers to the fact that on February 28, 2014, an error caused Enova to debit 78 customer accounts more than once for amounts owed. Enova identified the issue that same day and immediately initiated corresponding credits to the 78 accounts for the inadvertent extra debits. Customers received those credits on the next business day.¹⁰ Enova

⁹ See CFPB Bulletin 2013-06.

¹⁰ Because February 28, 2014 was a Friday, the next business day was the following Monday.

promptly sent emails to the impacted customers explaining the issue and offering reimbursement of any bank fees they sustained as a result of the error.

Enova's actions with respect to this issue are commendable. The Company cannot understand what more it could have done: it self-identified the issue on the same day it occurred, immediately attempted to correct the error, promptly sought to provide remediation, transparently communicated with consumers regarding the issue the same day it occurred, and then self-reported the issue to CFPB examiners. Unless the Bureau is prepared to hold all industry participants to an unrealistic zero-error standard, Enova's conduct cannot fairly be deemed to constitute a UDAAP violation.

* * *

In conclusion, Enova maintains that none of the issues raised by the CFPB justifies bringing an enforcement action against the Company. The CFPB's UDAAP allegations stretch the definitions of "unfair" and "deceptive" well beyond their reasonable interpretations. The CFPB should not seek to invoke UDAAP theories of liability in an effort to circumvent Regulation E's one-year statute of limitations, and the CFPB should not compel the Company to provide consumer "remediation" that exponentially exceeds any conceivable financial injury. Enova is committed to making any impacted consumers whole, as it demonstrated through its proactive outreach to consumers upon identifying the issues and as it has stated throughout this investigation. To the extent that the CFPB believes further remediation efforts are necessary to make consumers financially whole, Enova suggests that the matter be referred to Supervision where CFPB examiners can discuss with the Company whether there are additional ways to identify customers who may have paid a bank fee. But Enova respectfully urges the CFPB not to push the envelope by bringing a punitive enforcement action requiring the Company to pay consumers exorbitant sums that are untethered to any injuries they could conceivably have suffered.

Enova endeavors at all times to operate its business consistent with federal and state consumer law. Enova is proud of the role it plays in offering credit to underserved consumers and small businesses, and believes it offers its customers valuable products and services. Enova has invested tremendously in enhancing its compliance program, operations, and technology since its spin-off from Cash America in 2014, and the Company is committed to responsible lending in the markets it serves. Enova self-identified the coding errors at issue, and proactively and voluntarily reached out to potentially impacted consumers to ascertain whether anyone was financially impacted as a result of the errors. Enova self-reported the issues to the CFPB, notwithstanding that the CFPB would almost certainly not have discovered the issues on its own. To bring a punitive enforcement action under these circumstances – particularly one seeking relief that grossly exceeds any actual consumer harm – would be unfair, and would discourage future self-reporting of issues to the Bureau.

We urge the CFPB to reconsider its position on these issues and return this matter to the Supervision team. If an in-person meeting would be helpful, we would be happy to travel to Washington for further discussions in an effort to resolve this matter.

Kristen Donoghue
Eric Blankenstein
June 18, 2018
Page 7

We request that you treat this letter and any copies thereof (hereafter, collectively, the “Confidential Materials”), as confidential and exempt from disclosure under the Freedom of Information Act, 5 U.S.C. § 552(b) (“FOIA”) and 12 C.F.R. § 1070. The Confidential Materials are exempt from disclosure under FOIA because they constitute “confidential investigative information” under 12 C.F.R. § 1070.2(h). The Confidential Materials include certain sensitive, non-public, proprietary, commercial, financial, and other information regarding the business operations of the Company. Enova would not make this information available to the public ordinarily, and it is not otherwise available in the public domain. The disclosure of the information contained herein would cause substantial competitive harm to Enova.

Sincerely,

/s/ Matthew P. Previn

Matthew P. Previn

cc: Redacted by the Committee, Senior Litigation Counsel

APPENDIX N

1700 G Street NW,
Washington, DC 20552



Decision Memorandum from the SEFL Policy Director

FROM	Eric Blankenstein, SEFL Policy Director
TO	Chris D'Angelo, SEFL Associate Director; Kristen Donoghue, Assistant Director for Enforcement
SUBJECT	Authority to Settle with Enova International, Inc.

I authorize the Office of Enforcement to settle with Enova International, Inc. consistent with the recommendation by the Office of Enforcement on October 3, 2018.

Eric Blankenstein
SEFL Policy Director
Bureau of Consumer Financial Protection

10/3/2018

Date



October 3, 2018

Recommendation Memorandum for the SEFL Policy Director

FROM	Redacted by the Committee , Cara Petersen, and Kristen Donoghue, Office of Enforcement
THROUGH	Chris D'Angelo, SEFL Associate Director
SUBJECT	Authorization to Enter into Settlement with Enova International, Inc. Outside of Previously Authorized Parameters, or to File Suit

Recommendation

The Office of Enforcement recommends that you authorize a settlement in this matter under the parameters described below.

I. Overview

Based on the SEFL Policy Director's modification of the settle-or-sue authority in this matter described below, the Bureau should seek to settle with Enova International, Inc. (Enova) outside of previously authorized parameters.

Former Director Cordray authorized the Bureau to settle or sue on its potential claims against Enova on July 27, 2017. The Bureau and Enova began settlement negotiations in August 2017. On November 7, Enova offered to settle the matter for \$1,367,567 in redress to consumers and a \$1.2 million penalty. The redress portion of Enova's offer consisted of the following:

- Full refunds for payday customers whose bank accounts Enova debited without authorization;
- Refunds for up to four debits for installment loan and line-of-credit customers whose bank accounts Enova debited without authorization;

- \$35 per transaction for up to four debits for all consumers whose bank accounts Enova successfully debited without authorization;
- \$35 per transaction for all consumers whose bank accounts Enova attempted to debit without authorization; and
- \$35 per transaction for consumers for whom Enova failed to honor loan extensions.

On December 4, Enova indicated that it was reassessing its settlement position and has provided no further counter-offer since that time. On June 28, 2018, pursuant to the Acting Director's delegation of his authority, the SEFL Policy Director modified the settle-or-sue authority, eliminating several claims and modifying the relief to be sought, as described below.¹

This memorandum includes only facts relevant to the revised parameters. A copy of the previously approved recommendation memorandum with a more complete discussion of the facts is attached. The count numbers referenced in this memorandum correspond to the previously approved draft complaint against Enova, which is also attached.

II. Claims

The SEFL Policy Director declined to reauthorize three claims previously authorized by Director Cordray. The SEFL Policy Director directed Enforcement to eliminate deception claims relating to Enova's unauthorized debiting of consumers' bank accounts and its failure to honor loan extensions to consumers (Counts II and IV). The SEFL Policy Director also directed Enforcement to eliminate the Regulation E claim (Count VI). Further, the SEFL Policy Director directed Enforcement to drop the unfairness claim with respect to Enova's debiting consumers' accounts twice for the same monthly payment (Count V), if the claim proves to be a bar to settlement.

At the direction of the SEFL Policy Director, Enforcement will no longer pursue Counts II, IV and VI.

¹ The SEFL Policy Director's instructions are set forth in an e-mail to the Enforcement Director dated June 28, 2018.

III. Restitution

After discussion with the Office of Enforcement, the Legal Division, and the Acting Director, the SEFL Policy Director directed Enforcement not to seek restitution of loan principal or fees in connection with Count I. The loan principal and fees in question were legally owed, but unlawfully collected.²

The SEFL Policy Director also directed Enforcement not to seek restitution for any incidental NSF fees or overdraft charges incurred by consumers as a result of Enova's unauthorized debiting, given the impossibility of calculating restitution with certainty for each affected consumer. The precise amount of fees incurred by each affected consumer cannot be calculated with certainty because many of these transactions occurred over eight years ago and few, if any, consumers will have retained the relevant records for that length of time.

The SEFL Policy Director also directed Enforcement to seek restitution based on fees and penalties incurred as a result of erroneous charges (addressed in Counts III and V) only to the extent they can be calculated with certainty for each consumer. For the same reasons described above, these amounts cannot be calculated with certainty.

Thus, Enforcement will no longer seek consumer restitution for Counts I, III, or V.

IV. Penalties

Based on the facts developed during this investigation, since at least July 21, 2011, Enova acted recklessly by initiating over 14,000 debits from consumers' bank accounts without authorization, using account information obtained from lead generators. Further, a Missouri regulator notified Enova of the illegal debiting on

² Enforcement previously recommended, and received authorization to require as part of a settlement, refunds of amounts Enova unlawfully collected notwithstanding that consumers owed those amounts. The Legal Division subsequently prepared a memorandum addressing whether consumers may suffer "substantial injury" when a creditor (or debt collector) unlawfully collects debt that the consumer actually owes, and whether the Bureau has legal basis to require a creditor under those circumstances to return to consumers the funds that the creditor unlawfully collected. That memorandum concludes that consumers may suffer substantial injury under those circumstances, and that the Bureau could properly require the creditor to provide refunds for debts that were legally owed, but unlawfully collected, but that the Bureau would not be compelled to seek that remedy. Enforcement's previous negotiations with Enova contemplated that the company would retain the ability to collect amounts refunded to consumers to the extent permitted by law.

April 15, 2014, yet Enova knowingly continued to initiate an additional 5,600 debit payments from consumers' bank accounts without authorization after that notification. Accordingly, the facts would support a civil money penalty of nearly \$500 million from Enova before consideration of the statutory mitigating factors.

When considering the statutory factors required by 12 U.S.C. § 5565(c)(3), particularly relevant to this matter are the (1) severity of the risks or losses to consumers, (2) the size of Enova's financial resources, and (3) such other matters as justice may require. For the reasons discussed below, a civil money penalty of between \$3 million and \$5 million properly takes into account the required statutory factors.

i. The size of financial resources and good faith of the person charged.

While Enova is one of the largest and most profitable online lenders, generating over \$840 million in revenue in 2017, it likely does not have sufficient resources to pay a penalty in the range of \$500 million without significant negative impacts on its operations and offerings to consumers. Accordingly, some mitigation is warranted based on the size of Enova's financial resources.

ii. The gravity of the violation or failure to pay.

Here, the gravity of the violation does not serve as a mitigating factor on the recommended penalty range. Enova acted recklessly and at times, knowingly, and its misconduct involved unlawfully debiting millions of dollars from consumers' bank accounts without authorization. Failing to impose a significant civil penalty for the violations described above would not promote the goals of specific and general deterrence.

iii. The severity of the risks to or losses of the consumer, which may take into account the number of products or services sold or provided.

The "Flash Cash" and "Double Debit" issues impacted a small number of consumers relative to the total number of loans Enova makes on an annual basis, and the damages associated with these claims are less than \$100 on average for each consumer. The size of these claims may serve as a mitigating factor. With respect to Enova's unlawful debits, while consumers owed the amounts Enova unlawfully debited, as described above, consumers were nevertheless substantially injured by this unlawful conduct. It is therefore not, in Enforcement's view,

appropriate to consider the fact that the amounts debited were owed by consumers a significant mitigating factor here.

iv. The history of previous violations.

Enova is a recidivist. It was the subject of a 2013 consent order that resulted from misrepresentations it made to the Bureau exam staff and its efforts to conceal information from Bureau exam staff during an exam. Similarly, there is evidence suggesting that Enova has misrepresented to the Bureau when it became aware of its unauthorized debiting. Enova's history of similar violations and its misrepresentations to the Bureau thus do not provide a basis for mitigation.

v. Such other matters as justice may require.

As described in the previously approved recommendation memorandum, Enforcement previously recommended prioritizing obtaining redress for consumers over obtaining the maximum justifiable civil penalty. Now that the Bureau is no longer authorized to seek restitution for consumers, that consideration does not warrant further mitigation.

In addition to the statutory mitigating factors, the Bureau is authorized to "compromise, remit, or modify" the penalty in an enforcement action,³ including in the interest of obtaining a negotiated settlement. Enforcement recommends doing so here. We previously recommended a penalty in the range of \$1 million to \$3 million and restitution of \$2.1 million, prioritizing restitution over the penalty to be imposed. In light of the revisions to the claims and relief described herein, we believe a penalty of between \$3 million and \$5 million is appropriate as the monetary component of a settlement. Enova unlawfully collected approximately \$2.6 million from consumers' accounts (even leaving aside its other violations). Absent consumer redress, a penalty in an amount substantially less than \$3 million is likely insufficient to force the company to internalize the impact of its misconduct. The company likely will perceive its litigation risk to have decreased with the elimination of several claims and withdrawal of the Bureau's request that it provide redress to consumers, and may not be willing to settle, short of litigation, for an amount it might previously have been willing to pay. That said, we believe there is a realistic chance that it will agree to settle within these monetary parameters.

³ 12 U.S.C. § 5565(c)(4).

V. Injunctive Relief

The Bureau should seek appropriate injunctive relief that would, among other things, prohibit Enova from engaging in the conduct described in the revised draft complaint. Relevant injunctive terms should include a bar on debiting consumers' accounts without authorization, failing to honor loan extensions, and debiting consumers' bank accounts twice for the same monthly payment.

Attachments:

Tab 1: Draft Decision Memo from the SEFL Policy Director.

Tab 2: July 26, 2017 Recommendation Memorandum.

Tab 2a: July 26, 2017 Decision Memo

APPENDIX O

Consumer Financial Protection Bureau
1700 G Street NW
Washington, D.C. 20552



January 18, 2019

Recommendation memorandum for the Director

FROM	[Redacted by the Committee], Kristen Donoghue Office of Enforcement
THROUGH	Eric Blankenstein, SEFL Policy Director; Chris D'Angelo, SEFL Associate Director
SUBJECT	Consent Order and Stipulation – Enova International, Inc. – ENF Matter No. 2015-1636-02

ECS/Gaten 4/18/19

Recommendation

We recommend that you execute the Consent Order attached at Tab 1.

Timing Considerations

The attached consent order reflects a negotiated agreement between the Bureau and the Company to resolve the Bureau's investigation. Once entered, it will impose relief including conduct restrictions and monetary relief, and should therefore be addressed as soon as practical.

Background

On July 27, 2017, Director Cordray authorized the Bureau to settle with Enova for violating sections 1031 and 1036 of the Consumer Financial Protection Act of 2010 (CFPA), 12 U.S.C. §§5531, 5536 and section 1005.10(d)(2) of Regulation E, 12 C.F.R. § 1005.10(d)(2). See Tab 2. Under the delegation of authority from Acting Director Mulvaney for matters in which Director Cordray had previously authorized

Enforcement to settle or sue, the SEFL Policy Director revised the parameters for settlement. Those revisions are memorialized in an October 3, 2018 memo from Enforcement to the SEFL Policy Director. See Tab 3.

The attached Consent Order settles the Bureau's claims against Enova within those parameters.¹ The Consent Order includes the following terms:

- A civil money penalty of \$3.2 million;
- Injunctive relief related to the conduct at issue; and
- Reporting of compliance measures.

Attached as Tab 4 is the Stipulation and Consent to the Issuance of the Consent Order, which has been executed by Enova.

Release Sequence and Cadence Plan

Consistent with past practice, the Office of Enforcement will draft a short press release and an FAQ document that the Communications Office can use when the matter is made public.

Attachments

- Tab 1: Consent Order for your signature.
- Tab 2: July 27, 2017 Settle or Sue Authority (includes Enova's NORA Response).
- Tab 3: October 3, 2018 Authority to Revise Settlement Parameters (without attachments).
- Tab 4: Executed Enova Stipulation.
- Tab 5: Case Summary.

Pls assess whether the release & FAQ doc cover the case I've seen seeking the one pager or summarizing each enforcement matter. HJM to just keep those in some cases. Just don't want them to get too lengthy/involves go beyond

¹ During the course of negotiations, Enforcement agreed to eliminate the unfairness claim relating to Enova's double debiting of consumers' accounts to facilitate settlement, consistent with the revised settlement parameters.

Good/short summary for my reference later. Thanks.

APPENDIX P

**IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK**

Bureau of Consumer Financial
Protection and the People of the State of
New York, by Letitia James, Attorney
General for the State of New York,

Plaintiffs,

v.

Sterling Jewelers Inc.,

Defendant.

Case No.

COMPLAINT

The Bureau of Consumer Financial Protection (Bureau) and the People of the State of New York (State of New York), by its Attorney General (NYAG), bring this action against Sterling Jewelers Inc. (Sterling) and allege as follows:

INTRODUCTION

1. Sterling operates roughly 1,500 jewelry stores in malls and off-mall locations in all 50 states, including roughly 130 stores in New York State. Sterling does business as Kay Jewelers, Jared The Galleria of Jewelry, and a variety of regional brands, including JB Robinson Jewelers, Marks & Morgan Jewelers, Belden Jewelers, Goodman Jewelers, LeRoy's Jewelers, Osterman Jewelers, Rogers Jewelers, Shaw's Jewelers, and Weisfield Jewelers.

2. Sterling is a wholly owned subsidiary of Signet Jewelers Limited (Signet). Signet is the largest specialty-jewelry retailer in the United States, United Kingdom, and Canada. Sterling entities account for more than 60% of Signet's total annual sales of about \$6.4 billion.

3. Since 1990, and until at least October 2017, Sterling offered in-house credit financing directly to consumers to make purchases in its stores.

4. Consumers who visited Sterling's stores were typically encouraged by Sterling's salespeople to finance their purchases. Roughly 60% of Sterling's total sales are financed by consumers using Sterling's in-house credit. From 2014 through 2017, Sterling had over three million open credit accounts each year, and Sterling generated more than \$300 million in net revenue each year from such accounts.

5. Sterling's company culture, reflected in its training materials and sales-performance standards, pressures employees to enroll consumers in company credit cards and to sell its financing plans and payment-protection insurance.

6. The Bureau and the State of New York bring this action under §§ 1031, 1036(a)(1), 1054, and 1055 of the Consumer Financial Protection Act of 2010 (CFPA), 12 U.S.C. §§ 5531, 5536(a)(1), 5564, 5565, the Truth in Lending Act (TILA), 15 U.S.C. § 1601 *et seq.*, and its implementing regulation, Regulation Z, 12 C.F.R. part 1026, in connection with Sterling's credit-financing practices, including (1) submitting credit applications for consumers and causing credit cards to be issued without consumers' knowledge or consent; (2) misrepresenting credit-financing terms and conditions; and (3) enrolling consumers in payment-protection insurance without their knowledge or consent. The State of New York also brings this action under New York Executive Law (Exec. Law) § 63(12) and New York General Business Law (GBL) § 349.

JURISDICTION AND VENUE

7. This Court has subject-matter jurisdiction because this action is brought under “Federal consumer financial law,” 12 U.S.C. § 5565(a)(1), presents a federal question, 28 U.S.C. § 1331, and is brought by an agency of the United States, 28 U.S.C. § 1345. This Court has supplemental jurisdiction over the State of New York’s state-law claims because they are so related to the federal claims that they form part of the same case or controversy. 28 U.S.C. § 1367(a).

8. Venue is proper in this district because Sterling conducts business in this district. 12 U.S.C. § 5564(f).

PARTIES

9. The Bureau is an agency of the United States charged with regulating the offering and provision of consumer-financial products and services under “Federal consumer financial laws.” 12 U.S.C. § 5491(a). The Bureau has independent litigating authority to enforce “Federal consumer financial laws.” *See* 12 U.S.C. § 5564(a)–(b).

10. The State of New York, by its Attorney General, is authorized to take action to enjoin repeated and persistent fraudulent or illegal conduct under Exec. Law § 63(12) and deceptive business practices under GBL § 349. The NYAG is also authorized to initiate civil actions in federal district court to enforce provisions of the CFPA. *See* 12 U.S.C. § 5552(a)(1).

11. Sterling, an Ohio corporation, maintains its headquarters at 375 Ghent Road, Akron, Ohio 44333. Sterling operates jewelry stores and offers credit products to consumers in all 50 states, including in the State of New York. Sterling engages in

offering a “consumer financial product or service” under the CFPB. 12 U.S.C. § 5481(5)(A), (15)(A)(i). Sterling is therefore a “covered person” under the CFPB. 12 U.S.C. § 5481(6).

FACTS

12. Sterling offers consumers a credit card that provides a line of credit that can be used only at Sterling’s stores; it is not a general-purpose credit card.

13. Signing up consumers for Sterling credit cards built brand loyalty and caused consumers to be more likely to purchase goods at Sterling’s stores. According to one of its recent annual reports, “[t]he lifetime value of a customer obtained through the in-house credit program is estimated to be 3.5 times that of a customer not obtained through the in-house credit program.”

14. In connection with offering its credit products, Sterling’s salespeople misrepresented financing terms or omitted information necessary for consumers to understand the credit offer.

15. Store employees failed to inform consumers that they were applying for credit and misstated the reasons for requesting consumers’ personal information.

16. In many instances, Sterling’s sales representatives offered to check for a consumer whether the consumer qualified for a line of credit. In fact, the sales representative actually submitted a credit application for the consumer.

17. In many instances, Sterling’s sales representatives told consumers when they applied for credit that there would be no “hard inquiry” or negative impact on

consumers' credit reports because Sterling offered "in-house" financing. In fact, for each application for credit from Sterling, Sterling made a credit-report inquiry.

18. In many instances, Sterling's sales representatives induced consumers to provide their personal information by purporting to sign up consumers for a store "rewards card," loyalty program, newsletter, or mailing list. In fact, the sales representatives used consumers' personal information to submit a credit application.

19. In other instances, Sterling's sales representatives informed consumers that they were collecting personal information for a "survey" or to place a custom order for the consumer when, in fact, the information was used to complete a credit application.

20. Many of Sterling's store managers and district managers encouraged deceptive tactics to induce consumers to apply for a credit card, and many turned a blind eye to such conduct.

21. For example, Sterling's store managers and district managers told sales representatives not to use the term "credit card" but instead to refer to the credit card as a store card or a "Kay card."

22. Sterling's training materials instructed employees to offer credit to every customer who visited a store, and they included tips that enabled salespeople to distract the consumer, such as "offer to clean your Guest's jewelry while you fill out the credit application," and "completing the in-house credit account application for the Guest on the [in-store] tablet allows him/her to focus on his/her reason for visiting the Store, and not on completing paperwork."

23. Sterling's credit-card applications have been in both paper and electronic formats.

24. Sterling's training materials instruct employees to "[a]lways fill out the paper credit application or type the credit application into the Graphical POS for the Guest."

25. Because the credit application usually was completed not by the consumer, but by a salesperson on paper or on the employee-operated electronic tablet, many consumers never saw their credit-card application or any applicable terms and conditions.

26. In many instances, consumers were never given any written or oral credit disclosures or any indication they were applying for credit. Sometimes, consumers were given inaccurate oral disclosures about the terms of the credit.

27. Sterling's employees experienced pressure to obtain and submit completed credit-card applications.

28. Employees were rated, retained, and compensated based on their ability to meet certain performance standards, including for obtaining credit-card applications.

29. Sterling's companywide, formal performance standards required employees at stores located in shopping malls to complete "one credit card application a day." Employees at standalone stores were required to obtain one credit application every two days.

30. In some instances, employees who failed to meet the company's credit-application quota received counseling and additional training from store managers;

other employees were terminated for failing to meet credit-application performance standards.

31. Bonuses for certain Sterling's managers were determined, in part, based on the number of credit-card applications obtained by employees the managers supervised.

32. From 2013 through 2017, over one million Sterling credit-card accounts were opened based on applications completed and submitted in Sterling's stores and then never used by the consumers who had supposedly applied for them.

33. When consumers knew they were applying for credit, Sterling's employees sometimes misled consumers about the type of financing for which they were applying, as well as the applicable terms of the financing, such as the interest rate and monthly payment amount.

34. In such instances, consumers applied for credit from Sterling after employees presented them with certain terms—a low monthly payment or interest-free period—that were not honored. These consumers received credit cards and billing statements that did not match the representations made by the salespeople at the time consumers applied for credit.

35. Sterling's employees offered, and were trained to promote, interest-free financing.

36. In many instances, consumers were offered interest-free financing in connection with a purchase, only to find out upon receiving a billing statement that they were enrolled in a regular, interest-bearing credit plan.

37. Sterling's stores generally offered 6-, 12-, and 18-month interest-free promotional financing to customers, provided the customers met a minimum purchase amount and made a 20% down payment at the time of purchase.

38. In many cases, Sterling's employees offered customers promotional financing but then determined that the customers could not make a down payment at the time of purchase and thus did not meet the eligibility requirements for interest-free financing. In these instances, Sterling's employees instead enrolled the consumers in a regular interest-bearing financing plan without disclosing this to the consumer. Consumers often did not learn of this until they noticed it on a billing statement weeks or months later.

39. In other cases, consumers were quoted a monthly payment amount based on interest-free financing and were later quoted a lower monthly payment without Sterling's employees explaining that the lower monthly payment was not available with interest-free financing and instead required extending the repayment period on a regular, interest-bearing plan. In these instances, Sterling's employees did not tell consumers that they were getting regular financing, rather than promotional financing, and they did not disclose the changed financing terms to consumers at the time of purchase or obtaining credit.

40. Until roughly June 2017, Sterling offered to its credit customers Payment Protection Plan (PPP) insurance through a third-party insurance provider. PPP insurance was offered at the point-of-sale in 33 states, including the State of New York.

Although a third party administered PPP, Sterling was responsible for the marketing and sale of PPP.

41. PPP generated significant revenues for Sterling. In fiscal year 2016, for example, PPP sales generated more than \$60 million in revenues.

42. PPP insurance was an optional credit-insurance program offered to Sterling credit customers to help them make their monthly payments in the event of death, disability, loss of property due to burglary or perils, or loss of work. The PPP terms varied depending on the customer's state of residence.

43. PPP insurance was directly tied to the consumer's credit card because its function was to make monthly credit-card payments if the consumer met certain criteria. PPP insurance was not offered to customers, and could not exist, independent of the credit card.

44. In states where PPP insurance was offered, Sterling's employees were required to enroll customers in it to meet company performance standards.

45. Sterling's employees enrolled some consumers in PPP insurance without their knowledge or consent. In many instances, consumers were asked to "sign here" or select "Yes" on an electronic "PIN-pad" in order to hold an item, process an order, or verify their information when, in fact, their signature was used to enroll them in PPP.

46. Customers enrolled in PPP insurance at the store by electronically consenting to coverage on the PIN-pad they used to complete their purchase transaction.

47. The cost of PPP insurance varied depending on the type of coverage and state in which it was offered, but it averaged around \$0.97 per \$100 purchase or balance amount. This amount was charged monthly to the consumer's credit-card billing statement. In New York State, the cost of PPP insurance was \$0.224 per \$100 of account balance per month.

48. In many instances, PPP insurance was added to consumers' accounts or purchases without their knowledge or consent.

49. Consumers did not realize that they were electing to purchase credit insurance on the PIN-pad, often noting that they assumed they were signing in connection with the purchase, special order, or, if they were aware of it, the credit application, which occurred at the same time and as part of the same transaction as PPP enrollment.

50. Consumers often only discovered that they were enrolled in, and were being charged for, PPP insurance after noticing it on their billing statements.

51. In some instances, Sterling's employees told consumers about the PPP insurance and asked them to sign up so that the employees could meet their quotas—while promising the consumers that the employees would cancel the insurance before the consumers were charged. But the PPP insurance was not canceled and consumers were charged for a product they did not want.

52. In other instances, Sterling's employees told consumers that they were signing up to receive an informational packet to gauge their interest in PPP insurance; in fact, and unbeknownst to them, consumers were purchasing the product.

CAUSES OF ACTION

Count I—Deception under the CFPB Regarding Credit-Card Applications, Asserted by the Bureau and the State of New York

53. The allegations in paragraphs 1-52 are incorporated by reference.

54. An act or practice is deceptive if there is a representation or omission of information that misleads or is likely to mislead a consumer; the consumer's interpretation of the act or practice is reasonable under the circumstances; and the misleading act or practice is material. 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

55. In many instances, Sterling's employees represented to consumers that they were completing a survey, enrolling in a rewards program, or checking to see how much they would qualify to spend in the store when, in fact, the consumers were completing credit-card applications or Sterling's employees were completing applications for consumers without their knowledge or consent.

56. These misrepresentations were likely to mislead consumers acting reasonably under the circumstances because consumers believed they were providing personal information for other purposes and consumers relied on store employees' representations that consumers were doing something other than applying for a credit card.

57. These misrepresentations were material because many consumers likely would not have provided their personal information and signature if they knew they were applying for credit, given that they may not have wanted an extension of credit or the potential negative impact it could have on their credit file or ability to obtain credit in the future.

58. Furthermore, a reasonable consumer would want to know that his personal information and signature would be used to apply for a credit-card account at Sterling's stores.

59. The fact that the credit-card application disclosed the actual nature of the transaction does not correct the misrepresentations made to consumers.

60. Sterling's statements or omissions to consumers regarding credit applications were false or misleading and constituted deceptive acts and practices, in violation of the CFPA. 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

**Count II—Unauthorized Issuance of Credit Cards
under TILA and Regulation Z, Asserted by the Bureau**

61. The allegations in paragraphs 1-52 are incorporated by reference.

62. TILA provides that “[n]o credit card shall be issued except in response to a request or application therefor.” 15 U.S.C. § 1642.

63. Regulation Z states that no credit card may be issued to any person except in response to an oral or written request or application for the card. 12 C.F.R. § 1026.12(a)(1).

64. Sterling issued credit cards to consumers without their knowledge or consent and not in response to an oral or written request for the card.

65. Therefore, Sterling has violated TILA and Regulation Z. 15 U.S.C. § 1642; 12 C.F.R. § 1026.12(a)(1).

**Count III – Pursuant to New York Executive Law § 63(12),
Violation of TILA and Regulation Z, Asserted by the State of New York**

66. The allegations in paragraphs 1-52 are incorporated by reference.

67. N.Y. Exec. Law § 63(12) authorizes the NYAG to bring an action to enjoin repeated illegal acts or persistent illegality in the carrying on, conducting, or transaction of business.

68. TILA provides that “[n]o credit card shall be issued except in response to a request or application therefor.” 15 U.S.C. § 1642.

