Consumer Finance Monitor (Season 7, Episode 22): An Insider's View of the CFPB

Speakers: Alan Kaplinsky and John Tonetti

Alan Kaplinsky:

Welcome to the award-winning Consumer Finance Monitor Podcast, where we explore important new developments in the world of consumer financial services and what they mean for your business, your customers, and the industry. This is a weekly show brought to you by the Consumer Financial Services Group at the Ballard Spahr Law Firm, and I'm your host, Alan Kaplinsky, the former practice group leader for 25 years, and now senior counsel of the Consumer Financial Services Group at Ballard Spahr, and I'll be moderating today's program. For those of you who want even more information, don't forget about our blog, which also goes by the name of Consumer Finance Monitor. We've hosted the blog since July 21, 2011, the day that the CFPB became operational. We also regularly host webinars on subjects of interest to those in the industry.

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I'm very pleased to tell our listeners that our podcast show was ranked by Good to Be Social as the number one podcast show among law firm podcast shows in the U.S. devoted exclusively to consumer financial services. Good to Be Social is a prominent law firm consulting firm owned by the company called Best Lawyers. We're very gratified by this recognition from one of the country's leading social media consultants for law firms. So today I have a very special guest and we're going to talk about a very special topic. We're going to be talking about an insider's view of the CFPB, and my guest today is somebody that really spent a lot of time at the CFPB and has a lot of insight, which he will be able to share with you to help you better prepare if you become subject to an enforcement action or if you're already subject, or later become subject to supervision by the CFPB.

And my guest is John Tonetti, and he is a former senior risk executive in financial services with over 30 years of executive risk and operations experience. He also served, as I said, a lot of time with the CFPB. He had been there for a period of about 10 years, and we'll get into that in a little bit. He spent over 20 years on the credit issuer side of the industry serving as a senior executive at Citigroup, American Express, Household International, and JPMorgan Chase. At Chase, John was an executive director and risk management responsible for collections governance for the consumer and community banking division. He also coordinated Chase's Risk Management Division's response to the extensive OCC consent order that was issued in 2013.

At the CFPB. John was the first program manager for debt collections in the Office of Research Markets and Regulations, and a senior policy analyst in the Office of Supervision Policy where he was a subject matter expert for debt collections and credit reporting, and he participated in a number of supervisory exams. He has extensive experience in consumer lending, risk management, operations and compliance. He was also a founder and president of First Performance Corporation, a third-party debt collector of consumer debt. So John, a very warm welcome to you.

John Tonetti:

Alan, thank you for having me. I'm honored to be on this podcast.

Alan Kaplinsky:

Okay. Well, I want to get a little more detail about your time at the CFPB. I know you were there for 10 years and I think you had told me that you were there for a period of time, left and then came back. So tell us first, when did you first go to the CFPB and why did you go?

John Tonetti:

I started with the CFPB, Alan, in 2011. I responded to an ad and I'd actually been talking with some of the people at the CFPB. A friend of mine who worked for the Federal Reserve Bank put me in touch with them when they were looking for someone that would have expertise in debt collections. So I went to work for them in December of 2011 before it actually had a confirmed director, and was the first program manager for debt collections in the Office of Regulations Markets and Research, and I was there for... I did that for close to two years. I left in 2013 to go to Chase.

Alan Kaplinsky:

Why did you leave at that time?

John Tonetti:

That's a good question. I had a son that was going to college and he went to a rather expensive college, and Chase made me an offer that would allow me to pay cash for his tuition as opposed to him or I taking on student loans.

Alan Kaplinsky:

Yeah, I see. Okay. In other words, didn't have anything to do with your dissatisfaction or unhappiness at the CFPB?

John Tonetti:

No, I was very involved. When I joined the CFPB, one of the reasons I was interested in it was that it was really the first regulator that ever did examinations of debt collections, and in talking to the people that I knew that were already there, they didn't seem to have a lot of people around that knew too much about the debt collections industry, and so I thought it would be beneficial both to me and to the industry and to the Bureau to have someone that had actually worked in the industry as an assist for whatever policies and procedures they wanted to put together in terms of examinations. In fact, I was a co-author of the first, back then they used to call them major complex policies that dealt with debt collections.

Alan Kaplinsky:

When you joined them, they had not yet issued their larger participant rule for debt collection, am I right?

