Payments Pros – The Payments Law Podcast: **Unraveling the Legal Threads: A Deep Dive into Earned Wage Access**
Hosts: Keith Barnett, Josh McBeain, and Carlin McCrory

Keith Barnett:

Welcome to another episode of *Payment Pros*, a Troutman Pepper podcast focusing on the highly regulated and ever evolving payment processing industry. This podcast features insights from members of our fintech and payment practice, as well as guest commentary from business leaders and regulatory experts in the payments industry. My name is Keith Barnett, one of the hosts of the podcast. Before we jump into today's episode, let me remind you to visit and subscribe to our blog, ConsumerFinancialServicesLawMonitor.com. And don't forget to check out our other podcast on Troutman.com/Podcast. We have episodes that focus on trends that drive enforcement activity, digital assets, consumer financial services and more. Make sure to subscribe to hear these latest episodes.

Today I'm joined by two of my co-hosts, Carlin McCrory and Josh McBeain, to discuss earned wage access, or EWA, as it's commonly referred to, and the federal and state laws that regulate this service. Carlin and Josh, I'm looking forward to the discussion today. I hope you are as well.

Carlin McCrory:

Definitely.

Josh McBeain:

Yes, for sure.

Keith Barnett:

Just so our audience knows, we decided to do an episode on this topic in response to the increased questions we have received from fintechs, payment processors and payroll processors who offer or who are thinking about offering EWA. And for those of you who do not know, EWA is a means by which an employee can receive the funds that they have already earned but have not yet been paid because the employer's payroll cycle has not yet occurred. EWA allows employees to get paid on demand as long as they have earned the wages. And there are different EWA models, which we will discuss in more detail and how that relates to the state and federal laws, that you can have models where the money is coming from the employer to models where money is coming from a third party fintech that is partnered with an employer.

These can implicate state laws on advances money transmission and lending laws. And there also can be costs that are paid by the employer to the third party fintech, so it's free to the employee. But you could also have a program where costs are paid by the employee, and that could also implicate some state laws. In some EWA programs, there could be limits on the percentage that a person can get to ensure that there's no overpayment. And limits like that are especially important in states like California, which make it hard for employers to recoup funds from employees that have been overpaid.

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The bottom line here is state regulators have weighed in by sending inquiries to fintechs, payment processors, payroll processors regarding money transmission, regarding lending. State lawmakers have also weighed in by proposing or adopting laws that cover EWA. And the federal government has also weighed in through the CFPB and other means. And that's where we'll start with Josh. Josh, could you provide the audience with your analysis on federal laws as they relate to EWA?

Josh McBeain:

Sure. Thank you, Keith. I think from a consumer finance perspective, there are some potentially applicable federal laws. Let's start with the Truth in Lending Act, or Regulation Z. The truth in Lending Act, or TILA, applicability will depend on multiple factors. For example, is the EWA product a credit product? What fees are associated with the EWA product, if any? Whether the Truth In Lending Act, or Reg Z, apply will sort of determine on an analysis of the specific facts related to these key topics. And interestingly enough, the CFPB's opined on this.

In 2020, the CFPB issued an advisory opinion on EWA products and held that a very narrowly defined EWA program did not create debt within the meaning of the Truth in Lending Act. The CFPB noted that the EWA program in question met seven specific criteria, and also based its conclusion that TILA did not apply on the theory that the EWA transaction did not create liability of the employee, but rather facilitated employees access to wages that they have already earned and to which they were already entitled. Thus, the EWA program functionally operates like an employer that pays its employees earlier than the scheduled payday.