69. Regulation Z states that no credit card may be issued to any person except in response to an oral or written request or application for the card. 12 C.F.R. § 1026.12(a)(1).

70. Sterling issued credit cards to consumers without their knowledge or consent and not in response to an oral or written request for the card.

71. Therefore, Sterling has violated TILA and Regulation Z. 15 U.S.C. § 1642; 12 C.F.R. § 1026.12(a)(1).

72. By its actions in violation of TILA and Regulation Z, Sterling has engaged in repeated and persistent illegal conduct in violation of N.Y. Exec. Law § 63(12).

**Count IV—Violation of the CFPA,
Asserted by the Bureau and the State of New York**

73. The allegations in paragraphs 1-52 are incorporated by reference.

74. Sterling’s violations of TILA and Regulation Z, described in Count II, constitute violations of § 1036 of the CFPA. 12 U.S.C. § 5536(a)(1)(A).

Count V—Deception under the CFPA Regarding Promotional Financing Terms, Asserted by the Bureau and the State of New York

75. The allegations in paragraphs 1-52 are incorporated by reference.

76. Sterling’s employees misrepresented certain financing terms to consumers, including the applicable interest rate, monthly payment amount, and eligibility for promotional financing.

77. In these instances, consumers did not know the terms of the extension of credit they received until they noticed them on a billing statement.

78. Consumers reasonably relied on Sterling’s employees’ statements regarding the terms of the extension of credit they would receive, and consumers opened lines of credit and made purchase decisions on the understanding that they would receive the terms represented to them by Sterling’s employees.

79. Sterling’s statements or omissions to consumers regarding the terms of or consumers’ eligibility for promotional financing plans were false or misleading and constituted deceptive acts and practices, in violation of the CFPA. 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

Count VI—Unfairness under the CFPA Regarding PPP Enrollment, Asserted by the Bureau and the State of New York

80. The allegations in paragraphs 1-52 are incorporated by reference.

81. Under the CFPA, an act or practice is “unfair” where the Bureau has “a reasonable basis” to conclude that “the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers,” and that “such substantial injury is not outweighed by countervailing benefits to consumers or to competition.” 12 U.S.C. § 5531(c)(1).

82. Sterling's employees enrolled consumers in PPP insurance without their knowledge or consent.

83. This practice typically occurred when employees enrolled consumers in PPP insurance without informing them that they were being enrolled or misled consumers about what they were signing up for.

84. This conduct was likely to cause substantial injury because consumers were charged a monthly fee for the coverage in an amount proportional to their purchase or balance amount, which consumers could not reasonably avoid because they were not aware that they had the option to accept or decline coverage.

85. The harm to consumers from being enrolled in and charged for PPP insurance without their knowledge was not outweighed by countervailing benefits to consumers or competition; Sterling's practice of enrolling consumers in its optional PPP insurance without their knowledge or consent did not provide any benefits that would encourage legal business practices or competition.

86. Therefore, Sterling committed unfair acts or practices, in violation of §§ 1036(a)(1)(B) and 1031(c)(1) of the CFPA. 12 U.S.C. §§ 5536(a)(1)(B), 5531(c)(1).

**Count VII—Fraudulent Practices under
Executive Law § 63(12), Asserted by the State of New York**

87. The allegations in paragraphs 1-52 are incorporated by reference.

88. Exec. Law § 63(12) authorizes the NYAG to seek injunctive relief and other equitable relief and damages when a person or entity engages in repeated or persistent fraudulent conduct in the operation of a business.

89. Exec. Law § 63(12) broadly defines fraud to include “any device, scheme or artifice to defraud and any deception, misrepresentation, concealment, suppression, false pretense, false promise or unconscionable contractual provisions.”

90. Sterling has engaged in repeated fraudulent acts and practices in the operation of a business by conduct, including but not limited to: i) deceiving consumers about credit-card applications and enrollment; ii) misrepresenting to consumers the terms and conditions of Sterling’s promotional financing; and iii) failing to disclose that consumers are enrolling in payment-protection insurance.

91. Sterling has therefore engaged in repeated and persistent fraud in violation of Exec. Law § 63(12).

**Count VIII—Deceptive Practices under New York
General Business Law § 349, Asserted by the State of New York**

92. The allegations in paragraphs 1-52 are incorporated by reference.

93. GBL § 349 provides that “[d]eceptive acts or practices in the conduct of any business . . . in this state are hereby declared unlawful.”

94. GBL § 349 authorizes the NYAG to bring an action for an injunction, restitution, and civil penalties when any individual has engaged or is about to engage in deceptive practices in the State of New York.

95. Sterling’s employees have engaged in deceptive acts and practices by, including but not limited to: i) deceiving consumers about credit-card applications and enrollment; ii) misrepresenting to consumers the terms and conditions of Sterling’s promotional financing; and iii) failing to disclose that consumers are enrolling in payment-protection insurance.

96. Sterling has therefore engaged in deceptive acts or practices in violation of GBL § 349.

DEMAND FOR RELIEF

The Bureau and the State of New York request that the Court:

- a. enjoin Sterling from committing future violations of the CFPA, Truth in Lending Act, Regulation Z, Exec. Law § 63(12), and GBL § 349;
- b. order Sterling to pay damages, restitution, or other monetary relief to consumers;
- c. order Sterling to pay disgorgement or compensation for unjust enrichment;
- d. impose a civil money penalty under the CFPA;
- e. impose a civil money penalty for each violation of GBL § 349 pursuant to GBL § 350-d;
- f. order Sterling to pay the costs incurred in connection with prosecuting this action; and
- g. award additional relief as the Court may determine to be just and proper.

Respectfully submitted,

KRISTEN A. DONOGHUE
Enforcement Director
JEFFREY PAUL EHRLICH
Deputy Enforcement Director

s/ Patricia H. Hensler
PATRICIA H. HENSLER (FL 102303)

LETITIA JAMES
*Attorney General of the State of
New York*

JANE M. AZIA (NY 1539600)
*Bureau Chief, Consumer Frauds
and Protection Bureau*

STEFANIE ISSER GOLDBLATT (NY 2750594)
NAVID VAZIRE (NY 4520391)
Enforcement Attorneys
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington, D.C. 20552
Telephone (Hensler): 202-435-7829
Telephone (Goldblatt): 212-328-7011
Telephone (Vazire): 312-577-7670
Facsimile: 202-435-7722
E-mail: Patricia.Hensler@cfpb.gov
E-mail: Stefanie.Goldblatt@cfpb.gov
E-mail: Navid.Vazire@cfpb.gov
Attorneys for Plaintiff
Bureau of Consumer Financial Protection

CAROLYN FAST (NY 4095535)
Assistant Attorney General
28 Liberty St.
New York, N.Y. 10005
Telephone (Azia): 212-416-8727
Telephone (Fast): 212-416-6250
Facsimile: 212-416-6003
E-mail: Jane.Azia@ag.ny.gov
E-mail: Carolyn.Fast@ag.ny.gov
Attorneys for Plaintiff
State of New York

APPENDIX Q



~~9 August 24, 2018~~ ~~August 9, 2018~~

Recommendation Memorandum for the Acting Director

FROM	Redacted by the Committee [REDACTED] Jeff Ehrlich, and Kristen Donoghue, Office of Enforcement
THROUGH	Eric Blankenstein, SEFL Policy Director; Chris D'Angelo, SEFL Associate Director
SUBJECT	Authority to Settle with Sterling Jewelers, Inc. and to File Suit—ENF Matter No. 2016-1806-02

Recommendation

The Office of Enforcement recommends that you authorize it (1) to settle with Sterling Jewelers, Inc. (Sterling) under the parameters described in Section IV below; (2) if settlement negotiations are successful, to file an administrative consent order or a complaint and consent order in federal court effectuating the settlement; and (3) if settlement negotiations are unsuccessful, to commence an enforcement action either administratively or in federal court, consistent with the attached complaint.¹ This investigation was conducted in partnership with the New York State Attorney General's Office, and, if authorized, the Bureau would file a joint complaint with that office.

I. Overview

Sterling operates roughly 1,500 jewelry stores in malls and off-mall locations in all 50 U.S. states under national banners that include Kay Jewelers and Jared The Galleria of Jewelry, as well as a variety of mall-based regional stores such as J.B. Robinson, Marks & Morgan, and Belden Jewelers. Sterling is a wholly-owned subsidiary of Signet Jewelers Limited (Signet), the largest specialty-jewelry retailer in the United States, United Kingdom, and Canada. Sterling entities provide over 60% of Signet's total sales of about \$6.4 billion. Since 1990, and until recently, Sterling has had a centralized consumer-financing program through which it has extended credit directly to consumers.² As part of its in-house credit program, Sterling has offered "interest-free"

¹ Enforcement also seeks authority to make non-material changes before filing.

² In October 2017, Signet, through Sterling, sold a portion of its consumer-lending portfolio—\$1 billion of its prime-credit business—to Alliance Data Systems. In March 2018, Signet announced

and interest-bearing financing, subject to certain conditions, and, in most states, it also offered third-party credit insurance. Roughly 60% of Sterling's total sales are credit sales, and the fees and charges from Sterling's credit-financing programs have totaled roughly \$300 million on average for each of the past three years. As part of the investigation, Enforcement (i) interviewed former employees and customers; (ii) supervised secret-shopping trips to a wide range of stores to observe sales practices and techniques; (iii) reviewed Sterling's internal training materials and employee-incentive structure; and (iv) analyzed thousands of consumer complaints. As described further below, the Office of Enforcement has found and concluded that Sterling employees are signing consumers up for credit cards without their authorization or consent, misrepresenting credit financing terms and conditions to consumers, and enrolling consumers in optional payment-protection insurance without their knowledge or consent.

Commented [Re]: Global comment: Given Sterling's arguments in its NORA response that the sales practices here were isolated incidents and do not reflect systemic problems, it would be helpful for the fact section to provide more detail about the scope of the investigation

Commented [R7]: How many?

Commented [R3]: How many?

Commented [BE4]: Is present tense appropriate given that Sterling is exiting the credit business?

Commented [Re]: Could we clarify the time period during which these practices have occurred?

The Bureau has authority to address Sterling's conduct because it offers credit to consumers. Sterling is not subject to the CFPA's "merchant exemption" because it regularly extends credit subject to a finance charge and is significantly engaged in offering or providing consumer-financial products or services.³

~~The Bureau should resolve this matter through settlement. This matter would best be resolved through settlement.~~ Because the specific terms of any consent order will be subject to negotiation and ongoing modification, a draft consent order is not attached to this memorandum. The Office of Enforcement will discuss any proposed order with the Legal Division before submitting it to you. If settlement negotiations fail, the Bureau should file suit, either administratively or in federal court, consistent with the attached complaint.

II. Factual Background

Customers report that they were given credit cards that they did not want. In some instances, consumers knew they were being offered credit but ~~allege claim~~ that Sterling employees presented them with certain terms—a low monthly payment or interest-free period—that were then not honored. These consumers received credit cards and billing statements that did not match the representations made by the salespeople at the time consumers applied. Consumers were also enrolled in Payment Protection Plan (PPP) insurance and claimed it was without their knowledge or consent. In many instances, consumers report that they were asked to "sign here" in order to hold an item, process an order, or verify their information, when in fact these consumers were signing up for PPP.

Commented [BE6]: What is the source of this? Complaints to the Bureau? Interviews? Something else?

The Bureau's investigation focused on three issues related to Sterling's credit business: (1) consumers received unauthorized credit cards; (2) credit-financing terms and conditions were not accurately disclosed; and (3) consumers enrolled in payment-protection insurance without their knowledge or consent.

that it would sell the remaining portion, Sterling's non-prime receivables, to investment funds managed by CarVal Investors.

³ See 12 U.S.C. § 5517(a)(2)(B)(iii), (a)(2)(C)(i).

A. Unauthorized Accounts

When a consumer applies for credit in one of Sterling's stores, Sterling store employees request personal information from the consumer, complete the application on the consumer's behalf, and serve as the primary source of information for the consumer. Because the employee holds the application, consumers do not see that it is an application for credit, nor do they see the applicable credit disclosures, which are displayed in general terms, e.g., APR 5% to 24.99%, in fine print on the back or folded portion of a paper application and, for electronic applications completed on a tablet, are not provided on any screen shown to consumers. There does not appear to be any process or requirement for consumers to receive written or oral disclosures at the time of the transaction, and many consumers specifically describe not receiving any oral or written disclosures. Consumers report that Sterling employees do not show consumers the credit application and misrepresent the reason for which they are requesting consumers' personal information. In many instances, consumers unknowingly and without giving consent, apply for Sterling's store-brand credit cards.

Consumers allege that Sterling sales representatives offered to see whether the consumer was qualified for a line of credit but then proceeded to submit a credit card application for the consumer. These consumers indicate they did not intend to apply for a credit card and only thought the sales person was gauging their creditworthiness. Bureau investigators conducting undercover store visits also noted that Sterling's salespeople offered "to run [their] credit for approval" and stated it would only be a "soft inquiry" on their credit report. One Jared store employee told a Bureau investigator, "Jared has its own bank and therefore the credit approval process is done in-house and doesn't affect your credit report." Although consumers must actually apply for credit in order to verify how much they are qualified to spend in the store, they do not understand—and Sterling employees did not inform consumers—that by agreeing to have a store employee assess their credit-worthiness, they were in fact applying for credit. In some instances, Sterling employees explicitly assured consumers that because the store offers "in-house" credit, it does not have any impact on consumers' credit reports. In other instances, employees simply offered to check consumers' credit without informing them it will result in a card being issued.⁴

Consumers were also asked to provide personal information to sign up for the store "rewards card," newsletter, or mailing list, when the information was in fact used to apply for a credit card. In numerous consumer complaints, consumers alleged that they believed they were providing information for a "survey" and only later learned they were applying for credit. Consumers consistently report that they were never given written disclosures or any indication that they were applying for credit.

Here are a few complaints from consumers. Representative consumer complaints include:

- "I bought an engagement ring from Jared the Galleria of Jewelry. I stated from the beginning I would be paying for the ring and all charges with my American Express Card. The salesperson then filled out forms to open a credit card for me without my

Commented [BE(7)]: What is the basis of these statements? Mystery shopping? Consumer complaints? Are we sure that these statements are representative of the process in all of Sterling's stores, as opposed to a few bad apples? If so, how?

Commented [R(8)]: What about the credit card agreement brochure discussed on page 9 of the NORA?

Commented [R(9)]: Could we clarify where this information is coming from – e.g., consumer complaints or interviews? And can we provide a sense of the volume of complaints/interviews that we're relying on? Part I of the memo says there were thousands of complaints, but it isn't clear how many complaints were related to the unauthorized accounts issue

Commented [R(10)]: Could we clarify how many undercover visits were conducted? Were problematic statements made during all of the undercover visits, or some?

Commented [R(11)]: In its NORA response, Sterling claims that customers see disclosures regarding their credit application when they sign paper applications or on tablets. See pp 10-11, 23. Can we address that here?

Commented [BE(12)]: Do we have a number? Was this observed by our undercover shoppers? If so, how many? If it is based on complaints, how many of this nature do we have?

Commented [BE(13)]: Did that information include SSN and annual salary? Would someone acting reasonably under the circumstances think that information as necessary to sign up for a mailing list?

Commented [R(14)]: Can we be more specific?

Commented [R(15)]: Same comment

⁴ Consumer complaints, consumer interviews, and direct observations through undercover store visits support these facts.

knowledge. When it was time to close the sale, they presented the form to me, saying it was required to order the diamonds/ring that I wanted so I signed it. They had the paper form folded in such a way that I could not see that it was for a credit card.... [T]hey opened a credit card in my name without my consent via deceptive sales practices and outright manipulation....”

- “I was told that I was signing up for an employee loyalty program at JARED Jewelry that would send me coupons and cash back on further purchases. I explicitly asked multiple times if they were setting up a credit card, and the sales representative assured me he was not. I became suspicious once he asked for more personal information such as employment history and my Social Security Number. I asked again if this was signing me up for a credit card, and the sales representative told me no. He stated they were only doing an internal background check but no credit would be opened. A few days later, I went to sign up for a credit card from a company I actually wanted a credit card from, and I was declined. They stated the reason was that I had too much credit open in my name... A few days later, I received in the mail a credit card from JARED....”
- “I would like to file a complaint against Kay Jewelers. They signed my fiancé and myself up for a credit card without telling us...the sales representative...said we were signing an agreement for the custom ring they were going to design for us...We were signed up for not one, not two, but THREE cards which were received in the mail a week after starting the process with them. They just tell you it's a contract for the custom ring, if we had known it was a credit card application we would have refused to fill out the paperwork.”
- “[A] Kay Jewelry saleswoman wanted me to fill out a form so that I can take care of some kind of 'promotional coupon' that would be sent in the mail... I received a letter from the Kay Jeweler's Credit Operations Division which stated that they turned down my application to open some kind of credit account because I do not make enough money. First, respectfully, the saleswoman took my social security number because she told me that it was only to prevent fraud and that they would not use it for anything else (I have no idea how it would prevent fraud, but she seemed honest)! Second, she never took my income information down...so I don't even know how Kay Jewelers was able to find out how much I make without me divulging that information unto them. This dishonest tactic may lower a great credit score.”
- “The representatives I worked with, Patricia and Katrina, said they would like to screen my credit in order to determine the price range of rings we could qualify for. I insisted repeatedly that I did not want a credit card as we had not yet determined where we would be buying a ring, but they stated explicitly that they would be doing a preliminary screening of my credit only. They said they would not be issuing a credit card, and this was a standard procedure to see what amount someone can qualify for. After the "preliminary screening," I was told I was approved for a \$10,000 credit limit, and that any questions I had would likely be answered with the paperwork that would be coming with my credit card in the mail. I reminded them that I did not want a credit card, and that they said this was supposed to be preliminary screening, and they replied saying it was fine because if I didn't want the card, it would be closed in 2 years if I don't use it. I did not want the credit card, and was lied to in order for them to set up an account in my name.”

Commented [BE(16)]: Not saying take this out, but I'm dubious about the causation allegations here given the credit and furnishing cycle

Interviews with former store employees further substantiate consumers' reports. Specifically, multiple employees at various stores in different geographical locations stated that they were trained to ~~coerce~~ mislead customers into applying for credit cards—telling consumers they were signing up to be “preferred customers,” specifically refraining from using the term “credit card” and instead asking consumers to open a “rewards card,” and asking consumers to help the employee “win a contest” by filling out a form for a “customer account.” Former employees said they would offer discounts on jewelry for opening a card—even where items were already discounted without opening an account—or offer free watch-battery replacement to consumers if they open an account.

Commented [R17]: Can we be more specific here, and identify the number of employees interviewed, number of stores they worked in, etc.?

Commented [BE18]: Formal training or guidance from managers/co-workers? If the former, do we have documents to substantiate?

Sterling's performance standards require its store employees to sell credit cards to consumers. Mall-store employees are required to obtain one credit-card application a day, while standalone-store employees are required to obtain one credit-card application every two days. Employees who fail to meet these thresholds receive counseling and additional training from store managers and, in some instances, are terminated. Interviews with consumers and former employees suggest that there was intense pressure to meet Sterling's goals. Hundreds of anonymous employee reviews on www.glassdoor.com, a database of employee-authored company reviews, reiterate employees had trouble meeting their credit-card quotas.

Commented [BE19]: How many?

Commented [BE20]: Did we request personnel files of individuals we think were terminated for not meeting sales goals to verify?

Commented [BE21]: Formal or informal? Companywide? Documented?

Commented [BE22]: How would consumers know this?

Commented [BE23]: To us or to glassdoor.com?

Commented [BE24]: Number? Were they at the same location/region?

Former employees reported that employees who did not meet credit-card quotas were “written up,” had to go in to the store on their days off or before or after work for credit-card meetings, and were lectured on “getting their numbers up.” Several former employees said there was a training for “employees not meeting their numbers” that was a two to four-hour drive away from their store's location. Former employees also said that they could be fired for failing to obtain credit-card applications.

Commented [Re25]: Did any former employees say that the pressure to meet the numbers drove employees to engage in the deceptive sales practices we allege?

In addition to rating employees on their ability to meet or exceed the standard for new credit-card applications, Sterling runs an annual four-week credit-application contest that awards cash to employees at all levels, including sales representatives, store managers, and district managers, who obtain the most credit-card applications.

Sterling's training materials instruct store employees to offer credit early and often to every customer. They include tips such as “offer to clean your Guest's jewelry while you fill out the credit application” and “completing the in-house credit account application for the Guest on the CASSi tablet allows him/her to focus on his/her reason for visiting the Store, and not on completing paperwork.” In fact, because the in store credit-application process is largely completed on the employee-operated tablet, most consumers never see a full credit-card application—nor do they see applicable terms and conditions or disclosures. Regardless of the type of application, employees are instructed to “[a]lways fill out the paper credit application or type the credit application into the Graphical POS for the Guest” so customers do not see the credit application. Sterling also provides guidance to store employees on how to overcome consumers' objections to credit accounts and additional suggestions, such as presenting a credit line with a piece of jewelry to distract the customer.

Commented [Re26]: Even if the policies and training weren't followed, it would be helpful to acknowledge here that Sterling's policies and training provide that customers must understand that they are applying for credit and comply with applicable law. See NORA response at 11-12.

Commented [BE27]: Basis? Would it be more accurate to say “at least some consumers”?

The Bureau obtained from Sterling data identifying the number of company credit-card accounts that were opened but never used. Sterling stores issued about 285,000 credit cards each year that

had no activity on them. Over a three-year period, the total number of Sterling accounts opened without any purchases made was nearly one million.

Commented [BE{28}]: I think this is great circumstantial evidence, but we should at least acknowledge the Sterling argument that people don't use the cards because they don't get qualified for enough credit to cover the purchase they want to make (if we address it below we should drop an FN directing the reader to that section)

B. Deceptive Representations About Financing

Consumers report that Sterling employees provide certain financing plan information at the point-of-sale that turns out to be different than the financing plan terms they receive. Employees offer, and are trained to promote, "interest-free" financing. Numerous consumers indicate that consumers were offered interest-free financing in connection with a purchase only to find, once they receive their first billing statement, that they were actually enrolled in a regular, interest-bearing credit plan. In these cases, the consumers were often quoted a monthly payment amount and other terms that differ from the terms of the plan for which they are enrolled.

Commented [Re{9}]: As above, it would be helpful to get more specific information about the volume of complaints about this practice, given Sterling's assertion that we are relying on isolated incidents

Sterling stores generally offer interest-free promotional financing for periods of 6, 12, and 18 months to customers who meet a minimum purchase amount and pay a 20% down payment. Consumer complaints and interviews of employees indicate that, in many cases, customers who expected to receive interest-free financing were actually given regular, interest-bearing financing. This typically happened for one of two reasons. First, if a customer could not make a down payment at the time of purchase and thus did not meet the eligibility requirements for interest-free financing, he would in many instances be signed up for a regular financing plan instead without being told by the employee of the switch. Second, if a consumer indicated that he could not afford the monthly payment amount that was calculated based on the promotional period for the interest-free plan, he would in many instances be given a lower payment amount that was calculated based on a longer repayment term and regular interest-bearing financing, also without having the changed terms explained. In both scenarios, Sterling employees explained the availability of interest-free financing and consumers believed they would receive it, but didn't clearly inform consumers that they would not after it became clear that they didn't qualify for or couldn't afford the payments required for the interest-free promotion.

Commented [R{30}]: Same comment

Interviews with former employees corroborate consumer complaints alleging misinformation and changed credit-card financing terms. Former employees mentioned that they would incentivize customers to open accounts by promising "12-months interest-free"—though this required a minimum purchase amount, which they did not disclose—and "no down payment," which voids interest-free financing options. For example, one former employee said that for items below \$500 there was not an interest-free financing option, but employees would pitch "no interest" in the hope that no one would notice.

Commented [BE{31}]: (Hoping this is addressed later) Do we plan to seek restitution for these practices? If so, how do we intend to seek the affected population given that all of the alleged deceptive statements were made orally and therefore there would be no record?

Commented [BE{32}]: Global – though noted in other places, where we attribute statements to former employees we should make it clear that we talked to people in different stores/regions so that we have legitimate basis to believe that the conduct is company-wide and not limited in scope

C. Payment Protection Plan

Similar to the credit-card-application quota, Sterling employees were required to enroll customers in optional PPP insurance to meet performance standards. PPP is a credit-insurance program that was offered to Sterling credit customers to help those customers make their monthly payments in the event of death, disability, loss of property due to burglary or perils, leave of absence, job retraining, or involuntary loss of employment. Because the insurance protected consumers' credit payments, it was directly related to the credit financing that Sterling

Commented [BE{33}]: This is a serious charge Is it supported by documents?

offers, and it provided a direct benefit to Sterling by protecting its accounts receivable from loss due to non-payment.

Sterling stores sold PPP to credit customers through Assurant,³ a state-licensed insurance company, from at least 2009 to October 2017. PPP was offered at the point-of-sale in 33 states. The cost of PPP varied depending on the type of coverage and state, but it was typically around \$.78 cents per \$100 purchase amount. This amount was charged monthly on the consumer's credit-card billing statement based on the account balance. Although Assurant administered PPP, Sterling was responsible for the marketing and sale of PPP.

Customers were routinely enrolled in PPP insurance at the time of their credit application or purchase transaction without knowing they were doing so and without ever viewing the insurance terms and conditions or costs. Customers in many instances "agreed" to enroll in PPP at Sterling stores by electronically consenting to coverage on the PIN-pad they used to complete their purchase transaction. The customer-acknowledgment was presented on the PIN-pad device, but the terms and conditions and costs for PPP were not displayed. In some instances consumers may have been shown a brochure detailing, in general terms, the PPP benefits; however, many consumers did not see any disclosures, particularly those consumers who enrolled in PPP without their knowledge or consent.

Commented [BE34]: Are we sure about this? Did we ask in the investigation for screenshots of information displayed on PIN pads to confirm? Or is this only based on customer/employee statements?

According to Sterling's training materials, customers were prompted to indicate, on the PIN-pad, "Yes" or "No" as to whether they would like to purchase the PPP, immediately after the store employee swiped the customer's credit card. If the customer selected "Yes," the employee was instructed to enter the customer's birthdate, and the customer was then prompted to sign the PIN-pad. If a customer selected "No," they were still required to sign the PIN-pad, confirming that they were opting-out of coverage. The PIN-pad sequence mirrored a typical retail transaction where, after providing payment, the consumer indicates "Yes" as to the purchase amount or form of payment, before signing the PIN-pad to complete the transaction. Here, consumers did not realize that they were electing to purchase credit insurance, often noting that they assumed they were signing in connection with the purchase, special order, or, if they were aware of it, the credit application, which occurred at the same time and as part of the same transaction.

Commented [BE35]: In the next paragraph we note that the pin pad displayed more than a simple Yes/No. We should update this description to more accurately reflect the information provided to the customers.

There is no indication that employees necessarily provided the customer with any written terms and conditions or costs of the PPP. Sterling's internal materials state that store employees "may" present product benefits, coverages, and rate information to customers. As noted above, there was a hard-copy brochure. But (1) employees were not required to provide the brochure to consumers; (2) the applicable insurance terms were in small, very fine print; and (3) the terms referenced the various types and costs of insurance but did not provide any specific coverage or cost for the individual consumer. Sterling's PPP materials indicate that the PIN-pad displayed: "Yes, I would like to purchase optional Payment Protection Plan Credit Insurance." But there were no specific terms and conditions or costs displayed on the PIN-pad, and the text that was

Commented [BE36]: Relevance?

³ Sterling Jewelers Insurance Agency, Inc., a wholly-owned subsidiary of Signet, provided insurance licensing functions for Sterling's credit-insurance programs.

displayed was in small font and not easily visible due to the limited clarity and contrast of the PIN-pad screen.

Commented [R37]: Do we have any documents or pictures showing how the PIN-pad text appeared to consumers?

Former Sterling employees indicated that customers would be hurried through the point-of-sale transaction and told to "initial here"—encouraging the customer to enroll in PPP.⁶ One former employee explained: "you didn't tell people about the product, you just put it on there." That is, sales associates signed people up for PPP insurance without asking, and if someone noticed and complained, they'd remove it. Another former store manager said that district managers told store managers to check "Yes" for PPP even if customers didn't ask for it, noting that the store could always cancel it the next day but that the store would be "credited" for it even if it was later canceled, so "always check 'Yes.'" Based on this evidence, it seems it may be possible for store employees to select "Yes" for the customer and add PPP to consumers' accounts without the consumer affirmatively selecting "Yes."⁷

Commented [BE38]: Declined?

Consumers complain that PPP is added to their account without their knowledge or consent. Some consumers complain that Sterling employees asked them to sign up for PPP to help the employees meet their quotas; the employees promised that they would cancel the insurance before the customer would be charged, but they failed to do so. In one complaint, the consumer reported that he was told by the salesperson to select "Yes" and sign the PIN-pad to receive an insurance packet to gauge his interest and then discovered when the packet arrived that he had agreed to purchase the insurance. In response to such a complaint, Sterling's internal account notes indicate that the store apologized for putting PPP on without the consumer's knowledge, canceled the PPP, and refunded charges. In other cases, consumers allege that they believed they were rushed through the transaction at the point-of-sale and later discovered that they had inadvertently signed up for PPP. Most commonly, consumers discovered that they were being charged for PPP only after noticing it on their billing statements.

Commented [R39]: Could we specify the number of complaints relating to this issue?

