Consumer Finance Monitor (Season 4, Episode 50): What Every CEO and General Counsel Needs to Know About New CFPB Director Chopra, with Special Guest Raj Date, Managing Partner of Fenway Summer LLC

Speakers: Alan Kaplinsky, Chris Willis, James Kim, Rich Andreano, and Raj Date

Alan Kaplinsky:

Welcome to Consumer Finance Monitor Podcast, where we explore important new developments in the world of consumer financial services. I'm Alan Kaplinsky, I'm senior counsel of Ballard Spahr, and I'm the former chair of the Consumer Financial Services Group at Ballard Spahr.

Alan Kaplinsky:

During today's podcast, we are very pleased to be reprising one of the best webcasts, I think, that we've ever done. That is, a webcast that was entitled, What Every CEO and General Counsel Needs to Know About New CFPB Director Chopra.

Alan Kaplinsky:

And we very intentionally put into the title, not what everybody should know, but what every CEO and general counsel should know about new CFPB Director Rohit Chopra. General counsels and CEOs don't want all the detail. They don't want to get into the weeds, and we're not going to get into the weeds.

Alan Kaplinsky:

We're going to look at this at a much higher level, and I don't think we have anybody that could be better qualified to join us as a guest today, than Raj Date. Raj, for those of you who don't know him, he is managing partner of Fenway Summer, an advisory and investment firm focused on financial services and financial technology.

Alan Kaplinsky:

He previously served as the CFPB's acting director, its first deputy director, and he worked very closely with Rohit Chopra, when they were both at the CFPB together. Raj will provide a unique perspective on Director Chopra's views and likely actions as CFPB director.

Alan Kaplinsky:

I am joined today by three of my colleagues from Ballard Spahr, Chris Willis, Rich Andreano, and James Kim. Let me just very briefly introduce each of them.

Alan Kaplinsky:

Chris is the co-leader of our Consumer Financial Services Group, Rich is the co-leader of our Mortgage Banking Group, and James Kim is the co-leader of our FinTech and Payments Team. Like Raj, James was formally at the CFPB. James was an enforcement attorney, working out of the Manhattan office.

Alan Kaplinsky:

Now, what we're going to do today, we're going to have a unique procedure. First of all, I'm going to turn the program, in a moment, over to Raj, who is going to describe his connection and relationship to Rohit Chopra. Then we will launch into a discussion of a number of really key areas that all of us believe are going to be areas of focus for Director Chopra.

Alan Kaplinsky:

The areas that we're going to talk about are fair lending and digital redlining, student lending, Big Tech, and FinTech, the Office of Innovation at the CFPB, enforcement issues, and where we think directive Chopra will focus. We'll talk about rulemaking, the ongoing rulemaking, or partially completed, but now totally complete rulemaking, pertaining to payday lending, small business lending, debt collection rules, whether there'll finally be an installment lender larger participant rule,. We'll talk about mortgage servicing, and the ongoing on mortgage servicing, of the pandemic.

Alan Kaplinsky:

We will talk about a reconsideration of the new General QM rule, and the new Season Loan QM Rule. We'll talk about the Home Mortgage Disclosure Act. And we'll talk about of the new consumer products that have been launched only within the past few years, and a joint consumer group request to revoke guidance on earn wage access, and certain other kinds of non-credit products.

Alan Kaplinsky:

We'll talk about regulation by enforcement. Finally, we'll talk about the auto finance, dealer finance charge issue. So with that, let me extend a very warm welcome to Raj. Raj, first of all, very warm welcome, and thank you for being on our program today.

Raj Date:

Thank you. Appreciate it.

Alan Kaplinsky:

Yeah, it's our pleasure. Raj, your time at the CFPB gave you quite a bit of exposure to Rohit, because Rohit was also a senior person at the bureau, was Ombudsman in the Student Loan Area for awhile, and he had some other positions.

Alan Kaplinsky:

I'm wondering if you could briefly to our audience, in a little more detail, exactly what your relationship was with Rohit, what you know about him from that period of time, and also, moving forward in his career, as he became a commissioner at the FTC. Because we'd be interested, at a high level, getting your thoughts on what you think his priorities are going to be. And then we're going to get into a little more detail on some of these things.

Raj Date:

Yeah, sure. I met Rohit back in 2010, so shortly after I came down after Dodd-Frank was signed, to join the Treasury Department. Recall that I came down originally with the idea of just spending two or three, months helping to put together the CFPB.

Raj Date:

That is to say, design an organization structure, recruit some key people, help set out some early priorities, and then decamp back to New York, to get on with my life. Things just more or less snowballed after that, so I ended running the policy apparatus, and then stepping into Senator, well, then-Professor Warren's seat, as the acting head of the place, when she left to run for the Senate. And in those early days is when I met Rohit.

Raj Date:

Rohit, we had recruited with the Student Loan Ombudsman in mind, which, organizationally, was a circling a key leader role, in terms of the expansiveness of the skill set required, as well as the elasticity of style and elasticity of mind. The reason for that is that, unlike most of the other roles at the bureau at that level, it was simultaneously consumer facing, in that it's meant to be an ombudsman role for work consumers.

Raj Date:

It was industry facing, in what was then and is now, a pretty concentrated student lending market. It was skill facing, because of periodical reports required, to be issued in relatively frequent appearances in front of the committees of jurisdiction. Then, finally, it was market facing.

Raj Date:

So, to find someone who combined all of those things, and had the intellectual, just curiosity of mind, to be able to delve into, and stay within a product market, that after all is important, but is not necessarily as expansive as some others, was a challenge. And it turned out to be a great, a really terrific fit for him.