John Tonetti:

That is correct. I assisted what the Office of Regulations' Tom Paul in putting together the ANPR for that. You may recall that that was issued kind of... It was issued shortly after I left, but I was involved in its actual construction before I left.

Alan Kaplinsky:

Let me ask you this, and I've always been curious from the industry side and very few industry people were at the CFPB. I mean, there have been some of course, and I know a number of them, but it's really dominated by people who were more consumer advocates, who were academics, who come from state attorney general offices, because when it got created, it was the brainchild of Elizabeth Warren and the Dodd-Frank provisions that created it, made it a very, very consumer-oriented agency. Did you feel a little bit like a fish out of water there?

John Tonetti:

Well, Alan, I spent a lot of time trying to convince people that debt collectors don't eat children for breakfast. I mean, I won't say that I was not accepted, but a lot of times I felt like I was a fish swimming upstream. When we did the major complex policy, which was basically to outline what issues the Bureau should pursue in the debt collection arena, we had two-hour meetings twice a week for almost a year to come up with this policy with stakeholders from all across the Bureau. I was the only one in that meeting that was from the industry, and we spent a fair amount of time arguing about what happened and what actually happened versus the public perception that people get from reading the New York Times and the Washington Post.

Alan Kaplinsky:

Right, right. So you were sort of the lone voice there to provide them with insight about the industry. Were you ever able to carry the day? Do you think that your time spent at the CFPB, when they were trying to decide how to do a larger participant rule, and what issues they needed to focus on when they started examining third-party debt collectors and debt buyers, if you hadn't been there, things have been a lot worse from an industry standpoint, do you think?

John Tonetti:

I'm not going to take credit for anything or blame for that matter that the Bureau does. I think that I was pretty persuasive in terms of arguing... I wouldn't say that I was an advocate for the industry, Alan, but I was an advocate for how things worked in the real world, and whether... I'm a risk manager by trade, so I'm very quantitative, and I've always believed that while the plural of anecdote is not data, if you have enough anecdotes, it can become data, and there were a lot of times where part of my argument was basically like, "How many times do these circumstances actually happen in the real world?"

And one of the things that I learned very quickly, because the Bureau is heavily populated with lawyers, was how to read case law and how to relate to case law, because I was quite often presented with, "Well, in this case this was what happened," and then I could quite come back quite often and say, "Yeah, but in this case, in this case, in this case, it went the other way." Yeah, I would like to think that I had a critical role in how entities are examined, for example, how entities are selected, as well as just giving people within the Bureau an understanding of how the industry actually worked.

Alan Kaplinsky:

Right, right. Right. Okay, so you joined the Bureau, 2000... What was it? 2011, after it was stood out, shortly after, and I take it Raj Date was... Was he the acting director at that point?

John Tonetti:

That's correct. Raj was the acting director. I believe Rich was confirmed, if memory serves, June of 2012 or something like that as a recess appointment. Yeah.

Alan Kaplinsky:

Okay. And then you left to join Chase, and you went back there. Why did you go back there? Did your kid graduate college, or?

John Tonetti:

That happened, yes, of course, but the other thing was I've always really believed in the mission of the Bureau. I mean, I think that there needs to be an advocate for the consumer side, but it needs to be balanced, and not everything a consumer tells you, and you learn this from years being in debt collection, is actually the truth, and I think that having some balance to that was very important. And being at Chase and working on the consent order, I mean, one of the...

Very early on in my tenure at Chase, the guy that was my boss at the time, we had a very extensive consent order from the OCC, and then we subsequently got another consent order, and I can't remember what it was about, but it wasn't related to what we were working on, and my boss said to me, "There's a reason that we get all these consent orders," he said, "Because we screw a lot of things up." And in some cases... And I did spend a lot of time at Chase discussing with people the fact that a 2% error rate when you have a hundred million customers affects a lot of real people, so it's not acceptable. So when an opportunity arose to go back to the Bureau and take a more active role in how entities were examined, I thought that was a really good place to go back to. My wife and I had been living in Pennsylvania and we wanted to move a little bit further south, and D.C. seemed like a good place to go, and so I lept at the chance.

Alan Kaplinsky:

So when you went back there, who was director at that time?

John Tonetti:

Rich was still director when I went back in 2016.

Alan Kaplinsky:

And then you stayed until... When did you leave?

John Tonetti:

2023 I left. I retired from federal service last June.

Alan Kaplinsky:

I see. Okay. So you were there for each of the acting directors and each of the confirmed directors, am I right?