I know I already said this, but it's worth noting again that this was a very narrowly defined opinion, and it created some confusion with the industry. The CFPB addressed this. The original opinion was in 2020. And in 2022, the CFPB issued a general counsel letter. And in that letter, the CFPB cited significant confusion that the original 2020 opinion letter had caused in the marketplace. And the CFPB's general counsel wanted to clarify in the letter that advocates of EWA programs that allow for optional fees or tips cannot claim any support from the original 2020 CFPB opinion. The General counsel went on to conclude that there's been repeated reports of confusion caused by the original 2020 advisory opinion due to its focus on a limited set of facts. And the general counsel stated that he planned to recommend to the director that the CFPB consider how to provide greater clarity on these types of issues, specifically whether the Truth in Lending Act would apply. That was in 2020, and the CFPB has not yet issued any additional guidance to provide that greater clarity.

Keith Barnett:

Thanks, Josh. Are there any other federal consumer financial laws that may apply to an EWA product?

Josh McBeain:

Yes, Keith. The Equal Credit Opportunity Act, or ECOA, and it's implementing Regulation B, it applies to a wider range of transactions than Regulation Z because Regulation Z excludes certain types of credit transactions. CFPB actually found in at least one very narrow instance that Regulation Z did not apply to an EWA program. Reg B applies to a broader set of transactions. Anyone with a program or looking to build a program would want to analyze

regulation being ECOA to determine if the specifics of that EWA program would be subject to Reg B. The Military Lending Act prohibits extensions of credit to members of the active military and their dependents at annual percentage rates exceeding 36%, it prohibits mandatory arbitration provisions in loan agreements governed by the MLA, and imposes a number of additional limitations on such credit extensions. It is important to analyze whether these protections apply to any EWA program.

It's also worth mentioning Regulation E. If an EWA program includes payments for advanced wages or is considering the inclusion of payments for advanced wages, Regulation E's compulsory use provisions should be evaluated with respect to the EWA program.

And finally, I'll mention the Payday Lending Rule. The Payday Lending Rule has not yet become effective because of ongoing litigation with the CFPB. Even though the Payday Lending Rule is not yet effective, the Payday Lending Rule is something to keep in mind for EWA products because the CFPB's final rule specifically excludes certain EWA providers and products and does not exclude others. Thus, an EWA provider would want to parse the Payday Lending Rule if it ever becomes effective to determine the applicability of an EWA program.

Keith Barnett:

Thanks, Josh. That's very helpful. Following off of that, another thing to keep in mind is the UDAAP catchall, whether there's one A through the FTC, or two A through the CFPB. These two federal regulators have a history of enforcement action against payment processors, money transmitters, and sometimes even payroll processors. And they have done this alone, they've done it together, and they've also done it with the states. And areas to look out for with respect to EWA from a UDAAP perspective includes among other things, advertising. For example, are you telling customers or consumers, or I guess they would be employees in this instance, everything that they need to hear to make an informed decision on whether to use EWA? For example, do you say that using your EWA platform is free to the consumer, but there are charges that are not disclosed?

You may have UDAAP issues if that's the case. And if you charge fees and disclose them, you want to make sure that it cannot be construed by the regulator as a loan. For example, the California Department of Financial Protection and Innovation issued an advisory opinion a couple of years ago, stating that charging fees does not necessarily mean that an EWA product is a lending product if the amount charged is minimus.

But like I said at the top of the podcast, some states have recently addressed EWA head on in their legislation and by other means, and Carlin is here to talk about that. Carlin, can you share with the audience some the state law activity?

Carlin McCrory:

Yeah. There are four states that I'd like to discuss, the first being Missouri that actually passed a law that prohibits any person from engaging in the business of earned wage access without registering with Missouri's Division of Finance, by filling out a registration form and paying a $1,000 registration fee, which is due annually on July 1st of each year.

What is engaging in the business of EWA? Technically, it's defined as the person is in the business of delivering proceeds to consumers prior to the next date on which an obligor is obligated to pay salary, wages, compensation, or other income to a consumer. The thing that we want to note here is that the law doesn't define the term delivering. So, if you're providing EWA services and you are not the employer, but let's say you're a third-party provider, sending payment messages to direct funds from an employer account to the consumer's account, you should analyze the law to see if you potentially fall within the purview in the scope of this law.