Here are a few consumer complaints about PPP:

- "I signed up for a credit card with Jared. When I paid off the promotional, '1 year no interest' balance in just 3 months, I learned that a credit protection fee had been being assessed/added to my balance. After call[ing] to question it, the associate, Lila #3666, insisted that I hadn't questioned it early enough, so she would only remove 45 of the \$224 assessed. Only after speaking with a manager did they pull up my agreement, acknowledge that I had never agreed to purchase the insurance, and agree to reimburse me for the fees charged. Research needs to be done/legal action take[n a]gainst Jared for charging me and other consumers fees for services they did not agree to."⁸

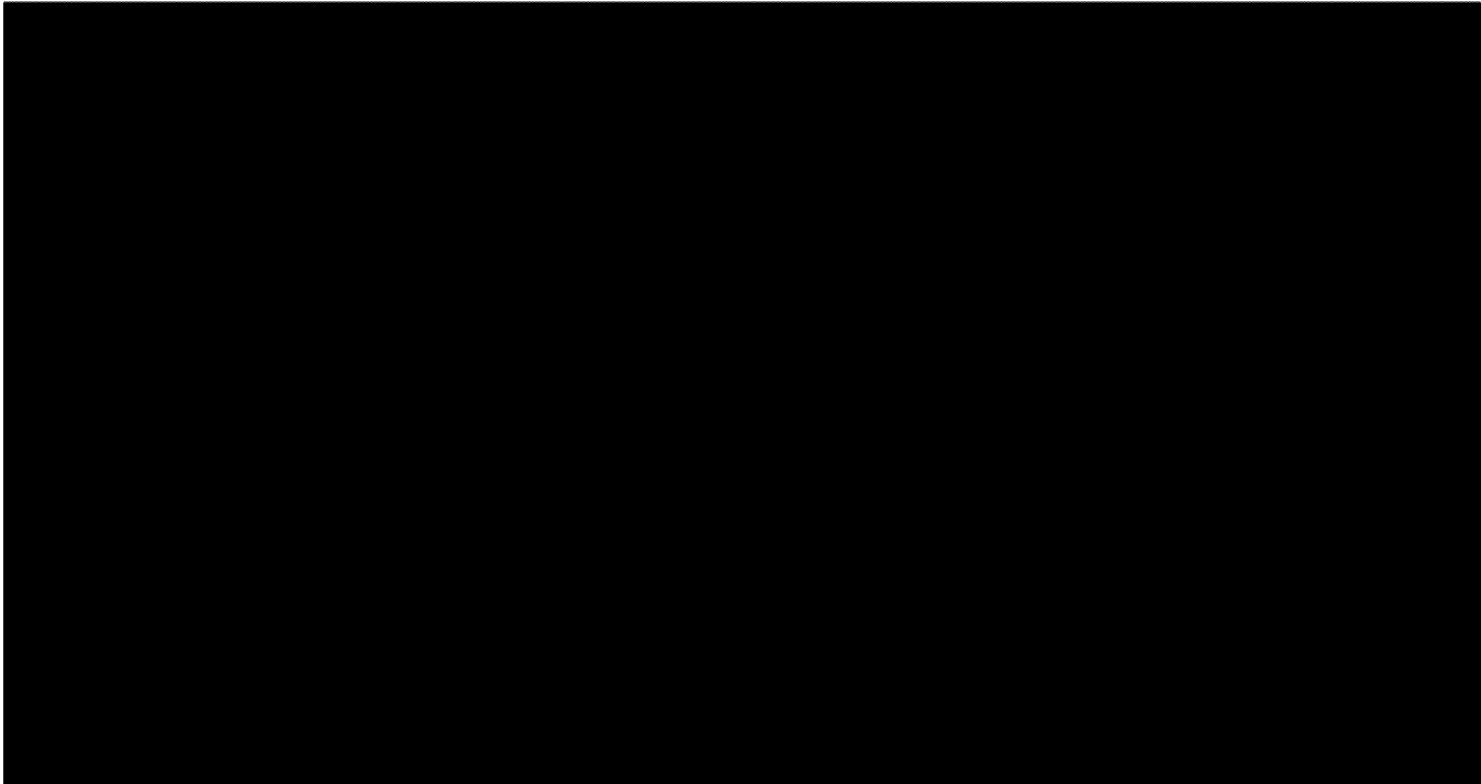
⁶ Sterling's training document instructs: "Use an assumptive close when closing PPP."

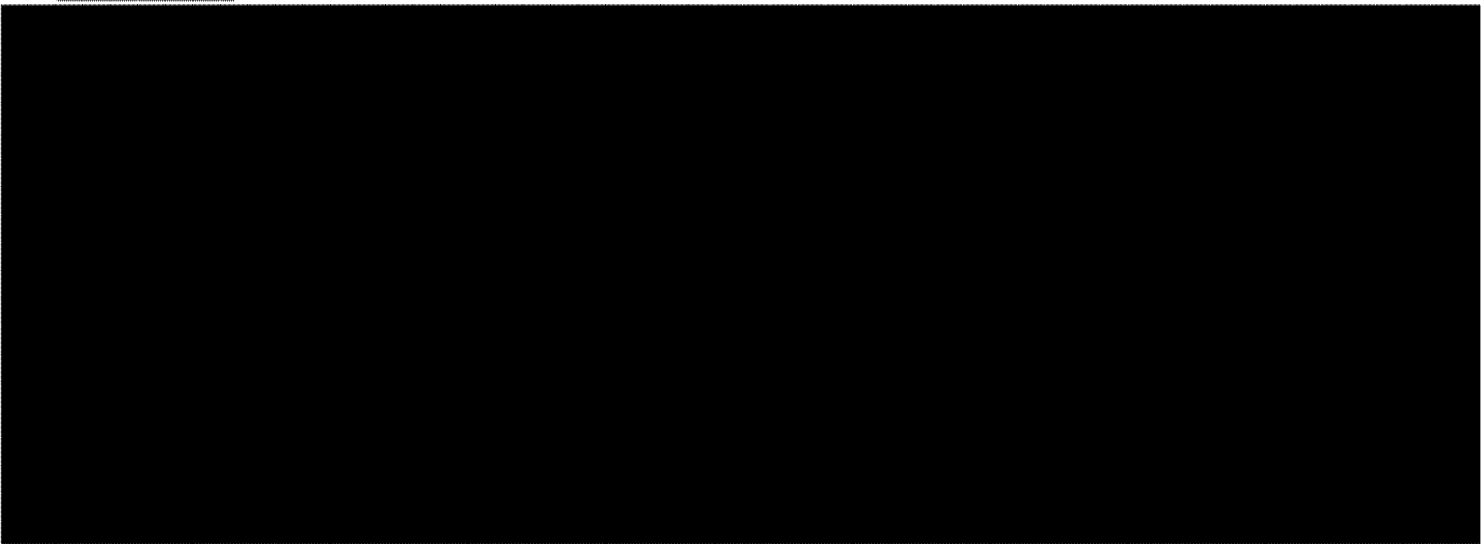
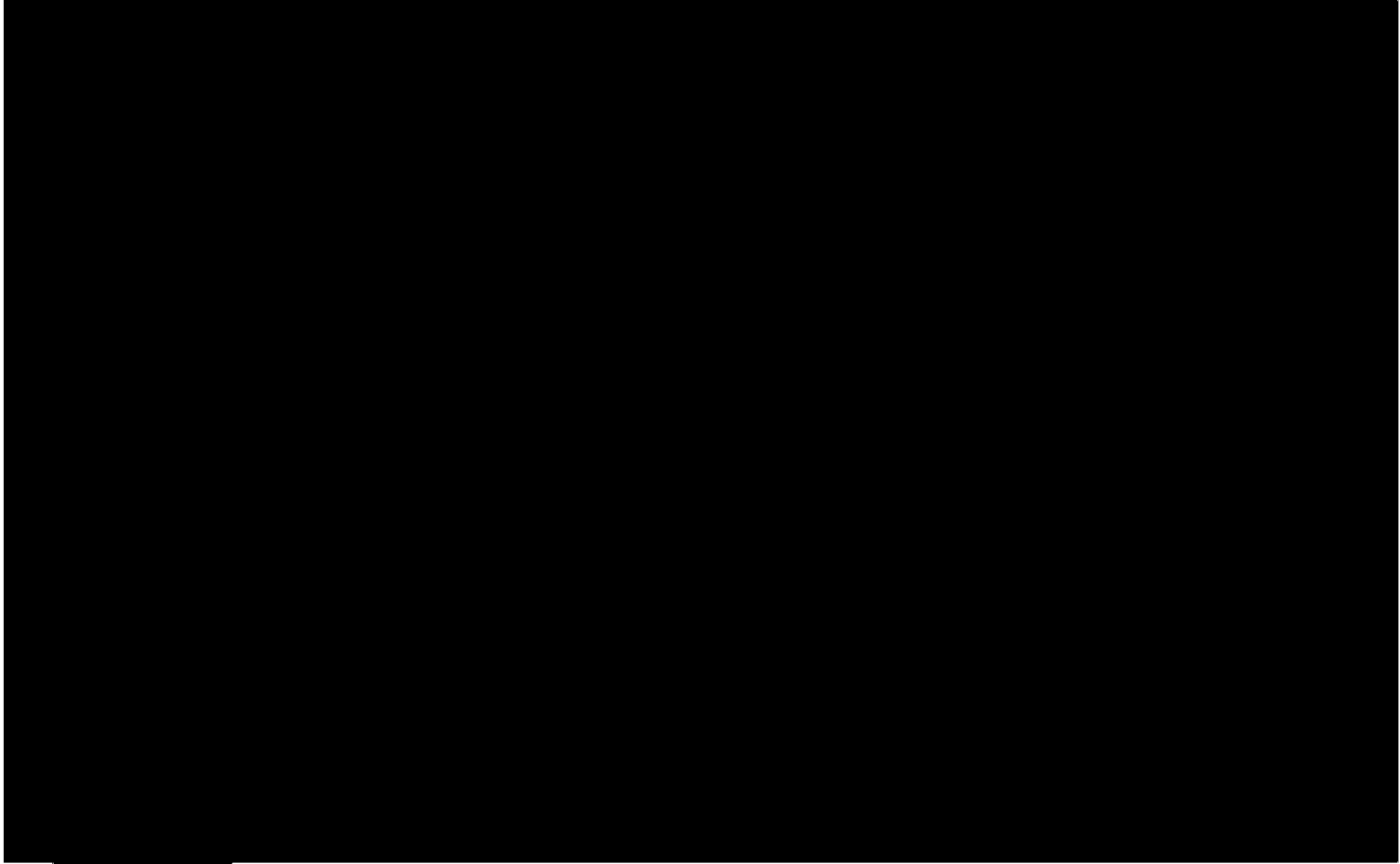
⁷ In addition, Sterling's PPP enrollment procedures specify steps the employee must take "[i]f you do not have a customer's signature either via the PIN-pad or on the sales slip," which suggests it was technically possible enroll a consumer without obtaining a signature.

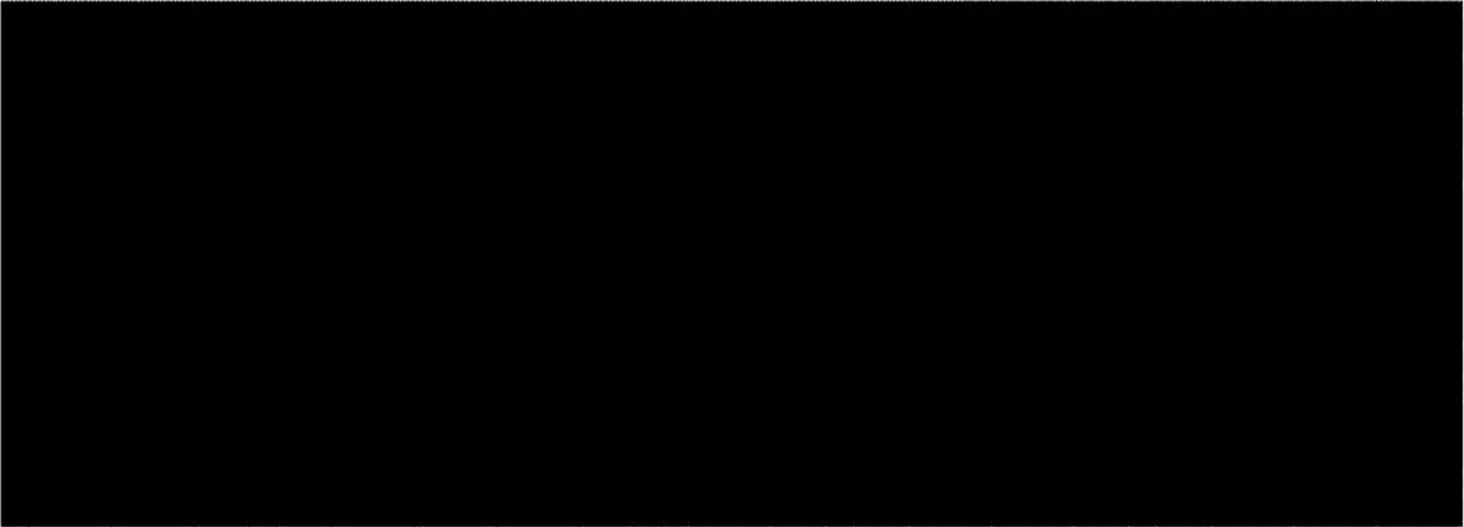
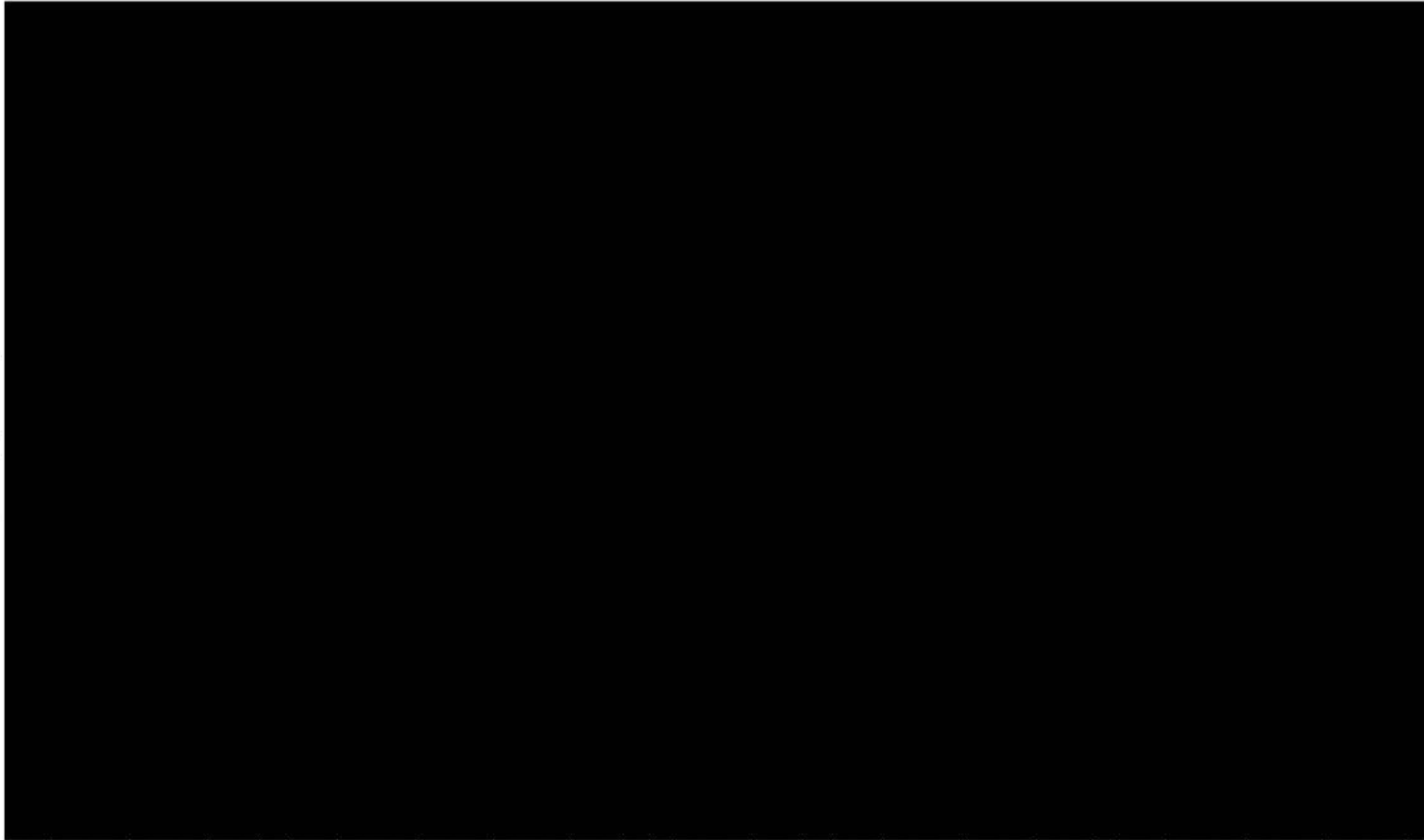
⁸ Sterling responded: "In your case, even though our system indicates that PPP had been accepted at the time of sale, we were unable to locate a signature confirmation of enrollment. In light of the missing signature, a supervisor authorized a return of \$224.20 that your account had been billed in total for PPP."

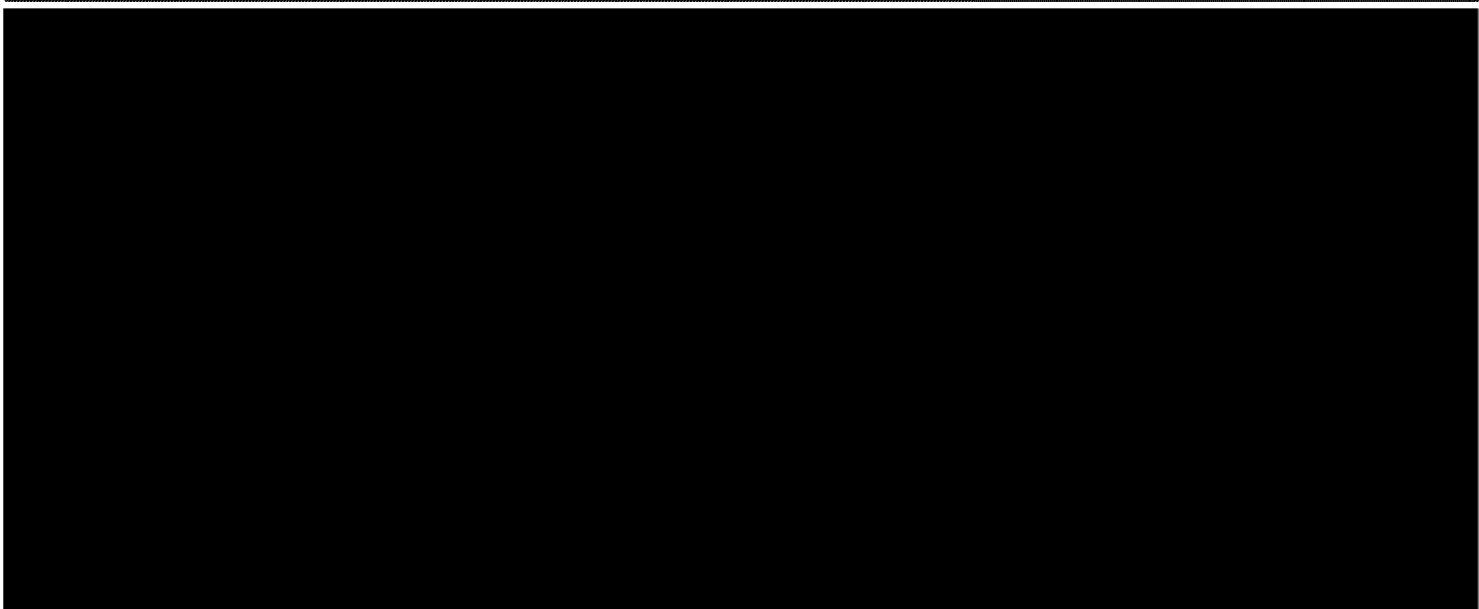
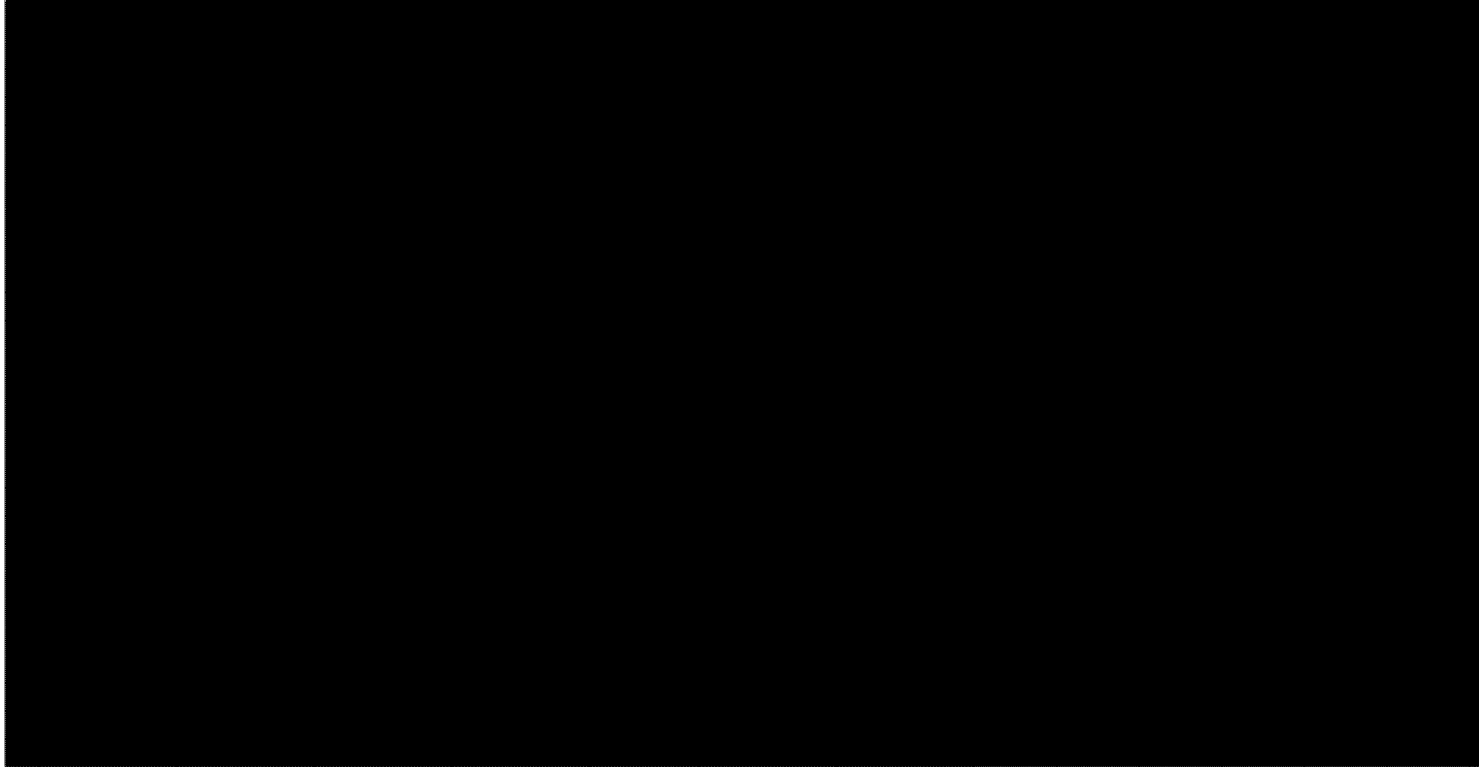
- “[The store employee] tried to get me to enroll in their ‘PPP’ or personal payment protection plan (i.e. credit and life disability insurance) all at an obscene rate.... He told me to sign it and he would have it removed before the first statement, in order for him to receive credit for selling it.... I told him [I] would not sign it and if he wanted credit for it he would have to do that on his own. Much to my surprise 3 months into the account being opened I had already accrued an enormous amount of interest and fees, because my rate was at 21% and the PPP was on my account. I called [the store] and they told me that [I] signed for it. I spent the next 1 1/2 yrs trying to have them remove it.... I requested my signatures in July.... They finally removed the PPP and gave a \$100 towards the PPP fees.... By the time the signatures got here [I] realized that it was not my signature; I am disgusted with the process. I also do not know how to proceed. I feel I have an obvious forgery and most likely need to see a lawyer.”
- “I recently purchased several items on my kay card and was told my signature for the insurance was simply to receive a packet to gauge my interest. This was a bold face[d] lie. I received a packet today indicating that I agreed to sign up for the insurance.”
- “I purchased [an] engagement ring from Jared and the sales person signed me up for a payment protection plan without my knowledge. This is the first time [I] noticed this fee, which is \$88.97 each month.”⁹