John Tonetti:

That is correct. I have served under Raj, Rich Cordray, Mick Mulvaney, Kathy Kraninger, Dave Uejio, and Rohit Chopra most recently.

Alan Kaplinsky:

Yeah. Yeah, good. I forgot about Uejio, or Uejio. So one of the criticisms that I've had for sure, and a lot of other people in the industry have had that is that this bureau shouldn't be subject to management by only a sole director, it ought to be more like the Federal Trade Commission where there's a commission of five commissioners and it has to be bipartisan, and there's generally three from the... Whatever party controls the presidency at a particular time gets three, and the minority party gets two. CFPB hasn't done it that way, and it just strikes me as a real infrastructure weakness, I guess is maybe a way for me to put it, that depending upon who's director of the CFPB, things can change on a dime. It can do a 180, and we saw that at least as an outside observer when Mick Mulvaney came in and then Kathy Kraninger things, people weren't in the industry even though they were continuing with enforcement.

And they did. There was plenty of enforcement matters. Our firm handled a bunch of them. People weren't as afraid of the CFPB as they were during the Richard Cordray era, and now things changed again. Once Chopra was appointed as director, we went back the other way, and actually it went back further, I think, than under the Cordray regime. I'd like to get your reaction to that as an insider who was there. I'm just giving you my observation as a practicing lawyer that had to deal with the agency all the time because I had to give my clients advice, and it was very often my advice changed once the leadership changed.

John Tonetti:

Yeah, I think that's a fair observation. I have always believed that one of the faults of the Dodd-Frank Act is installing a single director who, in essence, dictates regulations to the largest financial system ever in the world, and that having in large institutions, banks, for a collection agency, the stability and the predictability and the degree to which all stakeholders have input into how the regulations affect them matters, and I think my impression and my experience was that under Raj and Rich and to a certain extent under Kathy Kraninger, within the Bureau, it was a lot more consultative. I mean, I think one of the criticisms internally of Rich was that he wanted to build a consensus, and it took a long time to get that consensus, and a lot of times things were relitigated that you thought had already been decided. I think that was one of the issues.

I mean, when I left after the ANPR was issued for the debt collection rulemaking, I never expected that if I came back three years later that the rule wouldn't have been issued by then, but I think part of that was just trying to solidify the positions and make sure that the Bureau was presenting relatively fair and balanced arguments for what it wanted to do, and I think the evidence that they did a pretty good job on the rulemaking is that nobody was 100% happy. I mean, everyone was kind of like, "Yeah, this is great for the industry, but this is not so great," and the same with the consumer advocacy side where they would say, "Well, we got this, but we didn't get this, and we think this is good, but this is terrible." So I think that's evidence that it was a good process.

My feeling was is that kind of changed, really changed under Director Chopra where... I watched recently an interview, I think it was a panel discussion, with a former colleague of mine, Kelvin Chen, in which he said, "Under Cordray and other directors, it was like the Bureau did the research, and based upon the research it did and the input that got from stakeholders struck out and made regulations, and took the input from the industry and from the consumer advocates and from the consumers that they wanted, and considered all of those positions, whereas now it almost seems as though the Bureau has already decided what it's going to do and then develops research to support its point of view."

Alan Kaplinsky:

Yeah. Well, that's the impression that I've had as an insider. I mean, you just knew, particularly with a lot of the rulemakings that the CFPB has been involved in last year and the beginning of this year, you know what the outcome is going to be as soon as you hear that they're delving into an area. It's sort of preordained and it's very frustrating, and I've heard it's been very difficult for a lot of industry people to get an audience with Director Chopra. That's not to say that he hasn't spoken with the industry, but...

John Tonetti:

I don't believe that industry representatives, and in this case I'm thinking of the Creditors Rights Attorneys Association, the ACA or RMAI. I don't know that any of them have ever actually had a sit-down meeting with the director, perhaps with some of his advisors. I'm not even sure how high they've been able to get there. My impression is that most of the time they probably get as high as John McNamara, and that's as high as they get in the organization.

Alan Kaplinsky:

Who's actually a reasonable guy. I mean, he seems to be... Didn't he come from the industry, and it seems to me like he tries to... He does listen to everybody.

