The Consumer Finance Podcast: CFPB's War on Junk Fees
Host: Chris Willis
Guest: Jason Cover

Chris Willis:

Welcome to The Consumer Finance Podcast. I'm Chris Willis, the co-leader of Troutman Pepper's Consumer Financial Services regulatory practice. And I'm glad you're joining us for today's episode where we're going to talk all about the CFPB's war on junk fees.

But before we jump into that very interesting topic, let me remind you to visit and subscribe to our blog, consumerfinancialserviceslawmonitor.com, where you'll see all the updates going on every day about what's going on in the consumer finance industry. And don't forget to check out our other podcasts. We have the *FCRA Focus*, all about credit reporting, *The Crypto Exchange*, about all things crypto, and *Unauthorized Access*, which is our privacy and data security podcast. All of those are available on all the popular podcast platforms just like this one. And speaking of this podcast, if you like it, leave us a review on your podcast platform of choice and let us know how we're doing.

Now, as I said, today we're going to be talking about the CFPB'S self-declared war on what it calls junk fees across the financial services industry. And I'm joined today by my partner Jason Cover. Jason is one of our premier regulatory lawyers in our consumer financial services group, and he's very conversant with this issue and counsels clients on it all the time. So, Jason, welcome to the podcast. Thanks for being here.

Jason Cover:

Thanks, Chris. Great to be here.

Chris Willis:

So, the thing that really prompted us to do this episode of The Consumer Finance Podcast about junk fees is that the CFPB issued a "special edition" Supervisory Highlights focused on junk fees, and I guess predictably, finding that junk fees are literally everywhere in the consumer financial services economy. Can you just talk to the audience about this special edition, what it says and how it fits into the broader initiative on junk fees that the director announced, I feel like, at the beginning of 2022?

Jason Cover:

Yeah, that's right, Chris. I think the first announcement was an announcement of the initiative in January, 2022, and that the CFPB's stated goal is to save billions of dollars per year by reducing junk fees. And the supervisory highlights are the most recent in a flurry of activity from the CFPB. In the last year, we've seen materials on NSF fees and late fees, advisory opinions on pay-to-pay fees in the context of debt collection, the recent rulemaking initiated about reducing or eliminating the safe harbor for credit card late fees. So this is all kind of part and parcel to the same thing. And interestingly enough, this seems to even be a part of a broader political policy initiative. If anyone watched the State of the Union address, President Biden announced at least proposed legislative activity to reduce so-called junk fees of all nature.

So, I think it's all part and parcel to the same genre, the so-called war on junk fees. But as we'll talk about a little bit, I think some of this is also common sense and isn't new. I mean, the CFPB has been talking about a lot of these things since its inception, and overdraft fees has always been a hot topic for them. Payment fees always have been a hot topic for them, really since inception, for both those topics. So I don't think this is all out of the blue. Some of the emphasis and repeated guidance that's coming out is, but the principles I think are the same.

Chris Willis:

Well, what does seem out of the blue to me, Jason, is this political angle that you mentioned because it seems to me that both the director of the CFPB and some folks within the White House have decided that this fee issue has some political legs to it, and that's why you're seeing so much public emphasis on it, even as you noted in the State of the Union address. When was the last time we had a consumer finance issue in the State of the Union address? It's amazing. But we know the war is on junk fees and the CFPB and the Federal Trade Commission, and now the state AGs are all using that term "junk fees" all the time, which is very pejorative, but not very descriptive and not very helpful to financial institutions when it comes to giving them compliance advice. So what exactly is a junk fee, as we understand the CFPB'S understanding of it?

Jason Cover:

So interestingly enough, the supervisory highlights give us a definition. The CFPB defined junk fees as an unnecessary charge that inflates costs while adding little to no value to the consumer. And then it's usually unavoidable or surprise and it's often hidden or disclosed only at a later stage in the consumer's purchasing process or sometimes not at all.

And I think that is kind of a good starting point. I'd add that in my view, the CFPB is likely looking to see whether it's profit motivated. So if the fee is to cover a service, that's one thing. If it's the service plus additional amounts to make profit on, that's another. I think it's often unrelated to the core function of the product. So, on a loan product for instance, it's not related to the extension of credit, it's not interest, it's not those types of things that we typically associate with the core product. It's something extra like a payment fee or an expedited payment fee, things of that nature. And then it's often not commensurate with the incidental service that's being provided. So again, in the context of an expedited payment or a phone processing fee, it's $30 not $2 that's more associated with maybe how much it costs to staff the phone or something of that nature.

