Regulatory Oversight Podcast: 12 Days of Regulatory Insights - Day 6: Regulatory Shifts in Consumer Financial Services
Speakers: Mike Yaghi, Chris Willis, and Lane Page
Date Aired: December 12, 2024

Lane Page:

Welcome back to the special holiday edition of our *Regulatory Oversight* podcast, "The 12 Days of Regulatory Insights." This 12-episode series is focused on key highlights and trends from the past year in various areas and is designed to keep you informed and engaged during the holiday season.

I'm Lane Page, a member of our Regulatory Investigations, Strategy, and Enforcement Practice. Before we get started today, I want to remind all of our listeners to visit and subscribe to our blog at RegulatoryOversight.com, so you can stay up to date on developments and changes in the regulatory landscape.

Today, I'm joined by my colleagues, Mike Yaghi and Chris Willis, to discuss anticipated changes in federal and state oversight and enforcement in the consumer financial services industry. Mike is a member of our State Attorney General's Team and Regulatory Investigation, Strategy, and Enforcement Practice. He represents high-profile clients and regulatory enforcement investigations involving all facets of their business. Chris co-leads the firm's Consumer Financial Services Regulatory Practice Group, advising financial institutions on compliance issues, and defending them in government investigations, consumer lawsuits, and enforcement actions.

Mike and Chris, thank you both for joining me today.

Chris Willis:

It's great to be here, Lane. Thanks for having me.

Michael Yaghi:

Yes, agreed. It's great to be with both of you.

Lane Page:

Let's just jump right in and broadly ask. So what changes do you expect at the federal level with respect to oversight and enforcement in the consumer financial services industry? Mike, I'll give it to you first.

Michael Yaghi:

Yes. We have a little bit of history to key off of, I think, with the first Trump administration, right? We saw a lot of states perceiving the federal government not doing as much in the financial services space. You might see a little bit of a slowdown with CFPB and/or FTC and not be as aggressive in enforcement in the consumer protection space, which essentially a lot of the states, including regardless of political party, by the way, will step up their enforcement activity.

That's not something that's unusual when you see a new administration come in, and it's a political party that people perceive as more friendly with business and less aggressive in the consumer protection space. In many instances, the states try to fill a gap. There's some expectation that maybe there'll be a little bit of a lax federal enforcement in the financial services industry, maybe not as aggressive as the current administration, whether it's junk fees, consumer lending, that sort of thing. States are always ready to step up their game in those areas to help make sure that they're protecting their constituents. There is some of that expectation with the new administration coming in. I don't – Chris, if you have something to add to that.

Chris Willis:

Sure. I think it's – I agree with you, Mike, that the best place to look first would be what was our experience under the last Trump administration. Although the CFPB and some of the other federal regulators were less aggressive in enforcement, there was still plenty of enforcement going on, particularly in the latter two years of the first Trump administration. What I'd also say is in terms of positions, what we experienced with the CFPB last time around was they didn't go backwards in terms of any of the focus areas that the bureau had had prior to the first Trump administration. But there wasn't this continual pushing the envelope and coming up with new theories and new claims as we have seen characteristic of this administration's CFPB.

In other words, the ratchet goes forward during some administrations, but it doesn't really go backwards. At least it didn't during the last Trump administration. The one X factor, though, that we really do need to watch with the CFPB and other federal regulators is whether the populist influence within the Republican Party will have any anti-industry expression in regulatory affairs at the federal level. I mean, President-elect Trump, for example, taught during the campaign about imposing a 10% interest rate cap on credit cards, which doesn't seem like a very industry-friendly thing to do if you're a credit card issuer. So it'll be interesting to see if any of that populist sentiment makes its way into the regulatory landscape. It didn't last time around, but we'll see if it does this time.

Lane Page:

I think that is helpful in kind of understanding or deciding what to expect in terms of broad state enforcement trends. Can you speak a little bit to particular areas within the consumer financial service industry that you expect state regulators to focus more on during the next, I guess, four years?