Raj Date:

If I want to just say the outset, and I know that we're going to talk about different product markets, let me talk about priorities, as they might evolve through a different, more thematic lens. I mean, Rohit, in my opinion, like a lot of people with roughly his background, and I suppose I have roughly his same background here. We are both alums of McKinsey, in the financial institutions practice, as well as with some of the same private sector firms in the industry.

Raj Date:

But a lot of people like that, including me, develop a sort of parochialism of microeconomic thinking, which boils down to, markets work like markets, and competition they're in. We tend to identify unserved markets, unpriced risk, and fill them with products and services, in order to fill those voids. They do so efficiently, except, when they don't.

Raj Date:

That's where this sort of orthodoxy meets, really, antitrust in competition theory, which is that markets can't be expected to fill competitive voids, where you have structural problems that persist. So, structural problems like information asymmetry, structural problems, like agency problems, structural problems like market power and concentration.

Raj Date:

One of the things that I think is useful, when you think about where it is, that the new director will spend time and energy, and not coincidentally, where the agency will end up spending some energy, are going to be in areas where there are at least plausible causes to believe that there are persistent market structural issues that are difficult to remedy on their own, without some kind of regulatory intervention. It's through that, by the way, that the fact that he was an FTC commissioner, which is one of the, I suppose, two federal agencies charged with competition authority of one kind or another, it's a pretty striking combination of backgrounds, between consumer protection and antitrust thinking, which I think will continue to be threaded throughout his view of the consumer finance markets, and indeed, I'd argue, already have.

Raj Date:

We talked just a little bit about some of the reasons why I would expect the bureau to be considerably, even dramatically more energetic in the years to come than it has been in the last few. And then, let me just highlight a few, what my guess is, are going to be some challenges that the new director and his team will have to confront.

Raj Date:

I think it's important to realize that Chopra has zero of the three drawbacks, the three handicaps that the proceeding two directors had. I think that, certainly at the outset, both Mulvaney and Kraninger were, suffered from, A, didn't have much of a background in the actual industry, B, didn't take out much space within the universe, the constellation of other federal regulators. And then, finally, didn't come in with a reputation, or a pre-existing trust level, with the senior staff.

Raj Date:

Rohit has none of those handicaps. He definitely knows the industry, as he has spent, depending on your point of view, is he has either spent or wasted his entire career around it. He's got an intellectual curiosity about it.

Raj Date:

When he was nominated, out of curiosity, I went back through my e-mails to find some of the earliest exchange changes between him and me, and they include some of the most bizarre, arcane topics. He's inquiring about the mode by which municipal authorities bought interest rate swaps in the pre-crisis era. It indicates a level of intellectual curiosity about the industry itself that not everybody has, and I think that will help him quite a bit.

Raj Date:

Second, he's got a bunch of pre-existing relationship on the Hill, and with the leaders of other agencies, that matter. It will allow him to have a level of influence that extends beyond the positional authority of CFPB itself, whether that's within the formal confines of, say, the FSTAR, or the FYC Board, or more broadly, just in general, as an agenda setting, from a policy point of view, role.

Raj Date:

Then, finally, most of the senior staff already knows him, either directly or by reputation, and that helps, especially out of the gate here. Let get back to just a couple of challenges, that realistically, I think that he and his team are going to have to confront.

Raj Date:

Number one, and probably the most important is just talent, right? There are a bunch of acting positions, a bunch of holes in, within the leadership structure of the bureau, that realistically have got to be filled with really adept people. People sometimes don't like it when I point this out, but regulatory agencies are just like other professional services environments.

Raj Date:

If you don't have the right people, you shouldn't expect great results. And 80% of the great work tends to be done by 20% of the best people, and those 20% know who they are.

Raj Date:

So you need to be able to continue to recruit or train fantastic talent. And if you're not attentive to it, you end up with kind of an adverse retention problem.

Raj Date:

It happens in other organizations too, sooner or later, you're going to discover that people, if they're bored and they're not doing anything, the only people who hang around with people who all wish they'd moved on, so that you really have got to reenergize an approach to talent.

Raj Date:

From the outside, it appears that they're doing that. When I see the name of people who are in the mix for roles over there, I'm pretty impressed. That's something that's going to very much be a priority.

Raj Date:

The second challenge, I think is, even more so now, I would say more so now, than at any time, post-financial crisis, important moves the shape of the financial services competitive landscape is being contoured by firms, including those that don't have any supervisory relationship with the CFPB. And in my opinion, and I assume, the opinion of most, the supervisory lever is an important piece of the overall policy arsenal at the bureau.

Raj Date:

And you don't have it, with respect, to say, small banks, or you don't have it with respect to tech firms, not directly, anyway. That is going to be a significant handicap, that for the first time, really in the post-crisis period, becomes a real issue that has to be grappled with.

Raj Date:

Then, finally, the reality is that the bureau was not designed, and one of the things, maybe, if I could go back in time, maybe I would do differently. But even the culture, the governance, the norms of the agency, were not designed with the idea of the director changing with every election.

Raj Date:

And there is, I think, a question of the durability of policy changes, post '20, what year would that be, post 2024 elections that could create a little bit of what would appear to be now, a permanent recurring pall over policy changes, and the industry's embrace of them, if you don't really know what's going to be, have staying power in the next election or not. So why don't I pause there?

Alan Kaplinsky:

Very interesting, Raj, really appreciate your insight. Okay. We're now going to talk about an area, drill down a little bit more, into an area that, at least, based on what we've heard from public announcements from Rohit, and others on the staff, is going to be a major priority area that cuts across a whole range of products, namely fair lending, and it's offshoot digital redlining. So I'm going to turn to Chris, to have Chris set the stage for you, Raj, and then, love to get your reaction.

Chris Willis:

Yeah, thanks, Alan. Anybody who hasn't lived the last year off the grid, it will be evident to you that fair lending is one of the major priorities of the bureau, since the administration changed earlier this year.