John Tonetti:

Yeah, and I think that within the Bureau, my impression has been that Rohit manages very top-down, and so there is some input that comes from the bottom-up as to what impacts might certain aspects of rulemaking or certain features of rulemaking might have, but that ultimately they may not get listened to because it's not what... I mean, this weekend I was watching a Netflix documentary about Bernie Madoff, and they talked about regulatory capture of the SEC and how the SEC had looked at Bernie's operation several times and always gave it a clean bill of health because everyone liked Bernie. I think these days you have the same sort of happenstance with the consumer advocacy groups, like the consumer advocacy groups did a lot of say, and maybe they should get some say, but in my impression, the consumer advocates don't always get it right.

In 2013, we organized a joint round table with the FTC and the CFPD, and one of the things that I put together was on the second day, we had basically a sit down with the advocacy groups, the industry groups, attorneys. I'm not sure if there were any consumers there, I don't think there were. And sort of the predominant feeling before we put this together was no one's going to come out of that room without being bloodied up, that it was going to be a bloodbath, and we had a very good meeting, but I think one of the most cogent things was when one of the consumer advocacy people said, "All of my clients are our low moderate income consumers. They were all getting sued. None of them have any money," blah, blah, blah, blah, blah.

And one of the people from the industry who I think was the council for RMAI at the time, said, "Can you tell us who those people are? Because we don't want to sue those people. There's no point in us suing people that don't have any money. We're just putting good money after bad money. We don't want to sue people that don't have any money," and he also made the point that your reference point is a very narrow sliver of the population. So when you're saying, "None of my clients have any money," that doesn't mean that everyone that gets sued has no money, because it doesn't make sense to sue people with no money.

Alan Kaplinsky:

Right, right. So getting back to sort of management style, it sounds to me like when Raj was first there... And I happen to know Raj very well, I think he would've made a terrific director if he had been appointed to that position permanently. And even when Cordray was there, things were more consultative. They would seek input from all sources. I guess there would be meetings in which different people who, staff of the Bureau, had different points of view could express their points of view. The same thing with Kathy Kraninger. What happened with Chopra? Just that he feels that he doesn't need to get the input because he's already knowledgeable in the area, or he is got a small little group of people that he might tap into, but he never brings everybody together to get a consensus? Not a consensus-maker.

John Tonetti:

I did not witness Rohit making any attempts to build consensus among various stakeholders. I wasn't privy to every meeting, of course, but my impression has been that Rohit has an agenda, and it may be part of the president's all of government methodology for putting out his agenda, and so we, being the Bureau, are going to follow that agenda regardless of the downstream impacts.

Alan Kaplinsky:

Yeah. I mean, a lot of people say that, that, for example, they blame the Seila Law opinion of the Supreme Court, which gave the president the right to remove the director with or without cause, that that made the director really sort of a pawn of the president, whoever that would be at that time. Maybe it's had some effect, and I mean, in the sense certainly with respect to junk fees, I see the very, very close tie in. But I think even if Seila Law hadn't come down, and even if he could only be... Or if it came down the other way, only if the president could remove the director for cause, I don't think that would've changed Rohit Chopra. I think his agenda would've been largely the same. Do you agree?

John Tonetti:

Yeah. I think the Seila Law decision cut both ways. I mean, on the one hand, prior to Seila Law, it was once the director was appointed, he was there for five years unless there was cause to remove him, and as you can see in some of the congressional hearings that have gone on for the last eight years, it's really hard to remove someone from their office. But it gets back to your original point, which is, is a sole director the right way for a regulatory agency that governs the largest financial system that's ever existed, the right way to go? I would argue that the FTC is largely captured now too. I mean, the two minority commissioners don't seem to get too much say, but at least there's more of a discussion, at least in the press, so that people understand what the minority position is, whereas when you have a sole director, nobody knows what that is.

I mean, I think that if you look at some of the rulemaking, like the late fee rules, you see that the arguments that the Bureau presents in its discussion, they say, "Well, some people brought up this. We considered that, we reject it." Okay, what does that mean? Why do you reject it? There's no explanation.

Alan Kaplinsky:

Right. Yeah. Well, let's talk a little bit about some of the more recent rulemakings, and I guess the junk fee initiative is a good place to start. It really got my goat, and I blogged about this several times, that the labeling of a late fee as a junk fee is just, in my mind, absurd, but yet that got thrown in, and of course, in my own view, it was simply a political move that Biden decided it was a good thing to run on in terms of a platform for reelection. Nobody likes to pay junk fees, I certainly don't like paying them, but a late fee, there isn't anything that's more heavily disclosed than let's say the annual percentage rate on a loan or a credit card, right?