Michael Yaghi:

I Wouldn't say they're going to focus more on, but they're going to continue to focus on consumer lending and fees that borrowers and consumers are paying. We've seen a lot of activity in the area of junk fees, for example. States like California and Minnesota passed laws to regulate junk fees. Other states like Connecticut and other jurisdictions were trying to pass those laws in 2024.

Now, going forward, I would say that we're going to continue to see that activity, where states are focused on what kind of fees, mandatory fees that companies or borrowers are required to pay in various lending contexts, and are those fees clearly inconspicuously disclosed. State regulators are going to continue to focus on those areas. One thing I didn't know with the new administration on CFPB and FTC with new leadership coming into those agencies over time as the new administration takes over the government. It'll be interesting what those priorities are. Whether those priorities focus on consumers' fees or not, the states are definitely going to continue that activity, and they're going to stay focused in those areas.

I think another area where states are going to focus is artificial intelligence. We know like Massachusetts and Colorado. Or there's another one that's – I think California, for example, have various guidelines on artificial intelligence and making sure that artificial intelligence is developed in a reasonable and sensible way to protect consumers, to protect their constituents, whether it has to do with privacy rights, financial rights, access to things like health care and things to that effect.

But I also would flag that states are not going to wait for guidelines or even laws on artificial intelligence. We've seen, for example, Texas recently settled a first of its kind — a settlement with an AI company on grounds that, basically, the allegations were that the company was not adequately disclosing the accuracy of its artificial intelligence in assessing and summarizing medical records.

I think it's not going to be unique to just health care across all industries, including financial services. If companies are deploying artificial intelligence, they're going to want to understand and know that state regulators aren't going to wait for new laws in those areas. They're going to enforce their broad UDAP laws if they think companies are using AI in a way that's adversely impacting borrowers or consumers.

Lane Page:

Thanks, Mike. Chris, do you have any thoughts on top of junk fees, which we expect to continue to be enforced in the state line one in addition to AI?

Chris Willis:

Yes. There's a few more that I wanted to highlight that I think will be active for the states during the coming four years. The first one is redlining. Now, of course, mortgage redlining has historically been the exclusive province of the federal regulators. But over the last few years, we've seen an increase in interest in the topic by several state attorneys general, so Pennsylvania, North Carolina, recently New Jersey.

Then there was a reverse redlining case brought and still pending by the Texas Attorney General. So even though I don't expect them to churn out the volume of redlining cases that DOJ did during this past four years, I think there'll be an increasing interest in redlining cases and maybe even reverse redlining cases brought by state AGs.

The scope of those cases can even now go beyond mortgage because starting in 2026, absent some intervening development, small business lenders are about to start having to report their hum do like data under the 1071 rule, and it'll become public in the latter part of 2026. The first batch of it will. The kinds of analytics that regulators do to bring traditional mortgage redlining cases will now be available for regulators of all types and private litigants for bringing redlining cases in the small business area. That's one area, I think, to watch.

The second one is non-credit products. The idea that you have products that are structured not to be credit like income share agreements or earned wage access type agreements, merchant cash advances, things like that. Being recharacterized as credit for purposes of state, user or your consumer protection laws is an idea that the CFPB has been active on during this administration, but it really was born with the states. The states were really the first ones to go after those products and say that they were credit. I think there's no reason to believe that they'll lay off of that. In fact, we expect a continuing high emphasis on trying to recharacterize non-credit products as credit by the states. Any product that has a look of credit but is structured not to be, I think we have to watch out for state interest in those kinds of products of the same nature that we've had over the last several years.

Then the final one that I want to mention is bank partnership agreements, where you have a bank partnering with a non-bank, either a fintech or some other non-bank, to offer a lending product in the state, especially if the interest rates exceed the state's user limit that would apply to a non-bank doing the loans on its own. During a Republican administration, you might expect that the federal regulators would be more permissive about those kinds of bank, non-bank partnerships, and so there may be more of them.

