

B2B or Not B2B, That Is the Question: The CFPB and Applicability of Federal Consumer Financial Laws to Small Business and Business-Purpose Lending

Nearly five years after announcing it would “expeditiously” implement provisions of the Dodd-Frank Act concerning data collection on small business lending, the Consumer Financial Protection Bureau (“CFPB” or the “Bureau”) finally seems to be taking action. Not only is it moving to promulgate the required regulations, but it has placed fair lending to the small business community among its top 10 priorities. As the CFPB begins to focus on aspects of small business and business-purpose lending, this Legal Update describes the scope of the Bureau’s authority over the industry.

Section 1071 of the Dodd-Frank Act amended the Equal Credit Opportunity Act (ECOA) to require creditors to collect, and report to the CFPB, certain information designed to effectuate federal fair lending laws with respect to women-owned, minority-owned and small businesses.¹ On April 11, 2011, the CFPB issued guidance indicating that obligations under Section 1071 would not go into effect until the Bureau issued implementing regulations, which it indicated it would do “expeditiously.”² To date, however, the CFPB has not promulgated so much as a proposed rule implementing the Section 1071 amendments.

But movement seems to be afoot on the matter. After first appearing on the CFPB’s Fall 2015 regulatory agenda,³ the Section 1071 implementation has been carried over to the

CFPB’s 2016 rulemaking agenda, in which the Bureau indicated it was in the “very early stages” of the implementation process and would focus on outreach and research that would eventually lead to a proposed rulemaking.⁴ In addition, in February 2016, the CFPB announced that ensuring fair lending in the small business lending market will be one of nine top priorities over the next two years.⁵ The CFPB stated that it intends to create a small business lending team and begin market research and outreach for a rulemaking on business lending data collection, to build the infrastructure to intake and analyze small business lending complaints and to continue to examine small business lenders for compliance with fair lending laws.⁶ The Bureau is also among the federal agencies identified by the US Treasury Department in a proposal to coordinate efforts to regulate online marketplace lending, one element of which would be consideration of the extent to which consumer protection laws apply to, or should be expanded to cover, small business and business-purpose lending.⁷

This Legal Update draws out the boundaries of CFPB jurisdiction over small business and business-purpose lending based on the statutory authority granted by the Dodd-Frank Act. The first section defines important terms under the Dodd-Frank Act that affect the CFPB’s authority over small business and business-purpose lending and includes an analysis of the “Federal

consumer financial law” applicable to typical forms of small business and business-purpose lending. The second and third sections then address the reach of the Bureau’s supervisory and enforcement authorities, respectively.

Applying “Consumer Financial Products and Services” and “Federal Consumer Financial Law” to Small Business and Business-Purpose Lending

CONSUMER FINANCIAL PRODUCTS AND SERVICES

Under the Dodd-Frank Act, the scope of the CFPB’s supervisory and enforcement authorities is substantially constrained by the definition of “consumer financial products and services.” As described in more detail below, the term plays a significant role in determining (i) whether a nondepository entity will be supervised by the CFPB; (ii) the breadth of the CFPB’s examination authority for entities—including both depositories and nondepositories—that it supervises; and (iii) the claims the CFPB may investigate and pursue under its enforcement authority.

The Dodd-Frank Act defines “consumer financial product or service” to include “any financial product or service that is described in [certain sections of the Dodd-Frank Act] and is offered or provided for use by consumers *primarily for personal, family, or household purposes.*”⁸ Therefore, small business and business-purpose lending would fall outside the scope of the term “consumer financial product or service” in most cases, as the product or service would not be offered or provided primarily for personal, family or household purposes.

