CFPB Brings Payday Blues with Final Ability to Repay Rule

On October 5, 2017, the Consumer Financial Protection Bureau (CFPB) released its much-anticipated rule regulating payday and other small consumer loans ("Payday Lending Rule" or "Rule").

The core of the Payday Lending Rule is a new ability-to-repay underwriting requirement for short-term loans and certain longer-term balloon loans. The rule also imposes payment processing restrictions on a broader set of short-term and longer-term higher-interest loans and creates a set of information furnishing, disclosure and compliance management requirements to support its more substantive requirements.

A variety of stakeholders are likely to feel the effects of the Payday Lending Rule—in some cases, as much for what the CFPB left out as what it included. One welcome development in that regard, as explained below, is that the rule will not impose its ability-to-repay requirement on longer-term loans unless those loans have a balloon payment. In the CFPB's 2016 proposal, longer-term loans would have been subject to an ability-to-repay requirement that was structured similarly to that for short-term loans; however, the CFPB admitted in the final rule that its concern about re-borrowing for longer-term loans was focused primarily on longer-term balloon loans. Payday lenders may be able to shift from traditional deferred presentment check products or short-term, single-payment loans to longer-term installment loans, where permissible under state law.[1] Other options available for payday lenders may include limiting activity to certain loans that the CFPB "conditionally exempts" from its underwriting rules (as explained below), or developing partnerships with banks issuing credit cards, which are exempt from the rule and subject to ability-to-repay requirements that may not be as burdensome.

The 21 months before the rule becomes effective leaves time to ponder many potential legal and political obstacles. For instance, although Congress is bogged down with other issues, it could still vent its frustrations with the CFPB by enacting a resolution to scrap the rule. Industry group plaintiffs could sue to challenge the agency's first use of its authority to prohibit unfair, deceptive, or abusive acts or practices. In any event, it appears that this time the CFPB heeded calls for regulatory relief from smaller community banks and credit unions, which can take advantage of certain exemptions under the rule to accommodate their customers who need emergency cash.

In this Legal Update, we describe the requirements imposed by the Payday Lending Rule and its potential effects on creditors offering payday loans and/or payday alternative credit products, as well as the broader consumer financial industry.

What Types of Loans Does the Rule Cover?

COVERED LOANS

While this Legal Update often refers to the CFPB's rulemaking as the Payday Lending Rule, the rule covers any short-term loan and longer-term loan with a balloon payment feature. In addition, certain parts of the rule apply to longer-term, higher-cost loans if the lender has a right to withdraw payments from the borrower's account, addressing the Bureau's concern that after two consecutive failed attempts to withdraw funds from an account, further attempts are not only unlikely to succeed but also would clearly impose harms on affected consumers.

The proposed rule would have subjected longer-term, higher-interest loans to a similar underwriting requirement as was proposed and ultimately adopted for short-term loans and longer-term balloon loans. The CFPB declined to impose additional underwriting requirements on other longer-term loans, although it warned that it may revisit such a requirement in the future.

Specifically, for purposes of the ability-to-repay requirement, a "covered loan" generally means a consumer-purpose extension of credit (other than those that are excluded as listed below) that the consumer must substantially repay within 45 days of consummation (or must repay an advance within 45 days of the advance). In addition, a "covered loan" generally includes a longer-term loan (more than 45 days) when the consumer must repay substantially the entire balance of the loan (or an advance on a loan) in a single payment or through at least one payment that is more than twice as large as other payment(s).

The rule also addresses loans for which the cost of credit exceeds 36 percent per year and that provide for a "leveraged payment mechanism," although such loans are not subject to the ability-to-repay requirement. In this regard, the CFPB offered another surprise, dropping its proposed "cost of credit" calculation in favor of the more familiar annual percentage rate (APR). The CFPB had originally proposed a calculation of the cost of credit similar to that used under the Military Lending Act, which would include amounts otherwise excluded from the APR (e.g., charges for credit insurance, debt cancellation, or debt suspension plans, application fees or plan participation fees). The Bureau decided, however, that since the cost-of-credit threshold is relevant under the final rule only to impose payment restrictions on certain longer-term loans, lenders would be less likely to "modify their fee structures simply to avoid application of those provisions,"[2] so sticking with an APR calculation would be sufficient. As explained below, the rule imposes limits on the lender's ability to use such a mechanism.

As under the proposed rule, a leveraged payment mechanism is a right to initiate a transfer of money from a consumer's account, other than by initiating a single immediate payment transfer at the consumer's request.

LOANS NOT COVERED

As indicated above, the rule generally imposes an ability-to-repay requirement on short-term loans and longer-term balloon loans. However, certain types of consumer credit are excluded from that requirement, and certain other types of loans are considered "conditionally exempt."

Excluded Loans

First, the following types of products are exempt from the Payday Lending Rule in its entirety (although of course other regulations, including certain ability-to-repay requirements, may otherwise apply):

- Purchase money loans: credit extended for the sole and express purpose of financing a consumer's initial purchase of a good when the credit is secured by the property being purchased.