Chris Willis:

That was true under the acting director, Dave Uejio, and it will certainly be true under Director Chopra, as well. And it seems like nearly every public statement that one of them has made, or makes now, features the theme of discrimination, racial equity, justice, and fair lending.

Chris Willis:

So there's an expected outcome of a focus on fair lending, and that is a return to the types of enforcement matters and supervisory matters that we've seen from the federal agencies in the past, like a concentration on judgmental underwriting and pricing, a focus on mortgage redlining, the classic type of redlining. Nobody would really be surprised to see a lot of that activity happen, under the new leadership of the bureau.

Chris Willis:

But what's interesting is, the seeming hostility that the director has manifested in recent public statements, about the use of machine learning models to engage in credit underwriting. And that is, really, to me, in a lot of contrast to statements made by the bureau in previous iterations.

Chris Willis:

The bureau has written three reports about credit invisibles, people who don't have enough of a credit file to have a credit score, and has pointed out the fact that they have problems accessing credit, and in fact, that credit invisibles tend to be over representative of protected classes, under the Equal Credit Opportunity Act.

Chris Willis:

So when you've seen the bureau write about and talk about machine learning models and the use of alternative data in the past, the tone seemed to be suggestive of the fact that those underwriting methods were really the best promise to make the credit market more inclusive for these credit invisibles, and again, many of whom were members of protected classes. But when Director Chopra made a press statement in connection with the Trustmark settlement several weeks ago, he made some very negative comments about what he called discriminatory black box models, and essentially announced the conclusion that those were cutting off access to credit for members of protected classes.

Chris Willis:

In the meantime, of course, the industry has begun to widely adopt the use of machine learning models and the use of alternative data over the past several years. And there's a huge business push behind that, as well, because the models are just better. So Raj, I'd really love to hear your thoughts on what seems to be a difficult position for the industry, where there's been a lot of uptake of this new technology, and previously relatively neutral, and maybe even encouraging statements from the CFPB about it, even from people in the CFPB's Fair Lending Office, who've always been there, and are still there today, as contrasted with Director Chopra's recent statements, that seem to be quite a bit more hostile.

Raj Date:

I think this is one of these cases, Chris, where market realities are going to push us towards some resolution here, and if that ends up in litigation on a red B issue, then that's the way it's going to be. And the reason I say that is that for high credit content populations, that is to say, where credit risk, the ambient level of credit risk is high, you cannot compete with somebody through a cycle who is using a better decisioning model than you are.

Raj Date:

Because they are swapping in otherwise good credits, and which means they're swapping out to you, worse credits, and you can't really fight that battle very long. So I think this particular cat is out of the bag, is racing around and biting all the other cats. There is going to be more embrace of machine learning models, because they bloody work, not for super prime credits or something.

Raj Date:

For the bottom, call it, three deciles in terms of creditworthiness in the country, they work, they work better, because they're using a wider set of data that otherwise can be kind of productively used than traditional long regression model, based on bureau attributes. That's just fact. That is, in fact, the state of affairs, and there's no practical way to move it backwards, absent, just sort of regulatory fiat.

Raj Date:

And I'm just not sure, at least under current law, that there is some magical way to just ban the use of wider data sets like that. Nor by the way, obviously, as you can tell, nor do I think that that would be a good idea.

Raj Date:

So I think, therefore, we may be either headed to some particular kind of litigation posture here, or this will just always inhabit the realm of press statements, but then nothing, nothing actually with force of law. Now, if one were to have a defining rod to where, if there was a case to be brought, where it would be brought, I think you would look for indicia of otherwise bad facts, which is why across our portfolio, anyway ... I guess I should point out is, the last time I practiced law was 25 years ago, and there's a reason for that.

Raj Date:

But through a non-legal, more just, sort of business judgment lens, the way in which I think about these issues is, if you have a trio of features, you are much more likely to, have to withstand considerably more skepticism and scrutiny. Those are about substantive transparency, just, customers get what they're getting, or not, a question of normative fairness. Like, would you put your mother into this product, or not? And then, a question of practical suitability.

Raj Date:

By that, I mean, a good example for this is the HELOC business, pre-crisis. Seems like an awesome product, why wouldn't you want to consolidate your credit card debt into a much lower tax deductible thing?

Raj Date:

That sounds great, but in reality, what would happen is, everyone would borrow against their cards, almost right away, and then be right up against their credit limits again. So everyone ended up worse off.

Raj Date:

Anyway, in my opinion, if you look for those underlying features of bad facts, then you start having a sense of, "Well, where is it that a case like this might get brought?" Because I do think it's an area that if the agency has an opportunity to paint its fact pattern, in terms of moving this forward.

Alan Kaplinsky:

Chris, wondering, you raised the subject of fair lending. If you could set the stage for something that certainly absorbed a lot of time during the Cordray era, and that is the auto finance upcharge issue, and would like to get both your reaction, and Raj's reaction, to what you think is going to happen there?

Chris Willis:

Sure, of course. Well, the bureau put out a bulletin in 2012, describing a theory of disparate impact liability, based on indirect auto finance companies permitting auto dealers to negotiate retail interest rates with their automobile purchasers. The bureau then brought a series of enforcement actions against several banks, and several large captives, alleging that to be a violation of the Equal Credit Opportunity Act, between 2013 and about 2016.

Chris Willis:

Then, after the election in 2016, the bureau stopped on that. The bulletin was then overruled by Congress in 2018, May of 2018, as I recall, and the bureau has been quiet about this issue ever since.

Chris Willis:

One question that clients are asking me a lot is, do we think the bureau is going to go back to the indirect auto finance, dealer finance charge issue that was characteristic of that series of consent orders? I'm just going to go on a limb and say, "I don't think the bureau will go there again."