The CFPB, however, has relied on broad interpretations of a company’s business activity to assert jurisdiction in the past. In 2015, J.G. Wentworth filed a petition to set aside a Civil Investigative Demand (CID) issued by the

CFPB.⁹ It argued, in part, that it did not offer or provide a “consumer financial product or service” because its product—“purchasing future streams of income, such as structured settlement and annuity payments”¹⁰—was a purchase of receivables rather than a loan or other extension of credit and therefore did not fall within any of the categories of “financial products or services” enumerated by the Dodd-Frank Act.¹¹ The CFPB rejected J.G. Wentworth’s petition on multiple grounds, including that the company could be “providing financial advisory services ... to consumers on individual matters [or relating to proprietary financial products or services].”¹² Specifically, the CFPB noted that certain requirements in connection with a federal tax exemption imposed an obligation on the company to determine that any given purchase of a structured settlement was “in the best interest of the payee, taking into account the welfare and support of the payee’s dependents,” and reasoned that the company may be providing consumers with financial advisory services as part of meeting that obligation.¹³

The CFPB has not publicly relied on similar arguments in connection with small business lending to date. Nevertheless, even companies whose core products and services do not appear to be “consumer financial products and services” may find value in reviewing the manner in which they market and originate products to evaluate whether any prongs of the definition, including “providing financial advisory services,” could be stretched by the CFPB to include their business activities.

FEDERAL CONSUMER FINANCIAL LAW

The scope of the CFPB’s supervisory and enforcement authorities also depends, in large part, on the extent to which an entity’s business activities implicate the requirements of a “Federal consumer financial law.”¹⁴ A “Federal consumer financial law” is defined to include the

Dodd-Frank Act (including the prohibition on unfair, deceptive or abusive acts or practices [UDAAPs]), as well as certain “enumerated consumer laws.”¹⁵ The “enumerated consumer laws” are:

- Alternative Mortgage Transaction Parity Act of 1982 (the “Parity Act”);
- Consumer Leasing Act of 1976 (CLA);
- Electronic Fund Transfer Act (EFTA);
- Equal Credit Opportunity Act (ECOA);
- Fair Credit Billing Act (FCBA);
- Fair Credit Reporting Act (FCRA);
- Homeowners Protection Act of 1998 (“HPA” or “PMI Act”);
- Fair Debt Collection Practices Act (FDCPA);
- Certain subsections of Section 43 of the Federal Deposit Insurance Act;
- Certain sections of the Gramm-Leach-Bliley Act (GLBA);
- Home Mortgage Disclosure Act of 1975 (HMDA);
- Home Ownership and Equity Protection Act of 1994 (HOEPA);
- Real Estate Settlement Procedures Act of 1974 (RESPA);
- S.A.F.E. Mortgage Licensing Act of 2008 (SAFE Act);
- Truth in Lending Act (TILA);
- Truth in Savings Act (TISA);
- Mortgage Acts and Practices Rule (MAP Rule); and
- Interstate Land Sales Full Disclosure Act. (ILSFDA)¹⁶

Most of these laws have little or no applicability to small business or business-purpose lending. Several, such as TISA and ILSFDA, do not relate to the provision of credit products. Others, such as TILA and RESPA, do not apply to activity that is primarily for business, commercial or agricultural purposes.¹⁷ Small business lending should not fall within the scope of these laws,

although lenders should be careful to classify their lending activity appropriately by developing an understanding of how their customers will use loan proceeds. Well-papered loan files, including certifications or affidavits regarding loan use from borrowers, co-borrowers and/or guarantors, may allow a lender to provide better defenses should the business-purpose nature of its activities be challenged by a regulator or in court.

Certain Federal consumer financial laws, however, are not expressly limited to consumer-purpose transactions and may apply to some or all small business lending activity. Of the Federal consumer financial laws, ECOA is the most broadly applicable to business-purpose lending. Disclosure requirements under ECOA are relaxed somewhat for business lending,¹⁸ but the remainder of ECOA’s requirements, including anti-discrimination requirements and requirements regarding appraisals of residential property, apply regardless of loan purpose. Moreover, information collection requirements under Section 1071 of the Dodd-Frank Act will eventually apply specifically to small business lending once the CFPB finalizes regulations on the matter.