But to the extent they are higher interest rate products, there's every reason to believe that the states will come after those via regulatory actions based on a true lender type theory or under state licensing or other laws that they use to try to govern those agreements or even states trying to opt out of DIDMCA as Colorado has attempted to do, and there's litigation going on relating to that and its effect right now. That seems like a very likely area of state interest during the next four years, responding to the likely uptick in bank, non-bank partnerships that I think we're going to see.

Michael Yaghi:

In redlining, it's interesting. Over the last four years, the FTC, we've seen civil investigative demands focusing on redlining and asking a lot of questions, sort of targeting how lenders are treating different segments, protected classes, et cetera. Whether we see that scale back in the next administration or not, states are definitely going to – I think we're expecting to see more of that, at least from the states, over the next four years and a lot of – sure, we're going to see subpoenas where they're focusing in those areas or asking questions and asking for data and documents that are clearly indicating they're focused in that area. I think that's something company or lenders want to be aware of and prepared for.

Lane Page:

Thanks, Mike, and thank you, Chris. Going back to one topic, the non-traditional credit products, I know that a few states have enacted laws specifically classifying particularly earned wage access as a credit product. But other states have gone the opposite direction and said that it's not credit. How do both of you expect that to play out over the next few years? I imagine more states will lean towards classifying it as credit. But can you give us your thoughts on that, and also how do you expect businesses to figure out how to comply with conflicting state laws?

Chris Willis:

Yes. I mean, my view on that is because of ideological differences among the states, you tend to have the more aggressive positions concentrated in 10, 12 states, something like that. Other states don't tend to follow along with every single thing that those bellwether states tend to do. I wouldn't expect uniformity. You've already said, Lane, there isn't uniformity. There's fractiousness among the states in terms of how they deal with this issue. I would guess that the aggressive states are going to continue on their path, and then we might see a few more added in that vein. We may see a few go the other way and then a number of them where there's just probably no activity.

In terms of compliance, for companies that are offering products that are so targeted, when you have an aggressive state, particularly one that legislates or that takes an enforcement action against your type of product, you have to decide. Is it worth continuing to do business? Can I structure the product to comply with the law? Do I want to do business in a state like this or not? You might end up having companies pull out of states because of regulatory pressure like that or make the necessary adjustments to their programs to fit within whatever regulatory regime the state is trying to force them into.

Michael Yaghi:

Yes. I think at a broad level, if you think about just state consumer protection statutes, from a regulatory perspective, they'll look at these. Did the employee fully understand what they were getting, right? In the Earned Wage Access where a company is not – the scrutiny, I think, is going to focus on were they engaging in some unfair or deceptive practice because they weren't transparent with the employees. My point is they're not going to – even though these, and I'll defer to Chris on this, may not be typical credit products, states will always look at it from not just a deception, a fairness standard, right, which is such a broad standard.

Are you unfairly paying employees or giving them wages ahead of time but having hidden fees, for example, or not fully disclosing how the product works and harming consumers, et cetera? I do think if it's not credit and charging interest, but there's some other angle that the regulators can say you're still harming consumers from an unfair standard practice, they're not going to sit around and worry about an artificial intelligence with Texas to sell it, right? They're not going to wait for new regulations or specific grounds to go after companies. They're going to try to use their broad UDAP statutes to do it anyway.

Chris Willis:

Yes, that's exactly right. It's notable in that vein, Mike, that state UDAP statutes are never limited to just consumer financial product or service like the CFPB's UDAP is. It reaches anything, and so they don't have to recharacterize it as a credit product in order to make a UDAP claim against it. Now, I mean, they can do that for purposes of making a disclosure or a usury claim on it, and we've seen states do that. But you're right. The threat is not limited to recharacterization.

Lane Page:

That makes sense. I think that overall message there is just to always be aware of potential UDAP enforcement, regardless of characterization or any other applicable law. I think we are running out of time. But, Mike and Chris, I want to thank you both for joining me today. I know our listeners enjoyed your valuable insights. I want to thank our audience for tuning in to this special holiday series. Tune in next time as we continue our “12 Days of Regulatory Insights” series. Please make sure to subscribe to this podcast via Apple Podcast, Google Play, Stitcher, or whatever platform you use. We look forward to next time.