Chris Willis:

I think that the legal environment for that claim has become more hostile, because of the congressional disapproval of the bulletin. But more than that, it was an investment of time and resources by the bureau that earned it a very significant amount of political blowback through the then-House Financial Services Committee, and of course, arousing the ire of the auto dealers' lobby.

Chris Willis:

For all that trouble, the bureau got no change whatsoever to the prevailing market practice. Auto finance contracts are priced today exactly the way they were in 2012, and there's been no change to that. To me, it's not a positive risk/reward calculus for the bureau to hit that issue. again.

Chris Willis:

I think the bureau will be interested in other fair lending issues that have not yet been explored. That's just my prediction, but Raj, what do you think?

Raj Date:

I would agree with that. I mean, let's face facts. In 2012, right, we were all already operating in a backdrop where, it's not like Congress didn't think about whether or not auto dealers should be subject to CFPB supervisor jurisdiction, right?

Raj Date:

They did consider that, and they decided not to do that, pretty explicitly. I still remember Hill staffers yelling at me about it during the Dodd-Frank deliberations, actually.

Raj Date:

So, from the point of view of a lot of people on the Hill, this is, "It was asked and answered, thank you very much." The bureau took a more aggressive line, and ultimately, we're right back to where we started with. So I agree with all of that.

Raj Date:

I also think that, just as a secular matter, the relative ease of competitive direct lending offerings, is monotonically increasing, which means that you have the ability to, over time, chip away at the primacy of the point of sale of lending channel within auto finance, which puts you in a backdrop, where this is a problem that kind of, sort of, to the extent it exists, gets chipped away on its own, anyway. So I think I end up same place as you, Chris.

Alan Kaplinsky:

Yeah, Chris, while you're on a roll, let's turn to the subject of student lending, an area that we know from Raj's, from Rohit's prior tenure at the CFPB, that he was very intimately involved in that area. Why don't you set the stage on the student origination and servicing front?

Chris Willis:

Sure, yeah. Of course, in addition to the fact of Director Chopra's previous role at the bureau, as Student Loan Ombudsman, his recent hiring of Seth Frotman back into the bureau, to be a special advisor to the director, and I believe, acting general counsel of the bureau, I also think sends a relatively strong signal that this will be a priority area.

Chris Willis:

The interesting thing about student lending, and its attention under the bureau, under Rich Cordray, was that there was a decided emphasis on servicing, rather than origination. It was thought, I think, that because the majority of student debt is federal student debt, and of course, the bureau can't do anything about the origination of that debt, that servicing was the place to make the most good happen for the most number of consumers.

Chris Willis:

What I think will be interesting under director Chopra's tenure is there seems to be a renewed interest in private student loan origination. In particular, there's a lot of swirling controversy on the Hill among consumer advocates, including Seth Frotman's group, about the use of certain variables in private student loan underwriting, like where you go to school, or what your course study is, or what your occupation is going to be, when you get out of school.

Chris Willis:

Those attributes, from the data I've seen are undeniably predictive of student loan repayment performance, and so, seemingly should be fair game to put into a model to approve or decline student loan applicants. But yet, there's this intense criticism of them, along with the historic grandparent of all of those variables, which is the Department of Education's cohort default rate.

Chris Willis:

I feel like, where we are headed, based on what is being said publicly, as well as what we're seeing privately in some enforcement investigations, is that the bureau is going to make certain school-related attributes off limits for private student loan underwriting. And that I think is where it looks like we're headed, based on all the pressure that's building up around that. But Raj, what do you think the bureau's particular focus in student lending will be?

Raj Date:

Yeah, I could see that. I mean, the reality, though, is that the market has evolved rather dramatically, since the pre-crisis private student lending era. And by that, I mean, specifically, the vast majority of dollars that are lent in the private student lending market are, have got co-signers, in other words, like parents, grandparents, et cetera, who are typically prime or super prime credits. And it's really the parent who you're underwriting, and not the student.

Raj Date:

Now, I personally believe ... Oh, and by the way, the vast majority of the private student lenders, in fact, are tending to suppress the kind of variables that you're talking about. So student-specific, course of study kind of things, notwithstanding the fact that they manifestly work, they do in fact split risk, for the reasons that you quite common sensibly point out to.

Raj Date:

Like, if you graduate, you tend to feel that there's more value in this giant loan that you just took out, and your earnings is considerably higher. You are obviously a way better credit if you're going to graduate, so why don't I just look for someone who's going to actually finish their degree?

Raj Date:

The problem with that is, walk around in America. I can guarantee you, that if you built a model to predict whether or not somebody is going to graduate from college, that model is going to have to look a heck of a lot like something that basically is sloping risk based on SAT scores. That, for sure, is going to result in disparate impact. As a result, the industry, by and large, just doesn't use those variables. And I think that's a miss.

Raj Date:

I think that's a miss for the education finance industry, broadly, and indeed, for education broadly. Because if we are going to default, as we already have, into a situation where we're just going to underwrite parent, otherwise, "You've got to get grants, there is no credit available to you," well, that to me feels regressive, and further entrenches an intergenerational access to education, which is almost exactly the opposite of what we should be doing.

Raj Date:

Unfortunately, that's where we are right now. Because I don't see substantial changes in the offing, when there remains this cloud about, the use of disproving, in fact, doctrine in this area, yeah.

Alan Kaplinsky:

Okay.

Chris Willis:

That is a terrific point, by the way, it underwriting the parents means that only super prime parents' kids get to go to college.

Raj Date:

Yeah. And the notion that somehow, that's the right outcome? It boggles the mind.

Alan Kaplinsky:

Okay. Thank you, Raj and Chris. Now, I want to turn to James Kim, and James heads up our FinTech Practice Group within our Consumer Financial Services Group.