Other Federal consumer financial laws potentially applicable to small business or business-purpose lending in certain circumstances include:¹⁹

- EFTA—potentially applicable if loan payments are received by electronic fund transfer from a consumer account, rather than a segregated business account;²⁰
- FCRA—potentially applicable if a party involved in small business or business-purpose lending activity obtains, or furnishes information to, an individual’s credit report that may be used in connection with consumer-purpose lending, determinations regarding employment or other permissible purposes for use of consumer reports under FCRA;²¹

- GLBA—potentially applicable if a party involved in small business or business-purpose lending activity (i) is a “financial institution under the GLBA” and (ii) engages in such activity with a borrower to whom it also offers or provides consumer-purpose financial products or services;²²
- HMDA—potentially applicable if a party involved in small business or business-purpose lending activity extends dwelling-secured credit;²³
- HPA—potentially applicable if a party involved in small business or business-purpose lending activity extends credit secured by the borrower’s principal residence;²⁴ and
- UDAAP—potentially applicable if the CFPB were to determine that an aspect of small business or business-purpose lending activity constituted a “consumer financial product or service,” although such application would likely require a creative application of the term to the specific facts of a given small business or business-purpose lending program.²⁵

The CFPB’s Supervisory Authority

The Dodd-Frank Act imbues the CFPB with a multipronged supervisory authority. Section 1024 of the act provides the CFPB with the authority to supervise certain nondepository “covered persons,” including: (i) participants in certain consumer-purpose mortgage-related activities; (ii) larger participants, as defined by rule, in markets for other consumer financial products or services; (iii) persons determined, after notice and a reasonable opportunity to respond, to pose risk to consumers in connection with the offering or provision of consumer financial products and services; (iv) participants in the private education loan market (as defined by, and subject to, the federal Truth in Lending Act (TILA), which inherently limits such participants to those offering consumer-purpose loans²⁶); or (v) participants in the payday

lending industry.²⁷ Section 1025 of the act then provides additional supervisory authority over certain “very large banks, savings associations, and credit unions” and their affiliates.²⁸

Under either section, the CFPB’s supervisory authority extends to examinations assessing compliance with Federal consumer financial laws, obtaining information about activities subject to such laws and associated compliance management systems or procedures, and detecting and assessing risks to consumers and to markets for consumer financial products and services.²⁹ Accordingly, the applicability, if any, of the CFPB’s supervisory authority to small business lending depends in substantial part on the definitions of “covered person” (for nondepositories), “consumer financial products and services” and “Federal consumer financial law.” As noted above, “covered person” and “consumer financial products and services” are limited in scope to consumer-purpose activity. “Federal consumer financial law,” however, is defined to be an enumerated set of laws and regulations, some of which are applicable, in whole or in part, to small business and business-purpose lending.

Once the CFPB has supervisory authority over an entity, its ability to examine for compliance with “Federal consumer financial law” or to assess the strength of associated compliance management systems or procedures is not expressly limited by statute to the entity’s “consumer financial products and services.” An entity that is supervised because it engages in consumer-purpose activity or because it is a “very large” depository institution arguably may be examined across its entire scope of activities that relate to compliance with “Federal consumer financial law,” including those laws that apply to small business and business-purpose lending. Moreover, understanding the compliance implications of certain small business and business-purpose lending practices may require developing a relatively complete understanding of the product, as well as how it is

offered or provided to its intended market. Therefore, while a compliance examination may be targeted at developing facts necessary to evaluate compliance with a limited scope of “Federal consumer financial law” that has some applicability to small business and business-purpose lending, it may be difficult to limit examination inquiries to a narrower set of business practices than would be assessed in a full-fledged examination (such as one might expect the CFPB to conduct in connection with true consumer products and services).

A company that offers both consumer financial products and services and small business or business-purpose lending may find itself within the scope of the CFPB’s supervisory authority for its traditional consumer-facing activities. If that occurs, the CFPB may have authority to examine the company’s small business or business-purpose lending activities to evaluate risks related to consumer financial laws and regulations, some of which apply in whole or part to small business or business-purpose lending.

The CFPB’s Enforcement Authority

Sections 1051 through 1058 of the Dodd-Frank Act structure the CFPB’s enforcement authority. In general, Section 1052 provides the Bureau the authority to investigate *any person* who may have information relevant to a violation of any Federal consumer financial laws;³⁰ Sections 1053 and 1054 carry forward similar authority through the administrative adjudication and litigation phases of enforcement;³¹ and Section 1031 makes these powers available to effectuate the act’s prohibition on UDAAPs in connection with consumer financial products and services.³² Essentially, therefore, the applicable limitation on the CFPB’s enforcement authority in connection with small business and business-purpose lending is the extent to which the Federal consumer financial laws and the prohibition on UDAAPs may be applied to such

lending, as described in the “Federal Consumer Financial Law” section above.

