



COMPLIANCE UNIVERSITY

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**What Do Service Providers Expect From Lenders and
What Do Lenders Expect From Service Providers?**

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Jonathan Pompan is co-chair of Venable’s CFPB Task Force and leads Venable’s debt and credit services team. Jonathan has extensive experience representing debt and credit services related companies, including some of the largest debt buyers and collectors and advertisers of financial services in the country, other consumer financial services providers, and their service providers. This work gives him considerable insight into successful strategies for satisfying new and evolving regulatory expectations.

Jonathan has assisted clients in bet-the-company government investigations and litigation pursued by federal agencies such as the CFPB and the FTC, as well as in-state enforcement proceedings involving state attorneys general. His experience includes several CFPB investigations and examination preparation and appeals. In addition, he provides ongoing compliance and general counseling advice to several clients in the debt collection and credit services, lenders, and advertising and marketing sectors.

Jonathan is a frequent speaker, organizer, and moderator of conference panels, and author on legal and regulatory issues of significance to debt buyers and collectors. Jonathan recently presented on the “CFPB Turns Five” at the ACA International Convention on June 17, 2016, and will be moderating “Lead Gen Legal Responsibility and Accountability: A Sit Down” at the 2016 LeadsCon New York on August 23, 2016.

IMPORTANT INFORMATION ABOUT THIS PRESENTATION

This presentation is for general informational purposes only and does not represent and is not intended to provide legal advice or opinion and should not be relied on as such. Legal advice can only be provided in response to specific fact situations.

This presentation does not represent any undertaking to keep recipients advised as to all or any relevant legal developments.

Covered Person and Service Provider Liability

- Title X of the Dodd-Frank Wall Street Reform Act gives the CFPB authority to regulate any “Consumer Financial Product or Service” offered by any “covered person.”
 - “**Consumer Financial Product or Service**” is defined as those that are offered or provided for use by consumers primarily for personal, family, or household purposes, or that which is offered or provided in connection with such products. 12 U.S.C § 5481(5).
 - A “**covered person**” is **any person** engaged in offering or providing a consumer financial product or service, **any affiliate** if such affiliate acts as a **service provider**, and any **related person**.
 - A “**service provider**” is defined to include “any person that provides a **material** service to a **covered person** in connection with the offering or provision by such covered person of a consumer financial product or service.” 12 U.S.C § 5481(26).
 - This includes providers that design, operate or maintain the product or service, or that process transactions. It does not include ministerial or non-material support services offered to businesses generally and those who provide advertising space.
 - A service provider shall be deemed a covered person to the extent it engages in the offering or provision of its own consumer financial product or service.
 - Key Question: How broad should “service provider” be interpreted? Legislative history suggests not as broad as CFPB may want.
 - A “**related person**” is
 - any director, officer, or employee charged with managerial responsibility for, or controlling shareholder of, or agent for, such covered person;
 - any shareholder, consultant, joint venture partner, or other person, as determined by the Bureau (by rule or on a case-by-case basis) who materially participates in the conduct of the affairs of such covered person; and
 - any independent contractor (including any attorney, appraiser, or accountant) who knowingly or recklessly participates in any—
 - violation of any provision of law or regulation; or
 - breach of a fiduciary duty.