Alan Kaplinsky:

And James is going to talk about what I think is one of the more controversial initiatives that Rohit has embarked upon early in his tenure, that is, going after Big Tech. So James, why don't you set the stage for that?

James Kim:

Thanks, Alan. And I'm very happy to join this, Raj, so this I think is a juicy, interesting topic. Undoubtedly, it caught the attention of pretty much anybody that bothers to follow the CFPB.

James Kim:

One of Director Chopra's very first actions, as the director of the agency, was to open an inquiry into the six large technology companies that offer payment platforms and other related financial products. Although they are, most of them, not all of them, are primarily technology companies, not financial service providers, at least the way that they would describe themselves.

James Kim:

Within a week or so of opening that inquiry, he testified before Congress. It was his first trip to the hill as the director, as opposed to a nominee. And before the House, he testified, "I am very, very worried, as I think many in the regulatory community have been, about Big Tech taking more control over the US dollar, and the global flow of payments."

James Kim:

And then he called out particular concern on top of that. There are many people who feel that their data is being misused or abused. There's a lot to unpack there.

James Kim:

So I'd love to get your thought, Raj, about the inquiry, but also his remarks. And if you could read some tea leaves, and tell us where you think this is going, that would be fantastic.

Raj Date:

Yeah. Well, I don't know where this is going, but I do think that it's a real thing. It has, just as a threshold matter there is a possibility, right, that all of this is essentially sort of posturing in it, for a positive reception among the constituents that matter, including those on the Hill.

Raj Date:

For example, back when I would go up to the Hill, to be beaten by various members, Congress, a tried and true pivot, to more or less any question, was to talk about how much you love the community banking business. It wouldn't even have to be relevant, but that then forces for the interlocutor to go on this lengthy mutual lovefest of ...

Raj Date:

And there's a chance, that this is kind of like that, irrespective of the line of inquiry, if you turn it into skepticism about Big Tech, and the shadowy dangers therein, it could be that everybody has to agree with that skepticism. And that's a good place to be.

Raj Date:

But I think it's quite a bit more than that. I do, in fact, think at this moment in time, I mean, when you look at some of these, some of, what is it, six firms that received these requests, their financial services offerings today, in some cases, are breathtakingly successful. I mean, really quite remarkable in terms of size already, speed of growth, a feature set. It's real. And it's real right now.

Raj Date:

And Rohit, by virtue of the fact of his background at the FTC, has already been steeped in some of the antitrust-like thinking that would make him a pretty uniquely good convening for some of the policy dialogue, that absolutely is going to surround some of these firms. And if you put that there's inevitably going to be a fair amount of theatrics involved, but it is an important set of questions.

Raj Date:

And I do think that the bureau, by virtue of Chopra's leadership is in a very good position to be the locus around, the nexus around which a lot of this policy discourse happens. But I'm curious to hear your thoughts about it.

James Kim:

Yeah, very interesting. So yeah, I think you hit upon one of the things I noticed, which is, his remarks had an antitrust component to it, in addition to consumer protection, and to what extent, if at all, it translates into CFPB policy making or actions, to be determined.

James Kim:

But yeah, I agree 100%, that who he is, and what his background is, and how he thinks, I imagine that he's thinking about it with some perspective of the antitrust angle, as well as the consumer protection angle.

James Kim:

The one thing I would add too is, so he focuses on payments, I think, rightfully so, for obvious reasons. But in his remarks, there was kind of a throwaway in there, about credit reporting and the FCRA.

James Kim:

I just want to call that out for people, too, because again, when you're in taking that much data, and then you're doing something with it, assembling and evaluating, in some way, shape or fashion, and then you are providing that data to third parties for compensation, so that data could be used for eligibility determinations. I just recited the FCRA elements for being a credit reporting agency.

James Kim:

It's just something that I think he mentioned briefly. But in my view, there's the payment angle, and then there's the FCRA angle, seem to be the primary legal areas in which, if he's going to do anything, if the agency's going to do anything, those would be the legal hooks.

James Kim:

So, just switching gears a little bit, but staying on technology, I think, very generally. Raj, this is kind of a two-part question, so let's take the first part.

James Kim:

Back in October 12th, about 100 organizations, primarily consumer organizations, submitted a letter urging the CFPB to revoke or substantially overhaul its earlier advisory opinion and policy guidance about earned wage access products. I'd love to get your thoughts about the merits of it.

James Kim:

But to me, the bigger question is, those actions, those prior actions, it was an advisory opinion, and there was some guidance, more general, were all issued by the Office of Innovation. The Office of Innovation was created by, initially, acting director Mick Mulvaney, and then kind of continued, with Kathy Kraninger.

James Kim:

But the head of that office was appointed by Mick Mulvaney, and then he stayed on, Paul Watkins, throughout the Kraninger era. What's interesting about the Office of Innovation is that it was very active during that period. They issued a bunch of statements and programs. So I'm curious to get your thoughts about the future or the fate of the Office of Innovation.

James Kim:

Interestingly, I point out to people it's not in the statute, it's not in Dodd-Frank. So, when Mr. Mulvaney said, "The agency, I'm going to do my job, it's going to fulfill its mission, but not do a letter more than what the statute says I should do," he still created the Office of Innovation, even though it wasn't in the statute. So it was a pet project for him.

James Kim:

But anyway, just pause there. I'd love to get your thoughts, generally, about the Office of Innovation. But if you have thoughts about the earned wage access, I'd love to hear it as well.

Raj Date:

Well, again, I'm not a lawyer, but I think that the reasoning on the earned wage access guidance is internally consistent, anyway. And I think, as a market matter, if one were to extrapolate to a natural market penetration of a product like that, it would be like a meteor hitting the payday business, right?

Raj Date:

Like, it basically is pulling forward in time into a positively selected product, most of the volume that otherwise would get done in payday, or trigger an overdraft, or something, that otherwise, it recourses to the same cash flow. So it's just a way better structural solution to meet a problem. And it's hard to bet against those things, on average, over time.