John Tonetti:

I would argue with you that maybe overdraft fees, which are also considered junk fees in this administration, might be more disclosed, and in fact, when this was first presented as an initiative that the Bureau wanted to undertake, I was in a meeting and I basically said to the presenter, who was a colleague of mine, "Help me understand how a feed that is not only fully disclosed, but that the consumer has to opt into is a junk fee. The consumer has to make a decision to do that." Late fees, I would agree with you that I would have a hard time categorizing late fees as junk fees. I can tell you that 30 years ago, I had no idea how they came up with an $8 late fee. I mean, that to me, there's no disclosure of how they came up with it. They said that they looked at some various economic data from the Fed that has never been used for anything like this before.

Alan Kaplinsky:

And it's never been... The industry doesn't have access to that data.

John Tonetti:

Exactly, and it's a summarization of data anyways. I mean, I can tell you having worked on consent orders and worked on interrogatories from various agencies when I was at JPMorgan Chase, that banks look at things and look at things very closely before they do anything that they're going to do, and when they talk about an $8 late fee... We would get these questionnaires from the Bureau and from the OCC, and you had everyone involved, first of all, in trying to interpret what the question means, and every bank probably goes through this, and every bank probably comes up with a different interpretation.

So categorization of expenses, I think, is really difficult to do. And the Bureau could do that. I mean, the Bureau has the authority to ask for specific information that relates to how they calculate late fees, but it didn't. It just took an arbitrary study. There's no capability. I think Andrew Nigrinis pointed this out on one of your podcasts. There was no capability for anyone to go back and audit how they got to the $8. I can tell you that 30 years ago when I worked for a large financial services firm, I ran a operating center that dealt with credit and collections, and we figured out one time that it costs us $16 for every delinquent account per month to manage delinquent accounts.

Alan Kaplinsky:

And that was 30 years ago.

John Tonetti:

That was 30 years ago. So $8 doesn't really help.

Alan Kaplinsky:

Well, it doesn't factor in deterrence. To me, a huge part of the reason why credit card issuers charged the late fees that they've been charging is that they want to deter people from being late. $8, if that's the late fee, that's just the cost of doing business. I mean, if you're trying to make a choice between what bills you pay each month, you're not going to worry about the credit card bill if it's only an $8 late fee, right?

John Tonetti:

Right, and the calculations are even kind of suspect beyond that. I mean, the Bureau disclosed that it discounted any post-charge-off collection fees. Why would you discount that? I mean, that money doesn't just happen.

Alan Kaplinsky:

So that our audience completely understands that, give me an idea or give the audience an idea, John, what that would be, a post-default collection fee, or post-collection cost, I should say.

John Tonetti:

After a credit card account defaults, there are a variety of avenues that bank or financial institution can pursue. They can try and collect it internally, so they have collectors and staff and infrastructure to support that. They can go externally, and there are really two main ways to do that. They can send it to a collection agency where they pay a commission on whatever the collection agency collects, or they can send it to a collection attorney where they pay court costs and a commission on whatever gets collected, and by the way, collecting is different from getting a judgment, so there's a cost of that as well.

Or they can sell the account, which typically a lot of financial institutions do. It gets presented, and it used to drive me crazy at the Bureau that people are buying these for pennies on the dollar, and I used to always put my hand up and say, "There's a reason why they're paying pennies on the dollar for this, because that's what they're worth." You don't collect all of it, you have cost of doing business. If it was that lucrative, everyone would be doing it, and yet you don't see that many debt buyers out there. There are a lot of debt buyers, but relative to the number of banks, there are not that many.

Alan Kaplinsky:

Right, right. Got it. Got it. Yeah, we've been talking about late fees, and we were chatting about this a little bit before we went on the air that the CFPB just took it in a chin in a lawsuit that got filed in federal court in Texas where the court very recently decided to issue a preliminary injunction against the late fee going into effect. I sometimes feel they went through it knowing they'd probably, at the end of the day, not succeed, but they didn't care. They were able to fight the good fight and that's all they wanted to do. And politically, it's probably a win for the president.

John Tonetti:

I would have to agree with you. I think that there is, under this administration at the CFPB, an attitude that we are going to do this regardless if we have the authority. I mean, I once said in a meeting that if it takes you three pages to explain why you have the authority to do something, then you probably don't, and in some cases, some of the stuff I felt... And I'm not a lawyer, but I do know how to read, and when I would see circular arguments that demonstrated that, well, we have the authority basically because we say we have the authority.