Notably, the law doesn't apply to banks or savings and loan associations whose deposits are covered by FDIC insurance, and it also doesn't apply to a credit union. And obviously those exclusions make sense here because there are protections for consumers in those cases, just like FDIC deposit insurance. The law also outlines the obligations and restrictions on an earned wage access provider, including how the services may be provided, the notices required to be given to consumers and the types of fees that may be charged. And as I hinted at earlier, the law applies to both direct to consumer EWA services and employer integrated EWA services.

A few other things. The law provides that there are a number of other substantive requirements. These can be policies and procedures, disclosures informing the customer when there's material changes, amongst other requirements. It also notes that EWA products offered by a registered provider won't be considered to be loans or credit, nor will they consider to be a money transmission activity.

Nevada also approved a bill that is scheduled to become effective in 2024, and it's substantially similar to Missouri's bill. We have the same issue with the definition in the delivery of the EWA services. Again, this bill applies to both direct to consumer services as well as employer integrated services and prohibits a person from providing these services without obtaining a license. Similarly, the law outlines the obligations and restrictions on how the service provider may engage in its business and has a number of substantive requirements. What we're seeing here and the differences between both these two laws that pass and also some of the proposed laws that didn't pass, these substantive requirements are where we have seen the differences.

So, for example, Nevada's law, while it requires policies and procedures and certain disclosures, there's also a requirement specific to responding to consumer complaints. So, there are some nuances here between the two different laws, even though I would say they are substantially similar. To sum up Nevada, this law also expressly excludes from EWA coverage, any laws regarding deferred deposit loans, high interest loans, title loans, money transmission check cashing services, et cetera.

Now, beyond these two laws, we also have two states that have issued opinions, and those are Arizona and Maryland. In December of 2022, Arizona issued an opinion that an EWA product that is offered as a no interest and non-recourse product doesn't fall within Arizona's definition of a consumer loan. The analysis goes on to state that first, an EWA product that is fully non-recourse represents a payment of wages already earned by the employee and isn't a consumer loan because the EWA product doesn't allow recourse against the employee in the event the provider is unable to recoup all or some of the portion of the advance. Secondly, the EWA product is not a consumer loan, so long as the provider doesn't impose a finance charge.

And then quite recently, on August 1st, 2023, Maryland issued what we consider a controversial opinion on EWA products. Maryland's OFR states that EWA products allow consumers to obtain

wages that they have earned but not yet received via employer payroll. That totally makes sense. In determining whether an EWA product is a loan requiring lender licensing, the guidance distinguishes between products provided directly from employers and then those provided by third parties. And then it also addresses products provided by employers with third party assistance.

The guidance concludes that EWA products provided by employers are not loans, but it's internally inconsistent whether this conclusion is limited to EWA products provided at no cost. So, the suggestion there is that the employer EWA products with the cost of the employee might possibly be loans requiring licensure is interesting because technically, Maryland's commercial loan law cited by the OFR provides very explicitly that the subtitle does not apply to a loan between an employer and an employee. So, we're really not sure where the OFR will shake out on this topic and the guidance.

The guidance also addresses EWA products provided by third party providers. It seems to suggest that a third-party EWA product could be a loan subject to usury limits and lender licensing requirements, but generally states that the arrangements, facts and circumstances must be analyzed to determine if those providers are deemed to be lenders and whether they would require a license. The guidance goes on to state that relevant facts and circumstances, at least where an employer and third party participate together in an EWA program include who bears the economic risk, what level of contact does the third party have with the employee, and who benefits from any fees or tips that the employee pays. So, we're not really sure about the Maryland guidance. It's a little unclear to say the least, and we're hoping that we'll see more on that topic from OFR.

The last thing that I want to mention is that several states, including Georgia, Kansas, Mississippi, New York, Vermont, Virginia, all proposed EWA laws that didn't pass. And again, as I analyze with Missouri and Nevada, these laws we all found were substantially similar and that they generally had the same definitions and requirements. But there were a few nuances and we do expect in the upcoming year to see more of these laws introduced and passed, and it's definitely something to keep our eye on for 2024.