Raj Date:

In terms of the Office of Innovation, it might be the only thing that I have ever agreed with Mick Mulvaney about, but I do think that there's an important structural role that either will be played by something called the Office of Innovation, or it will get just run out of the director's office in the way that, for example, we had Project Catalyst back in the day, when, well, this would have been 2012, I guess.

Raj Date:

And the idea, I think, is a good one. And it's born out of the observation that regulatory agencies over time grow to resemble their regulated charges, especially in a business that is gigantically scale intensive, like financial services is.

Raj Date:

Let me put it this way, getting back in the notion of the CFPB, like any other professional services organization, being a talent driven organization, you only have so many great people. Are you going to have them work on some kind of nothing product, that might develop someday into nothing at all? Or you're going to have them work on some gigantic extant business in a gigantic firm that serves, 20 million people?

Raj Date:

They're going to do the latter, and that, if you play the tape forward, then, it means that you are always going to be surprised by, and be ill-equipped to deal with, new developments in the marketplace. And that's just kind of a weird position to put oneself in, but it will happen, unless you have a deliberate, and possibly structural impulse, to break away from that incumbency bias that afflicts all of us, to pay attention to that which is new, and that is normal.

Raj Date:

So my hope is, whether it gets done at the director's office or a separate office, I don't think particularly matters. But I do think that that particular muscle needs to be exercised over time, or it absolutely will atrophy.

James Kim:

Yeah, no, I agree. Yeah, I agree. I'm less concerned about the labeling, or how they do it, but that they do it in substance. So, just real quick, I know Alan's going to move on to rich.

James Kim:

To me, there's an interesting contrast, because the previous advisory opinion about earned wage access took a position that the product was not credit. I'm not here to debate the legal aspects of it, but then, that was under the prior administration.

James Kim:

And then, one of the few consent orders that's come out recently was against a small non-for-profit. So it's not even a company, it's a non-for-profit that offers income share agreements, educational income share agreements, in, I think, only two states. And so that's a better future forward.

James Kim:

In the consent order, the CFPB took the position that ISAs, kind of generally, are extensions of credit without really any, much explanation for the legal analysis. So that, to me, it's interesting to compare and contrast.

James Kim:

Under the prior administration, they just used these different regulatory tools to try to give some transparency and guidance about a novel product, and whether it was credit or not. Then, more recently, it's done through a consent order.

James Kim:

The obvious question that I think people are asking generally, not necessarily about that consent order is, "Are we returning to regulation by consent order?" And my personal kind of area of interest is, what about smaller companies that are trying to be creative and innovative? How is the bureau going to treat them?

James Kim:

Are they going to try to engage with them, sandboxes, whatever it might be, softer tools? Or are they going to just drop the hammer with consent orders, and kind of take it case by case?

Raj Date:

Yeah, well, I think that on the margin, I think you absolutely are going to see, enforcement actions of one kind or another, via a bigger piece of the overall policy pie than they have been.

Raj Date:

I think, paradoxically, is this paradoxical. I think that one of the effects of the fact that, if the election goes the other way, say in 2024, it means that you have a relatively short fuse on the ability to affect change across the industry.

Raj Date:

Because, deliberately, rulemakings take a long time, it ends up paradoxically putting even more pressure on the use of consent orders as setting a new competitive terrain, than it would, had the governance of the bureau been something more apolitical, kind of pre to law. So yeah, I think you're right to expect more enforcement activity, and more, "policy making via" ... It's not unknown, right, in Anglo-American law.

Raj Date:

It's like, the notion of case by case progression of a common law around some of these concepts is not unique to consumer finance. But we're going to see more of it now, I think, than we have over the last several years.

Alan Kaplinsky:

Raj, you made a reference to rulemaking, and the fact that it takes a long time. That's certainly been proven by some of the experience that the CFPB has had in payday lending, and the arbitration rule.

Alan Kaplinsky:

Chris, why don't you set the stage there? Because I'm very curious as to what you and Raj may think about some of these ongoing rulemakings that are, in one sense or another, not yet finished?

Chris Willis:

Sure. I think there's a couple that are very obvious, that are underway now, that look like they would naturally be very high priorities under Director Chopra's leadership.

Chris Willis:

So one is, of course, the Section 1071 rulemaking, dealing with data collection for small business lending. The purpose of that data collection is to facilitate fair lending enforcement in small business lending. It's a rulemaking that I think would be very much in accord with Director Chopra's statement of the bureau's priorities under his leadership.

Chris Willis:

Then there's the Section 1033 rule making, which has to do with data aggregators and the use of consumer data. That rulemaking has not really progressed very far yet, but nevertheless, seems to strike a chord that's similar to the themes that Raj and James were talking about, with the orders to the large tech companies.

Chris Willis:

So it's not, I think, too difficult to anticipate that both of those will be prominent in the bureau's agenda. But the real question, from my standpoint, is will we see the bureau go back and revisit some already existing rulemakings, to make them more consumer protective?

Chris Willis:

The payday lending rule, for example, has been a political football that's gone back and forth based on the administration, and the leadership of the bureau. Will it go back to the way it was under Director Cordray?

Chris Willis:

And then, the debt collection rule, which was finalized about a year ago now, there was a pretty significant outcry from the consumer advocates that the debt collection rule, as finalized by the bureau late last year, didn't go far enough to protect consumers. And we've been suspicious, since that time, that there be an effort under the new administration to revisit that rule, to enact some of the protections that the consumer advocates were missing from that final rule.

Chris Willis:

Then the final thing, which, I think could be a priority for the bureau under Director Chopra, is a piece of unfinished business from when Rich Cordray was the director, and that is, an installment lending larger participant rule. The bureau hasn't done a larger participant rule in some years now, but it was on the agenda when Director Cordray resigned, having been unfinished.