Alan Kaplinsky:

Yeah. Well, let's talk about that, John, because something that has been a real concern on the part of the industry, and it's what I call pushing the envelope. Pushing the envelope, and trying to extend the jurisdiction of the CFPB beyond that intended by Congress, and I mean, I can give you just one example and I'd like to get your reaction to it. All of a sudden, literally out of the blue, a couple years ago they decided to change their UDAAP exam manual to indicate that it covers unfairness, covers discrimination, even though they'd never said that before.

Okay, totally out of the blue, and we have federal statutes that deal with credit discrimination, Equal Credit Opportunity Act, the Fair Housing Act. Now, Fair Housing is administered by HUD, but nevertheless, they really, really pushed the envelope there, and they got whacked again by a federal court again in Texas, concluding that they went too far, that Congress didn't give them the authority to regulate discrimination under the UDAAP authority, and they're going to lose that too. You agree with me on that, that that was too far? And it's not the first time that's happened.

John Tonetti:

I can think of another good example that we already kind of discussed sort of tangentially, which is the late fee rule. There's a reason why it doesn't apply to smaller banks, and that is because the CFPB doesn't have regulatory authority over those small banks. However, if you take the big banks and you force them into an $8 late fee, what do you think the small banks are going to do? I mean, they can't compete if they're offering... They're saying, "Well, our late fee is 32." Well, which way are you going to go? Are you going to go to a small bank where if you have a late payment, it's going to cost you 32 to 40 bucks, or you going to go to a big bank that it's only going to charge you eight bucks? So they have, in essence, extended their authority by basically pushing the envelope and saying, "Well, we want to increase competition." That's not going to be competitive. I mean, they have to go to the $8 late fee.

Alan Kaplinsky:

Right, right, right. No, you're absolutely right. And of course, there's one other thing that I'm sure was a factor in their thinking, they didn't want to convene a SBREFA panel, a panel where you'd have to get input from the smaller banks. They should have done that right at the beginning if they wanted to regulate everybody.

John Tonetti:

I would agree with that, because you may recall that by avoiding that, they avoided what I would think must've been an embarrassing situation that came out of the SBREFA panel on credit reporting where that panel said, "The Bureau hasn't considered any of these things, or at least hasn't shown it's considered any of these things that these smaller furnishers had brought up in these smaller businesses, and they have to," and I have to believe that was embarrassing to the Bureau to be told by a SBREFA panel, which is a relatively captured panel, that you didn't go through the right process.

Alan Kaplinsky:

Right, right. So let's talk about a few other things because we're beginning to run out of time, but wanted to talk about CFPB's recent determination of supervisory authority over world acceptance, and if you could tell the audience what's involved in that matter.

John Tonetti:

That is a... I guess the Supreme Court would call that a resurrection of a dormant authority that under, I think it's 1031(a)(1)(C)-

Alan Kaplinsky:

I think it's 1024(a)(1)(C).

John Tonetti:

1024(a)(1)(C), thank you. ... that the Bureau can, based upon, I think it's reasonable determination that an entity is a risk to consumers, and I called that kind of the Nice Little Business You Got Here, Shame If Something Happened to It Clause. The Bureau has taken the approach that it will tell entities that they think that they pose a risk to consumers and would like them to agree to be supervised by the CFPB, and so they have a choice. They can say, "Yes, I agree to be supervised," and then they get subject to the Bureau's supervision authority, and oh, by the way, the cost benefit to that, I think the Bureau uses a number of... An supervisory exam costs an entity $25,000, which I have no idea how they arrived at that figure, but I can tell you it's a lot more than that. It has to be.

Anyway. If you don't agree, then the CFPB just says, "By the way, we think Alan Kaplinsky is a risk to consumers, and therefore we're going to assert our authority to supervise them anyways." Now, whether you're a risk to consumers or not, they've already said you're at risk, so where do you go to get your reputation back?