- Mortgage loans: credit secured by any real property (or personal property used as a dwelling).
- Credit cards.
- Student loans.
- Non-recourse pawn loans.
- Overdraft services and overdraft lines of credit.
- Wage advance programs.
- No-cost advances.

In connection with purchase money loans (the first type of exclusion listed above), the final rule clarifies that such a loan is excluded even if the amount financed includes taxes or licensing or registration fees. Previously, the CFPB had proposed to include purchase money loans if any amounts over the purchase price were financed. The CFPB recognized that mandatory and largely unavoidable items should not cause a loan to lose its excluded status. However, financing ancillary products like extended service contracts or warranties will cause the loan to lose its excluded status.

The last two types of credit—wage advance programs and no-cost advances—are newly excluded in the final rule. First, the CFPB asked for public input on relatively new programs that provide consumers access to the accrued cash value of wages they have earned but for which they have not yet been paid (e.g., due to administrative or payroll processes). While certain types of programs do not constitute "credit" at all, the final Payday Lending Rule would still exclude those wage advance programs that do constitute a credit transaction under certain circumstances, including that the employee is not required to pay any charges or fees besides a charge for participating in the program; the advance is limited to the amount of accrued wages; and the entity advancing the funds warrants that it has no claim or remedy against the employee for failure to repay, will not engage in any debt collection activities, will not sell the debt to a third party, and will not report the debt to a consumer reporting agency. The advancing entity would not be prevented, by this exclusion, from obtaining a one-time authorization for repayment from the consumer's transaction account.

Second, the final Payday Lending Rule will not apply to another relatively new approach, no-cost advances, regardless of whether they are offered by an employer. The exclusion for no-cost advances contains similar conditions as those for wage advance programs, but the exclusion applies only where the consumer is not required to pay any charge or fee, even for participation. However, the exclusion for no-cost advances is not limited to the accrued cash value of the employee's wages.

Conditionally Exempted Loans

Beyond those types of credit discussed above that are excluded, and to which the Payday Lending Rule simply does not apply, the Rule also recognizes that certain short-term or other loans have terms or conditions that are less risky to consumers.[3] Those include "accommodation loans" and "payday alternative loans."

Accommodation loans are generally loans that are made by lenders that are not otherwise significantly engaged in the short-term lending business, and that the lenders do not widely advertise. The CFPB had proposed that one way to address loans offered simply as an accommodation to existing customers could be through a complex exemption for loans underwritten to achieve an annual portfolio default rate of not more than five percent. In the end, along with its decision to not apply its ability-to-repay requirements to covered longer-term loans, the CFPB dropped the five-percent default standard in favor of a standard based on the number of loans and the percentage of receipts from those loans. The final rule would thus exempt loans from the Payday Lending Rule if they are made by lenders that, collectively with their affiliates, made no more than 2,500 covered loans in the current calendar year and

no more than 2,500 such loans in the preceding calendar year. In addition, the exemption applies only if the lender and any affiliates generally derived no more than 10 percent of their receipts from those loans. The Rule establishes parameters for counting transactions and calculating receipts for this purpose.

The Rule also establishes a conditional exemption for a "payday alternative loan," the parameters of which are (as under the proposed rule) modeled closely after the National Credit Union Administration's (NCUA) program. A loan is exempt if it meets the following conditions: it is a closed-end loan, with a term from one to six months, in an amount of $200 to $1,000, that is repayable in two or more substantially equal amortizing payments that are due in substantially equal intervals, and for which the lender generally does not impose any charges other than the rate and permissible application fees. In addition, in order to qualify as a payday alternative loan, the consumer must not be indebted on more than three such loans within a 180-day period, and no more than one at a time. Plus, the lender must maintain and comply with policies and procedures for documenting proof of recurring income, although those procedures need not be the same as under the ability-to-repay requirements (described below). For example, the CFPB notes that for payday alternative loans, lenders could rely upon the NCUA procedures for its Payday Alternative Loan programs (e.g., two recent paycheck stubs).

Certainly, federal credit unions making loans meeting the conditions of the NCUA's Payday Alternative Loan are exempt from the Payday Lending Rule in connection with those loans.

What Does the Rule Require?

The Payday Lending Rule creates a new underwriting procedure for short-term loans with terms of 45 days or less and longer-term balloon loans. It also curbs lenders' repeated attempts to debit payments from a consumer's bank account. In addition, the Rule imposes obligations related to furnishing information, compliance management and record keeping. It also expressly prohibits taking an action with the intention of evading the rule's requirements.

UNFAIR AND ABUSIVE PRACTICES

The Payday Lending Rule identifies two practices as unfair and abusive: (1) making a covered short-term loan or longer-term balloon payment loan without determining that the consumer has the ability to repay the loan; and (2) absent specific consumer authorization, making attempts to withdraw payments from a consumer's account after two consecutive payments have failed.

Ability-to-Repay Determination

Lenders must assess borrowers' ability to repay short-term loans and longer-term balloon loans. The ability-to-repay requirement does not apply to other longer-term loans that do not contain a balloon payment feature.