Conclusion

The CFPB’s authority over small business lending does not extend quite as far as its expansive authority over consumer lending, but the Bureau nevertheless represents a risk that business-purpose lenders should consider. The CFPB may find it difficult to establish supervisory authority over entities solely engaging in business-purpose lending, but entities it supervises for other reasons (i.e., because they also offer certain consumer financial products and services or because they are very large depositories) may be subjected to examinations that evaluate compliance within their business-purpose lending activity. Additionally, the CFPB’s enforcement authority may result in investigations of, and enforcement proceedings against, small business and business-purpose lenders with respect to the subset of Federal consumer financial laws applicable to such activities.

While small business and business-purpose lenders cannot eliminate all exposure to the CFPB and the laws it administers, they may take steps to mitigate risks. First, they may assess the terms and market positioning of their products to determine which Federal consumer financial laws may apply to their current activities. As several of the Federal consumer financial laws that may apply to small business and business-purpose lending do so only through application of relatively narrow triggers (such as lending to individuals or upon the security of principal residences), modifying products to avoid application may be possible without substantial business impact in some cases. Second, they may strengthen their ability to support their exemption from certain laws by establishing written policies around the triggering conditions for the applicability of Federal consumer financial laws and enhancing documentation of the nature of their borrowers and/or the

business purpose behind any given extension of credit. Finally, they may proactively establish the levels of compliance management expected of consumer lenders, at least with respect to the Federal consumer financial laws applicable to their lending activities.

Entities already subject to the CFPB's supervisory authority, such as very large depositories, may find additional exposure to the CFPB within their small-business-credit lines of business to represent a marginal risk. If so, modifying products and practices to avoid triggering application of Federal consumer financial laws may not always be worth the business impact as long as acceptable consumer compliance structures exist enterprise-wide. On the other hand, other entities, including those involved solely in business-purpose lending activity, may see more leverage in avoiding application of some Federal consumer financial laws altogether. Regardless of the approach taken, a clear plan for managing compliance risk will become increasingly important as the CFPB progresses in its approach to small business lending and as other regulators at the federal and state levels continue to consider the appropriate level of regulation to apply to the industry.

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Endnotes

- ¹ See 15 U.S.C. § 1691c-2.
- ² Letter from CFPB to Chief Executive Officers of Financial Institutions under Section 1071 of the Dodd-Frank Act, "Section 1071 of the Dodd-Frank Act," 1 (April 11, 2011) available at <http://files.consumerfinance.gov/f/2011/04/GC-letter-re-1071.pdf>.
- ³ "Fall 2015 Rulemaking Agenda," CFPB, <http://www.consumerfinance.gov/about-us/blog/fall-2015-rulemaking-agenda/> (Nov. 20, 2015).
- ⁴ "Spring 2016 Rulemaking Agenda," CFPB, <http://www.consumerfinance.gov/about-us/blog/spring-2016-rulemaking-agenda/>.
- ⁵ Consumer Financial Protection Bureau, "Policy Priorities Over the Next Two Years" (Feb. 25, 2016), available at http://files.consumerfinance.gov/f/201602_cfpb_policy-priorities-over-the-next-two-years.pdf.
- ⁶ *Id.*
- ⁷ See "Opportunities and Challenges in Online Marketplace Lending," U.S. Treas. Dep't, 28, 32, https://www.treasury.gov/connect/blog/Documents/Opportunities_and_Challenges_in_Online_Marketplace_Lending_white_paper.pdf (May 10, 2016) (suggesting more robust small business borrower protections and the facilitation of interagency cooperation through the creation of a standing working group for online marketplace lending, among other recommendations).
- ⁸ 12 U.S.C. § 5481(5) (emphasis added). Additionally, note that the term "consumer" is defined to mean "individual or an agent, trustee, or representative acting on behalf of an individual," and does not carry with it any independent limitation of the scope of Dodd-Frank Act provisions to activity for personal, family, or household purposes. 12 U.S.C. § 5481(4).
- ⁹ J.G. Wentworth's Pet. to Set Aside Civil Investigative Demand, In re *J.G. Wentworth, LLC*, 2015-MISC-J.G. Wentworth, LLC-0001 (CFPB Oct. 2, 2015), available at http://files.consumerfinance.gov/f/201602_cfpb_petition-to-set-aside-civil-investigative-demand-jg-wentworth-llc.pdf.
- ¹⁰ *Id.* at 2.
- ¹¹ See *id.* at 9.
- ¹² CFPB's Decision and Order on Pet. by J.G. Wentworth, LLC to Modify or Set Aside Civil Investigative Demand, In re *J.G. Wentworth, LLC*, 2015-MISC-J.G. Wentworth, LLC-0001, 3 (CFPB Feb. 11, 2016) available at http://files.consumerfinance.gov/f/201602_cfpb_decision-and-order-on-petition-by-jg-wentworth-llc-to-modify-or-set-aside-civil-investigative-demand.pdf.
- ¹³ See *id.*
- ¹⁴ See 12 U.S.C. §§ 5481(14); 5563-5564.