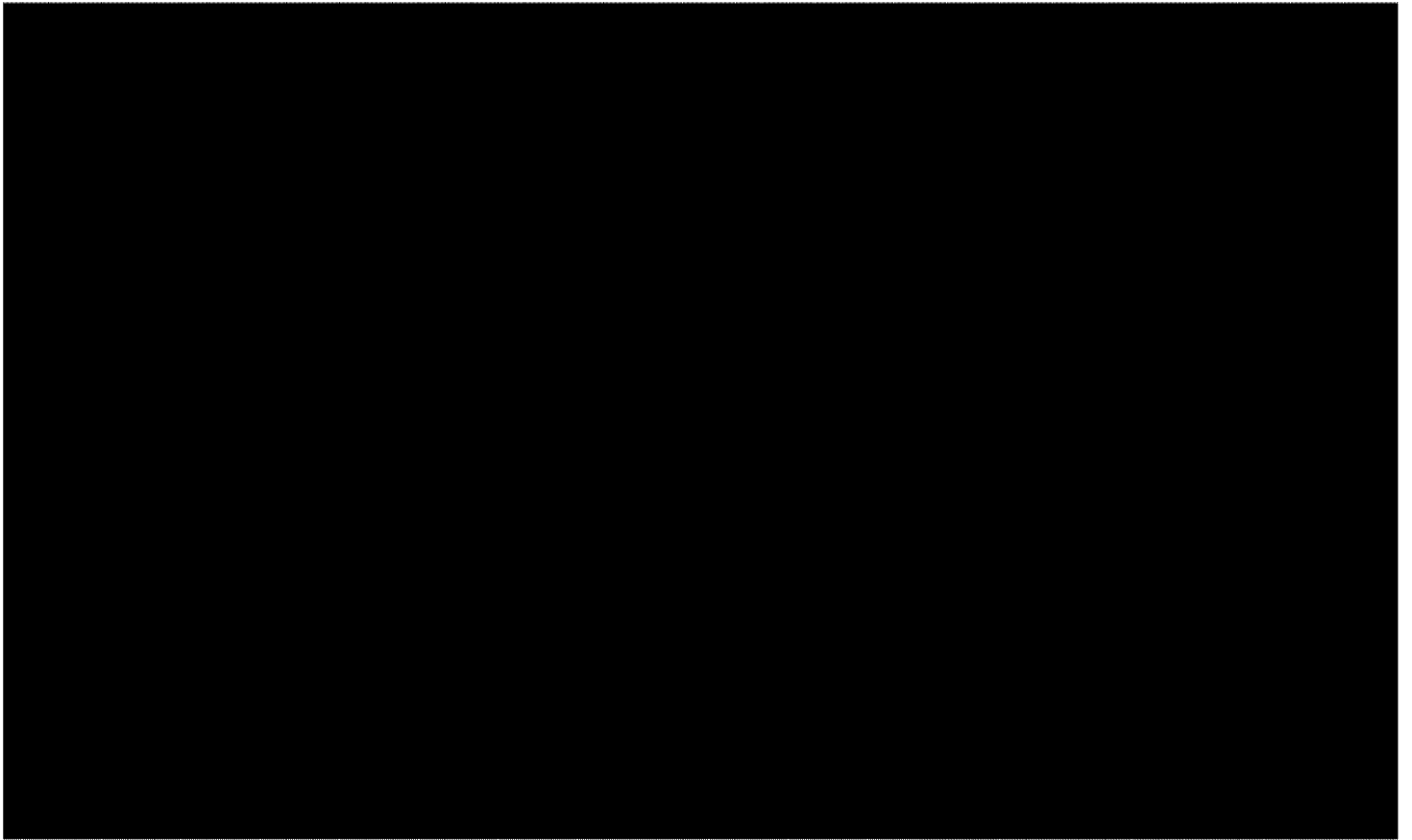
III. Legal Analysis

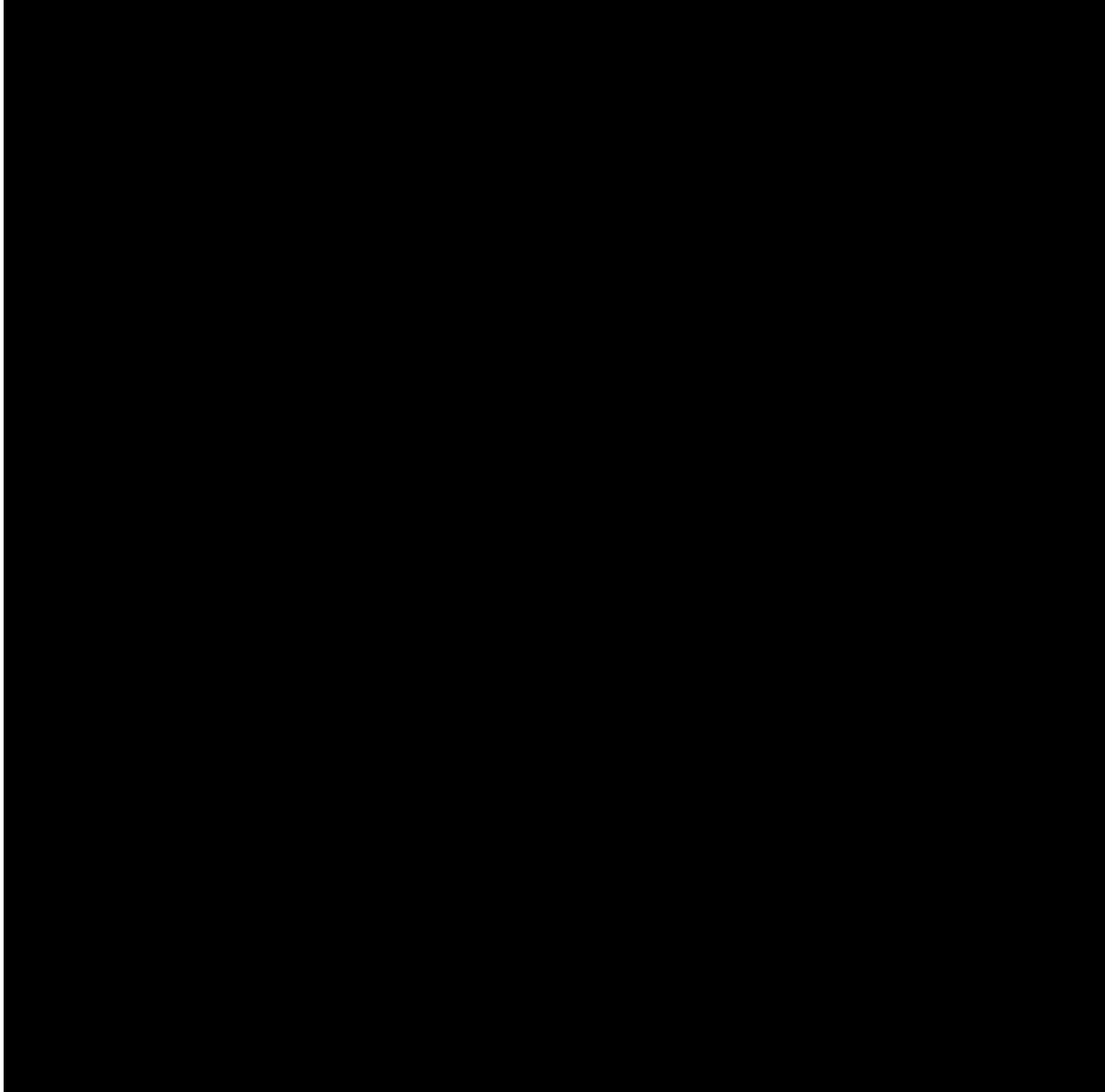


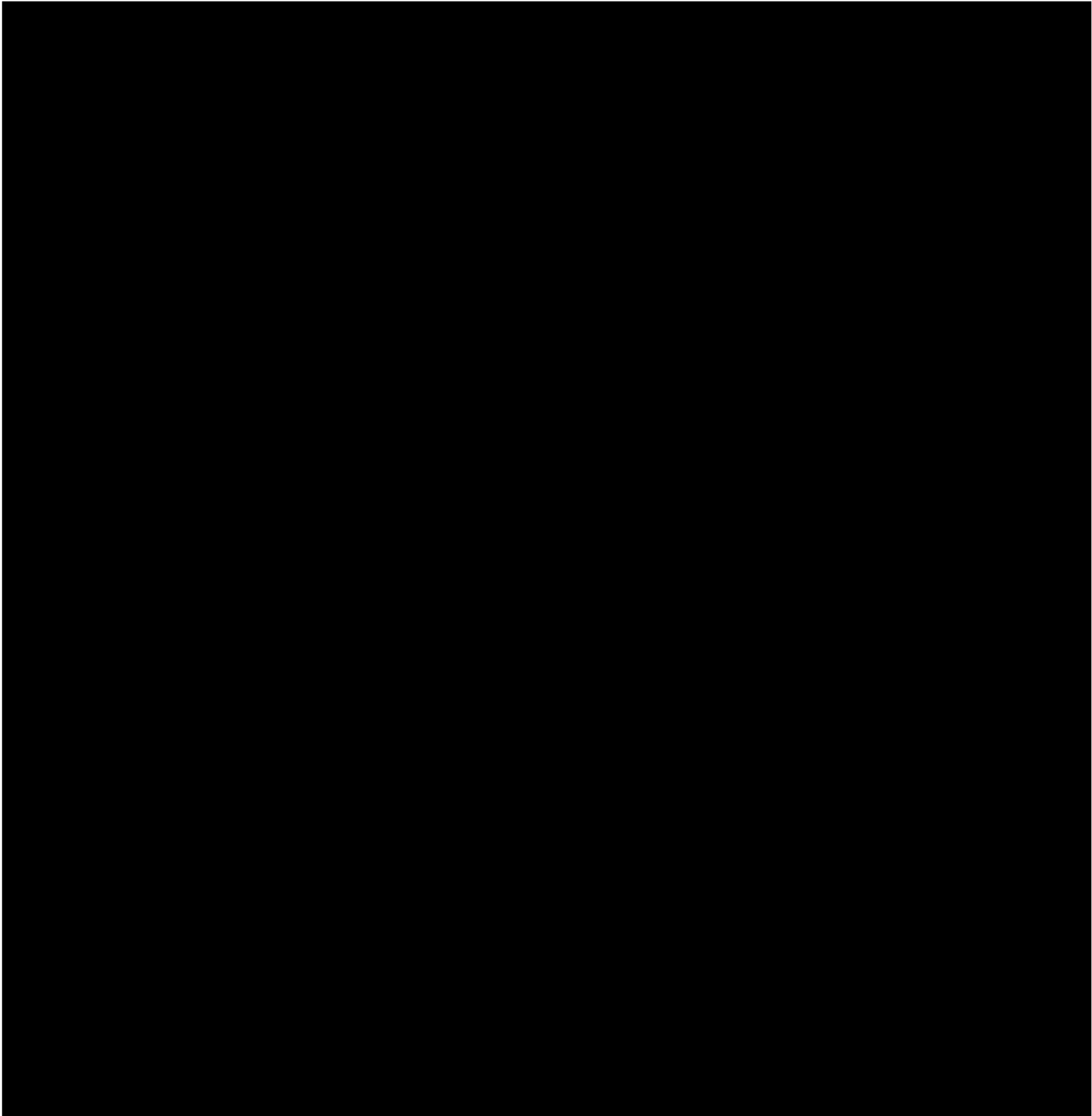






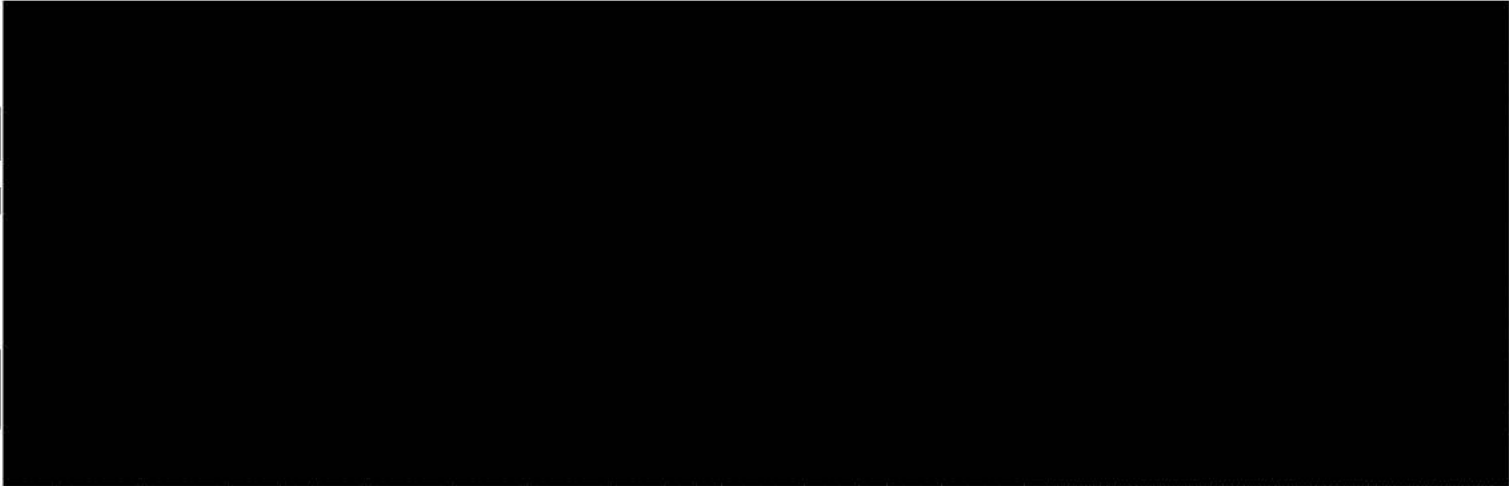






|





IV. Recommendation to Settle or Sue

To resolve this matter through settlement, ~~Enforcement recommends seeking~~ the Bureau should ~~seek~~ redress, injunctive relief, and a penalty.

A. Redress to Consumers

As part of a settlement, the Bureau should require redress for consumers who were enrolled in payment-protection insurance at the point-of-sale—except for those consumers who received a benefit from the insurance coverage—from at least February 2013 through the date a consent order is entered. For these consumers, ~~Enforcement recommends requiring the Bureau should require~~ Sterling to refund all fees charged in connection with consumers' PPP. This is similar to the redress ordered in the Bureau's other credit-card add-on matters, such as the Bureau's action against Capital One.²⁴ Sterling's revenue from optional credit insurance was over \$50 million for each fiscal year from 2014 to 2017. Because the Bureau does not yet have the data to calculate the total proposed redress, Enforcement recommends requiring that Sterling, within 60 days of

Commented [BE(74)]: Given that we have two causation issues (whether the customer would have purchased the insurance anyway, and whether the customer actually was informed by the employee about the insurance option), I think disgorgement is the more appropriate remedy



²⁴ Capital One was ordered to pay \$140 million in redress to about two million consumers, which included complete repayment plus interest, and a \$25 million penalty.

settlement, provide a redress plan for the Bureau's approval that identifies all affected consumers and calculates redress according to approved measures. This is how the Bureau proceeded in the Wells Fargo Sales Practices matter.

~~Enforcement would~~The Bureau should not, as part of a negotiated resolution, seek redress for consumers who had unauthorized credit-card accounts opened. While those consumers may have suffered harm in the form of negative impacts on their credit report and related issues, that harm would be very difficult, if not impossible, to identify and quantify in any systematic way.

~~Enforcement also would~~The Bureau also should not seek to obtain redress for consumers who were misled into thinking they would receive the benefit of promotional financing, but did not. These consumers, while they likely suffered identifiable harm, are not likely to be readily identifiable. There are no records of Sterling's employees' individual misrepresentations to consumers, and consumers affected in this way would appear in Sterling's records in the same way as consumers who were never offered promotional financing.

B. Injunctive Relief

~~Enforcement seeks authority to negotiate a consent order that would~~Any negotiated consent order should prohibit Sterling from engaging in the ~~unlawful~~ practices described herein.

C. Civil Money Penalty

The CFPB provides three tiers of statutory penalties. Effective January 15, 2018, those amounts are up to \$5,639 for ordinary violations, \$28,195 for reckless violations, and \$1,127,799 for knowing violations.²⁵ In this case, Sterling's violations were at least ordinary, if not reckless.

Sterling's culture and performance standards incentivize its employees to deceive consumers into completing credit-card applications and to ~~unfairly-abusively~~ open credit accounts on consumers' behalfs ~~without their knowledge or consent~~. In other instances, Sterling employees mislead consumers about the financing terms ~~to induce them to open credit accounts~~ and to tack on costly payment-protection insurance. Sterling has received thousands of complaints about these practices, which should at least have put it on notice that its employees are committing ~~unlawful~~ ~~improper~~ practices at the point-of-sale; but the company has not taken significant corrective actions and continues to maintain these performance standards.

Commented [BE(75): Not sure we have proven this; it also could have just been to induce them to make the purchase

Sterling has committed thousands, and likely hundreds of thousands, of violations of the kinds described above. Even at the lowest penalty tier, these violations would justify a significant penalty, before consideration of mitigating factors. Among the mitigating factors the Bureau must consider are the gravity of the violations, the severity of the risks to or losses of the consumers, the financial resources of the person charged, and "such other matters as justice may require."²⁶ For consumers who were enrolled in credit-card accounts without their knowledge or

²⁵ 12 U.S.C. § 5565(c)(2); 12 C.F.R. § 1083.1.

²⁶ 12 U.S.C. § 5565(c)(3). Another mitigating factor is the history of previous violations. Here, we are not aware that Sterling has been subject to any prior credit-related actions; ~~however, when~~

consent, there is potentially adverse impact to their credit; however, it is difficult to quantify this harm, and harm may not occur in every instance. In fact, there may be cases in which a consumer's creditworthiness is positively affected by the account. For consumers who were misled about financing terms, the harm is also hard to quantify but because the conduct at issue resulted in a higher cost of credit than consumers were anticipating, it likely left certain consumers unable to make monthly payments, and may have subjected them to late fees, charge-offs, and ultimately debt collection, with additional consequences for their credit histories. As to violations regarding PPP, the harm to consumers who unknowingly or unwillingly were signed up for insurance is likely to roughly equal the amount of their payments for the service. This practice likely negatively impacted hundreds of thousands of consumers.

The Bureau must also consider, as a mitigating factor, Sterling's financial resources and the financial impact on Sterling of a penalty levied here. Signet, Sterling's parent company, reported \$6.4 billion in total revenue in Fiscal Year 2017. Sterling accounted for about \$3.9 billion of this total, with more than 60% attributable to credit sales. Over the past four fiscal years, Sterling's annual revenue from credit products averaged more than \$300 million, and its annual revenue from optional credit insurance products averaged \$60 million, so the company has reaped significant financial gain from its credit-related business. Signet's dividends paid to common shareholders and repurchase of common shares also support the fact that Sterling's parent company is well-capitalized. In Fiscal Year 2017, Signet issued roughly \$75.6 million in dividends paid to common shareholders and repurchased roughly \$1 billion worth of common shares. Over the past three fiscal years, Signet's dividends paid to common shareholders and repurchase of common shares totaled about \$1.35 billion. As Signet's largest operational segment and highest revenue-earning company, Sterling has sufficient financial resources to pay a penalty.

As described, Sterling's violations could potentially justify a significant penalty based on the statutory factors. For the reasons described above, some mitigation is appropriate. But even with such mitigation, the potential penalties could total more than what the company would be willing to pay to settle the Bureau's claims. The CFPB allows the Bureau to compromise or modify a penalty before it is assessed,²⁷ and the Bureau should do so here to help resolve this case.

The most recent, comparable Bureau matter to draw from in determining an appropriate penalty amount is the action taken against Wells Fargo for its sales practices in 2016. In the Wells Fargo Sales Practices matter consumers were similarly subjected to unauthorized credit-card accounts and Wells Fargo paid a penalty of \$100 million. At the time that penalty was determined, the bank disclosed approximately 2,065,000 fake accounts. Dividing the total penalty of \$100 million by the 2.1 million fake accounts results in a \$48.43 penalty per account rate, or roughly 2.1 to 2.2%. The Office of Enforcement, applying a discount to Sterling's total number of accounts without purchases, estimates about 800,000 potentially unauthorized credit-card

our investigation was opened we learned that the NYAG had a parallel investigation underway. Signet has also been the subject of a large-scale sexual harassment and discrimination lawsuit as well as class actions asserting violations of federal securities laws.

²⁷ 12 U.S.C. § 5565(c)(4).

accounts. Using the per-account penalty rates derived from the Wells Fargo matter yields a penalty range of approximately of \$22.9 million to \$38.7 million. Obviously this precedent is not perfect because Sterling and Wells Fargo are different kinds of entities and the claims against each are different.

Commented [R76]: Could you clarify how this estimate reached the \$00,000 figure?

In Bureau credit-card add-on matters, which did not involve unauthorized accounts or misleading financing terms, the penalties range widely because they are tailored to the specific circumstances of each case and the assessment of mitigating factors. For example, in 2012 the Bureau imposed a \$25 million penalty on Capital One; in 2015 the Bureau ordered Citibank to pay a \$35 million penalty; in 2016 First National Bank of Omaha was ordered to pay \$4.5 million. In each of these matters the entity was found to have deceptively or unfairly charged consumers for credit-card add-on products.

Here, based on the unauthorized accounts, deceptive financing, and unfair PPP claims, and taking into account the precedent discussed above, the Bureau should seek to settle this matter for a penalty of at least \$10 million. A penalty in this amount would sufficiently deter similar violations and would impress upon the company the seriousness of the conduct at issue.

V. Assessment of Risks of the Recommended Approach

VI. Conclusion

The Bureau should settle this matter under the parameters described in Section IV. Further, if settlement negotiations are unsuccessful, the Bureau should file suit against Sterling.

Attachments

- Tab 1: Draft Decision Memorandum from the Acting Director.
- Tab 2: Draft Complaint.
- Tab 3: Signet's NORA Transmittal Letter.
- Tab 4: Signet's NORA Response.
- Tab 5: Exhibit A to Signet's NORA Response.
- Tab 6: Signet's Certificate of Factual Assertions in NORA Response.

APPENDIX R



October 29, 2018

Recommendation Memorandum for the Acting Director

FROM	Redacted by the Committee	Jeff
	Ehrlich, and Kristen Donoghue, Office of Enforcement	
THROUGH	Eric Blankenstein, SEFL Policy Director; Chris D'Angelo, SEFL Associate Director	EBB/gator
SUBJECT	Authority to Settle with Sterling Jewelers, Inc. and to File Suit—ENF Matter No. 2016-1806-02	10/29/18

Recommendation

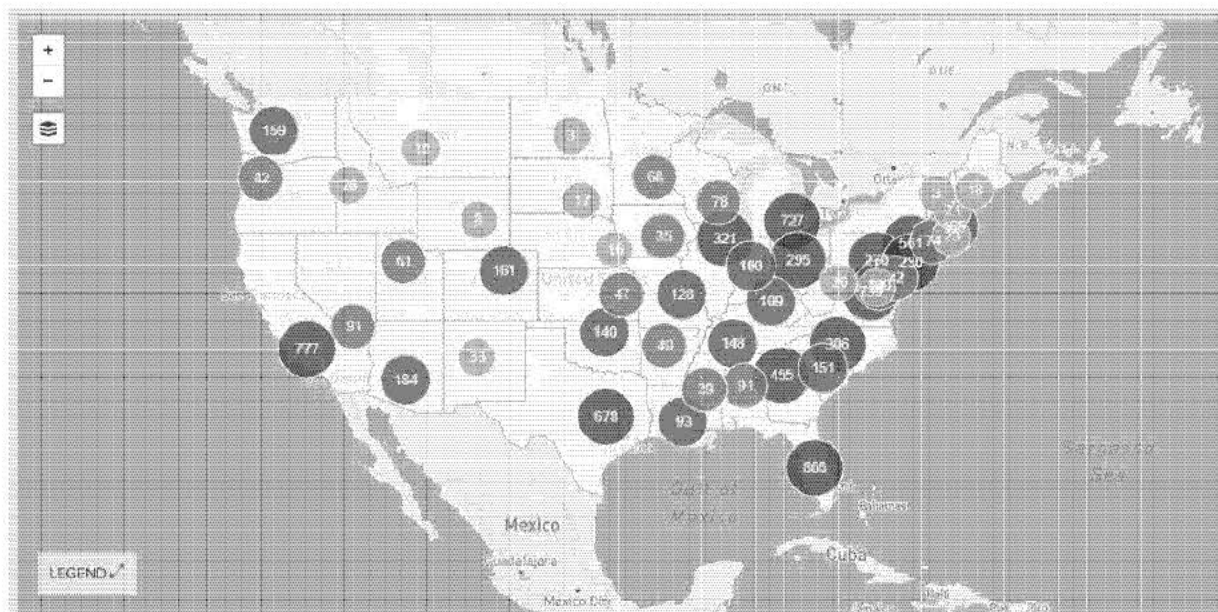
The Office of Enforcement recommends that you authorize it (1) to settle with Sterling Jewelers, Inc. (Sterling) under the parameters described in Section IV below; (2) if settlement negotiations are successful, to file an administrative consent order or a complaint and consent order in federal court effectuating the settlement; and (3) if settlement negotiations are unsuccessful, to commence an enforcement action either administratively or in federal court, consistent with the attached complaint.¹ This investigation was conducted in partnership with the New York State Attorney General's Office, and, if authorized, the Bureau would file a joint complaint with that office.

I. Overview

Sterling operates roughly 1,500 jewelry stores in malls and off-mall locations in all 50 U.S. states under national banners that include Kay Jewelers and Jared The Galleria of Jewelry, as well as a variety of mall-based regional stores such as J.B. Robinson, Marks & Morgan, and Belden Jewelers. Sterling is a wholly-owned subsidiary of Signet Jewelers Limited (Signet), the largest specialty-jewelry

¹ Enforcement also seeks authority to make non-material changes before filing.

retailer in the United States, United Kingdom, and Canada. Sterling entities provide over 60% of Signet’s total sales of about \$6.4 billion. Since 1990, and until recently, Sterling has had a centralized consumer-financing program through which it has extended credit directly to consumers.² As part of its in-house credit program, Sterling has offered “interest-free” and interest-bearing financing, subject to certain conditions, and, in most states, it also offered third-party credit insurance. Roughly 60% of Sterling’s total sales are credit sales, and the fees and charges from Sterling’s credit-financing programs have totaled roughly \$300 million on average for each of the past three years. As part of the investigation, Enforcement (i) interviewed 20 former employees and 32 customers; (ii) supervised 10 secret-shopping trips to Sterling stores in California, Florida, and Virginia to observe sales practices and techniques; (iii) reviewed Sterling’s internal training materials and employee-incentive structure; and (iv) analyzed thousands of consumer complaints from consumers all over the country, across Sterling’s different store brands (see complaint map below).



As described further below, the Office of Enforcement has concluded that from at least January 2014 through October 2017 Sterling employees signed consumers up for credit cards without their authorization or consent, misrepresented credit

² In October 2017, Signet, through Sterling, sold a portion of its consumer-lending portfolio—\$1 billion of its prime-credit business—to Alliance Data Systems. In March 2018, Signet announced that it would sell the remaining portion, Sterling’s non-prime receivables, to investment funds managed by CarVal Investors.

financing terms and conditions to consumers, and enrolled consumers in optional payment-protection insurance without their knowledge or consent.

The Bureau has authority to address Sterling’s conduct because it offers credit to consumers. Sterling is not subject to the CFPA’s “merchant exemption” because it regularly extends credit subject to a finance charge and is significantly engaged in offering or providing consumer-financial products or services.³

This matter would best be resolved through settlement. Because the specific terms of any consent order will be subject to negotiation and ongoing modification, a draft consent order is not attached to this memorandum. The Office of Enforcement will discuss any proposed order with the Legal Division before submitting it to you. If settlement negotiations fail, the Bureau should file suit, either administratively or in federal court, consistent with the attached complaint.

II. Factual Background

Customers report in complaints⁴ and interviews that they were given credit cards that they did not want. In some instances, consumers knew they were being offered credit but claim that Sterling employees presented them with certain terms—a low monthly payment or interest-free period—that were then not honored. These consumers received credit cards and billing statements that did not match the representations made by the salespeople at the time consumers applied. Consumers were also enrolled in Payment Protection Plan (PPP) insurance and claimed it was without their knowledge or consent. In many instances, consumers report that they were asked to “sign here” in order to hold an item, process an order, or verify their information, when in fact these consumers were signing up for PPP.

The Bureau’s investigation focused on three issues related to Sterling’s credit business: (1) whether credit card accounts were opened without consumer knowledge or consent; (2) whether credit-financing terms and conditions were accurately disclosed; and (3) whether consumers were enrolled in payment-protection insurance without their knowledge or consent.

A. Account Opening

³ See 12 U.S.C. § 5517(a)(2)(B)(iii), (a)(2)(C)(i).

⁴ Consumer complaints include those filed with the Bureau, the Better Business Bureau, the Federal Trade Commission’s Sentinel Network, and those filed directly with the company.

When a consumer applies for credit in one of Sterling's stores, Sterling store employees request personal information from the consumer, complete the application on the consumer's behalf, and serve as the primary source of information for the consumer. In fact, Sterling's training materials, which are used to train store employees across all of its regional and national brands, instruct employees to complete the credit application on behalf of consumers. Because the employee holds the application, consumers often do not see that it is an application for credit, nor do they see the applicable credit disclosures, which are displayed in general terms, e.g., APR 5% to 24.99%, in fine print on the back or folded portion of a paper application and, for electronic applications completed on a tablet, are not provided on any screen shown to consumers.⁵ There does not appear to be any process or requirement for consumers to receive written or oral disclosures at the time of the transaction,⁶ and many consumers specifically describe not receiving any oral or written disclosures. In complaints and interviews, consumers report that Sterling employees do not show consumers the credit application and misrepresent the reason for which they are requesting consumers' personal information. In many instances, consumers unknowingly and without giving consent, apply for Sterling's store-brand credit cards.⁷

Consumers allege that Sterling sales representatives offered to see whether the consumer was qualified for a line of credit but then proceeded to submit a credit card application for the consumer. These consumers indicate they did not intend to apply for a credit card and only thought the sales person was gauging their

⁵ The Bureau requested from Signet in a civil investigative demand issued in November 2016 all information relating to the credit application process, including all disclosures given to consumers in connection with that process. The tablet screenshots Signet produced do not show that any credit terms and conditions are displayed. Moreover, Sterling's training materials, which apply to employees at all its regional and national stores, state that store employees should complete credit applications for consumers, and statements from consumers who claim they did not see, or were not made aware of, credit terms provide evidence that these statements are representative of the process in most, if not all, of Sterling's stores.

⁶ When paper applications were used, employees typically controlled and held the application so consumers did not see the credit card agreement and terms. With credit applications completed via tablet, Sterling did not produce any documents or screenshots showing that consumers were shown credit card agreement terms.

⁷ Signet produced roughly 50,000 consumer complaints over a three-year period. The manner in which the complaints were produced—raw, shorthand/abbreviated notes with inconsistent descriptions of the consumer's complaint/inquiry—make it difficult to accurately report the number of complaints relating to certain claims. That said, Signet reported there are 1,359 complaints associated with accounts without purchases. Currently, 382 complaints about unauthorized credit cards have been reviewed and tagged in Relativity.

creditworthiness. Bureau investigators conducting undercover store visits also noted that in some instances Sterling’s salespeople offered “to run [their] credit for approval” and stated it would only be a “soft inquiry” on their credit report. One Jared store employee told a Bureau investigator, “Jared has its own bank and therefore the credit approval process is done in-house and doesn’t affect your credit report.” Consumer complaints corroborate the experience of Bureau investigators, and describe similar statements from store employees about how the store card is “in-house” and won’t affect consumers’ credit. Although consumers must actually apply for credit in order to verify how much they are qualified to spend in the store, they may not understand—and Sterling employees usually did not inform consumers—that by agreeing to have a store employee assess their credit-worthiness, they were in fact applying for credit. Moreover, as discussed further in Section III, alleged misrepresentations by Sterling’s would not be cured by statements on the paper credit application because Sterling consumers often did not see the actual credit application. In some instances, Sterling employees explicitly assured consumers that because the store offers “in-house” credit, it does not have any impact on consumers’ credit reports. In other instances, employees simply offered to check consumers’ credit without informing them it will result in a card being issued.⁸

Consumers also claim that they were asked to provide personal information to sign up for the store “rewards card,” newsletter, or mailing list, when the information was in fact used to apply for a credit card. In at least 35 consumer complaints, consumers alleged that they believed they were providing information for a “survey” and only later learned they were applying for credit. Consumers consistently report that they were never given written disclosures or any indication that they were applying for credit. For example, here is how a consumer described the process during a chat inquiry with a Sterling representative:

2016-07-09 20:33:27 [customer]: Hi [Sterling representative]. I was at the Brookfield square mall last week and I was told that I was filling out a form for a survey to win \$xxxx but when I got home from work today, there was a Kay credit card in my mail box

2016-07-09 20:34:03 [customer]: I never consented to being signed up for a credit card and I am very upset; not at you, but at the sales person that was in the mall;

⁸ Consumer complaints, consumer interviews, and direct observations through undercover store visits support these facts.

2016-07-09 20:35:19 [Sterling representative]: The form the associate in store had you fill out, did it ask for your personal information along with your social security number?

2016-07-09 20:36:52 [customer]: Yes it did. She filled it out for me, so I never [saw] it. But as she read from the paper, she asked for my social security number, my home address and previous address, she also asked for a family members name, phone number, and city of residence.

2016-07-09 20:37:00 [customer] And she asked about my employment information

2016-07-09 20:37:37 [customer] She did this with both me and my fiancé and the only time we [saw] the form was when she had us sign the bottom

2016-07-09 20:38:56 [customer] Also, we asked why she needed our social and she said so they could verify that we are who we say we are. And when she handed us the paper to sign, she had it folded and said it was for security reasons because our social security numbers were on it

2016-07-09 20:40:39 [Sterling representative] The form that was filled out for you in store was a credit application for a Kay Jewelers card. By signing the form, you gave us permission to run the application for credit approval. I apologize you were not told by the associate you were applying for a Kay account.

Although it may seem that providing such personal information for a rewards program, store card, mailing list, survey, contest, etc. is not reasonable, when assured by a store employee that the information is necessary consumers relied on store employees' representations and complied with employees' requests. A consumer acting reasonably under the circumstances would not expect that a store employee is attempting to open a credit card on behalf of a consumer. The significant volume of complaints – 1,359 relating to unauthorized accounts – is evidence that reasonable consumers were not aware that they were completing credit-card applications and that these practices are widespread and affected more than a handful of consumers.

Representative consumer complaints include:

- “I bought an engagement ring from Jared the Galleria of Jewelry. I stated from the beginning I would be paying for the ring and all charges with my American Express Card. The salesperson then filled out forms to open a credit card for me without my knowledge. When it was time to close the sale, they presented the form to me, saying it was required to order the diamonds/ring that I wanted so I signed it. They had the paper form folded in such a way that I could not see that it was for a credit card.... [T]hey opened

a credit card in my name without my consent via deceptive sales practices and outright manipulation. . . .”