Chris Willis:

Will the bureau seek to assert supervisory jurisdiction over installment lenders, as was planned, during the tail end of Director Cordray's tenure at the bureau? So Raj, what do you think? Do you think my obvious picks are right, and do you think that any of those prior rulemakings will get a revisit under Director Chopra?

Raj Date:

I'm taking the second one first. If I were a betting man, which I suppose I am, I would bet on the payday being revisited. And I personally would welcome that, at least in part, because the industry has changed pretty substantially over the course of the last several years.

Raj Date:

And I think that refreshing a consumer level research effort, if they get to the heart of some of the issues I talked about earlier, substantive transparency, normative fairness, practical suitability, I think one could do some pretty good research work now into those questions, around payday and associated products, in a way that would not have been as feasible, five or 10 years ago. So I think, both from a policy, kind of biased perspective, plus the availability of new research and analytics and insights, I would fully expect the payday rule to get revisited.

Raj Date:

I'm less sure about debt collection or some of the other things. And as between 1071 and 1033, I mean, they're both going to move forward, but my prediction is 1071 will ultimately, any downstream impacts or improvements in the marketplace, will be slow to materialize.

Raj Date:

Again, that measure that progress in something that looks more like decades, than years or quarters. But 1033, even if we don't get to a final rule any time soon, I think, is one of the most single most important sets of issues across financial services today.

Raj Date:

So I'm glad to see it being taken up. Again, I think that this director is very well suited to be at the nexus of the policy dialogue that 1033 will involve.

Alan Kaplinsky:

Hey Raj, but one thing Chris didn't mention, that I'd like to get your reaction to, as well, is arbitration. Whether you think, in light of the experience that Richard Cordray had, that is, devoting a lot of bandwidth to, to writing a rule in the area, which he had to do, the study was required by Dodd-Frank.

Alan Kaplinsky:

Then he issues the rule banning class action waivers. Then, of course, Congress jumps into the fray and they repeal the rule. You think this is something that Rohit is going to revisit, or will he basically say, "Let Congress deal with that issue?"

Raj Date:

My observation of the new director is, he's a pretty savvy character. He was at 30 years old, so the intervening decade has done nothing to blunt that.

Raj Date:

I think a relatively savvy person would do a quick calculation on risk and reward, on revisiting the arbitration questions that you raised. I think that the answer ends up being "No, no, no, no. We're not going to pick up the pencil again on this."

Alan Kaplinsky:

No?

Raj Date:

Yeah, maybe I'm wrong about it, but I would be astonished.

Alan Kaplinsky:

Okay. Now I want to go to Rich. We're now getting to, really, one of the most important areas.

Alan Kaplinsky:

Rich, I know you had three subtopics. But why don't you take it from here, and take us to the finish line?

Rich Andreano:

Sure, glad. And thank you for joining us, Raj. First, in terms a mortgage servicing, the bureau has not been subtle in its messaging to the mortgage servicing industry, that they really need to comply with all laws, including fair lending laws, when assisting borrowers facing financial hardships because of COVID-19.

Rich Andreano:

That includes placing them in forbearance, when they're nearing the end of the forbearance period, presenting all available loss mitigation options to them. And then, in fact, moving them into a permanent loss mitigation solution. And the bureau has been very clear that unprepared will be deemed unacceptable.

Rich Andreano:

In fact, it joined other regulators in withdrawing, recently, some flexibility to the servicing industry, with the message being, "You've had time to adjust to COVID-19." So what do you think, in particular, Director Chopra may do, in focusing on the mortgage servicing industry in assisting borrowers, who are facing COVID 19 hardships.

Raj Date:

I don't know that there will be much more concrete that happens, beyond kind of the pronouncements and the guidance that's already been supplied. The reason for that is mostly market driven, in my opinion.

Raj Date:

I mean, if you rewind by whatever, it's been 18 months, people, including I, were very much expecting a wave of delinquency and foreclosure, which never materialized. The fact of the matter is, unemployment is way down, and households are flush with cash, and there's a reason why credit performance looks so good.

Raj Date:

It's very difficult to amount a kind of interventionist approach with respect to a market where there is no manifest problem that has occurred. That said, I personally remain frustrated that both within mortgage special servicing and student loan servicing, that we have the same problems that we've had for a decade, which is, in order to do it right, you don't get paid enough in order to be able to handle special servicing.

Raj Date:

When you have a basic economic problem, that because credit has been so good for so long, we have just sort of ignored it. As a people, we should find that intolerable. But that said, I don't see a ton more concrete in mortgage servicing, beyond what the bureau's already done.

Rich Andreano:

Yeah, I'd agree. It's amazing that the basic economic structure of the servicing industry hasn't been adjusted to reflect the technology and human resources demands placed on them. So it is an ongoing issue.

Rich Andreano:

Another thing happened before Director Kraninger's tenure, two very significant rules in the mortgage origination area, the new qualified mortgage rule that replaced the original 43% debt to income ratio rule, and replaced it with a loan pricing structure, and then, something completely new, a seasoned loan qualified mortgage, that instead of using a loan pricing structure to get QM status, it uses a good payment history of about 36 months. Then those rules both went effective in March.

Rich Andreano:

The new QM rule was supposed to, essentially, mandatory compliance date, July 1 of this year, mainly, meaning it would be the main QM rule left. Once we hit that the patch, GC patch, would go away, the old general QM would go away.

Rich Andreano:

But the bureau under, Acting Director Uejio, proposed and adopted an extension of that mandatory compliance state, from this July to next year, October 1 of next year. Now, industry, and frankly, a number of consumer groups, opposed that, thinking that the ulterior motive of the bureau was to revisit the new general QM rule, which they like, and also, to perhaps revisit the season loan QM rule.