¹⁵ 12 U.S.C. § 5481(14).

¹⁶ 12 U.S.C. § 5481(12).

¹⁷ See 12 U.S.C. § 2606(a)(1), 15 U.S.C. § 1603(1).

¹⁸ See 12 C.F.R. § 1002.9(a)(3).

¹⁹ While not the focus of this Legal Update, note that laws administered by federal agencies other than the CFPB (such as anti-money laundering requirements, sanctions requirements and the Fair Housing Act) and state laws regulating financial activities (such as licensing obligations, interest rate and fee restrictions, mandatory and prohibited contractual terms, and required disclosures) may apply, in whole or in part, to small business and business-purpose lending. Determining the appropriate set of laws applicable to any given business credit product may require assessment of product terms, borrower characteristics and the manner in which the product is offered.

²⁰ See 12 C.F.R. §§ 1005.2(b)(1) (defining “account” to be limited to an account “established primarily for personal, family, or household purposes”) and 1005.3(a) (limiting the scope of the regulation to “any electronic fund transfer that authorizes a financial institution to debit or credit a consumer’s account”).

²¹ See 15 U.S.C. § 1681a(c)-(d) (defining “consumer” and “consumer report”).

²² See 15 U.S.C. § 6809(3), (4), (9) (defining “financial institution,” “nonpublic personal information” and “consumer”).

²³ See 12 C.F.R. § 1003.2 (defining terms relevant to the coverage of HMDA without distinguishing between consumer-purpose and business-purpose lending). See also, M. Brody, C. Shelton, and S. Schoenfeld, “HMDA and Revised Regulation C: Guidance for Multifamily Lenders” (March 31, 2016), available at <https://www.mayerbrown.com/files/Publication/7da7252d-4a1e-4cd2-b43f-5a4a42af90b2/Presentation/PublicationAttachment/f1494cf4-1160-4826-867c-fe302a51bb56/160331-UPDATE-FSRE.pdf>.

²⁴ See 12 U.S.C. § 4901(15) (defining “residential mortgage transaction”).

²⁵ See 12 U.S.C. §§ 5531(a) and 5536(a)(1)(B) (establishing the CFPB’s authority with respect to UDAAPs).

²⁶ See 12 C.F.R. § 1026.3(a)(1) (excluding business-purpose lending from the scope of TILA regulation).

²⁷ 12 U.S.C. §§ 5514-5516.

²⁸ The supervisory authority for banks, savings associations and credit unions extends to any insured depository institution or credit union with total assets exceeding \$10 billion and any affiliate thereof. 12 U.S.C. § 5515(a).

²⁹ See 12 U.S.C. §§ 5514-5516.

³⁰ 12 U.S.C. § 5562(c)(1) (emphasis added).

³¹ 12 U.S.C. §§ 5563-64. The CFPB’s authority to initiate “cease-and-desist proceedings,” however, is limited to “covered persons.” *Id.*, § 5563(b)(1)(A). The scope of the CFPB’s administrative enforcement authority under section 5563(a)—which is applicable to “any person”—is not entirely clear, as the statutory provisions describing administrative enforcement are all contained in section 5563(b).

³² 12 U.S.C. § 5531.

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