



## CFPB Establishes Procedures Relating to Supervisory Authority Over Certain Nonbanks

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### Background

The Consumer Financial Protection Bureau (the “CFPB”) has issued a final rule, effective August 2, 2013, that establishes procedures to implement the provisions of section 1024(a)(1)(C) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”) and bring under the CFPB’s supervision certain nonbanks whose activities it has reasonable cause to determine pose risks to consumers. Generally speaking, a nonbank subject to the rule is a company that offers or provides consumer financial products or services, but does not include banks, saving institutions or credit unions. In addition to bringing nonbanks under the CFPB’s authority based on possible risk to consumers, the CFPB also has authority under Dodd-Frank to supervise nonbanks, regardless of size, in the following three areas: mortgage originators, brokers and servicers (including loan modification or foreclosure relief services); payday lenders; and private education lenders. The CFPB may also supervise “larger participants” in nonbank markets as it may define by rule. The CFPB has already issued two rules defining larger participants; the consumer reporting market and the debt collection market. The CFPB has proposed a third larger participant rule covering the student loan servicing market.

Under Dodd-Frank, the CFPB has the authority to supervise any nonbank covered by the rule that it “has reasonable cause to determine, by order, after notice...and a reasonable opportunity... to respond...is engaging, or has engaged, in conduct that poses risks to consumers with regard to the offering or provision of consumer financial products or services.” Examples of such conduct are potentially unfair, deceptive or abusive acts or practices, or acts or practices that potentially violate Federal consumer financial law. The CFPB must base such reasonable cause determination on complaints collected by the CFPB (from its newly developed Consumer Complaint Database) or on information collected from other sources. The CFPB is authorized to, among other things, require reports from, and conduct examinations of, nonbanks subject to its supervision. The CFPB is authorized to supervise nonbanks covered by the rule for purposes of (i) assessing compliance with the requirements of Federal consumer financial law, (ii) obtaining information about such nonbank’s activities and compliance systems or procedures and (iii) detecting and assessing risks to consumers and to markets for consumer financial products and services. It is worth noting that the CFPB expressly stated that it did not see the need to define the terms “reasonable cause” or “risk to consumers”.

### Summary of the Rule

The rule is divided into four subparts. Subpart A contains general provisions, including provisions regarding scope and purpose and definitions applicable to the entire rule. Subpart B sets forth the procedures relating to the determination process, including: (1) issuing a notice commencing a



proceeding, (2) contents of a notice, (3) service of a notice, (4) response to a notice, (5) conduct of a supplemental oral response, (6) manner of filing and serving papers, (7) issuance of recommended determinations, (8) determinations by the director of the CFPB, (9) voluntary consent to the CFPB's authority, (10) notice and response included in an adjudication proceeding otherwise brought by the CFPB, and (11) relief available sought in a civil action or administrative adjudication. Subpart C sets forth a post-determination process whereby a respondent may, after two years, petition the director for the termination of CFPB supervision. Subpart D sets forth the rules for the construction of time limits, change of time limits, and effect of deadlines.

Under the rule, a notice commencing a proceeding does not constitute a notice of charges for any alleged violation of Federal consumer financial law or other law. The proceedings under the rule are informal and do not constitute an adjudication proceeding with a hearing on the record under the Administrative Procedure Act. Accordingly, no discovery is permitted, a supplemental oral response does not constitute a hearing on the record, and no witnesses may be called as part of a supplemental oral response.

The process begins upon the CFPB delivering a notice to the nonbank that it may have reasonable cause to determine that the nonbank is engaging, or has engaged, in conduct that poses a risk to consumers. The recipient of the notice has 30 days to provide a written response, including, if desired, a request for the opportunity to present an in-person response. Failure to timely respond to the notice may result in a default determination that the nonbank is subject to CFPB supervision. The staff of the CFPB will have 45 days following its receipt of a timely response to make its recommendation to the director of the CFPB. The director of the CFPB will then have 45 days to render his determination regarding the applicability of the rule to the subject nonbank. If the recipient of the notice requested an in-person response, the staff's 45 day period within which to make a recommendation is extended to 90 days.

It is also important to note that the CFPB may exert supervision over service providers (not defined) to any covered nonbank to the same extent that it could if such service provider were providing services to a bank and the CFPB were its federal bank regulator.

The market impact of the CFPB's new rule is likely broad and deep. The exact extent of the information to be required and the scope of the examinations to be conducted by the CFPB will be determined over time. This likely will create a heightened degree of uncertainty in the marketplace. This rule reinforces that Dodd-Frank provided the CFPB an enormous level of authority to supervise the providers of consumer financial products and services. The CFPB did not provide guidance on what products or services might be covered by the new rule, and while not a comprehensive listing, the following businesses may be covered: structured settlement, credit repair, debt settlement, tax preparation and tax restructuring companies. These entities should begin to examine their operations and procedures in order to avoid possible additional supervision.

Please let us know if you would like additional detail regarding the final rule and its application to nonbanks.

For more information on the matters discussed in this *Locke Lord QuickStudy*, please contact the authors:

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