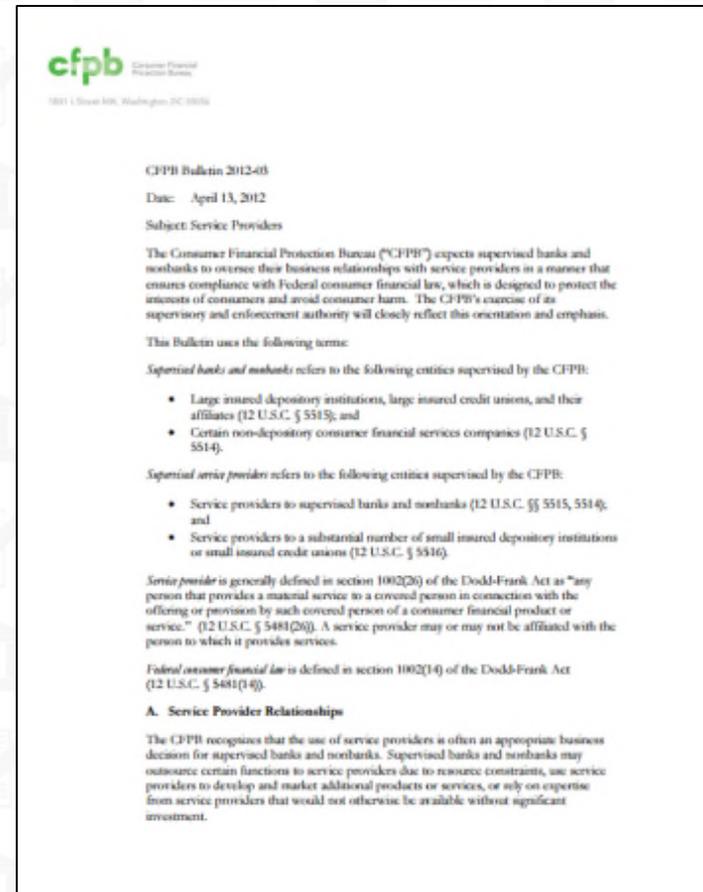
Substantial Assistance

- Telemarketing Sales Rule (FTC & CFPB)
- Consumer Financial Protection Act (CFPB)
 - It prohibited for **any person, even if not a covered person or service provider, to knowingly or recklessly provide substantial assistance to a covered person or service provider** in violating section 1031 of the Dodd-Frank Act. See Dodd-Frank Act, § 1036(a)(3), 12 U.S.C. § 5536(a)(3).
 - Analogous to “aiding and abetting” prohibitions
 - Limited to “knowingly or recklessly” and “substantial” + recipient of the assistance itself must be liable for a UDAAP
 - Broadly applies to “any person” and liability equivalent to recipient of the assistance.
 - Allows CFPB to impose individual liability against owners and managers of closely held companies; and counterparties of entities alleged to have committed UDAAP violations.

CFPB Bulletin 2012-03: Service Providers

“Consumers are at a real disadvantage because they do not get to choose the service providers they deal with—the financial institution does, Consumers must not be hurt by unfair, deceptive, or abusive practices of service providers. Banks and nonbanks must manage these relationships carefully and can be held accountable if they break the law.”

- Richard Cordray, April 13, 2012



What are the CFPB's Expectations on Service Provider Relationships

The CFPB recommends that supervised financial institutions take steps to ensure that business arrangements with service providers do not present unwarranted risks to consumers. These steps include:

- Conducting thorough **due diligence** to verify that the service provider understands and is capable of complying with the law;
- Requesting and **reviewing the service provider's policies, procedures, internal controls, and training materials** to ensure that the service provider conducts appropriate training and oversight of employees or agents that have consumer contact or compliance responsibilities;
- Including in the **contract** with the service provider clear expectations about compliance, as well as **appropriate and enforceable consequences** for violating any compliance-related responsibilities;
- Establishing **internal controls and on-going monitoring** to determine whether the service provider is complying with the law; and
- Taking prompt action to **address fully any problems identified** through the monitoring process.

Service Provider Enforcement Examples:

- In re U.S. Bank, N.A.:
 - The CFPB ordered U.S. Bank to provide an estimated \$48 million in relief to consumers harmed by illegal billing practices based on 3rd party vendor.
 - The CFPB found that U.S. Bank customers were unfairly charged for certain identity protection and credit monitoring services that they did not receive.
 - \$48 million refund to 420,000 consumers, \$5 million civil penalty.

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UNITED STATES OF AMERICA
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING
File No. 2014-CFPB-0013

In the Matter of: CONSENT ORDER
U.S. Bank National Association

The Consumer Financial Protection Bureau (Bureau) has reviewed the practices of Respondent Bank, U.S. Bank National Association (Respondent or Bank, as defined below), relating to add-on products and has identified violations of law. Under sections 1053 and 1055 of the Consumer Financial Protection Act of 2010 (CFPA), 12 U.S.C. §§ 5563 and 5565, the Bureau issues this Consent Order (Consent Order).

**I
Overview**

The Bureau finds that the Bank has engaged in violations of Sections 1031 and 1036 of the CFPA, 12 U.S.C. §§ 5531, 5536, in connection with its third-party service provider's billing and administration of Identity Protection Products to Customers (as defined below), which occurred during the period between 2003 and August 2012.

**II
Jurisdiction**

1. The Bureau has jurisdiction over this matter under Sections 1053 and 1055 of the CFPA, 12 U.S.C. §§ 5563, 5565.

Service Provider Enforcement

Examples: (cont'd)

- CFPB ordered Citibank, N.A. and its subsidiaries to provide an estimated \$700 million in relief to eligible consumers harmed by illegal practices related to credit card add-on products and services.
- Roughly 7 million consumer accounts were affected by Citibank's deceptive marketing, billing, and administration of debt protection and credit monitoring add-on products.
- A Citibank subsidiary also deceptively charged expedited payment fees to nearly 1.8 million consumer accounts during collection calls. Citibank and its subsidiaries will pay \$35 million in civil money penalties to the CFPB.