- “I was told that I was signing up for an employee loyalty program at JARED Jewelry that would send me coupons and cash back on further purchases. I explicitly asked multiple times if they were setting up a credit card, and the sales representative assured me he was not. I became suspicious once he asked for more personal information such as employment history and my Social Security Number. I asked again if this was signing me up for a credit card, and the sales representative told me no. He stated they were only doing an internal background check but no credit would be opened. A few days later, I went to sign up for a credit card from a company I actually wanted a credit card from, and I was declined. They stated the reason was that I had too much credit open in my name. . . . A few days later, I received in the mail a credit card from JARED. . . .”
- “I would like to file a complaint against Kay Jewelers. They signed my fiancé and myself up for a credit card without telling us. . . the sales representative. . . said we were signing an agreement for the custom ring they were going to design for us. . . . We were signed up for not one, not two, but THREE cards which were received in the mail a week after starting the process with them. They just tell you it's a contract for the custom ring, if we had known it was a credit card application we would have refused to fill out the paperwork.”
- “[A] Kay Jewelry saleswoman wanted me to fill out a form so that I can take care of some kind of ‘promotional coupon’ that would be sent in the mail. . . . I received a letter from the Kay Jeweler's Credit Operations Division which stated that they turned down my application to open some kind of credit account because I do not make enough money. First, respectfully, the saleswoman took my social security number because she told me that it was only to prevent fraud and that they would not use it for anything else (I have no idea how it would prevent fraud, but she seemed honest)! Second, she never took my income information down. . . so I don't even know how Kay Jewelers was able to find out how much I make without me divulging that information unto them. This dishonest tactic may lower a great credit score.”
- “The representatives I worked with, Patricia and Katrina, said they would like to screen my credit in order to determine the price range of rings we could qualify for. I insisted repeatedly that I did not want a credit card as we had not yet determined where we would be buying a ring, but they stated explicitly that they would be doing a preliminary screening of my credit only. They said they would not be issuing a credit card, and this was a standard procedure to see what amount someone can qualify for. After the

"preliminary screening," I was told I was approved for a \$10,000 credit limit, and that any questions I had would likely be answered with the paperwork that would be coming with my credit card in the mail. I reminded them that I did not want a credit card, and that they said this was supposed to be preliminary screening, and they replied saying it was fine because if I didn't want the card, it would be closed in 2 years if I don't use it. I did not want the credit card, and was lied to in order for them to set up an account in my name."

Interviews with former store employees further substantiate consumers' complaints. Specifically, 20 former employees at various stores across 12 states indicated that they were trained to mislead customers into applying for credit cards—telling consumers they were signing up to be “preferred customers,” specifically refraining from using the term “credit card” and instead asking consumers to open a “rewards card,” and asking consumers to help the employee “win a contest” by filling out a form for a “customer account.” Former employees said they would offer discounts on jewelry for opening a card—even where items were already discounted without opening an account—or offer free watch-battery replacement to consumers if they open an account.

Sterling's companywide, formal performance standards require its store employees to sell credit cards to consumers. Mall-store employees are required to obtain one credit-card application a day, while standalone-store employees are required to obtain one credit-card application every two days. Employees who fail to meet these thresholds receive counseling and additional training from store managers and, in some instances, are terminated. Interviews with former employees suggest that there was intense pressure to meet Sterling's goals. Hundreds of anonymous employee reviews on www.glassdoor.com, a database of employee-authored company reviews, reiterate employees had trouble meeting their credit-card quotas.

Representative Glassdoor.com reviews state:

- “One of the major downsides is the push to get guests to open a credit card. Each sales associate is expect[ed] to get 1 credit application a day.”
- “Upper management care more about you opening up credit cards than they do actual sales. I've seen employees do some really shady things in order to maintain their credit standard. Everything from using underage candidates to making up social security numbers and names. They get all the praise because they ‘met’ the standard. Then the associates who try to do it ethically get reprimanded.”

- “Credit Apps can be a problem. You are expected to sign people up for these every day and that is challenging at best. Many people are very wary about opening a credit card and rightfully so. So it should be an incentivized bonus if you do sign up someone for a credit card rather than a daily req.”
- “Not a particularly pleasant work environment between disgruntled employees and customers and unrealistic credit card goals made it seem like we were scamming to make a quota.”
- “Must open 1 new credit card everyday, people do not want another specialty card but management doesn't want to hear that.”
- “Also, the credit card is supposed to be a tool to help us close sales. Not pressure us to break company policy and in some cases the law.”
- “Very high pressure to get people to fill out credit apps. All the add-ons like the warranty and credit app were emphasized more than the actual selling of jewelry.”
- “If you don't make all of the 5 standards⁹ they'll terminate you after 6 months... Emphasis is placed solely on having sell credit card apps, not jewelry.”
- “You must be 6/6 standards (sales, addons, repairs, PPP, esp, and credit apps) at all times to be even be acknowledged you exist by upper management. They expect you to walk around the mall and harass people for credit apps. Upon getting hired, they expect you to also harass your friends and family to fill out a credit app. If you don't get your credit apps, you must go to weekly meetings or even call your district manager and tell him/her why you do not care about your job at the end of every shift. They will offer you a promotion, then give it to someone else the next day... Upper management sweeps unethical and illegal behavior under the rug as long as you have your numbers in.”
- “Mandatory early morning meetings on Sat. or Sun. (translate that punishment) for lack of credit apps.”“This type of job should be fun and enjoyable... instead, it has become a marathon of credit accounts, add-ons, ppp's, esp's, uwp's, repairs, and the stresses of keeping numbers up to avoid write-ups, cuts in hours, and mandatory punishment meetings. The response to this kind of constant pressure leads some employees to misrepresent things in order to achieve their numbers. Not a good thing for the customer...or the company.”
- “If you don't have your standard for sales and credit application, then [you] can kiss your job Goodbye! I understand the ‘trickle down’ effect, but there

⁹ In states that do not offer PPP there are only five performance standards.

needs to be some sort of relief from this stress of losing your job if credit isn't at 100%...and mandatory store meetings at 8am on Saturday morning for missed credit for the week has got to be a [form] of abuse [of] power.”

- “First month not at 6 for 6 standards---verbal/written counseling[.] Second month not at 6 for 6 standards---written counseling[.] Third month not at 6 for 6 standards---termination.”

Former employees reported during interviews that employees who did not meet credit-card quotas were “written up,” had to go in to the store on their days off or before or after work for credit-card meetings, and were lectured on “getting their numbers up.” At least ten former employees from stores in different states said there was a training for “employees not meeting their numbers” that could be a two to four-hour drive away from their store’s location. Eight former employees specified that Sterling employees could be fired for failing to obtain credit-card applications.

In addition to rating employees on their ability to meet or exceed the standard for new credit-card applications, Sterling runs an annual four-week credit-application contest that awards cash to employees at all levels, including sales representatives, store managers, and district managers, who obtain the most credit-card applications.

Sterling’s training materials instruct store employees to offer credit early and often to every customer. These materials require, in part, facially compliant credit-related practices and procedures that seek to ensure customers understand that they are applying for credit as well as the related credit terms and conditions. The training materials also include tips such as “offer to clean your Guest’s jewelry while you fill out the credit application” and “completing the in-house credit account application for the Guest on the CASSi tablet allows him/her to focus on his/her reason for visiting the Store, and not on completing paperwork.” Regardless of the type of application, employees are instructed to “[a]lways fill out the paper credit application or type the credit application into the Graphical POS for the Guest” so customers do not see the credit application. Sterling also provides guidance to store employees on how to overcome consumers’ objections to credit accounts and additional suggestions, such as presenting a credit line with a piece of jewelry.

Sterling provided data identifying the number of company credit-card accounts that were opened but never used. Sterling stores issued about 285,000 credit cards each

year that had no activity on them. Over a three-year period, the total number of Sterling accounts opened without any purchases made was nearly one million.

B. Representations About Financing

Consumers report that Sterling employees provide certain financing plan information at the point-of-sale that turns out to be different than the financing plan terms they receive. Employees offer, and are trained to promote, “interest-free” financing. Numerous consumers indicate that consumers were offered interest-free financing in connection with a purchase only to find, once they receive their first billing statement, that they were actually enrolled in a regular, interest-bearing credit plan.¹⁰ In these cases, the consumers claim that they were often quoted a monthly payment amount and other terms that differ from the terms of the plan for which they are enrolled.

Sterling stores generally offer interest-free promotional financing for periods of 6, 12, and 18 months to customers who meet a minimum purchase amount and pay a 20% down payment. Hundreds of consumer complaints and interviews of employees indicate that, in many cases, customers who expected to receive interest-free financing were actually given regular, interest-bearing financing. This typically happened for one of two reasons. First, if a customer could not make a down payment at the time of purchase and thus did not meet the eligibility requirements for interest-free financing, he would in many instances be signed up for a regular financing plan instead without being told by the employee of the switch. Second, if a consumer indicated that he could not afford the monthly payment amount that was calculated based on the promotional period for the interest-free plan, he would in many instances be given a lower payment amount that was calculated based on a longer repayment term and regular interest-bearing financing, also without having the changed terms explained. In both scenarios, Sterling employees explained the availability of interest-free financing and consumers believed they would receive it, but didn’t clearly inform consumers that they would not after it became clear that they didn’t qualify for or couldn’t afford the payments required for the interest-free promotion.

Interviews with former employees corroborate consumer complaints alleging misinformation and changed credit-card financing terms. Former employees from Sterling’s regional and national stores around the country mentioned that they

¹⁰ There are at least 375 complaints that have been reviewed and tagged that concern this claim.

would incentivize customers to open accounts by promising “12-months interest-free”—though this required a minimum purchase amount, which they did not disclose—and “no down payment,” which voids interest-free financing options. For example, one former employee said that for items below \$500 there was not an interest-free financing option, but employees would pitch “no interest” in the hope that no one would notice.

C. Payment Protection Plan

Similar to the credit-card-application quota, Sterling employees were required to enroll customers in optional PPP insurance to meet performance standards. PPP is a credit-insurance program that was offered to Sterling credit customers to help those customers make their monthly payments in the event of death, disability, loss of property due to burglary or perils, leave of absence, job retraining, or involuntary loss of employment. Because the insurance protected consumers’ credit payments, it was directly related to the credit financing that Sterling offers, and it provided a direct benefit to Sterling by protecting its accounts receivable from loss due to non-payment.

Sterling stores sold PPP to credit customers through Assurant,¹¹ a state-licensed insurance company, from at least 2009 to October 2017. PPP was offered at the point-of-sale in 33 states. The cost of PPP varied depending on the type of coverage and state, but it was typically around \$.78 cents per \$100 purchase amount. This amount was charged monthly on the consumer’s credit-card billing statement based on the account balance. Although Assurant administered PPP, Sterling was responsible for the marketing and sale of PPP.

Evidence gathered during the investigation suggests that customers were routinely enrolled in PPP insurance at the time of their credit application or purchase transaction without knowing they were doing so and without ever viewing the insurance terms and conditions or costs. Former Sterling employees indicated that customers would be hurried through the point-of-sale transaction and told to “initial here”—encouraging the customer to enroll in PPP.¹² One former employee explained: “you didn’t tell people about the product, you just put it on there.” That is, sales associates signed people up for PPP insurance without asking, and if someone noticed the charge on a billing statement and complained, Sterling would

¹¹ Sterling Jewelers Insurance Agency, Inc., a wholly-owned subsidiary of Signet, provided insurance licensing functions for Sterling’s credit-insurance programs.

¹² Sterling’s training document instructs: “Use an assumptive close when closing PPP.”

remove it. Another former store manager said that district managers told store managers to check “Yes” for PPP even if customers didn’t ask for it, noting that the store could always cancel it the next day but that the store would be “credited” for it even if it was later canceled, so “always check ‘Yes.’” Based on this evidence, it seems it may be possible for store employees to select “Yes” for the customer and add PPP to consumers’ accounts without the consumer affirmatively selecting “Yes.”¹³

At least 175 consumers submitted complaints alleging that PPP was added to their account without their knowledge or consent. Some consumers complain that Sterling employees asked them to sign up for PPP to help the employees meet their quotas; the employees promised that they would cancel the insurance before the customer would be charged, but they failed to do so. In one complaint, the consumer reported that he was told by the salesperson to select “Yes” and sign the PIN-pad to receive an insurance packet to gauge his interest and then discovered when the packet arrived that he had agreed to purchase the insurance. In response to such a complaint, Sterling’s internal account notes indicate that the store apologized for putting PPP on without the consumer’s knowledge, canceled the PPP, and refunded charges. Most commonly, consumers discovered that they were being charged for PPP only after noticing it on their billing statements.

Here are a few consumer complaints about PPP:

- “I signed up for a credit card with Jared. When I paid off the promotional, ‘1 year no interest’ balance in just 3 months, I learned that a credit protection fee had been being assessed/added to my balance. After call[ing] to question it, the associate, Lila #3666, insisted that I hadn't questioned it early enough, so she would only remove 45 of the \$224 assessed. Only after speaking with a manager did they pull up my agreement, acknowledge that I had never agreed to purchase the insurance, and agree to reimburse me for the fees charged. Research needs to be done/legal action take[n a]gainst Jared for charging me and other consumers fees for services they did not agree to.”¹⁴

¹³ In addition, Sterling’s PPP enrollment procedures specify steps the employee must take “[i]f you do not have a customer’s signature either via the PIN-pad or on the sales slip,” which suggests it was technically possible enroll a consumer without obtaining a signature.

¹⁴ Sterling responded: “In your case, even though our system indicates that PPP had been accepted at the time of sale, we were unable to locate a signature confirmation of enrollment. In light of the missing signature, a supervisor authorized a return of \$224.20 that your account had been billed in total for PPP.”

- “[The store employee] tried to get me to enroll in their ‘PPP’ or personal payment protection plan (i.e. credit and life disability insurance) all at an obscene rate.... He told me to sign it and he would have it removed before the first statement, in order for him to receive credit for selling it.... I told him [I] would not sign it and if he wanted credit for it he would have to do that on his own. Much to my surprise 3 months into the account being opened I had already accrued an enormous amount of interest and fees, because my rate was at 21% and the PPP was on my account. I called [the store] and they told me that [I] signed for it. I spent the next 1 1/2 yrs trying to have them remove it.... I requested my signatures in July.... They finally removed the PPP and gave a \$100 towards the PPP fees.... By the time the signatures got here [I] realized that it was not my signature; I am disgusted with the process. I also do not know how to proceed. I feel I have an obvious forgery and most likely need to see a lawyer.”
- “I recently purchased several items on my kay card and was told my signature for the insurance was simply to receive a packet to gauge my interest. This was a bold face[d] lie. I received a packet today indicating that I agreed to sign up for the insurance.”
- “I purchased [an] engagement ring from Jared and the sales person signed me up for a payment protection plan without my knowledge. This is the first time [I] noticed this fee, which is \$88.97 each month.”¹⁵

III. Legal Analysis

[REDACTED]

[REDACTED]

[REDACTED]

¹⁵ Sterling refunded \$626.88 in PPP fees in response to this complaint.

enrolling in a store card or “rewards card” (as opposed to a store credit card), or

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

transaction—then arguably it could have no meaning, because it is not clear in

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



IV. Recommendation to Settle or Sue

To resolve this matter through settlement, the Bureau should seek redress, injunctive relief, and a penalty.

A. Redress to Consumers

The Bureau should not, as part of a negotiated resolution, seek redress for consumers who had unauthorized credit-card accounts opened. While those consumers may have suffered harm in the form of negative impacts on their credit report and related issues, that harm would be very difficult, if not impossible, to identify and quantify in any systematic way.

The Bureau also should not seek to obtain redress for consumers who were misled into thinking they would receive the benefit of promotional financing, but did not. These consumers, while they likely suffered identifiable harm, are not likely to be readily identifiable. There are no records of Sterling's employees' individual misrepresentations to consumers, and consumers affected in this way would appear in Sterling's records in the same way as consumers who were never offered promotional financing.

Each of the potential remedies for the PPP claim has drawbacks.

Normally, where an institution is accused of inducing consumers to enter into transactions through unfair or deceptive means, restitution is appropriate. But merely identifying the proper restitution population may be impossible, given that there are likely no records of which consumers were subject to the specific practice of being misled about the PPP product or being enrolled without having provided affirmative consent. And even though the Bureau need not prove causation in order to secure restitution, there also is the question of whether any specific customer would not have purchased insurance but for the unfair or deceptive conduct of a Sterling employee. As a result, blanket redress to all PPP consumers would

potentially provide a windfall to those who were not proximately harmed by Sterling's practices.

Despite this, as part of a settlement, the Bureau could seek redress for consumers who were enrolled in payment-protection insurance at the point-of-sale—except for those consumers who received a benefit from the insurance coverage—from at least February 2013 through the date a consent order is entered. This would be similar to the redress ordered in the Bureau's other credit-card add-on matters, such as the Bureau's action against Capital One.⁵⁰ Given the low utilization rates of the product,⁵¹ this restitution likely would not provide a windfall to consumers, as many likely received no tangible benefit from the product. Additionally, the Bureau intends to pursue this case jointly with New York. New York likely would seek redress for New York consumers who enrolled in PPP, which will both make it appear odd that the Bureau did not also seek restitution, and potentially make settlement more difficult, as Sterling would not be guaranteeing finality, as other state AGs could bring suit seeking restitution under applicable state laws. The Office of Enforcement favors this approach.

Alternatively, disgorgement of the PPP proceeds may be more appropriate. Or the Bureau could not order any specific monetary relief for this violation, but rather take it into account when determining the penalty amount.

B. Injunctive Relief

Any negotiated consent order should prohibit Sterling from engaging in the practices described herein.

C. Civil Money Penalty

The CFPB provides three tiers of statutory penalties. Effective January 15, 2018, those amounts are up to \$5,639 for ordinary violations, \$28,195 for reckless violations, and \$1,127,799 for knowing violations.⁵² In this case, Sterling's violations were at least ordinary, if not reckless.

⁵⁰ Capital One was ordered to pay \$140 million in redress to about two million consumers, which included complete repayment plus interest, and a \$25 million penalty.

⁵¹ See n. 38, *supra*,

⁵² 12 U.S.C. § 5565(c)(2); 12 C.F.R. § 1083.1.

Sterling’s culture and performance standards incentivize its employees to deceive consumers into completing credit-card applications and to open credit accounts on consumers’ behalves without their knowledge or consent. In other instances, Sterling employees misled consumers about the financing terms and tack on costly payment-protection insurance. Sterling has received thousands of complaints about these practices, which should at least have put it on notice that its employees are committing improper practices at the point-of-sale; but the company has not taken significant corrective actions and continues to maintain these performance standards.

Sterling potentially has committed thousands, and perhaps hundreds of thousands, of violations of the kinds described above. Even at the lowest penalty tier, these violations would justify a significant penalty, before consideration of mitigating factors. Among the mitigating factors the Bureau must consider are the gravity of the violations, the severity of the risks to or losses of the consumers, the financial resources of the person charged, and “such other matters as justice may require.”⁵³ For consumers who were enrolled in credit-card accounts without their knowledge or consent, there is potentially adverse impact to their credit; however, it is difficult to quantify this harm, and harm may not occur in every instance. In fact, there may be cases in which a consumer’s creditworthiness is positively affected by the account. For consumers who were misled about financing terms, the harm is also hard to quantify but because the conduct at issue resulted in a higher cost of credit than consumers were anticipating, it likely left certain consumers unable to make monthly payments, and may have subjected them to late fees, charge-offs, and ultimately debt collection, with additional consequences for their credit histories. As to violations regarding PPP, the harm to consumers who unknowingly or unwillingly were signed up for insurance is likely to roughly equal the amount of their payments for the service. This practice likely negatively impacted hundreds of thousands of consumers.

The Bureau must also consider, as a mitigating factor, Sterling’s financial resources and the financial impact on Sterling of a penalty levied here. Signet, Sterling’s parent company, reported \$6.4 billion in total revenue in Fiscal Year 2017. Sterling accounted for about \$3.9 billion of this total, with more than 60% attributable to credit sales. Over the past four fiscal years, Sterling’s annual revenue from credit products averaged more than \$300 million, and its annual

⁵³ 12 U.S.C. § 5565(c)(3). Another mitigating factor is the history of previous violations. Here, we are not aware that Sterling has been subject to any prior credit-related actions.

revenue from optional credit insurance products averaged \$60 million, so the company has reaped significant financial gain from its credit-related business. Signet's dividends paid to common shareholders and repurchase of common shares also support the fact that Sterling's parent company is well-capitalized. In Fiscal Year 2017, Signet issued roughly \$75.6 million in dividends paid to common shareholders and repurchased roughly \$1 billion worth of common shares. Over the past three fiscal years, Signet's dividends paid to common shareholders and repurchase of common shares totaled about \$1.35 billion. As Signet's largest operational segment and highest revenue-earning company, Sterling has sufficient financial resources to pay a penalty.

As described, Sterling's violations could potentially justify a significant penalty based on the statutory factors. For the reasons described above, some mitigation is appropriate. But even with such mitigation, the potential penalties could total more than what the company would be willing to pay to settle the Bureau's claims. The CFPB allows the Bureau to compromise or modify a penalty before it is assessed,⁵⁴ and the Bureau should do so here to help resolve this case.

The most recent, comparable Bureau matter to draw from in determining an appropriate penalty amount is the action taken against Wells Fargo for its sales practices in 2016. In the Wells Fargo Sales Practices matter consumers were similarly subjected to unauthorized credit-card accounts and Wells Fargo paid a penalty of \$100 million. At the time that penalty was determined, the bank disclosed approximately 2,065,000 fake accounts. Dividing the total penalty of \$100 million by the 2.1 million fake accounts results in a \$48.43 penalty per account rate, or roughly 2.1 to 2.2%. Adjusting Sterling's total number of accounts without purchases, estimates about 800,000 potentially unauthorized credit-card accounts.⁵⁵ Using the per-account penalty rates derived from the Wells Fargo matter yields a penalty range of approximately of \$22.9 million to \$38.7 million. But this precedent is not perfect because Sterling and Wells Fargo are different kinds of entities, engaged in different kinds of behavior, and the claims against each are different.

⁵⁴ 12 U.S.C. § 5565(c)(4).

⁵⁵ Signet produced data showing that roughly 300,000 accounts without purchases were opened each year, totaling about one million such accounts from February 2014 through March 2017. Taking into account the explanation that some consumers were "shopping around" and intended to open a credit card without making any purchase, a 20% discount was applied to the total number of accounts, yielding an estimated 800,000 potentially unauthorized accounts.

In Bureau credit-card add-on matters, which did not involve unauthorized accounts or misleading financing terms, the penalties range widely because they are tailored to the specific circumstances of each case and the assessment of mitigating factors. For example, in 2012 the Bureau imposed a \$25 million penalty on Capital One; in 2015 the Bureau ordered Citibank to pay a \$35 million penalty; in 2016 First National Bank of Omaha was ordered to pay \$4.5 million. In each of these matters the entity was found to have deceptively or unfairly charged consumers for credit-card add-on products.

Here, based on the unauthorized accounts, deceptive financing, and unfair PPP claims, and taking into account the precedent discussed above, the Bureau should seek to settle this matter for a penalty of at least \$10 million. A penalty in this amount would sufficiently deter similar violations and would impress upon the company the seriousness of the conduct at issue.

V. Assessment of Risks of the Recommended Approach



VI. Conclusion

The Bureau should settle this matter under the parameters described in Section IV. Further, if settlement negotiations are unsuccessful, the Bureau should file suit against Sterling.

Attachments

- Tab 1: Draft Decision Memorandum from the Acting Director.
- Tab 2: Draft Complaint.
- Tab 3: Signet's NORA Transmittal Letter.
- Tab 4: Signet's NORA Response.
- Tab 5: Exhibit A to Signet's NORA Response.
- Tab 6: Signet's Certificate of Factual Assertions in NORA Response.

1700 G Street NW,
Washington, DC 20552



Decision Memorandum from the Acting Director

FROM	Mick Mulvaney
TO	Eric Blankenstein, SEFL Policy Director; Chris D'Angelo, SEFL Associate Director; Kristen Donoghue, Assistant Director for Enforcement
SUBJECT	Authorization to Enter into Settlement with Sterling Jewelers, Inc. or to File Suit – ENF Matter No. 2016-1806-02

I authorize the Office of Enforcement to enter into a settlement with or file a lawsuit against Sterling Jewelers, Inc. under the parameters recommended by the Office of Enforcement on October 29, 2018.

The Office of Enforcement's October 26, 2018 recommendation memorandum identifies three potential options for the remedy for the PPP claim in a settlement (in addition to injunctive relief and a civil money penalty). Of those three options, I authorize the following:

- Restitution
- Disgorgement
- Take absence of other monetary relief into account when negotiating penalty amount

Mick Mulvaney
Acting Director
Bureau of Consumer Financial Protection

Date

**IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK**

Bureau of Consumer Financial
Protection and the People of the State of
New York, by Barbara Underwood,
Acting Attorney General for the State of
New York,

Plaintiffs,

v.

Sterling Jewelers, Inc.,

Defendant.

Case No.

COMPLAINT

Plaintiffs, the Bureau of Consumer Financial Protection (Bureau) and the People of the State of New York (State of New York), bring this action against Sterling Jewelers, Inc. (Sterling) and allege as follows:

INTRODUCTION

1. Sterling operates roughly 1,500 jewelry stores in malls and off-mall locations in all 50 states, doing business as Kay Jewelers, Jared The Galleria of Jewelry, and a variety of other regional brands, including J.B. Robinson, Marks & Morgan, Belden Jewelers, Goodman Jewelers, LeRoy's Jewelers, Osterman Jewelers, Rogers Jewelers, Shaw's Jewelers, and Weisfield Jewelers.

2. Sterling is a wholly-owned subsidiary of Signet Jewelers Limited (Signet). Signet is the largest specialty-jewelry retailer in the United States, United Kingdom, and Canada. Sterling entities make up over 60% of Signet's total sales of about \$6.4 billion.

3. Since 1990, and until at least October 2017, Sterling has offered in-house credit financing directly to consumers to make purchases in its stores.

4. Consumers who visited Sterling's stores were typically encouraged by Sterling's salespeople to finance their purchases. Roughly 60% of Sterling's total sales are financed by consumers using Sterling's in-house credit. From 2014 through 2017, Sterling had over three million open credit accounts each year, and Sterling generated more than \$300 million in net revenue each year from such accounts.

5. Sterling's company culture, reflected in its training materials and sales-performance standards, pressures employees to enroll consumers in company credit cards and to sell its financing plans and payment-protection insurance.

6. The Bureau and the State of New York bring this action under §§ 1031, 1036(a)(1), 1054, and 1055 of the Consumer Financial Protection Act of 2010 (CFPA), 12 U.S.C. §§ 5531, 5536(a)(1), 5564, 5565, the Truth in Lending Act (TILA), 15 U.S.C. § 1601 *et seq.*, and its implementing regulation, Regulation Z, 12 C.F.R. part 1026, in connection with Sterling's credit-financing practices, including (1) submitting credit applications for consumers and causing credit cards to be issued without consumers' knowledge or consent; (2) misrepresenting credit-financing terms and conditions; and (3) enrolling consumers in payment-protection insurance without their knowledge or consent. The State of New York also brings this action under the General Business Law (GBL) § 349. [NY AG to add provisions]

JURISDICTION AND VENUE

7. This Court has subject-matter jurisdiction over this action because the action is brought under "Federal consumer financial law," 12 U.S.C. § 5565(a)(1),

presents a federal question, 28 U.S.C. § 1331, and is brought by an agency of the United States, 28 U.S.C. § 1345. This Court has supplemental jurisdiction over the State of New York's state-law claims because they are so related to the federal claims that they form part of the same case or controversy. 28 U.S.C. § 1367(a).

8. Venue is proper in this district because Sterling conducts business in this district. 12 U.S.C. § 5564(f).

PARTIES

9. The Bureau is an agency of the United States charged with regulating the offering and provision of consumer-financial products and services under "Federal consumer financial laws." 12 U.S.C. § 5491(a). The Bureau has independent litigating authority to enforce "Federal consumer financial laws." *See* 12 U.S.C. § 5564(a)–(b).

10. The State of New York, by its Attorney General (NYAG), is authorized to take action to enjoin deceptive business practices under N.Y. GBL § 349. The NYAG is also authorized to initiate civil actions in federal district court to enforce provisions of the CFPA. *See* 12 U.S.C. § 5552(a)(1).

11. Sterling, an Ohio corporation, maintains its headquarters at 375 Ghent Road, Akron, Ohio 44333. Sterling operates jewelry stores and offers credit products to consumers in all 50 U.S. states, including in the State of New York. Sterling engages in offering a "consumer financial product or service" under the CFPA. 12 U.S.C. § 5481(5)(A), (15)(A)(i). Sterling is therefore a "covered person" under the CFPA. 12 U.S.C. § 5481(6).

FACTS

12. Sterling offers consumers a credit card that provides a line of credit that can only be used at Sterling stores; it is not a general-purpose credit card.

13. In connection with offering its credit products, Sterling's salespeople misrepresented financing terms or omitted information necessary for consumers to understand the credit offer.

14. Store employees failed to inform consumers that they were applying for credit and misstated the reasons for requesting consumers' personal information.

15. In many instances, Sterling's sales representatives offered to check for a consumer whether the consumer qualified for a line of credit. In fact, the sales representative actually submitted a credit application for the consumer.

16. In many instances, Sterling's sales representatives told consumers when they applied for credit that there would be no "hard inquiry" or negative impact on consumers' credit reports because Sterling offered "in-house" financing. In fact, for each application for credit from Sterling, Sterling made a credit-report inquiry.

17. In many instances, Sterling's sales representatives induced consumers to provide their personal information by purporting to enroll consumers for a store "rewards card," loyalty program, newsletter, or mailing list. In fact, the sales representatives used consumers' personal information to submit a credit application.

18. In other instances, Sterling's sales representatives informed consumers that they were collecting personal information for a "survey" or to place a custom order for the consumer when, in fact, the information was used to complete a credit application.

19. Many of Sterling's store managers and district managers encouraged deceptive tactics to induce consumers to apply for a credit card, and many turned a blind eye to such conduct.

20. For example, Sterling's store managers and district managers told sales representatives not to use the term "credit card" but instead to refer to the credit card as a store card, or e.g., a "Kay card," rather than a "credit card."

21. Sterling's training materials instructed employees to offer credit to every customer who visits a store, and they included tips that were designed, at least in part, to distract the consumer, such as "offer to clean your Guest's jewelry while you fill out the credit application," and "completing the in-house credit account application for the Guest on the [in-store] tablet allows him/her to focus on his/her reason for visiting the Store, and not on completing paperwork."

22. Sterling's credit-card applications have been in both paper and electronic formats.

23. Sterling's training materials instruct employees to "[a]lways fill out the paper credit application or type the credit application into the Graphical POS for the Guest."