Alan Kaplinsky:

Yeah. I mean, it's you've been tried and convicted without any-

John Tonetti:

And I think the thing is, getting back to World Acceptance, is that... I mean, to me, that was a tremendously interesting read because World Acceptance pointed out that, "By the way, you guys were here, you did an enforcement action, it resulted in no action. How is it that a couple of years later, you now think we're a risk?" And the basic attitude was, "Well, that was under a different regime, and now we're back and we think you're a risk." The other thing that I thought was really fascinating is, and it kind of came out in a recent publication from the Bureau about limiting the amount of pages that you can write in your defense to that determination, but if you read the World Acceptance Order, there are many times where the CFPB said, "Well, that wasn't something that they brought to us when we told them that we were going to supervise them, so we're discounting that argument now." Well, if you tell me I can't say something and then say, "Well, you never said that because I told you not to," again, that's sort of a circular pattern that you find in a lot of CFPB documents.

Alan Kaplinsky:

We had a client that got a letter from CFPB saying that they had made a determination that they wanted them to be subject to supervision, and the client thought long and hard about what to do there, really thought the CFPB was off-base, but ultimately caved in. They just felt, you're going to fight a battle, but you're going to be convicted if you fight it, because the media is going to pick up on it and people will think you're bad. It's one of these things that it's a very unfair process, it lacks due process, and it had not been used until Rohit Chopra became director.

John Tonetti:

Right. I mean, I think that the determination that companies make is, "How long am I going to fight this battle? And even if I win, what's the outcome of that?" And Casey Stengel said you don't pick fights with people that buy ink by the drum. You don't pick fights with regulatory agencies that basically can print their own money, and they're going to outlast you. I mean, I think the late fee and the overdraft fee may have been a battle that the CFPB has picked on that people are willing to fight because it does have a profound impact upon the financial stability of the banking industry. And oh, by the way, the CFPB isn't concerned with safety and soundness, so that's not even a consideration. So I think that in this case, they might've tried to gore an ox that might be too big.

Alan Kaplinsky:

It's interesting. They always say... I think they're required to consult with the prudential regulators before they adopt a regulation, the FDIC, the Fed, the comptroller, but they never say how they consulted with them and what input they got from them, they just say in the federal register, like checking off one of the boxes, "We consulted with the federal prudential regulators," period.

John Tonetti:

Well, I think... Didn't Rohit recently come out and castigate one of the prudentials for working too slowly?

Alan Kaplinsky:

He certainly did.

John Tonetti:

I can't remember what it was regarding.

Alan Kaplinsky:

Oh, he's a member of the FDIC board of directors, and he castigated them. He wrote a separate opinion, basically castigating the FDIC, his own agency, and the other agencies who were supposed to work on a regulation promulgated under Dodd-Frank reining in incentive compensation.

John Tonetti:

Oh, that's right. Yes.

Alan Kaplinsky:

Yeah, I got a kick out of that, and I couldn't resist writing a blog, which I did, saying, "Those who live in glass houses shouldn't throw stones." Dodd-Frank contained 1071 of Dodd-Frank, requiring that there be a rulemaking with respect to data collection related to small business loans made to women and minority-owned enterprises, and it took many, many years, almost 13 years, for that regulation to get finalized, and of course, that's now subject to a lawsuit as well. What about consumer reporting, particularly medical debt, the proposed rule on consumer reporting? I'm wondering if you have any reaction there.

John Tonetti:

Yeah, one of the things that... And I said this quite frequently at the Bureau, is on the one hand, the Bureau talks about ability to repay when it comes to payday loans and how part of the original payday loan had this requirement, the payday lenders evaluate the ability to repay. When you take medical debt off of a credit report, you've just taken away a huge factor in trying to evaluate ability to repay. The Bureau maintains, and I have disagreed with this since the report was first issued, that medical debt is not predictive of credit performance. The Bureau's own report that they refer to, which is... Well, it was based on 2009, 2010 data. So it's, what, 13, 14 years old? That report doesn't say that. In fact, it almost says the opposite because in doing their analysis, the Bureau couldn't find credit reports that only had medical debt on them. So what they had to do was they separated them between mostly medical debt and mostly non-medical debt.

So if you had five credit card collections and six medical collections, then you were mostly medical. But the fact that there couldn't find enough to do that evaluation shows that there's a very high correlation between medical collections and other collections. The other thing that I've often disputed is, sure, there are people, and you hear the stories, and I probably know some people that have been in this situation that they can't afford to pay their medical bills because they have a major catastrophe, but the Bureau in their own reporting has shown that the average medical debt is somewhere around 500 bucks. I mean, I am certain that that is a catastrophe for a lot of people, but it's not an insurmountable catastrophe. So you're basically making a rule to accommodate one type of debt that is probably highly predictive.