Then it's often undocumented. The CFPB has been very clear about this, going back to the payment related fees in the debt collection context, if it's not in the agreement or it's not otherwise disclosed before the fee happens, it's a junk fee. So, I think we really have a lot to go on with that. In my mind, it's not necessarily as nebulous as some of the other statements that the CFPB puts out, and some of them I don't think it's hard to find the types of fees that the CFPB might be concerned about.

Chris Willis:

In that vein, Jason, I know you mentioned a couple of examples of junk fees from the supervisory highlights like overdraft and payment convenience fees. Are there other types of fees that the CFPB identified in the supervisory highlights as being also junk fees?

Jason Cover:

Absolutely. There's over a dozen types of fees or practices in a variety of industries, including financial institutions with deposit accounts, mortgage servicing, student lending, small dollar lending and auto. So, it really spans the entire consumer financial services industries as the types of fees that they're identifying. So, we know it's not necessarily any given industry that they're going after here. And I guess, Chris, what I kind of found surprising on some level, and I'll take all of this with a grain of salt because we don't really know more than is in the supervisory highlights and what actually went on behind the scenes, but on some level, these fees, the violations are kind of mundane. It isn't just, "Hey, we found a fee and we don't like it." They're practices that I think everyone should have been somewhat on notice about already.

Just a few examples here. Again, since its inception, we've known that the CFPB doesn't like overdraft fees, so it's not surprising to me at all that the CFPB would take issue with overdraft fees on authorized positive settle negative transactions for deposit accounts. Similarly, the cited issues with payment fees that far exceeded the cost of processing the payment. I think that's again relatively common sense. And then again, repossession fees with significantly higher than average repossession costs. These are all kind of basic core principles that we've been advising clients on for years as to fees. And then some are, I think, again, just kind of self-evident based on pre-existing CFPB guidance. For example, the CFPB spent years creating a small dollar payday loan rule, and in that rule, they make it abundantly clear that if you're initiating transactions that generate NSF fees for consumers, they will consider that a UDAP.

I guess it's more of a practice than a fee. But they noted that some lenders were charging fees where there were multiple payment transactions tied to the same initial payment. So not surprising to me. Similarly, they took issue with a payday lender that was conducting what we call ACH splitting transactions. So that's when you take $100 payment and submit it four different times for $25, and if none of those payments go through, it generates multiple NSF fees. So again, there's a consent order out on this. And thinking about this in the context the UDAPs identified in the payday rule, I just don't find these surprising necessarily. I find it more surprising that people were continuing to engage in ACH splitting.

Then some of these fees were I think just blatant violations. They alleged that people were charging a late fee that's greater than was authorized in that actual contract, or charging late fees that weren't authorized in the contract. Similarly, misrepresenting on billing statements that the consumer still owed private mortgage insurance premiums or otherwise charging PMI when it should have been terminated, charging fees during forbearance, charging late fees when a periodic statement listed the late fee as $0, repossession fees not authorized in the contract, charging fees and interest after reversing the payment it's related to. These are just kind of, I think, on some level line violations of common UDAAP principles more than they are a fee in and of itself that is untoward.

Chris Willis:

Right. But back to the sort of things that actually are fees, things like an overdraft fee that a financial institution charges or a payment convenience fee that's actually charged. Does this sort of crusade against junk fees mean that creditors can't charge any of these fees? I mean, are they totally off the table now?

Jason Cover:

I think it's highly fact and fee specific. The overdraft fees, I don't know. I think market at this point, Chris, and you this market pretty well, I think our clients have just stopped charging overdraft fees in most circumstances because of, frankly, the terror around it and the messaging from the CFPB from its inception. I think something like that is just you're playing a little bit fast and loose with expectations there. And again, I think something like the ACH splitting and things like that that will generate lots of NSFs or fees that a consumer can't control, the CFPB will always have issues with. But in the context of payment fees, setting aside state law issues, I think there's ways to set up fees of this nature when they generate some sort of value to the consumer as long as the costs are in line with the service that's being provided and they're clearly disclosed and contracted for things of that nature. I think there's a lot of ways to go about this and mitigate the risk if there are fees at play.

Chris Willis:

Got it. So, speaking of mitigating risk, Jason, let's say that a financial institution or a creditor wants to try to meet the standard and charge one of these more controversial fees because it thinks it's important from a consumer availability standpoint or for some other reason. What are some of the things that they can do to mitigate the risk of being in the next version of supervisory highlights themselves or worse yet having a consent order about this sort of issue?