24. Because the credit application was usually completed by the salesperson on paper or on the employee-operated electronic tablet, rather than by the consumer, many consumers never saw their credit-card application or any applicable terms and conditions.

25. Additionally, in many instances, consumers were never given any written or oral credit disclosures or any indication they were applying for credit. In other instances, consumers were given inaccurate oral disclosures.

26. Sterling's employees experienced intense pressure to obtain and submit completed applications.

27. Employees were rated, retained, and compensated based on their ability to meet certain performance standards, including for obtaining credit-card applications.

28. Sterling's companywide, formal performance standards required employees at stores located in shopping malls to complete "one credit card application a day." Employees at standalone stores were required to obtain one credit application every two days.

29. Employees who failed to meet the company's credit-application quota received counseling and additional training from store managers, were told that they could not leave the store until they met their goal, and, in some instances, were terminated for failing to meet performance standards.

30. From 2014 to 2017, nearly a million Sterling credit-card accounts were opened based on applications completed and submitted in Sterling's stores and then never used by the consumers who had supposedly applied for them.

31. When consumers knew they were applying for credit, Sterling's employees sometimes misled consumers about the type of financing for which they were applying, as well as the applicable terms of the financing, such as the interest rate and monthly payment amount.

32. In such instances, consumers applied for credit from Sterling after employees presented them with certain terms—a low monthly payment or interest-free period—that were not honored. These consumers received credit cards and billing statements that did not match the representations made by the salespeople at the time consumers applied.

33. Sterling's employees offered, and were trained to promote, interest-free financing.

34. In many instances, consumers were offered interest-free financing in connection with a purchase, only to find out upon receiving their first billing statement that they were enrolled in a regular, interest-bearing credit plan.

35. Sterling's stores generally offered six, 12, and 18-month, interest-free promotional financing to customers provided they met a minimum purchase amount and applied a 20% down payment at the time of purchase.

36. In many cases, Sterling's employees offered customers promotional financing but then determined that the customers could not make a down payment at the time of purchase and thus did not meet the eligibility requirements for interest-free financing, and Sterling's employees instead enrolled the consumers in a regular financing plan without disclosing this to the consumer. Consumers often did not learn of this until they received their first billing statement in the mail weeks later.

37. In other instances, consumers were quoted a monthly payment amount based on interest-free financing and later quoted a lower monthly payment without Sterling's employees explaining that the lower monthly payment was not available with

interest-free financing and instead required extending the repayment period on a regular, interest-bearing plan.

38. In these cases, Sterling's employees did not tell consumers that they were getting regular financing, rather than promotional financing, and did not disclose the changed financing terms to consumers at the time of purchase or obtaining credit.

39. Until October 2017, Sterling offered to its credit customers Payment Protection Plan (PPP) insurance through a third-party insurance provider. PPP insurance was offered at the point-of-sale in 33 states. Although a third party administered PPP, Sterling was responsible for the marketing and sale of PPP.

40. PPP insurance was an optional credit-insurance program offered to Sterling credit customers to help them make their monthly payments in the event of death, disability, loss of property due to burglary or perils, or loss of work. The PPP terms varied depending on the customer's state of residence.

41. PPP insurance was directly tied to the consumer's credit card because its function is to make monthly credit-card payments if the consumer meets certain criteria. PPP insurance was not offered to customers, and could not exist, independent of the credit card.

42. In states where PPP insurance was offered, Sterling's employees were required to enroll customers in it to meet company performance standards.

43. Sterling's employees enrolled some consumers in PPP insurance without their knowledge or consent. In many instances, consumers were asked to "sign here" or select "Yes" on an electronic "PIN-pad" in order to hold an item, process an order, or verify their information when, in fact, their signature was used to enroll them in PPP.

44. Customers enrolled in PPP insurance at the store by electronically consenting to coverage on the PIN-pad they used to complete their purchase transaction.

45. The cost of PPP insurance varied depending on the type of coverage and state, but it averaged around \$0.78 per \$100 purchase or balance amount. This amount was charged monthly on the consumer's credit-card billing statement.

46. In many instances, PPP insurance was added to consumers' accounts or purchases without their knowledge or consent.

47. Consumers did not realize that they were electing to purchase credit insurance on the PIN-pad, often noting that they assumed they were signing in connection with the purchase, special order, or, if they were aware of it, the credit application, which occurred at the same time and as part of the same transaction as PPP enrollment.

48. Former Sterling employees indicated that customers would be hurried through the point-of-sale transaction and told to "initial here"—encouraging the customer to enroll in PPP.

49. One former employee explained: "you didn't tell people about the product, you just put it on there." That is, Sterling's sales representatives signed customers up for PPP insurance without asking, and if someone noticed and complained, they'd remove it.

50. Consumers often only discovered they were enrolled in, and being charged for, PPP insurance after noticing it on their billing statements.

51. In some instances, Sterling’s employees told consumers about the PPP insurance and asked them to sign up so that the employee could meet their quota—while promising the consumer that the employee would cancel the insurance before the customer was charged. But the PPP insurance was not canceled and the customer was then charged.

52. In other instances, Sterling’s employees told consumers that they were signing up to receive an informational packet to gauge their interest in PPP insurance, when they were in fact purchasing the product itself.

CAUSES OF ACTION

Count I—Deception under the CFPB Regarding Credit-Card Enrollment, Asserted by the Bureau and the State of New York

53. The allegations in paragraphs 1-x are incorporated by reference.

54. An act or practice is deceptive if there is a representation or omission of information that misleads or is likely to mislead a consumer; the consumer’s interpretation of the act or practice is reasonable under the circumstances; and the misleading act or practice is material.

55. In many instances, Sterling’s employees have represented to consumers that they were completing surveys, enrolling in a store card or rewards card, or checking to see how much they would qualify to spend in the store when, in fact, the consumers were completing credit-card applications or Sterling’s employees were completing applications for consumers without their knowledge or consent.

56. These misrepresentations were likely to mislead consumers acting reasonably under the circumstances because consumers believed they were providing

personal information for other purposes and consumers relied on store employees' representations that consumers were doing something other than opening a credit card.

57. These misrepresentations were material because many consumers likely would not have provided their personal information and signature if they knew they were applying for credit, given that they may not have wanted an extension of credit or the potential negative impact it could have on their credit file or ability to obtain credit in the future.

58. Furthermore, a reasonable consumer would want to know that their personal information and signature could be used to open up a credit-card account at Sterling's stores.

59. The fact that the credit-card application disclosed the actual nature of the transaction does not correct the misrepresentations made to consumers.

60. Sterling's statements or omissions to consumers regarding credit applications were false or misleading and constituted deceptive acts and practices, in violation of the CFPA. 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

Count II—Unauthorized Issuance of Credit Cards under TILA and Regulation Z, Asserted by the Bureau and the State of New York

61. The allegations in paragraphs 1-__ are incorporated by reference.

62. TILA provides that no credit card shall be issued except in response to a request or application therefor. 15 U.S.C. § 1642.

63. Regulation Z states that no credit card may be issued to any person except in response to an oral or written request or application for the card. 12 C.F.R. § 1026.12(a)(1).

64. Sterling issued credit cards to consumers without their knowledge or consent and not in response to an oral or written request for the card.

65. Therefore, Sterling has violated TILA and Regulation Z. 15 U.S.C. § 1642; 12 C.F.R. § 1026.12(a)(1).

**Count III—Violation of the CFPA,
Asserted by the Bureau and the State of New York**

66. The allegations in paragraphs 1-__ are incorporated by reference.

67. Sterling's violations of TILA and Regulation Z, described in Count II, constitute violations of § 1036 of the CFPA. 12 U.S.C. § 5536(a)(1)(A).

**Count IV—Deception under the CFPA Regarding Promotional-Financing
Terms, Asserted by the Bureau and the State of New York**

68. The allegations in paragraphs 1-__ are incorporated by reference.

69. Sterling's employees misrepresented certain financing terms to consumers, including the applicable interest rate, monthly payment amount, and eligibility for promotional financing.

70. In these instances, consumers did not know the terms of the extension of credit they received until they received their first billing statement in the mail.

71. Consumers reasonably relied on Sterling's employees' statements regarding the terms of the extension of credit they would receive, and consumers opened lines of credit and made purchase decisions on the understanding that they would receive the terms represented to them by Sterling employees.

72. Sterling's statements or omissions to consumers regarding the terms of or consumers' eligibility for promotional financing plans were false or misleading and

constituted deceptive acts and practices, in violation of the CFPA. 12 U.S.C. §§ 5531(a), 5536(a)(1)(B).

Count V—Unfairness under the CFPA Regarding PPP Enrollment, Asserted by the Bureau and the State of New York

73. The allegations in paragraphs 1-__ are incorporated by reference.

74. Under the CFPA, an act or practice is “unfair” where the Bureau has “a reasonable basis” to conclude that “the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers,” and that “such substantial injury is not outweighed by countervailing benefits to consumers or to competition.” 12 U.S.C. § 5531(c)(1).

75. Sterling’s employees enrolled consumers in PPP insurance without their knowledge or consent.

76. This practice typically occurred when employees enrolled consumers in PPP insurance without informing them that they were being enrolled, or misled consumers about what they were signing up for.

77. This conduct was likely to cause substantial injury because consumers were charged a monthly fee for the coverage in an amount proportional to their purchase or balance amount, which consumers could not reasonably avoid because they were not aware that they had the option to accept or decline coverage.

78. The harm to consumers from being enrolled in and charged for PPP insurance without their knowledge was not outweighed by countervailing benefits to consumers or competition; Sterling’s practice of enrolling consumers in its optional PPP insurance without their knowledge or consent did not provide any benefits that would encourage legal business practices or competition.

79. Therefore, Sterling committed unfair acts or practices, in violation of §§ 1036(a)(1)(B) and 1031(c)(1) of the CFPA, 12 U.S.C. §§ 5536(a)(1)(B), 5531(c)(1).

Count VI—Deceptive Acts or Practices in Violation of New York GBL § 349, Asserted by the State of New York

80. The State of New York realleges and incorporates by reference paragraphs 1-__.

81. New York GBL § 349 provides that “[d]eceptive acts or practices in the conduct of any business [...] in this state are hereby declared unlawful.”

82. GBL § 349 authorizes the NYAG to bring an action for an injunction, restitution and civil penalties when any individual has engaged or is about to engage in deceptive practices in the State of New York.

83. Sterling’s employees have engaged in deceptive acts and practices by conduct including but not limited to: i) deceiving consumers about credit-card applications and enrollment; ii) misrepresenting to consumers the terms and conditions of Sterling’s promotional financing; and iii) failing to disclose that consumers are enrolling in payment protection insurance.

84. Sterling has therefore engaged in deceptive acts or practices in violation of GBL § 349.

DEMAND FOR RELIEF

Plaintiffs request that the Court:

- a. enjoin Defendant from committing future violations of the CFPA, Truth in Lending Act, Regulation Z, and New York State law;
- b. order Defendant to pay redress to consumers;
- c. impose civil money penalties on Defendants under the CFPA;

- d. order Defendant to pay the costs incurred in connection with prosecuting this action; and
- e. award additional relief as the Court may determine to be just and proper.

Respectfully submitted,

KRISTEN A. DONOGHUE
Enforcement Director
JEFFREY PAUL EHRLICH
Deputy Enforcement Director

s/ Patricia H. Hensler
PATRICIA H. HENSLER (FL 102303)
STEFANIE ISSER GOLDBLATT
Enforcement Attorneys
Bureau of Consumer Financial Protection
1700 G Street, NW
Washington, D.C. 20552
Telephone (Hensler): 202-435-7829
Telephone (Goldblatt): 212-328-7011
Facsimile: 202-435-7722
E-mail: Patricia.Hensler@cfpb.gov
E-mail: Stefanie.Goldblatt@cfpb.gov
Attorneys for Plaintiff
Bureau of Consumer Financial Protection

BARBARA UNDERWOOD
Acting Attorney General of the State of New York

JANE M. AZIA (NY 1539600)
*Bureau Chief, Consumer Frauds and Protection
Bureau*

CAROLYN FAST (NY _____)
Assistant Attorney General
120 Broadway
New York, N.Y. 10271
Telephone (Azia): 212-416-8727
Telephone (Fast): 212-416-6250
Facsimile: 212-416-6003
E-mail: Jane.Azia@ag.ny.gov
E-mail: Carolyn.Fast@ag.ny.gov
Attorneys for Plaintiff
State of New York

APPENDIX S

1700 G Street NW,
Washington, DC 20562



~~October 26, 2018~~~~October 23, 2018~~~~October 22, 2018~~

Recommendation Memorandum for the Acting Director

FROM	Redacted by the Committee and Kristen Donoghue, Office of Enforcement	Jeff Ehrlich,
THROUGH	Eric Blankenstein, SEFL Policy Director; Chris D'Angelo, SEFL Associate Director	
SUBJECT	Authority to Settle with Sterling Jewelers, Inc. and to File Suit—ENF Matter No. 2016-1806-02	

Recommendation

The Office of Enforcement recommends that you authorize it (1) to settle with Sterling Jewelers, Inc. (Sterling) under the parameters described in Section IV below; (2) if settlement negotiations are successful, to file an administrative consent order or a complaint and consent order in federal court effectuating the settlement; and (3) if settlement negotiations are unsuccessful, to commence an enforcement action either administratively or in federal court, consistent with the attached complaint.¹ This investigation was conducted in partnership with the New York State Attorney General's Office, and, if authorized, the Bureau would file a joint complaint with that office.

I. Overview

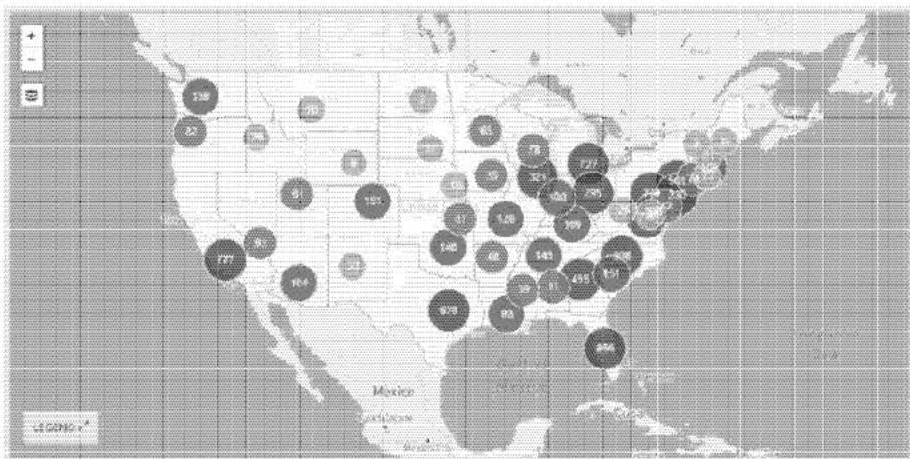
Sterling operates roughly 1,500 jewelry stores in malls and off-mall locations in all 50 U.S. states under national banners that include Kay Jewelers and Jared The Galleria of Jewelry, as well as a variety of mall-based regional stores such as J.B. Robinson, Marks & Morgan, and Belden Jewelers. Sterling is a wholly-owned subsidiary of Signet Jewelers Limited (Signet), the largest specialty-jewelry retailer in the United States, United Kingdom, and Canada. Sterling entities provide over 60% of Signet's total sales of about \$6.4 billion. Since 1990, and until recently, Sterling has had a centralized consumer-financing program through which it has extended credit directly to consumers.² As part of its in-house credit program, Sterling has offered "interest-free"

¹ Enforcement also seeks authority to make non-material changes before filing.

² In October 2017, Signet, through Sterling, sold a portion of its consumer-lending portfolio—\$1 billion of its prime-credit business—to Alliance Data Systems. In March 2018, Signet announced

and interest-bearing financing, subject to certain conditions, and, in most states, it also offered third-party credit insurance. Roughly 60% of Sterling's total sales are credit sales, and the fees and charges from Sterling's credit-financing programs have totaled roughly \$300 million on average for each of the past three years. As part of the investigation, Enforcement (i) interviewed 20 former employees and 32 customers; (ii) supervised ~~14~~ 10 secret-shopping trips to Sterling stores in California, Florida, ~~New York~~ and Virginia to observe sales practices and techniques; (iii) reviewed Sterling's internal training materials and employee-incentive structure; and (iv) analyzed thousands of consumer complaints from consumers all over the country, across Sterling's different store brands (see complaint map below).

Commented [BE(1)]: Are there formal reports of these trips? Can I see them?
 Commented [R(2R1)]: Yes, attaching sample reports. And removing NY as we did not supervise those secret-shopping trips.



As described further below, the Office of Enforcement has concluded that from at least January 2014 through October 2017 Sterling employees signed consumers up for credit cards without their authorization or consent, misrepresented credit financing terms and conditions to consumers, and enrolled consumers in optional payment-protection insurance without their knowledge or consent.

The Bureau has authority to address Sterling's conduct because it offers credit to consumers. Sterling is not subject to the CFPB's "merchant exemption" because it regularly extends credit subject to a finance charge and is significantly engaged in offering or providing consumer-financial products or services.³

This matter would best be resolved through settlement. Because the specific terms of any consent order will be subject to negotiation and ongoing modification, a draft consent order is not attached to this memorandum. The Office of Enforcement will discuss any proposed order with

that it would sell the remaining portion, Sterling's non-prime receivables, to investment funds managed by CarVal Investors.

³ See 12 U.S.C. § 5517(a)(2)(B)(iii), (a)(2)(C)(i).

the Legal Division before submitting it to you. If settlement negotiations fail, the Bureau should file suit, either administratively or in federal court, consistent with the attached complaint.

II. Factual Background

Customers report in complaints⁴ and interviews that they were given credit cards that they did not want. In some instances, consumers knew they were being offered credit but claim that Sterling employees presented them with certain terms—a low monthly payment or interest-free period—that were then not honored. These consumers received credit cards and billing statements that did not match the representations made by the salespeople at the time consumers applied. Consumers were also enrolled in Payment Protection Plan (PPP) insurance and claimed it was without their knowledge or consent. In many instances, consumers report that they were asked to “sign here” in order to hold an item, process an order, or verify their information, when in fact these consumers were signing up for PPP.

The Bureau’s investigation focused on three issues related to Sterling’s credit business: (1) ~~whether consumers received unauthorized credit cards~~ credit card accounts were opened without consumer knowledge or consent; (2) whether credit-financing terms and conditions were not accurately disclosed; and (3) whether consumers were enrolled in payment-protection insurance without their knowledge or consent.

A. ~~Unauthorized Accounts Opening~~

When a consumer applies for credit in one of Sterling’s stores, Sterling store employees request personal information from the consumer, ~~complete the application on the consumer’s behalf, and~~ serve as the primary source of information for the consumer. In fact, Sterling’s training materials, which are ~~universally~~ used to train store employees across all of its regional and national brands, instruct employees to complete the credit application on behalf of consumers. Because the employee holds the application, consumers often do not see that it is an application for credit, nor do they see the applicable credit disclosures, which are displayed in general terms, e.g., APR 5% to 24.99%, in fine print on the back or folded portion of a paper application and, for electronic applications completed on a tablet, are not provided on any screen shown to consumers.⁵ There does not appear to be any process or requirement for consumers to receive

Commented [BE(3)]: Usually?

Commented [Re(4R3)]: Edited to reflect it is typically the practice

⁴ Consumer complaints include those filed with the Bureau, the Better Business Bureau, the Federal Trade Commission’s Sentinel Network, and those filed directly with the company.

⁵ The Bureau requested from Signet in a civil investigative demand issued in November 2016 all information relating to the credit application process, including all disclosures given to consumers in connection with that process. The tablet screenshots Signet produced do not show that any credit terms and conditions are displayed. Moreover, Sterling’s training materials, which apply to employees at all its regional and national stores, state that store employees should complete credit applications for consumers, and statements from consumers who claim they did not see, or were not made aware of, credit terms provide evidence that these statements are representative of the process in most, if not all, of Sterling’s stores.

written or oral disclosures at the time of the transaction⁶ and many consumers specifically describe not receiving any oral or written disclosures. In complaints and interviews, consumers report that Sterling employees do not show consumers the credit application and misrepresent the reason for which they are requesting consumers' personal information. In many instances, consumers unknowingly and without giving consent, apply for Sterling's store-brand credit cards.⁷

Consumers allege that Sterling sales representatives offered to see whether the consumer was qualified for a line of credit but then proceeded to submit a credit card application for the consumer. These consumers indicate they did not intend to apply for a credit card and only thought the sales person was gauging their creditworthiness. Bureau investigators conducting undercover store visits also noted that in some instances Sterling's salespeople offered "to run [their] credit for approval" and stated it would only be a "soft inquiry" on their credit report. One Jared store employee told a Bureau investigator, "Jared has its own bank and therefore the credit approval process is done in-house and doesn't affect your credit report." Consumer complaints corroborate ~~store employees' the experience of Bureau investigators, and describe similar statements from store employees~~ about how the store card is "in-house" and won't affect consumers' credit. Although consumers must actually apply for credit in order to verify how much they are qualified to spend in the store, they ~~do not~~ may not understand—and Sterling employees usually did not inform consumers—that by agreeing to have a store employee assess their credit-worthiness, they were in fact applying for credit. Moreover, as discussed further in Section III, ~~alleged misrepresentations by the fact that Sterling's would not be cured by statements on the paper credit application states that it is a credit application is not persuasive because Sterling employees made contrary representations and, moreover,~~ consumers often did not see the actual credit application. In some instances, Sterling employees explicitly assured consumers that because the store offers "in-house" credit, it does not have any impact on consumers' credit reports. In other instances, employees simply offered to check consumers' credit without informing them it will result in a card being issued.⁸

Consumers also claim that they were ~~also~~ asked to provide personal information to sign up for the store "rewards card," newsletter, or mailing list, when the information was in fact used to apply for a credit card. In at least 35 consumer complaints, consumers alleged that they believed they were providing information for a "survey" and only later learned they were applying for

⁶ When paper applications were used, employees typically controlled and held the application so consumers did not see the credit card agreement and terms. With credit applications completed via tablet, Sterling did not produce any documents or screenshots showing that consumers were shown credit card agreement terms.

⁷ Signet produced roughly 50,000 consumer complaints over a three-year period. The manner in which the complaints were produced—raw, shorthand/abbreviated notes with inconsistent descriptions of the consumer's complaint/inquiry—make it difficult to accurately report the number of complaints relating to certain claims. That said, Signet reported there are 1,359 complaints associated with accounts without purchases. Currently, 382 complaints about unauthorized credit cards have been reviewed and tagged in Relativity.

⁸ Consumer complaints, consumer interviews, and direct observations through undercover store visits support these facts.

Commented [BE(5)]: Is the paper credit application ever given to the consumer? If so, when (especially when vis-a-vis the customer signing the application)?

Commented [Re6R5]: Our understanding is that Sterling moved from using a paper application to a tablet application at some point during the applicable period. With that understanding Enf does not think the paper application was given to the consumer as a matter of course, but certainly may have been in some instances. When the process was completed via paper application, the store retained the document and consumers reported (when they were aware) that they thought they were signing for something else – a custom order, reward/loyalty card, survey, etc. The footnote below (6) says "...employees typically controlled and held the application..." – not foreclosing the possibility that in some instances consumers were given the credit application

credit. Consumers consistently report that they were never given written disclosures or any indication that they were applying for credit. For example, here is how a consumer described the process during a chat inquiry with a Sterling representative:

2016-07-09 20:33:27 [customer]: Hi [Sterling representative]. I was at the Brookfield square mall last week and I was told that I was filling out a form for a survey to win \$xxxx but when I got home from work today, there was a Kay credit card in my mail box
2016-07-09 20:34:03 [customer]: I never consented to being signed up for a credit card and I am very upset; not at you, but at the sales person that was in the mall;
2016-07-09 20:35:19 [Sterling representative]: The form the associate in store had you fill out, did it ask for your personal information along with your social security number?
2016-07-09 20:36:52 [customer]: Yes it did. She filled it out for me, so I never [saw] it. But as she read from the paper, she asked for my social security number, my home address and previous address, she also asked for a family members name, phone number, and city of residence.
2016-07-09 20:37:00 [customer] And she asked about my employment information
2016-07-09 20:37:37 [customer] She did this with both me and my fiancé and the only time we [saw] the form was when she had us sign the bottom
2016-07-09 20:38:56 [customer] Also, we asked why she needed our social and she said so they could verify that we are who we say we are. And when she handed us the paper to sign, she had it folded and said it was for security reasons because our social security numbers were on it
2016-07-09 20:40:39 [Sterling representative] The form that was filled out for you in store was a credit application for a Kay Jewelers card. By signing the form, you gave us permission to run the application for credit approval. I apologize you were not told by the associate you were applying for a Kay account.

Although it may seem that providing such personal information for a rewards program, store card, mailing list, survey, contest, etc. is not reasonable, when assured by a store employee that the information is necessary consumers relied on store employees' representations and complied with employees' requests. A consumer acting reasonably under the circumstances would not expect that a store employee is attempting to open a credit card on behalf of a consumer. The significant volume of complaints – 1,359 relating to unauthorized accounts – is evidence that reasonable consumers were not aware that they were completing credit-card applications and that these practices are widespread and affected more than a handful of consumers.

Representative consumer complaints include:

- "I bought an engagement ring from Jared the Galleria of Jewelry. I stated from the beginning I would be paying for the ring and all charges with my American Express Card. The salesperson then filled out forms to open a credit card for me without my knowledge. When it was time to close the sale, they presented the form to me, saying it was required to order the diamonds/ring that I wanted so I signed it. They had the paper form folded in such a way that I could not see that it was for a credit card.... [T]hey opened a credit card in my name without my consent via deceptive sales practices and outright manipulation...."
- "I was told that I was signing up for an employee loyalty program at JARED Jewelry that would send me coupons and cash back on further purchases. I explicitly asked multiple times if they were setting up a credit card, and the sales representative assured me he was

not. I became suspicious once he asked for more personal information such as employment history and my Social Security Number. I asked again if this was signing me up for a credit card, and the sales representative told me no. He stated they were only doing an internal background check but no credit would be opened. A few days later, I went to sign up for a credit card from a company I actually wanted a credit card from, and I was declined. They stated the reason was that I had too much credit open in my name... A few days later, I received in the mail a credit card from JARED....”

- “I would like to file a complaint against Kay Jewelers. They signed my fiancé and myself up for a credit card without telling us... the sales representative... said we were signing an agreement for the custom ring they were going to design for us... We were signed up for not one, not two, but THREE cards which were received in the mail a week after starting the process with them. They just tell you it's a contract for the custom ring, if we had known it was a credit card application we would have refused to fill out the paperwork.”
- “[A] Kay Jewelry saleswoman wanted me to fill out a form so that I can take care of some kind of ‘promotional coupon’ that would be sent in the mail.... I received a letter from the Kay Jeweler’s Credit Operations Division which stated that they turned down my application to open some kind of credit account because I do not make enough money. First, respectfully, the saleswoman took my social security number because she told me that it was only to prevent fraud and that they would not use it for anything else (I have no idea how it would prevent fraud, but she seemed honest)! Second, she never took my income information down... so I don't even know how Kay Jewelers was able to find out how much I make without me divulging that information unto them. This dishonest tactic may lower a great credit score.”
- “The representatives I worked with, Patricia and Katrina, said they would like to screen my credit in order to determine the price range of rings we could qualify for. I insisted repeatedly that I did not want a credit card as we had not yet determined where we would be buying a ring, but they stated explicitly that they would be doing a preliminary screening of my credit only. They said they would not be issuing a credit card, and this was a standard procedure to see what amount someone can qualify for. After the “preliminary screening,” I was told I was approved for a \$10,000 credit limit, and that any questions I had would likely be answered with the paperwork that would be coming with my credit card in the mail. I reminded them that I did not want a credit card, and that they said this was supposed to be preliminary screening, and they replied saying it was fine because if I didn't want the card, it would be closed in 2 years if I don't use it. I did not want the credit card, and was lied to in order for them to set up an account in my name.”

Interviews with former store employees further substantiate consumers’ ~~reports~~ complaints. Specifically, 20 former employees at various stores across 12 states indicated that they were trained to mislead customers into applying for credit cards—telling consumers they were signing up to be “preferred customers,” specifically refraining from using the term “credit card” and instead asking consumers to open a “rewards card,” and asking consumers to help the employee “win a contest” by filling out a form for a “customer account.” Former employees said they would offer discounts on jewelry for opening a card—even where items were already discounted

without opening an account—or offer free watch-battery replacement to consumers if they open an account.

Sterling’s companywide, formal performance standards require its store employees to sell credit cards to consumers. Mall-store employees are required to obtain one credit-card application a day, while standalone-store employees are required to obtain one credit-card application every two days. Employees who fail to meet these thresholds receive counseling and additional training from store managers and, in some instances, are terminated. Interviews with former employees suggest that there was intense pressure to meet Sterling’s goals. Hundreds of anonymous employee reviews on www.glassdoor.com, a database of employee-authored company reviews, reiterate employees had trouble meeting their credit-card quotas.

Representative Glassdoor.com reviews state:

- “One of the major downsides is the push to get guests to open a credit card. Each sales associate is expect[ed] to get 1 credit application a day.”
- “Upper management care more about you opening up credit cards than they do actual sales. I’ve seen employees do some really shady things in order to maintain their credit standard. Everything from using underage candidates to making up social security numbers and names. They get all the praise because they ‘met’ the standard. Then the associates who try to do it ethically get reprimanded.”
- “Credit Apps can be a problem. You are expected to sign people up for these every day and that is challenging at best. Many people are very wary about opening a credit card and rightfully so. So it should be an incentivized bonus if you do sign up someone for a credit card rather than a daily req.”
- “Not a particularly pleasant work environment between disgruntled employees and customers and unrealistic credit card goals made it seem like we were scamming to make a quota.”
- “Must open 1 new credit card everyday, people do not want another specialty card but management doesn't want to hear that.”
- “Also, the credit card is supposed to be a tool to help us close sales. Not pressure us to break company policy and in some cases the law.”
- “Very high pressure to get people to fill out credit apps. All the add-ons like the warranty and credit app were emphasized more than the actual selling of jewelry.”
- “If you don't make all of the 5 standards⁹ they'll terminate you after 6 months... Emphasis is placed solely on having sell credit card apps, not jewelry.”
- “You must be 6/6 standards (sales, addons, repairs, PPP, esp, and credit apps) at all times to be even be acknowledged you exist by upper management. They expect you to walk around the mall and harass people for credit apps. Upon getting hired, they expect you to also harass your friends and family to fill out a credit app. If you don't get your credit apps, you must go to weckly meetings or even call your district manager and tell him/her why you do not care about your job at the end of every shift. They will offer you a promotion, then give it to someone else the next day... Upper management sweeps unethical and illegal behavior under the rug as long as you have your numbers in.”