Rich Andreano:

But that wasn't as near and dear to the hearts, to the industry, and consumer groups very much opposed that rule. So here we are now, with a new director, in these two significant mortgage origination rules. Any of your thoughts on what the director might do, just let him stand, or may he revisit them, and tinker?

Raj Date:

It's hard to say for sure, but let me give you at least a marker or two that I would be looking for, to get a sense. And specifically, it has to do with what talent the bureau is going to bring in-house, to allow it to be an intellectual peer of the realm with FHFA, and the enterprises.

Raj Date:

Because the contours of what Fannie and Freddie are and are not going to do in the market is the most important thing, period, full stop. And the bureau, under new leadership, has the ability to get one or more real intellectual peers of the realm around mortgage capital markets, and decisioning of the enterprise intervention they're in.

Raj Date:

I think that should shape how it is that the CFPB under Chopra thinks about further tinkering from here. And I just don't know. We will see that person emerge at the bureau, or we won't. And if we do, I think it makes sense to pay a lot more attention about the intersection between FHFA and CFPB.

Rich Andreano:

Right. Yeah, it is an interesting area. One reason the industry wanted the patch to go away, because they thought it was going to interfere with the resolution of Fannie and Freddie, and wanted to drive more competition of Fannie and Freddie.

Rich Andreano:

I remember when the bureau wanted to drop the patch, and FHFA said, "Please don't do it." But they went ahead, because they thought they needed the transition. So this is a very interesting area, where the mortgage market's going to grow, and what the secondary market's going to look like, and how much the bureau and FHFA may cooperate in that area going, going forward.

Raj Date:

Yeah, I can't resist, but I just feel I need to point out the bizarro circularity in logic of using pricing to inform regulatory risk, as opposed to having pricing be an outcome of regulatory risk. So that's all I'm gonna say. I don't like it.

Rich Andreano:

It is, and it's again asking the industry to behave rationally. And that last time we thought about that, we got Dodd-Frank as a result, and it'll be interesting.

Rich Andreano:

Last area where it looks like the bureau's now going to take a different path than under Director Kraninger, was revisiting the October 2015 HMDA rule, which dramatically expanded the data points to enhance the ability of the government and other parties to assess lenders in terms of discrimination. In May of 2019, there, Kraningner, CFPB, issued an advanced notice of proposed rulemaking, basically signaling they were going to look at probably cutting back on some of the data points, and revising others.

Rich Andreano:

Then in June of this year, now the CFPB was saying, "Well, no, we're not going to pursue that rulemaking. We're going to do an assessment of the HMDA rule."

Rich Andreano:

Just last week, the bureau issued a request for information about that rule, and characterized it as discrimination in lendings. So we're moving on from just data point, we're going to use this as a lever to further enhance fair lending. That was what I gathered from the messaging.

Rich Andreano:

Your thoughts in this area? Clearly, I see this, they view it as another tool, and to combat discrimination. That seems to be clearly where they're going with it.

Raj Date:

I think that's a fair inference, from what we've seen. I also think that the fact that there's movement on 1071 also creates an opportunity.

Raj Date:

Look, we're living in an environment now where data is, it's more expensive to get rid of data to keep it. To the extent that you're going to build an operation for scale in today's environment, you can automate things on the front end.

Raj Date:

So I guess I would urge the bureau under new leadership to think about, how can we get five times the richness of HMDA and 1071 data, that we otherwise could do at one-tenth of the cost of compliance? I feel that should be the aspiration here, and I'm pretty sure it can be done with sufficient kind of attention to it, and with the right talent.

Rich Andreano:

Right? The industry, main objection, is the operational compliance with collecting and reporting the data and some of the complexity with the way the data fields were designed.

Rich Andreano:

This will be an interesting rulemaking, to see where they may move forward. Obviously, the industry are going to focus on one of the main topics, which is operational cost of compliance.

Raj Date:

Yea, yup. I mean, look, if we're going to have a system in which a human being has to somehow touch any of this, it's going to, A, be wrong, and B, be expensive.

Raj Date:

So why would one do that? In a world in which the concentration and kind of LOS platforms is so high, I feel like there's a different way to ski this particular cat.

Rich Andreano:

Exactly, exactly. Well, thank you very much. And Alan, turn it back to you.

Alan Kaplinsky:

Well, thank you, Rich, thanks, Chris, and thanks, James, for participating in today's program. And also want to thank, in particular, our special guest, Raj Date, for providing as much insight as he did today about Rohit Chopra, and where he thinks the CFPB is headed.

Alan Kaplinsky:

Let me just remind all of you, that our podcast program is a weekly program, except that we take a week off during Thanksgiving week, and then again, during Christmas week. We have 50 programs a year.

Alan Kaplinsky:

Our podcasts are available, wherever you get your podcast programming, be it on Spotify, Google Play, or you can also find it on our website. And we have all of our older podcasts also available to you.

Alan Kaplinsky:

And make sure you subscribe to our blog, which also goes by the name of Consumer Finance Monitor. It used to be called CFPB Monitor, when we began more than 10 years ago, contemporaneously with the standing up of the CFPB.

Alan Kaplinsky:

So there's a lot of material that is on our blog, and particularly, a lot of material related to the new CFPB, that is, the one that was initially managed by acting Director Uejio, and more recently, and now, for the next several years, will be managed by Rohit Chopra.

Alan Kaplinsky:

Let me just mention that very recently, I'm very proud to announce, that our podcast received an honor from an organization that rated all the social media that law firms are engaged in, including podcasts, and our podcast's programs were ranked second in the country. So, very, very proud of that.

Alan Kaplinsky:

The final thing I want to say is to thank all of our listeners today, who downloaded the program. Thank you again.