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UNITED STATES OF AMERICA
CONSUMER FINANCIAL PROTECTION BUREAU

ADMINISTRATIVE PROCEEDING
File No. 2016-CFPB-0004

In the Matter of: **CONSENT ORDER**

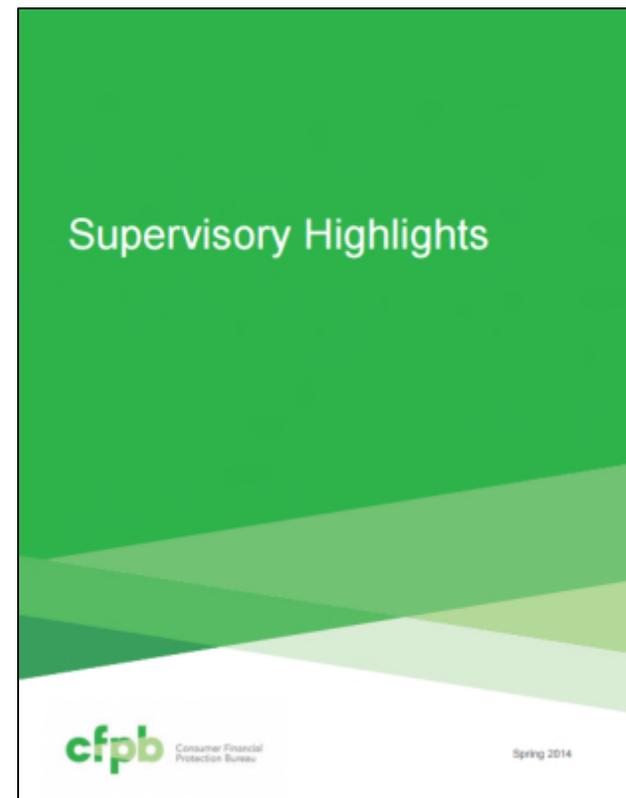
CITIBANK, N.A., DEPARTMENT STORES NATIONAL BANK, and CITIFINANCIAL SERVICING, LLC

The Consumer Financial Protection Bureau (Bureau) has reviewed the debt collection practices of Citibank, N.A. (Bank), Department Stores National Bank (DSNB), and CitiFinancial Servicing, LLC (CitiFinancial Servicing) (collectively, Respondent) and has identified the following law violations: Respondent, through its attorneys, filed Declarations in Collections Litigation in the New Jersey courts. Respondent's attorneys altered certain Declarations after they had been executed by altering either the date of execution, the balance allegedly owed on the Debt, or both. The altered Declarations constituted false representations concerning, among other things, the amount of the Debt allegedly owed and the legal status of the Debt. These false representations constitute deceptive acts or practices in connection with collecting Debt related to a consumer financial product or service in violation of the Consumer Financial Protection Act of 2010 (CFPA), 12 U.S.C. §§ 5531 and 5536. Under sections 1053 and 1055 of the CFPA, 12 U.S.C. §§ 5563, 5565, the Bureau issues this Consent Order (Consent Order).

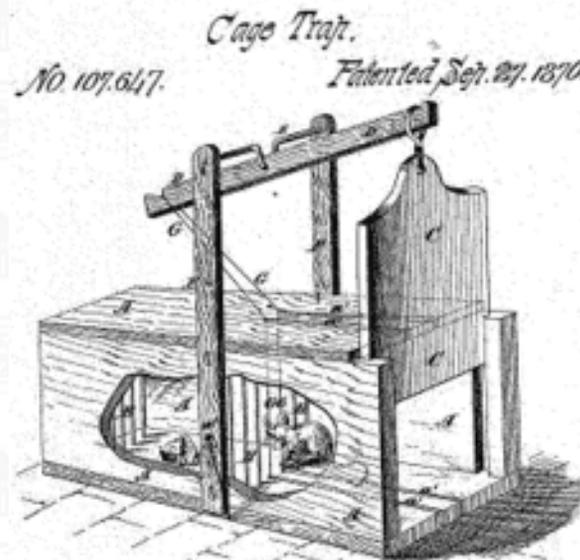
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Supervisory Examination Example

Finally, CFPB recognizes the importance of third-party service providers to the operations of many supervised entities. However, as the CFPB explained in Bulletin 2012-03, it expects entities to select these service providers carefully, include compliance expectations in contracts, and monitor service providers' work and complaints about their work. If a third-party service provider fails to perform properly, a supervised entity is expected to require remediation and to take measures that may include, in appropriate circumstances, termination of the service provider's contract. The fact that a supervised entity enters into a business relationship with a service provider does not absolve the supervised entity of responsibility for complying with Federal consumer financial law and, depending on the circumstances, it may be held legally responsible for violations by the third party.