⁹ In states that do not offer PPP there are only five performance standards.

- “Mandatory early morning meetings on Sat. or Sun. (translate that punishment) for lack of credit apps.” “This type of job should be fun and enjoyable... instead, it has become a marathon of credit accounts, add-ons, ppp's, esp's, uwp's, repairs, and the stresses of keeping numbers up to avoid write-ups, cuts in hours, and mandatory punishment meetings. The response to this kind of constant pressure leads some employees to misrepresent things in order to achieve their numbers. Not a good thing for the customer...or the company.”
- “If you don't have your standard for sales and credit application, then [you] can kiss your job Goodbye! I understand the ‘trickle down’ effect, but there needs to be some sort of relief from this stress of losing your job if credit isn't at 100%...and mandatory store meetings at 8am on Saturday morning for missed credit for the week has got to be a [form] of abuse [of] power.”
- “First month not at 6 for 6 standards---verbal/written counseling[.] Second month not at 6 for 6 standards---written counseling[.] Third month not at 6 for 6 standards---termination.”

Former employees reported during interviews that employees who did not meet credit-card quotas were “written up,” had to go in to the store on their days off or before or after work for credit-card meetings, and were lectured on “getting their numbers up.” At least ten former employees from stores in different states said there was a training for “employees not meeting their numbers” that could be a two to four-hour drive away from their store’s location. Eight former employees specified that Sterling employees could be fired for failing to obtain credit-card applications.

In addition to rating employees on their ability to meet or exceed the standard for new credit-card applications, Sterling runs an annual four-week credit-application contest that awards cash to employees at all levels, including sales representatives, store managers, and district managers, who obtain the most credit-card applications.

Sterling’s training materials instruct store employees to offer credit early and often to every customer. These materials require, in part, facially compliant credit-related practices and procedures that, ~~while not necessarily followed by store employees,~~ seek to ensure customers understand that they are applying for credit as well as the related credit terms and conditions. ~~They~~ The training materials also include tips such as “offer to clean your Guest’s jewelry while you fill out the credit application” and “completing the in-house credit account application for the Guest on the CASSi tablet allows him/her to focus on his/her reason for visiting the Store, and not on completing paperwork.” ~~In fact, because the in-store credit application process is largely completed on the employee-operated tablet, at least some consumers never see a full credit card application—nor do they see applicable terms and conditions or disclosures.~~ Regardless of the type of application, employees are instructed to “[a]lways fill out the paper credit application or type the credit application into the Graphical POS for the Guest” so customers do not see the credit application. Sterling also provides guidance to store employees on how to overcome consumers’ objections to credit accounts and additional suggestions, such as presenting a credit line with a piece of jewelry, ~~presumably to distract the customer.~~

Commented [BE(7)]: Since this paragraph deals with Sterling P&Ps, and the lack of consumer notice is discussed elsewhere, I suggest deleting

Commented [R(8R7)]: Deleted

~~The As further evidence that consumers were subject to unauthorized credit cards, the Bureau obtained from Sterling Sterling provided data identifying the number of company credit-card accounts that were opened but never used. Sterling stores issued about 285,000 credit cards each year that had no activity on them. Over a three-year period, the total number of Sterling accounts opened without any purchases made was nearly one million. Recognizing that there are instances in which a consumer applies for credit and decides for any number of reasons that they are not going to make a purchase, it seems unlikely that this explanation justifies nearly a million open accounts.~~

B. Deceptive Representations About Financing

Consumers report that Sterling employees provide certain financing plan information at the point-of-sale that turns out to be different than the financing plan terms they receive. Employees offer, and are trained to promote, “interest-free” financing. Numerous consumers indicate that consumers were offered interest-free financing in connection with a purchase only to find, once they receive their first billing statement, that they were actually enrolled in a regular, interest-bearing credit plan.¹⁰ In these cases, the consumers claim that they were often quoted a monthly payment amount and other terms that differ from the terms of the plan for which they are enrolled.

Sterling stores generally offer interest-free promotional financing for periods of 6, 12, and 18 months to customers who meet a minimum purchase amount and pay a 20% down payment. Hundreds of consumer complaints and interviews of employees indicate that, in many cases, customers who expected to receive interest-free financing were actually given regular, interest-bearing financing. This typically happened for one of two reasons. First, if a customer could not make a down payment at the time of purchase and thus did not meet the eligibility requirements for interest-free financing, he would in many instances be signed up for a regular financing plan instead without being told by the employee of the switch. Second, if a consumer indicated that he could not afford the monthly payment amount that was calculated based on the promotional period for the interest-free plan, he would in many instances be given a lower payment amount that was calculated based on a longer repayment term and regular interest-bearing financing, also without having the changed terms explained. In both scenarios, Sterling employees explained the availability of interest-free financing and consumers believed they would receive it, but didn’t clearly inform consumers that they would not after it became clear that they didn’t qualify for or couldn’t afford the payments required for the interest-free promotion.

Interviews with former employees corroborate consumer complaints alleging misinformation and changed credit-card financing terms. Former employees from Sterling’s regional and national stores around the country mentioned that they would incentivize customers to open accounts by promising “12-months interest-free”—though this required a minimum purchase amount, which they did not disclose—and “no down payment,” which voids interest-free financing options. For example, one former employee said that for items below \$500 there was not an interest-free financing option, but employees would pitch “no interest” in the hope that no one would notice.

¹⁰ There are at least 375 complaints that have been reviewed and tagged that concern this claim.

C. Payment Protection Plan

Similar to the credit-card-application quota, Sterling employees were required to enroll customers in optional PPP insurance to meet performance standards. PPP is a credit-insurance program that was offered to Sterling credit customers to help those customers make their monthly payments in the event of death, disability, loss of property due to burglary or perils, leave of absence, job retraining, or involuntary loss of employment. Because the insurance protected consumers' credit payments, it was directly related to the credit financing that Sterling offers, and it provided a direct benefit to Sterling by protecting its accounts receivable from loss due to non-payment.

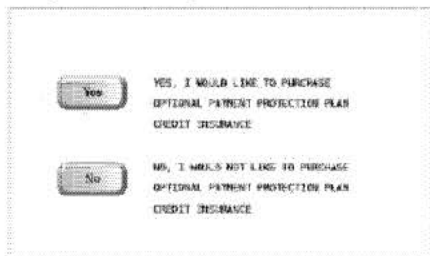
Sterling stores sold PPP to credit customers through Assurant,¹¹ a state-licensed insurance company, from at least 2009 to October 2017. PPP was offered at the point-of-sale in 33 states. The cost of PPP varied depending on the type of coverage and state, but it was typically around \$.78 cents per \$100 purchase amount. This amount was charged monthly on the consumer's credit-card billing statement based on the account balance. Although Assurant administered PPP, Sterling was responsible for the marketing and sale of PPP.

Evidence gathered during the investigation suggests that customers were routinely enrolled in PPP insurance at the time of their credit application or purchase transaction without knowing they were doing so and without ever viewing the insurance terms and conditions or costs. Customers in many instances "agreed" to enroll in PPP at Sterling stores by electronically consenting to coverage on the PIN pad they used to complete their purchase transaction. The customer acknowledgment was presented on the PIN pad device, but the terms and conditions and costs for PPP were not displayed. In some instances consumers may have been shown a brochure detailing, in general terms, the PPP benefits; however, many consumers did not see any disclosures, particularly those consumers who enrolled in PPP without their knowledge or consent.

According to Sterling's training materials, customers were prompted to indicate, on the PIN pad, "Yes, I would like to purchase optional Payment Protection Plan credit insurance" or "No, I would not like to purchase optional Payment Protection Plan credit insurance" after the store employee swiped the customer's credit card. If the customer selected "Yes," the employee was instructed to enter the customer's birthdate, and the customer was then prompted to sign the PIN pad. If a customer selected "No," they were still required to sign the PIN pad, confirming that they were opting out of coverage. The PIN pad sequence mirrored a typical retail transaction where, after providing payment, the consumer indicates "Yes" as to the purchase amount or form of payment, before signing the PIN pad to complete the transaction. Here, consumers did not realize that they were electing to purchase credit insurance, often noting that they assumed they were signing in connection with the purchase, special order, or, if they were aware of it, the credit application, which occurred at the same time and as part of the same transaction.

¹¹ Sterling Jewelers Insurance Agency, Inc., a wholly-owned subsidiary of Signet, provided insurance licensing functions for Sterling's credit-insurance programs.

There is no indication that employees necessarily provided the customer with any written terms and conditions or costs of the PPP. Sterling's internal materials state that store employees "may" present product benefits, coverages, and rate information to customers. As noted above, there was a hard copy brochure. But (1) employees were not required to provide the brochure to consumers; (2) the applicable insurance terms were in small, very fine print, and (3) the terms referenced the various types and costs of insurance but did not provide any specific coverage or cost for the individual consumer.⁴² Sterling's PPP materials indicate that the PIN pad displayed: "Yes, I would like to purchase optional Payment Protection Plan Credit Insurance." But there were no specific terms and conditions or costs displayed on the PIN pad, and the text that was displayed was in small font and not easily visible due to the limited clarity and contrast of the PIN pad screen. Here is a sample of the PIN pad screen:



Former Sterling employees indicated that customers would be hurried through the point-of-sale transaction and told to "initial here"—encouraging the customer to enroll in PPP.¹³ One former employee explained: "you didn't tell people about the product, you just put it on there." That is, sales associates signed people up for PPP insurance without asking, and if someone noticed the charge on a billing statement and complained, Sterling would remove it. Another former store manager said that district managers told store managers to check "Yes" for PPP even if customers didn't ask for it, noting that the store could always cancel it the next day but that the store would be "credited" for it even if it was later canceled, so "always check 'Yes.'" Based on this evidence, it seems it may be possible for store employees to select "Yes" for the customer and add PPP to consumers' accounts without the consumer affirmatively selecting "Yes."¹⁴

Formatted: Don't adjust space between Latin and Asian text, Don't adjust space between Asian text and numbers

At least 175 consumers submitted complaints alleging that PPP was added to their account without their knowledge or consent. Some consumers complain that Sterling employees asked them to sign up for PPP to help the employees meet their quotas; the employees promised that they would cancel the insurance before the customer would be charged, but they failed to do so. In one complaint, the consumer reported that he was told by the salesperson to select "Yes" and sign the PIN-pad to receive an insurance packet to gauge his interest and then discovered when the packet arrived that he had agreed to purchase the insurance. In response to such a complaint,

⁴² Even if a consumer reviewed the brochure they would not know the PPP cost or terms that apply to their account.

¹³ Sterling's training document instructs: "Use an assumptive close when closing PPP."

¹⁴ In addition, Sterling's PPP enrollment procedures specify steps the employee must take "[i]f you do not have a customer's signature either via the PIN-pad or on the sales slip," which suggests it was technically possible enroll a consumer without obtaining a signature.

Sterling's internal account notes indicate that the store apologized for putting PPP on without the consumer's knowledge, canceled the PPP, and refunded charges. ~~In other cases, consumers allege that they believed they were rushed through the transaction at the point of sale and later discovered that they had inadvertently signed up for PPP. Most commonly, consumers discovered that they were being charged for PPP only after noticing it on their billing statements.~~

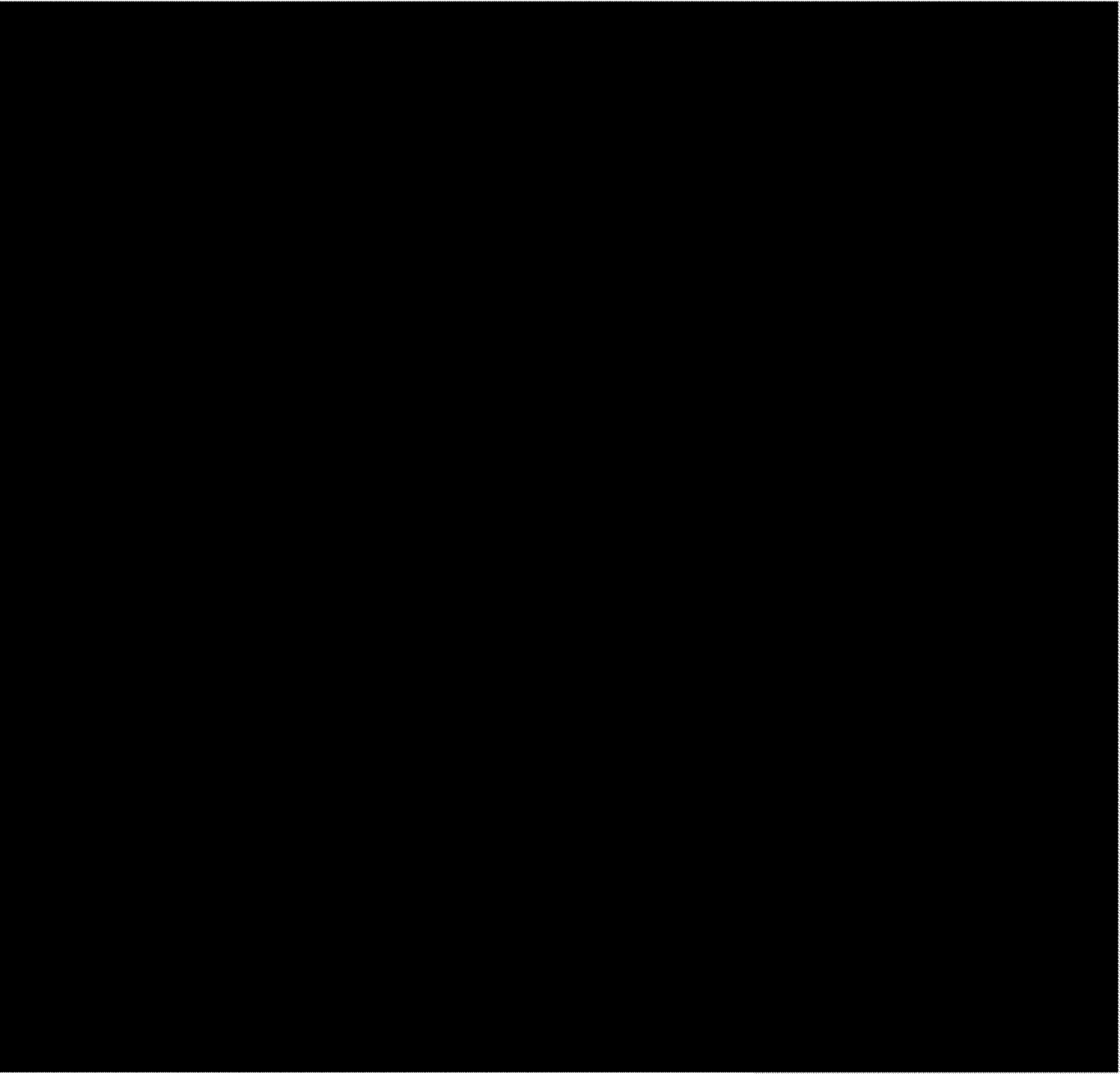
Here are a few consumer complaints about PPP:

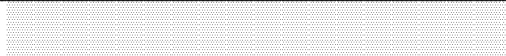
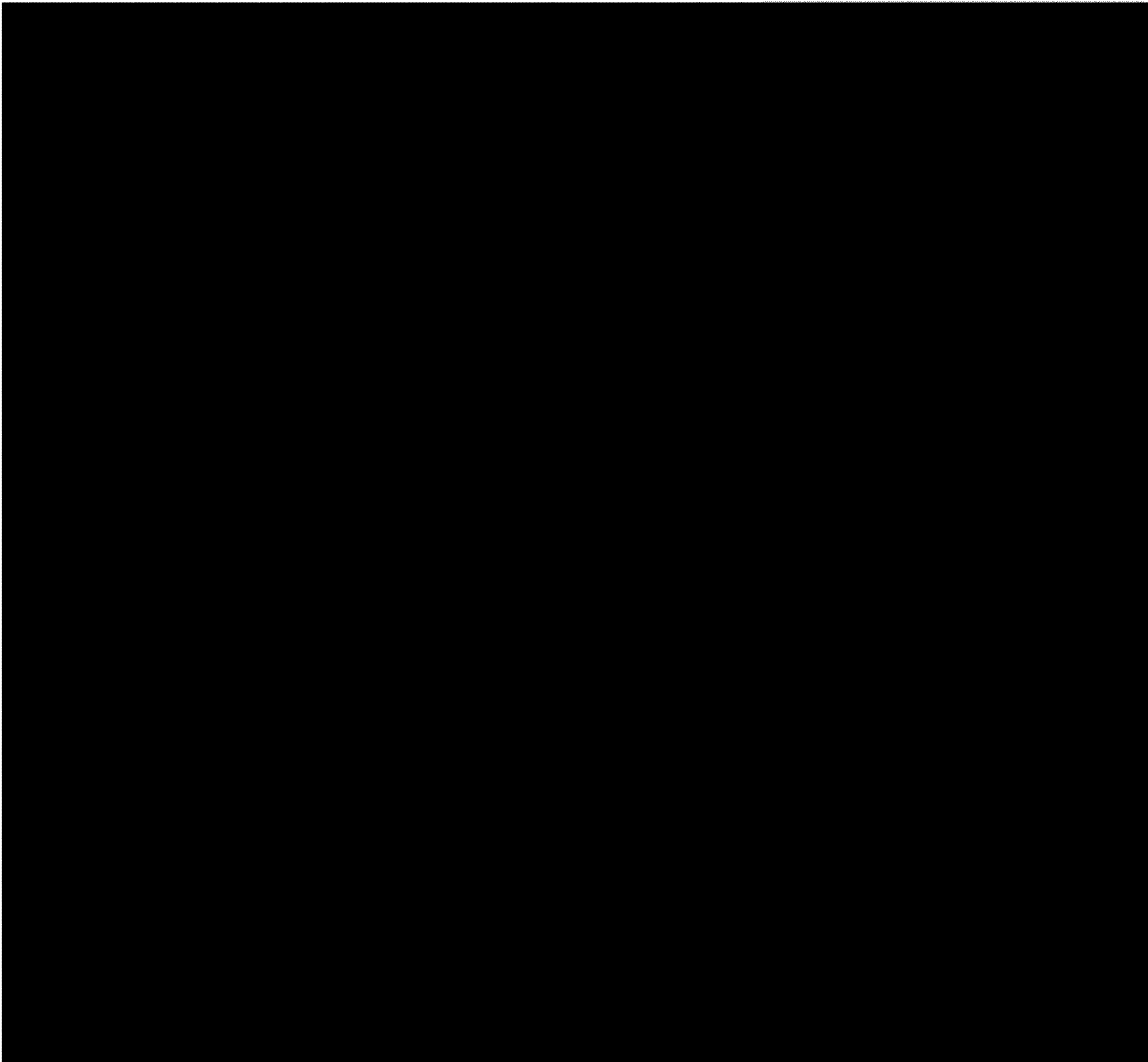
- "I signed up for a credit card with Jared. When I paid off the promotional, '1 year no interest' balance in just 3 months, I learned that a credit protection fee had been being assessed/added to my balance. After call[ing] to question it, the associate, Lila #3666, insisted that I hadn't questioned it early enough, so she would only remove 45 of the \$224 assessed. Only after speaking with a manager did they pull up my agreement, acknowledge that I had never agreed to purchase the insurance, and agree to reimburse me for the fees charged. Research needs to be done/legal action take[n a]gainst Jared for charging me and other consumers fees for services they did not agree to."¹⁵
- "[The store employee] tried to get me to enroll in their 'PPP' or personal payment protection plan (i.e. credit and life disability insurance) all at an obscene rate.... He told me to sign it and he would have it removed before the first statement, in order for him to receive credit for selling it.... I told him [I] would not sign it and if he wanted credit for it he would have to do that on his own. Much to my surprise 3 months into the account being opened I had already accrued an enormous amount of interest and fees, because my rate was at 21% and the PPP was on my account. I called [the store] and they told me that [I] signed for it. I spent the next 1 1/2 yrs trying to have them remove it.... I requested my signatures in July.... They finally removed the PPP and gave a \$100 towards the PPP fees.... By the time the signatures got here [I] realized that it was not my signature; I am disgusted with the process. I also do not know how to proceed. I feel I have an obvious forgery and most likely need to see a lawyer."
- "I recently purchased several items on my kay card and was told my signature for the insurance was simply to receive a packet to gauge my interest. This was a bold face[d] lie. I received a packet today indicating that I agreed to sign up for the insurance."
- "I purchased [an] engagement ring from Jared and the sales person signed me up for a payment protection plan without my knowledgc. This is the first time [I] noticed this fee, which is \$88.97 each month."¹⁶

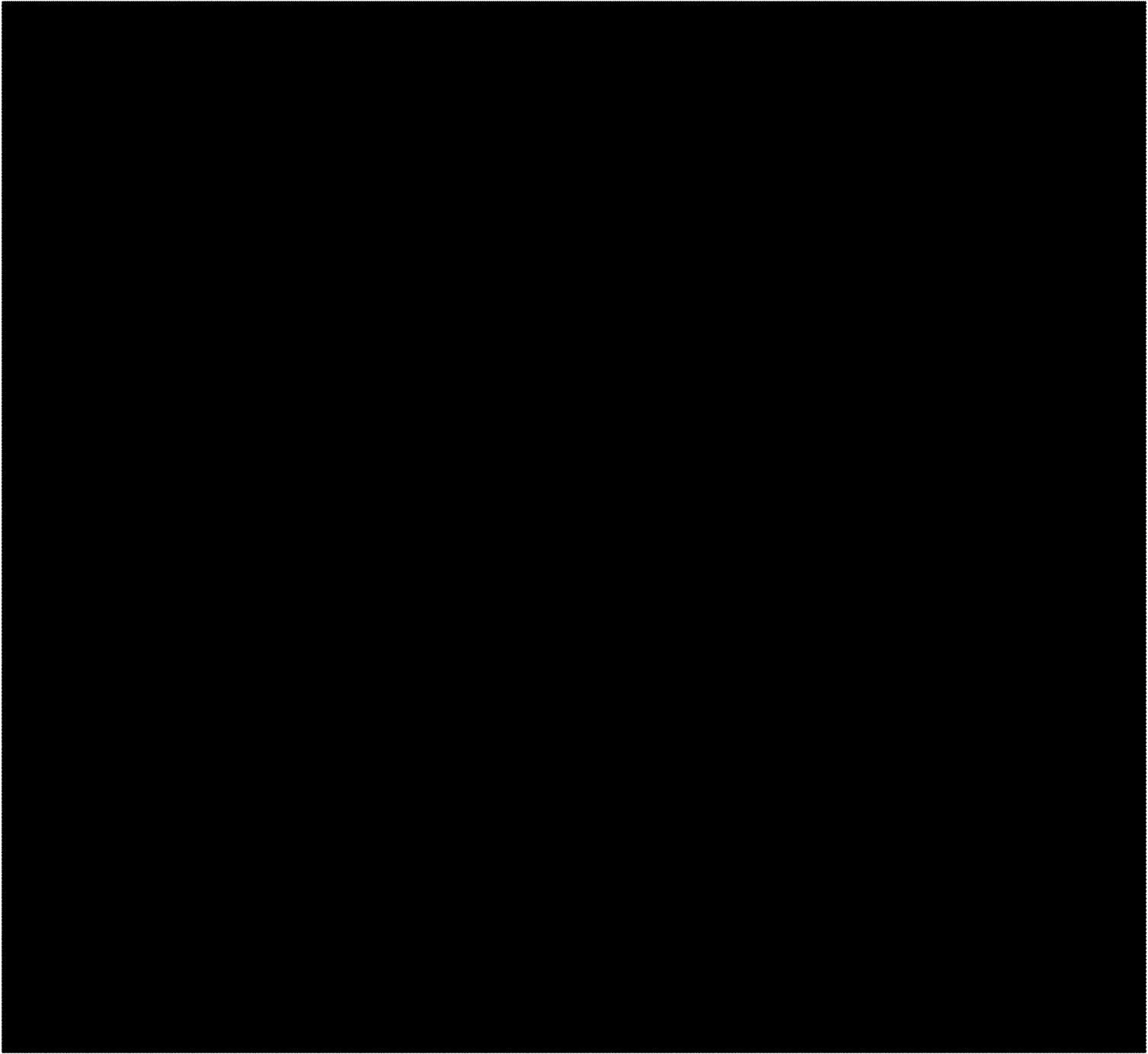
III. Legal Analysis

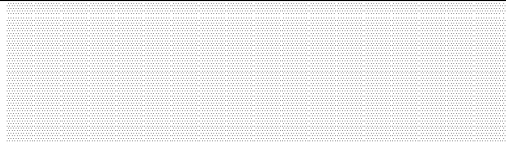
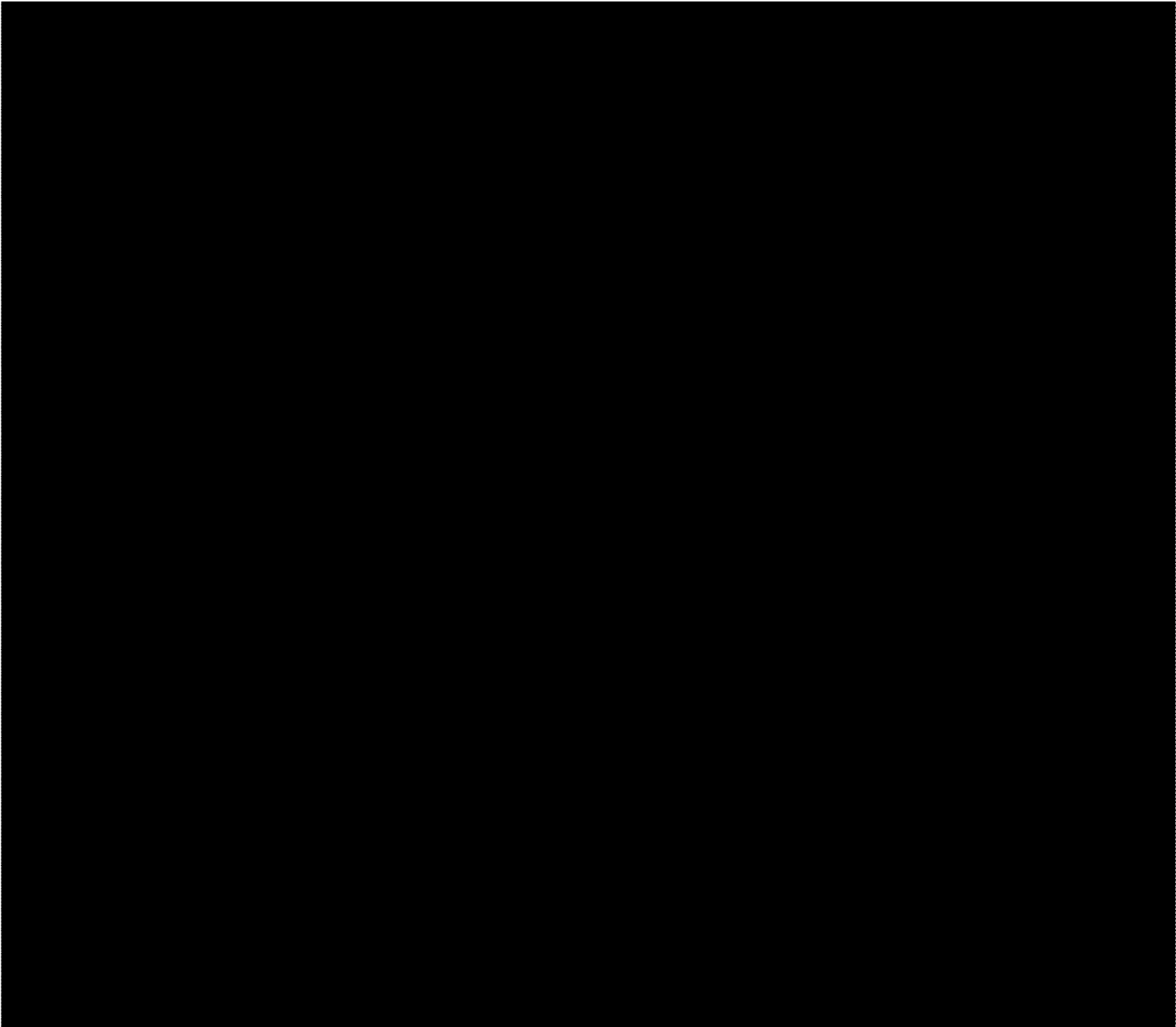
¹⁵ Sterling responded: "In your case, even though our system indicates that PPP had been accepted at the time of sale, we were unable to locate a signature confirmation of enrollment. In light of the missing signature, a supervisor authorized a return of \$224.20 that your account had been billed in total for PPP."