Jason Cover:

That's a great point, Chris, and I think interestingly enough, way back in 2017, the CFPB issued a bulletin on telephone payment fees and their expectations for supervised entities that charged those fees. One interesting note is this bulletin didn't say, thou shalt not charge telephone payment fees, or junk fees more broadly, right? It gives expectations on how to do so in a compliant fashion. And some of these, they align with the supervisory highlights, and I think what have largely eliminated a lot of those issues. So, the first expectation they give is to review applicable state and federal laws to confirm whether a fee or charge is permitted. This is good practice all of the time, right? We should not be charging fees that state law or other applicable law says we can't charge.

Reviewing the underlying agreements to determine whether such fees are authorized by the contract. Again, this goes in line with the supervisor highlights. If the agreement says a late fee should be $15, we can't charge $20 for it later. And I think this also goes to fees that aren't necessarily contracted for in the agreement. You need to disclose those in advance and make sure that the consumer understands them if you're going to head that route. The next expectation was reviewing internal and service providers policies and procedures on fees, including calls, scripts, and employee training materials and revising policies and procedures accordingly. So the same issue, if we're keeping a heads up on what we're doing in terms of customer communications, we should have good disclosure about these fees. If there's a payment fee, we know that the script is proper, discloses the fee gives cost free alternatives, so on and so forth so that it isn't a surprise to a consumer and then there isn't an expectation that it's unavoidable, which are obviously some of the CFPB'S major concerns with these fees.

Similarly, reviewing information on fees that's shared in account disclosures, loan agreements, periodic statements, company's website, over the phone or other mechanisms. I think this is crucial. Again, it helps reduce the risk to get the fee out there, have it known, have it be clear and conspicuous, letting folks know about cost free alternatives, so on and so forth. The CFPB then recommends regular monitoring and audits related to fees. And I think this is, again, kind of of obvious from some of the violations that were noted in the supervisory highlights. If you're auditing and monitoring your periodic statements, you should hopefully notice that there's an error and it says $0 when you're really supposed to be charging late fee. That's the type of thing that these activities should catch.

Reviewing consumer complaints. This is obviously a big one I think all of us know about at this point, but we should be reviewing our complaints through the CFPB's porthole, reviewing complaints that come to us directly or viewing gripe sites. And if there's a lot of smoke about a fee and customers are saying they don't understand it or didn't know they were going to be charged the fee, really need some extra scrutiny to see if there's issues with it, because the CFPB certainly will be reviewing those complaints. Performing regular reviews of service providers, we're responsible at the end of the day for our third-party service providers and we need to monitor their activities as well. And then taking corrective action any time violations are identified and reimbursing consumers as appropriate.

One thing that wasn't on the list that I think is very, very, very important, and we've talked about it a bit, Chris, is making sure that payment fees are commensurate with the cost or value of the service. This is really important in my view, and I think that's one of its CFPB's areas of focus. If the underlying cost of the fee is $3 and we're charging $30 for it, I think that's going to get their attention. And I think this is something companies can do in advance.

We can conduct studies to figure out our transactional costs and what our pass through costs is, et cetera, when charging these fees. We just need to make sure that we're charging something in line with that or that it's otherwise close to the average cost of the fee. We don't want to be a highly ahead of what the market is charging on a fee like this, and we want it to align with our costs. That's fair, right? Most of these fees shouldn't be profit seeking. A lot of them are kind of pass through fees, so taking a little bit off the top might be problematic in the CFPB's view.

Chris Willis:

Yeah, thanks, Jason. And I agree, that last topic is very important, even though it's not in the published guidance. Because I think it forms a large part of the CFPB'S motivation to go after a fee, even if it's not a source of a legal theory, addressing their motivation is also really important, obviously.

Thanks very much, Jason, for being on the podcast today. And obviously we're going to continue as a group watching what the Bureau does both publicly and privately with respect to so-called junk fees. So, stay tuned to our blog as well as to this podcast to hear more about that as it develops. And of course, thanks to our audience for listening today as well. Don't forget to visit our blog, consumerfinancialserviceslawmonitor.com and hit that subscribe button so that you can get all of the daily updates that we post about the financial services industry. And head over to troutman.com and add yourself to our Consumer Financial Services email list so you'll get the alerts that we send out and invitations to our industry only webinars. And of course, stay tuned for a great new episode of this podcast every Thursday afternoon. Thank you all for listening.