What does this mean for a compliance management system? A better mousetrap?



Vendor Management

Examiners should evaluate copies of any agreements between lenders and service providers acting on behalf of the lender for purposes of assessing risks to consumers.

1. Evaluate whether the lender has compliance management controls for selecting and monitoring affiliates and/or service providers.
2. Evaluate whether the lender takes steps to ensure that the service providers it uses are licensed or registered to the extent required.
3. Evaluate whether the lender performs initial due diligence concerning the service providers' prior regulatory compliance history before entering into an agreement (i.e., determining the existence and extent of any prior enforcement actions against the service providers).
4. Evaluate whether the lender monitors the screening, hiring, and training practices of service providers employees who perform services on the lender's behalf.
5. Evaluate whether the lender takes steps to ensure service providers compliance with the lender's privacy policy with respect to data that the service providers receives from or on behalf of the lender.
6. Evaluate whether the lender reviews the internal or external audit reports covering service providers' activities and whether the lender responds appropriately to identified concerns.

A Framework for Analysis of Service Provider Relationships

Legal Landscape

- Vendor management expectations sidestep formal rulemaking.
- Sources of scrutiny: (1) investigations; (2) examination; (3) vendor due diligence.
- Potential sources of liability for both:
 - Lenders, and
 - Vendors
- Substantial Assistance/Related Person; is there a distinction?
- Reputational Harm

Expectations

- Conduct due diligence.
- Request and review policies, procedures, internal controls, and training materials.
- Contracts with clear expectations and appropriate and enforceable consequences
- Establish internal controls and ongoing monitoring
- Take prompt action.

Considerations

- Sources of UDAAPs
 - State Law / Usury / Exemption?
 - CFPB enforcement actions have focused on legality of loan based on state where consumer resides
- Advertising and Marketing, including lead generation
- Application and Origination
- Servicing
- Fair Lending
- Payment Processing
- Debt Collection/Debt Sales
- Consumer Reporting
- Data Sharing

CFPB UDAP and Other Standards

An act or practice is **unfair** when:

- (1) it causes or is likely to cause substantial injury to consumers;
- (2) the injury is not reasonably avoidable by consumers; and
- (3) the injury is not outweighed by countervailing benefits to consumers or to competition.

A representation, omission, act, or practice is **deceptive** when:

- (1) the representation, omission, act, or practice misleads or is likely to mislead the consumer;
- (2) the consumer's interpretation of the representation, omission, act, or practice is reasonable under the circumstances; and the misleading representation, omission, act, or practice is material.

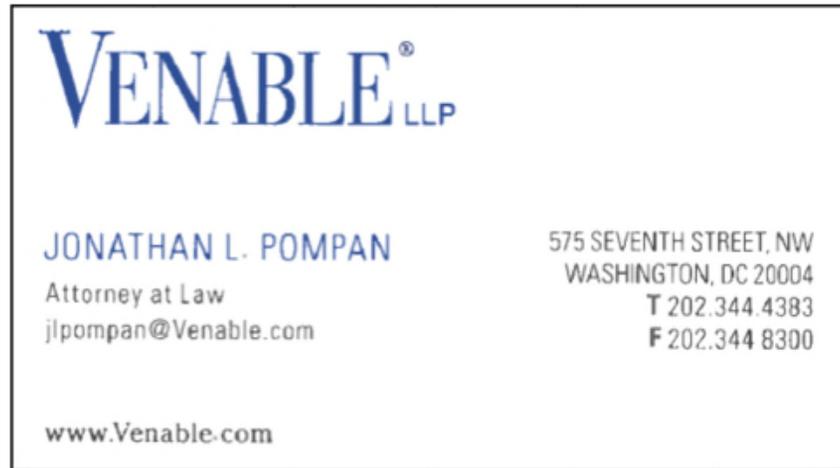
An **abusive** act or practice:

- (1) materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
- (2) takes unreasonable advantage of
 - a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
 - the inability of the consumer to protect its interests in selecting or using a consumer financial product or service; or
 - the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.

Other Standards:

- Truth-in-Lending Act/ Regulation Z
- Equal Credit Opportunity Act / Regulation B
- Fair Credit Reporting Act
- Fair Debt Collection Practices Act and Related Requirements
- Electronic Fund Transfer Act/ Regulation E
- Telemarketing Sales Rule
- Gramm-Leach-Bliley Act

More Information and Questions



For related articles and presentations, see www.venable.com/cfpb/publications.