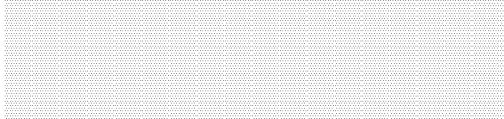
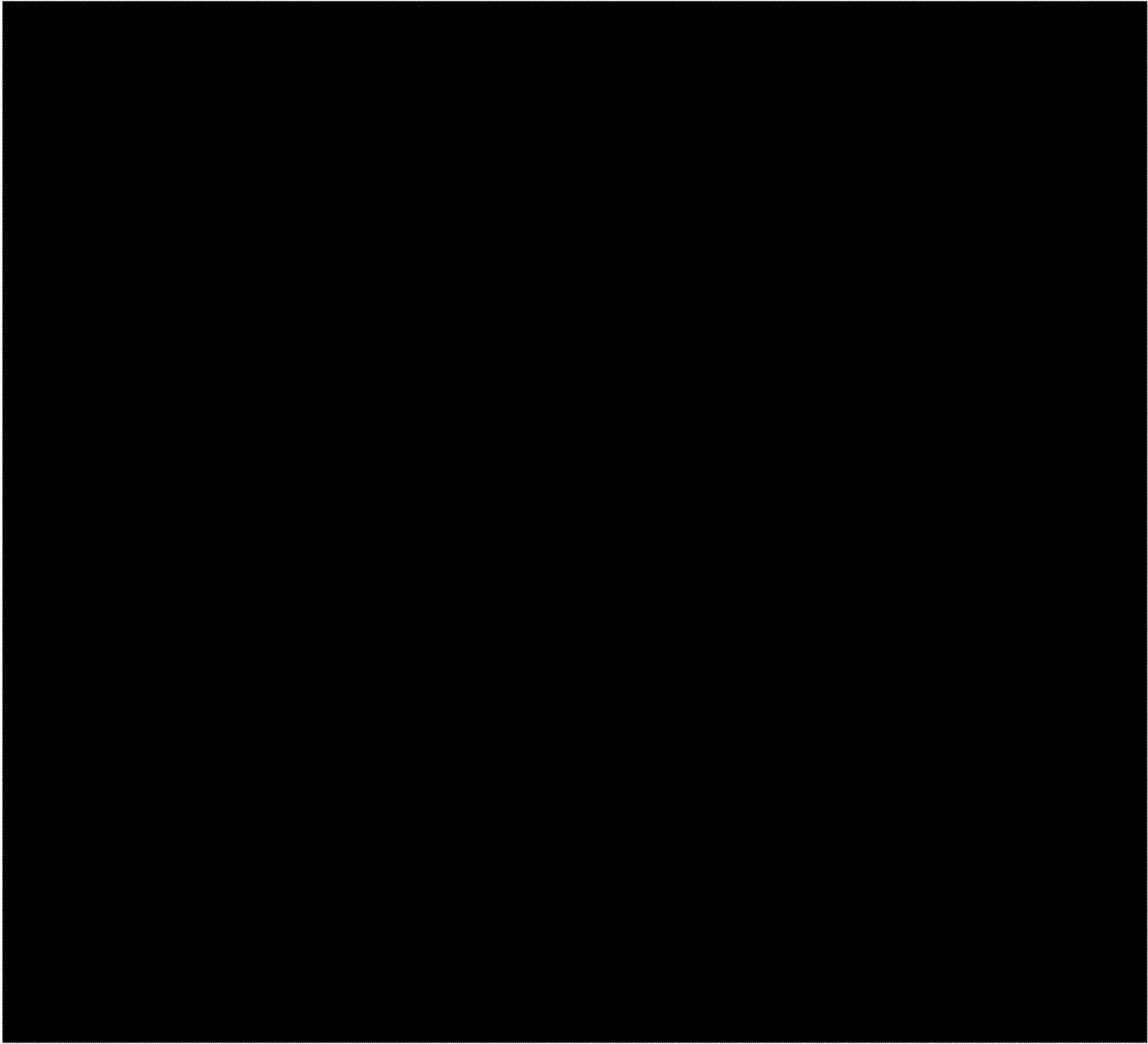
¹⁶ Sterling refunded \$626.88 in PPP fees in response to this complaint.

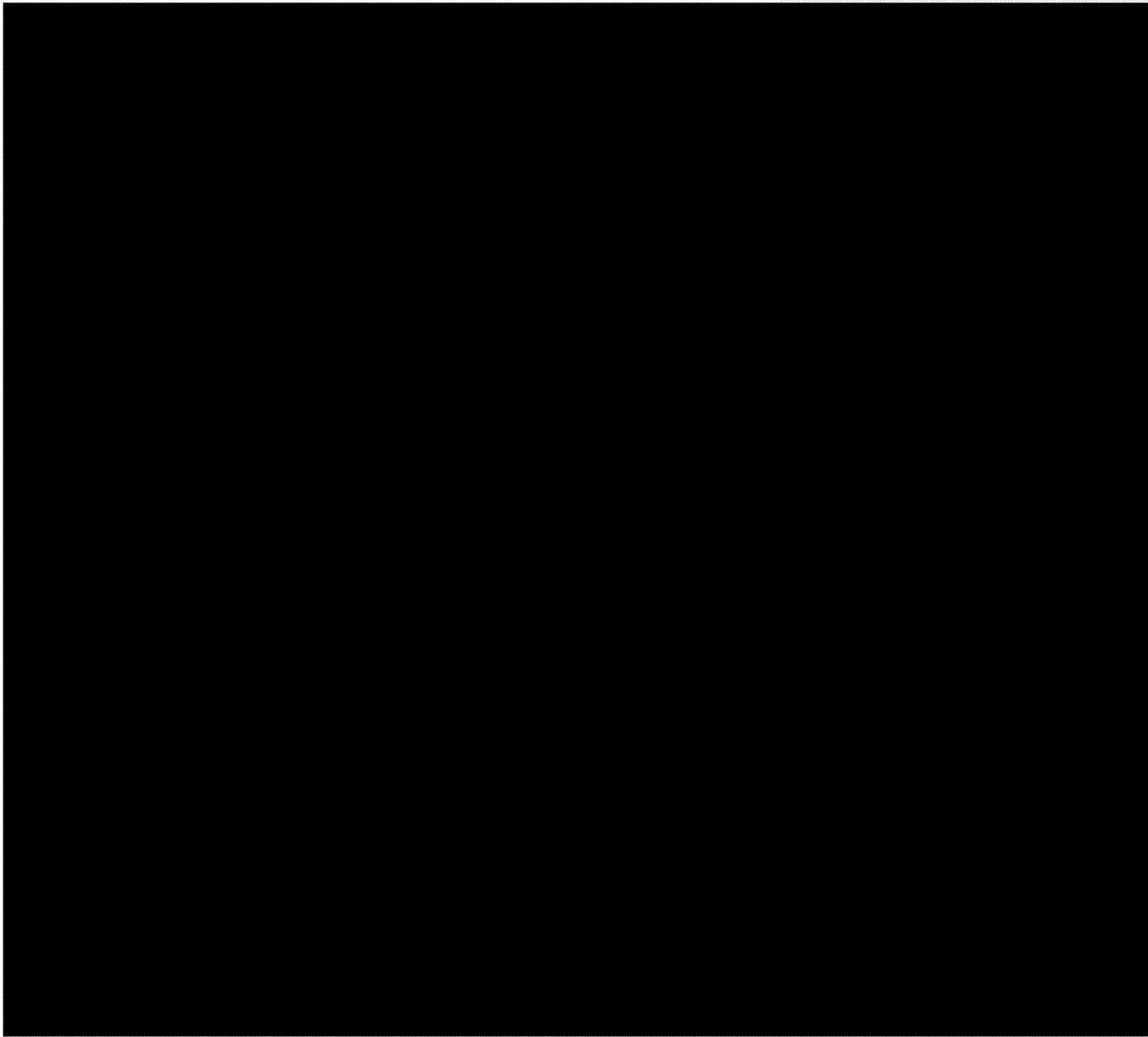


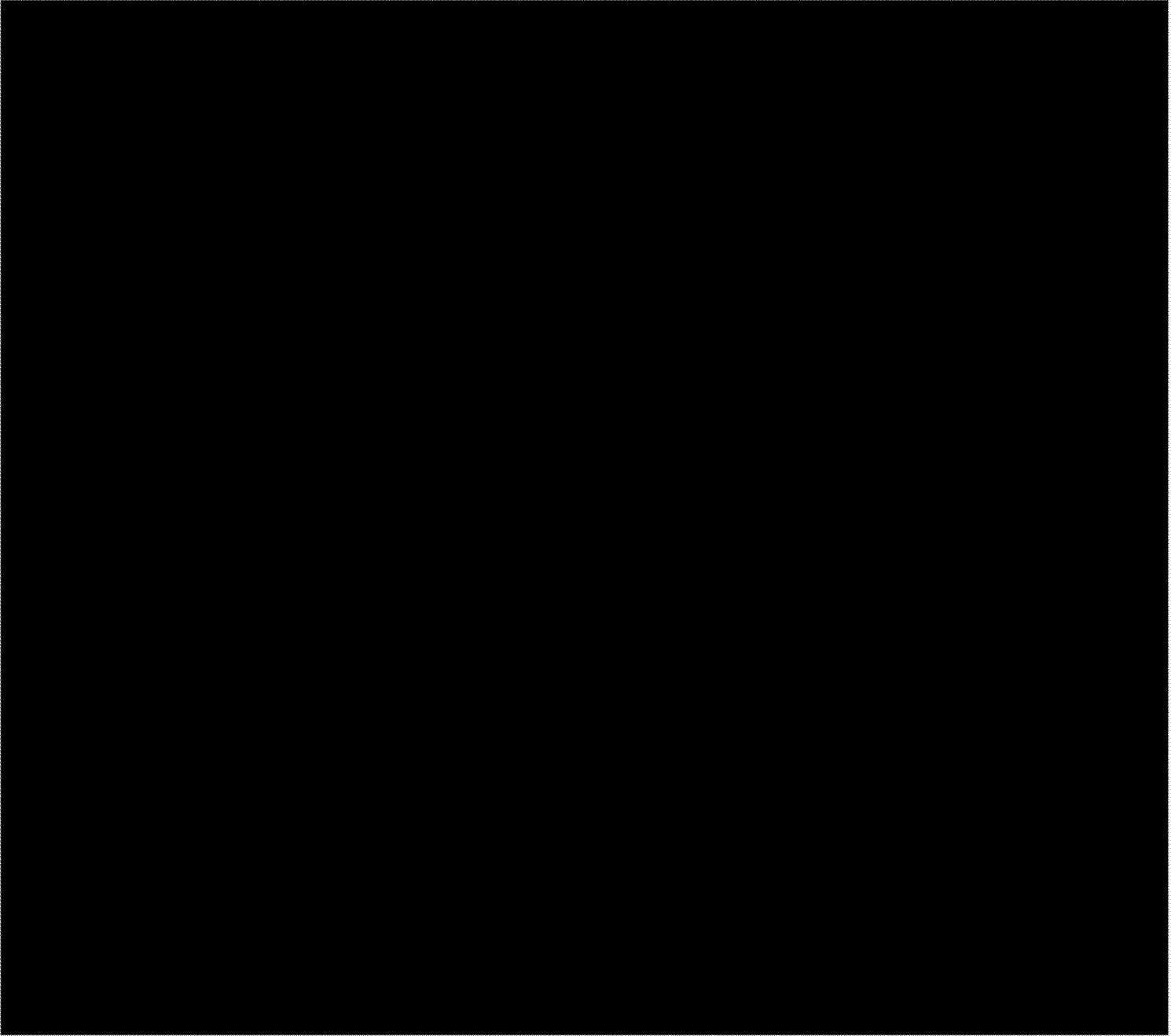




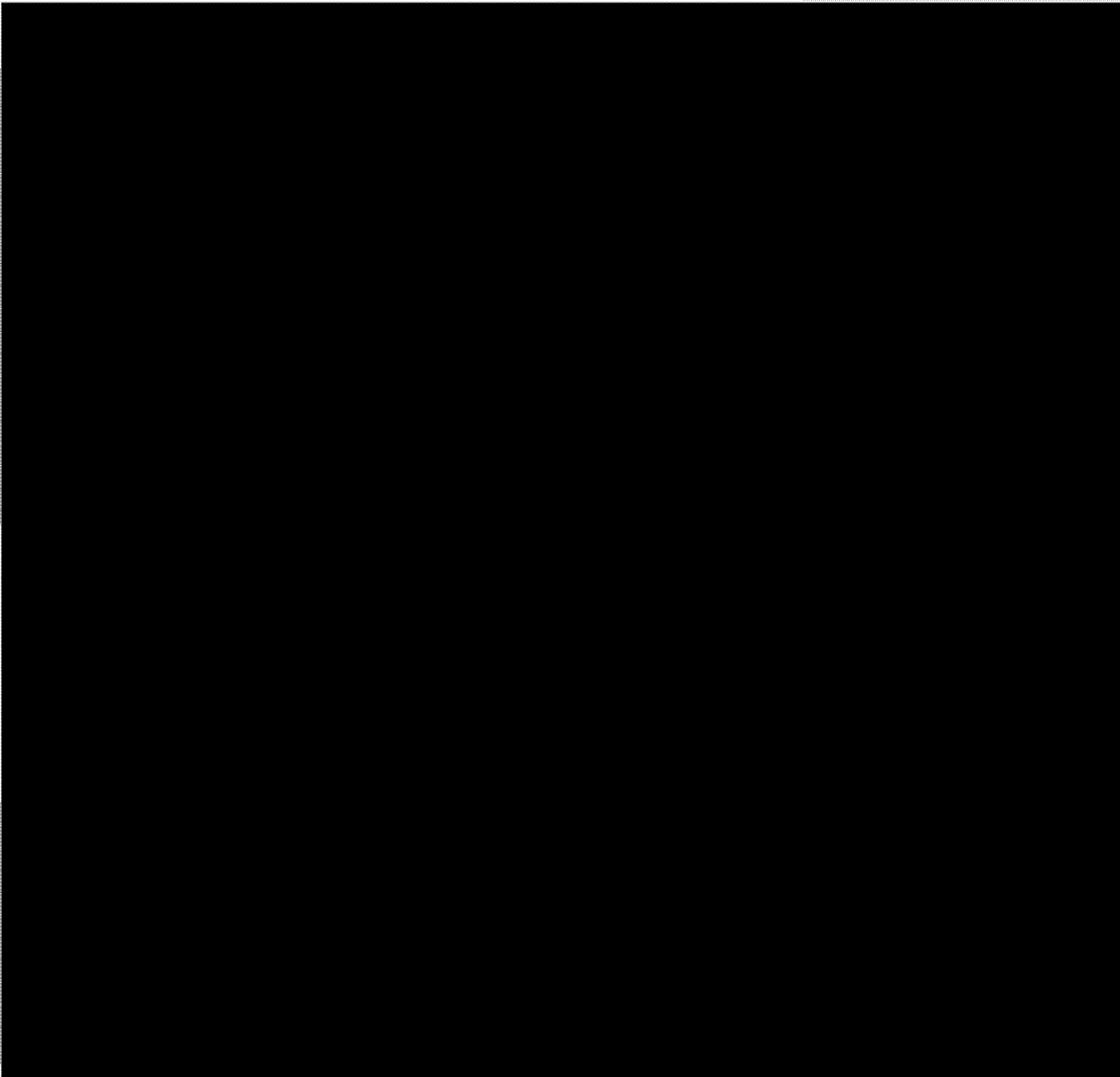














IV. Recommendation to Settle or Sue

To resolve this matter through settlement, the Bureau should seek redress, injunctive relief, and a penalty.

A. Redress to Consumers

The Bureau should not, as part of a negotiated resolution, seek redress for consumers who had unauthorized credit-card accounts opened. While those consumers may have suffered harm in the form of negative impacts on their credit report and related issues, that harm would be very difficult, if not impossible, to identify and quantify in any systematic way.

The Bureau also should not seek to obtain redress for consumers who were misled into thinking they would receive the benefit of promotional financing, but did not. These consumers, while they likely suffered identifiable harm, are not likely to be readily identifiable. There are no records of Sterling's employees' individual misrepresentations to consumers, and consumers affected in this way would appear in Sterling's records in the same way as consumers who were never offered promotional financing.

Each of the potential remedies for the PPP claim has drawbacks.

Normally, where an institution is accused of inducing consumers to enter into transactions through unfair or deceptive means, restitution is appropriate. But, merely identifying the proper restitution population may be impossible, given that there are likely no records of which consumers were subject to the specific practice of being misled about the PPP product or being enrolled without having provided affirmative consent. And, even though the Bureau need not prove causation in order to secure restitution, there also is the question of whether any specific customer would not have purchased insurance but for the unfair or deceptive conduct of a Sterling employee. As a result, blanket redress to all PPP consumers would potentially provide a windfall to those who were not proximately harmed by Sterling's practices.

Despite this, as part of a settlement, the Bureau could seek redress for consumers who were enrolled in payment-protection insurance at the point-of-sale—except for those consumers who received a benefit from the insurance coverage—from at least February 2013 through the date a consent order is entered. This would be similar to the redress ordered in the Bureau's other credit-card add-on matters, such as the Bureau's action against Capital One.²⁴ Given the low

²⁴ Capital One was ordered to pay \$140 million in redress to about two million consumers, which included complete repayment plus interest, and a \$25 million penalty.

Commented [BE(25)]: Given the identified causation issues below, and the fact that the improper practice is limited only to those instances where affirmative misrepresentations were made or where the consumer did not affirmatively select the PPP option, identifying the proper restitution population is probably impossible. As a result, we probably should not even be suggesting that restitution would be appropriate here.

Commented [R(26R25)]: We would like to seek authority to discuss negotiate redress as part of a settlement – but not require or file suit over it if such discussions fail. First, there may be a way the company can rebut the PPP population by identifying consumers who did/didn't affirmatively opt-in, or other options we could explore, such as a claims process, to identify affected consumers and ensure consumers do not receive a windfall. Second, NYAG is seeking redress for this claim so a global settlement may become more complicated if we cannot probe redress options, and could potentially leave the company open to further individual state AG actions.

utilization rates of the product,⁵⁵ this restitution likely would not provide a windfall to consumers, as many likely received no tangible benefit from the product. Additionally, the Bureau intends to pursue this case jointly with New York. New York likely would seek redress for New York consumers who enrolled in PPP, which will both make it appear odd that the Bureau did not also seek restitution, and potentially make settlement more difficult, as Sterling would not be guaranteeing finality, as other state AGs could bring suit seeking restitution under applicable state laws. The Office of Enforcement favors this approach.

Alternatively, disgorgement of the PPP proceeds may be more appropriate. Or the Bureau could not order any specific monetary relief for this violation, but rather take it into account when determining the penalty amount.

As part of a settlement, the Bureau should require redress for consumers who were enrolled in payment protection insurance at the point of sale—except for those consumers who received a benefit from the insurance coverage—from at least February 2013 through the date a consent order is entered. For these consumers, the Bureau should require Sterling to refund all fees charged in connection with consumers’ PPP. This is similar to the redress ordered in the Bureau’s other credit card add-on matters, such as the Bureau’s action against Capital One.⁵⁶ Sterling’s revenue from optional credit insurance was over \$50 million for each fiscal year from 2014 to 2017. Because the Bureau does not yet have the data to calculate the total proposed redress, Enforcement recommends requiring that Sterling, within 60 days of settlement, provide a redress plan for the Bureau’s approval that identifies all affected consumers and calculates redress according to approved measures. This is how the Bureau proceeded in the Wells Fargo Sales Practices matter. Alternatively, disgorgement of the PPP proceeds may be more appropriate.

~~Alternatively, disgorgement of the PPP proceeds may be more appropriate.~~ Even though the Bureau need not prove causation in order to secure restitution, there are two causation questions for each consumer: whether any specific customer would not have purchased insurance but for actions by a Sterling employee, and whether the Sterling employees actually did inform the customer of the insurance terms and conditions. Blanket redress to all PPP consumers would potentially provide a windfall to those who were not proximately harmed by Sterling’s practices.

The Bureau should not, as part of a negotiated resolution, seek redress for consumers who had unauthorized credit card accounts opened. While those consumers may have suffered harm in the form of negative impacts on their credit report and related issues, that harm would be very difficult, if not impossible, to identify and quantify in any systematic way.

The Bureau also should not seek to obtain redress for consumers who were misled into thinking they would receive the benefit of promotional financing, but did not. These consumers, while they likely suffered identifiable harm, are not likely to be readily identifiable. There are no records of Sterling’s employees’ individual misrepresentations to consumers, and consumers

⁵⁵ See n. 38, *supra*.

⁵⁶ Capital One was ordered to pay \$140 million in redress to about two million consumers, which included complete repayment plus interest, and a \$25 million penalty.

affected in this way would appear in Sterling's records in the same way as consumers who were never offered promotional financing.

B. Injunctive Relief

Any negotiated consent order should prohibit Sterling from engaging in the practices described herein.

C. Civil Money Penalty

The CFPA provides three tiers of statutory penalties. Effective January 15, 2018, those amounts are up to \$5,639 for ordinary violations, \$28,195 for reckless violations, and \$1,127,799 for knowing violations.⁵⁷ In this case, Sterling's violations were at least ordinary, if not reckless.

Sterling's culture and performance standards incentivize its employees to deceive consumers into completing credit-card applications and to open credit accounts on consumers' behalves without their knowledge or consent. In other instances, Sterling employees ~~mistakenly~~ misled consumers about the financing terms and tack on costly payment-protection insurance. Sterling has received thousands of complaints about these practices, which should at least have put it on notice that its employees are committing improper practices at the point-of-sale; but the company has not taken significant corrective actions and continues to maintain these performance standards.

Sterling potentially has committed thousands, and likely perhaps hundreds of thousands, of violations of the kinds described above. Even at the lowest penalty tier, these violations would justify a significant penalty, before consideration of mitigating factors. Among the mitigating factors the Bureau must consider are the gravity of the violations, the severity of the risks to or losses of the consumers, the financial resources of the person charged, and "such other matters as justice may require."⁵⁸ For consumers who were enrolled in credit-card accounts without their knowledge or consent, there is potentially adverse impact to their credit; however, it is difficult to quantify this harm, and harm may not occur in every instance. In fact, there may be cases in which a consumer's creditworthiness is positively affected by the account. For consumers who were misled about financing terms, the harm is also hard to quantify but because the conduct at issue resulted in a higher cost of credit than consumers were anticipating, it likely left certain consumers unable to make monthly payments, and may have subjected them to late fees, charge-offs, and ultimately debt collection, with additional consequences for their credit histories. As to violations regarding PPP, the harm to consumers who unknowingly or unwillingly were signed up for insurance is likely to roughly equal the amount of their payments for the service. This practice likely negatively impacted hundreds of thousands of consumers.

The Bureau must also consider, as a mitigating factor, Sterling's financial resources and the financial impact on Sterling of a penalty levied here. Signet, Sterling's parent company, reported \$6.4 billion in total revenue in Fiscal Year 2017. Sterling accounted for about \$3.9 billion of this

⁵⁷ 12 U.S.C. § 5565(c)(2); 12 C.F.R. § 1083.1.

⁵⁸ 12 U.S.C. § 5565(c)(3). Another mitigating factor is the history of previous violations. Here, we are not aware that Sterling has been subject to any prior credit-related actions.

total, with more than 60% attributable to credit sales. Over the past four fiscal years, Sterling's annual revenue from credit products averaged more than \$300 million, and its annual revenue from optional credit insurance products averaged \$60 million, so the company has reaped significant financial gain from its credit-related business. Signet's dividends paid to common shareholders and repurchase of common shares also support the fact that Sterling's parent company is well-capitalized. In Fiscal Year 2017, Signet issued roughly \$75.6 million in dividends paid to common shareholders and repurchased roughly \$1 billion worth of common shares. Over the past three fiscal years, Signet's dividends paid to common shareholders and repurchase of common shares totaled about \$1.35 billion. As Signet's largest operational segment and highest revenue-earning company, Sterling has sufficient financial resources to pay a penalty.

As described, Sterling's violations could potentially justify a significant penalty based on the statutory factors. For the reasons described above, some mitigation is appropriate. But even with such mitigation, the potential penalties could total more than what the company would be willing to pay to settle the Bureau's claims. The CFPB allows the Bureau to compromise or modify a penalty before it is assessed,⁵⁹ and the Bureau should do so here to help resolve this case.

The most recent, comparable Bureau matter to draw from in determining an appropriate penalty amount is the action taken against Wells Fargo for its sales practices in 2016. In the Wells Fargo Sales Practices matter consumers were similarly subjected to unauthorized credit-card accounts and Wells Fargo paid a penalty of \$100 million. At the time that penalty was determined, the bank disclosed approximately 2,065,000 fake accounts. Dividing the total penalty of \$100 million by the 2.1 million fake accounts results in a \$48.43 penalty per account rate, or roughly 2.1 to 2.2%. ~~The Office of Enforcement, applying a discount to~~ Adjusting Sterling's total number of accounts without purchases, estimates about 800,000 potentially unauthorized credit-card accounts.⁶⁰ Using the per-account penalty rates derived from the Wells Fargo matter yields a penalty range of approximately of \$22.9 million to \$38.7 million. ~~Obviously~~ But this precedent is not perfect because Sterling and Wells Fargo are different kinds of entities, engaged in different kinds of behavior, and the claims against each are different.

In Bureau credit-card add-on matters, which did not involve unauthorized accounts or misleading financing terms, the penalties range widely because they are tailored to the specific circumstances of each case and the assessment of mitigating factors. For example, in 2012 the Bureau imposed a \$25 million penalty on Capital One; in 2015 the Bureau ordered Citibank to pay a \$35 million penalty; in 2016 First National Bank of Omaha was ordered to pay \$4.5 million. In each of these matters the entity was found to have deceptively or unfairly charged consumers for credit-card add-on products.

⁵⁹ 12 U.S.C. § 5565(c)(4).

⁶⁰ Signet produced data showing that roughly 300,000 accounts without purchases were opened each year, totaling about one million such accounts from February 2014 through March 2017. Taking into account the explanation that some consumers were "shopping around" and intended to open a credit card without making any purchase, a 20% discount was applied to the total number of accounts, yielding an estimated 800,000 potentially unauthorized accounts.

Here, based on the unauthorized accounts, deceptive financing, and unfair PPP claims, and taking into account the precedent discussed above, the Bureau should seek to settle this matter for a penalty of at least \$10 million. A penalty in this amount would sufficiently deter similar violations and would impress upon the company the seriousness of the conduct at issue.

V. Assessment of Risks of the Recommended Approach

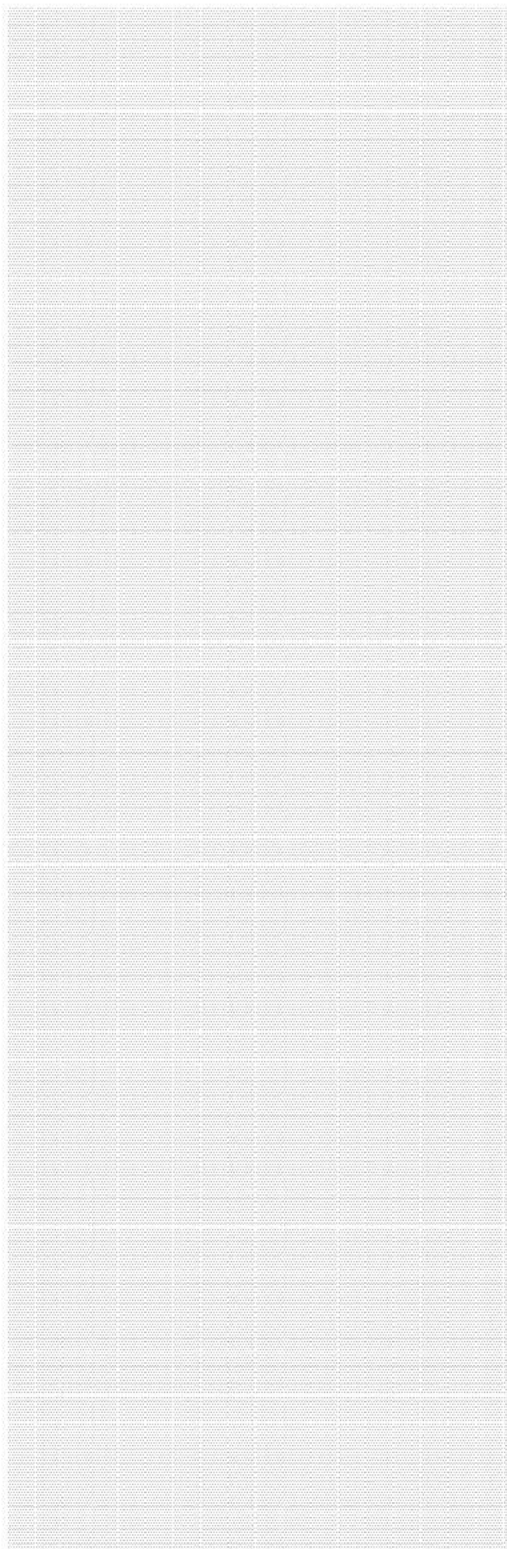
[REDACTED]

VI. Conclusion

The Bureau should settle this matter under the parameters described in Section IV. Further, if settlement negotiations are unsuccessful, the Bureau should file suit against Sterling.

Attachments

- Tab 1: Draft Decision Memorandum from the Acting Director.
- Tab 2: Draft Complaint.
- Tab 3: Signet's NORA Transmittal Letter.
- Tab 4: Signet's NORA Response.
- Tab 5: Exhibit A to Signet's NORA Response.
- Tab 6: Signet's Certificate of Factual Assertions in NORA Response.



APPENDIX T

1700 G Street NW,
Washington, DC 20552



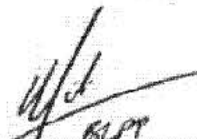
Decision Memorandum from the Acting Director

FROM	Mick Mulvaney
TO	Eric Blankenstein, SEFL Policy Director; Chris D'Angelo, SEFL Associate Director; Kristen Donoghue, Assistant Director for Enforcement
SUBJECT	Authorization to Enter into Settlement with Sterling Jewelers, Inc. or to File Suit – ENF Matter No. 2016-1806-02

I authorize the Office of Enforcement to enter into a settlement with or file a lawsuit against Sterling Jewelers, Inc. under the parameters recommended by the Office of Enforcement on October 29, 2018.

The Office of Enforcement's October 29, 2018 recommendation memorandum identifies three potential options for the remedy for the PPP claim in a settlement (in addition to injunctive relief and a civil money penalty). Of those three options, I authorize the following:

~~Restitution~~
~~Disgorgement~~
Take absence of other monetary relief into account when negotiating penalty amount



Mick Mulvaney
Acting Director
Bureau of Consumer Financial Protection

11-1-18

Date