And the fact of the matter is Alan, that when you remove the medical debt, it's one factor in a multivariate analysis that predicts credit worthiness, and the Bureau published a report that said removing medical debt will raise in some consumers their credit score by as much as 20 points, which is significant, but it doesn't. Changing that credit score doesn't make the model more predictive, it makes it less predictive, and it doesn't make that consumer more credit-worthy, it just distorts the model. So I think that by the CFPB's own admission, removing medical debt actually benefits very few people, it's to the detriment of medical service providers. I mean, the CFPB hasn't really dealt with how medical providers are supposed to get paid, and I know there's a lawsuit in California that's suing the CRAs for removing debts under $500.

I found it interesting, I think the general counsel for the Bureau gave a speech in front of some consumer advocacy group and was talking about there's no reason for healthcare providers to use credit reports, they have other avenues to collect, and I was sitting there thinking, "Well, wait a second. There are laws that say that they can't start collecting until six months to a year after the consumer's been billed," so that precludes collection agencies for a long period of time. I can't put it on their credit report, so there's no way to notify the consumer that they even owe the debt to send them periodic statements. What's left? I can sue them. Does the Bureau really want more consumers to be sued? I don't think so. That was not my perspective when I was there.

Alan Kaplinsky:

Right, right. Final thing I want to, before we wrap things up, John, is get your reaction to an amicus brief that they filed in the Carrasquillo case. I hope I pronounced it correctly. Tell us about that, and I know failed to mention something in that brief that it's pretty important.

John Tonetti:

That was a really interesting amicus brief, and maybe I shouldn't be reading all this stuff because it just makes me crazy, I'm supposedly retired, but in it, the case basically revolved around the consumer that was claiming that there was a violation of the FDCPA because he had filed bankruptcy. However, he never notified the collector that he had filed bankruptcy, and so the collector tried to collect, so he sued the collector. Well, in Carrasquillo, the district court said the consumer has a responsibility to advise the collector that he had filed bankruptcy, and in fact, section 1692g of the FDCPA says, "If you don't dispute this within 30 days in writing, we can assume that the debt is valid," and the CFPB totally left that out of their amicus brief, which really blew me away because the district court spent three or four pages discussing the consumer's responsibility, and the CFPB totally ignored that, and to me that was...

Alan Kaplinsky:

Well, it borders on being unethical, doesn't it? You have to be candid. There's an obligation to be candid with the court.

John Tonetti:

Exactly. I mean, I would say that if the CFPB were an opposing attorney, I could see the CFPB advising the court or saying to the court all the reasons that they put in their amicus brief, but they're not, they're a government body that is supposed to regulate on behalf of consumers writ large, and to totally ignore a critical piece just smacks of, "We're putting our finger on a scale and tipping it the way we want it to go, regardless of what the law says."

Alan Kaplinsky:

Right. Right. Yeah. Well, that's how an agency loses credibility with the court pretty quickly, and... Did you ever write a blog about that, or has anybody ever written a blog about that?

John Tonetti:

I put a short blurb on LinkedIn about it and how I was amazed that they could totally ignore that. I don't recall whether I got any responses to it, but I might have probably got some responses from debt collectors that said, "Yeah, how can you totally leave that out?" But I mean, it's a very critical piece of the FDCPA that gets cited and that the CFPB examines for virtually in every debt collection exam.

Alan Kaplinsky:

Yeah. Okay. Well, John, we've covered a lot of territory today, and time has gone by very quickly because we have come to the end of our program, and first, I want to really thank you a great deal for being a guest on our program and for sharing to the extent that you're able to, your experience of the CFPB and a lot of insights that you have. So again, my pleasure.

John Tonetti:

Thank you very much for having me. I would like to say that the mission of the CFPB, I think, is a good one. I think how it is being performed, it lacks credibility. I mean, I enjoyed my time at the CFPB for the most part, I worked with a lot of good people who really want to do the right thing. I can't say that about everyone at the CFPB, however.

Alan Kaplinsky:

Right, right. Got that. Okay. To make sure you don't miss any of our future episodes, please subscribe to our show on your favorite podcast platform, be it Apple, YouTube, Spotify, wherever you listen to your podcasts, and don't forget to check out our blog, consumerfinancemonitor.com for daily insights about the consumer finance industry, and if you have any questions or suggestions for our show, please email us at podcast, that's singular, at ballardspahr.com, and stay tuned each Thursday for a new episode of our show. Thank you very much for listening, and have a good day.