Josh, I definitely want to get your additional thoughts on state laws and state regulator EWA activity, especially as it relates to lending law applicability.

Josh McBeain:

It's interesting. In addition to the new EWA laws that you mentioned, it's worth noting that there are existing state lending laws that have substantive requirements and, in some instances, licensing requirements. Depending on how an EWA product is structured, it may be subject to the new laws that you mentioned or laws that will be passed. It sounds like you mentioned multiple that were proposed but didn't pass, so I'm sure there'll be more to come next year. But there's state licensed lending laws that may apply depending on how product is structured currently, and those would need to be parsed. For example, if an EWA products or credit product, it might inadvertently wade right into state lending law and licensing applicability. So that's something to keep in mind.

I also wanted to mention, because there's been a lot of regulator and state activity on this, I want to mention a few other things. Connecticut passed a law that will take effect on October

1st, 2023. And among other things, the law broadens the definition of small loan to include income sharing agreements. California has been active in the EWA space. In March 2023, the California Department of Financial Protection and Innovation ("DFPI") proposed new regulations under the California Financing Law that would update the definition of "loan" to include EWA products. In 2021, the California DFPI signed a memorandum of understanding with five fintech EWA providers. The DFPI said that they expect more MOUs to be signed with EWA providers in the future.

The MOUs allowed the EWA providers to continue operating in California, but required EWA providers to agree to follow best practices regarding their EWA products, required quarterly data submissions to the DFPI and required regular periodic onset examinations by the DFPI. In 2022, the Kansas Financial Services regulator issued an interpretive opinion on a single, just one single EWA product, and concluded that the one specific EWA provider did not require a license under the Kansas Uniform Consumer Credit Code. So that would be an example of this dichotomy that you mentioned, Carlin, where we've got these new laws that may impact an EWA program. Then we have the existing state lending laws that may or may not apply, and Kansas Financial Services regulator is opined on that at least one instance.

And then, and this is a little dated, but in 2019, the New York Department of Financial Services led a multi-state investigation into EWA products with 10 other states and Puerto Rico. The press release announcing the investigation stated among other things that the investigation focuses on whether companies are in violation of state banking laws, including usury limits, licensing laws, and other applicable laws regulating payday lending and consumer protection laws. This multi-state investigation is still ongoing.

Keith Barnett:

Thanks, Josh for that. I want to wrap this up by spending a little bit of time talking about general enforcement issues and how to deal with those things. Firstly, by talking about the CFPB and how they had issued a no action letter to an EWA provider way back when and was 2020 or 2021, stating that the EWA product did not violate federal laws that the CFPB enforces. But the CFPB rescinded that no action letter in June of 2022. Not because it felt as if the EWA provider was violating laws, but it looks like he was primarily withdrawn or rescinded due to the change of the director, from a Trump appointee to a Biden appointee.

And as we've learned from today, while there is significant federal influence with respect to EWA, EWA enforcement, at least the potential there, is primarily an animal state law. If there are not laws that directly address EWA, the state regulators will look at their lending laws, their money transmission laws, and their own UDAAP laws, just to name a few. And one of the things that fintechs, payroll processors and payment processors may want to do to get ahead of the states is to seek a no action letter from the states that issue them. If you have designed a product whereby you would be considered as a money transmitter or maybe even a lender by the state, if they might look into those types of things. Those are just a couple of additional things to keep in mind.

That's all we have today for this episode. Carlin and Josh, thank you for joining me today, and thank you to our audience for listening to today's episode. Do not forget to visit our blog, ConsumerFinancialServicesLawMonitor.com and subscribe so you can get the latest updates. Also, please be sure to subscribe to this podcast via Apple Podcasts, Google Play, Stitcher, or whatever platform you use, and we look forward to next time.