Under the rule, a lender may not make a covered short-term loan or covered longer-term balloon loan, or increase the credit available under such a loan, unless the lender first makes a reasonable determination that the borrower will have the ability to repay the loan according to its terms. For a covered loan that is a line of credit, the lender must make a new ability-to-repay determination prior to an advance that is more than 90 days after the date of a prior ability-to-repay determination for the line of credit.

A lender's determination is reasonable only if it uses a debt-to-income or residual income methodology to project the consumer's finances during the relevant monthly period. For covered short-term loans, the lender must determine whether the consumer can make payments under the loan, payments for major financial obligations, and meet basic living expenses during the shorter of the loan term or 45 days following consummation, and for 30 days after

the highest payment under the loan. For covered longer-term balloon loans, the lender must assess whether the consumer can make those payments and meet expenses during the relevant monthly period and for 30 days after the highest payment under the loan. The "relevant monthly period" is the month in which the highest sum of payments is due on the loan.

Projecting consumer income and financial obligations

Although lenders are expected to obtain reliable records of net income if they are readily available, if those records are not available, the lender can rely on the consumer's stated income. Permitting lenders to reasonably rely on stated income if verification evidence is not reasonably available is a change from the Bureau's proposed rule. The Bureau revised this aspect of the rule to address commenters' concerns that requiring income verification evidence in every situation would prevent consumers who are paid in cash from receiving a loan.

In order to rely on stated income, the lender must first determine that verification documentation is not reasonably available. Rule commentary addresses this issue, and suggests that the lender must consider whether there are reliable records of income from an employer or other source and whether the consumer's depository account records would document income. The example given for when income would *not* be reasonably available is a consumer paid in cash who does not deposit the cash into a depository account. The creditor must act in good faith and exercise due diligence as appropriate for the circumstances to determine whether another reliable record (or records) is reasonably available.[4]

The rule emphasizes the CFPB's expectation that in the vast majority of cases, the consumer will have a pay stub or transaction action history that serves as a reliable record to verify income. The Bureau notes that the test is not whether the consumer brings the records with him to the store, but whether such records *could* have been brought because they do exist.[5] Lenders that choose to reasonably rely on stated income where no reliable income records are reasonably available may be subjected to monitoring by the Bureau for evidence of systematic overestimation of income.

If the consumer has a reasonable expectation of access to income of another person, the rule grants lenders discretion to consider that income if it obtains verification evidence. The income of any other person is considered net income to which the consumer has a reasonable expectation of access if the consumer has direct access to those funds on a regular basis through a transaction account in which the consumer is an accountholder or cardholder.

Regarding debt obligations and alimony and child support, the rule requires lenders to obtain as verification evidence a national consumer report. The lender may either pull a new report or use a report that was obtained within the past 90 days by the lender or its affiliate, provided it checks the report again in connection with the new loan, and provided the consumer did not complete a loan sequence of three loans and trigger the 30-day cooling off period (described below) since the previous report was obtained. In addition, the lender must obtain a consumer report from a registered information system, if available. The lender also must consider major financial obligations and alimony and child support that are listed in a consumer's written statement even if the obligations do not appear in the consumer's credit report or other verification documentation.

The rule permits lenders to rely on consumers' written statements of rental housing expense where it is reasonable to do so. A lender reasonably relies on the consumer's written statement if the lender's actions are consistent with its policies and procedures and there is no evidence that the stated amount for rental housing expense is implausibly low or that there

is a pattern of the lender underestimating consumers' rental housing expense.[6]

Borrowing history

Lenders are obligated to review consumers' borrowing history to determine whether a cooling-off period is triggered. After the third loan in a sequence of covered short-term loans, covered longer-term balloon loans or a combination of each, there is a mandatory 30-day cooling-off period, which the CFPB refers to as a "circuit breaker."[7] A lender will be prohibited from making a fourth covered short-term loan or covered longer-term balloon loan in a loan sequence during the cooling-off period. The lender must make this borrowing history determination by reviewing its own records and those of any affiliates. The lender must also obtain a consumer report from a registered information system.

Conditional exemption for short-term loan up to $500—the "principal-payoff" option

A lender making a short-term covered loan can avoid these ability-to-repay requirements by making a loan up to $500 that satisfies the rule's conditional exemption from the requirement, set forth in section 1041.6.

For certain short-term loans up to $500, the lender need not make an ability-to-repay determination if the loan is a closed-end loan and the lender is not taking an auto title as collateral. It cannot be offered if the consumer has recent or outstanding covered loans, or where the consumer has had more than six short-term loans or loans outstanding for more than 90 days in any 12-month period. The CFPB refers to this as a "principal-payoff option," designed to allow the borrower to get out of debt gradually. Under this option, the lender can make a series of three loans in a step-down balance structure — the first loan could be not more than $500, the second loan not more than two-thirds of the first, and the third loan not more than one-third of the first. The lender is required to provide specific disclosures for each loan in the sequence.

As explained below, to qualify for the exemption, the loan terms have to meet certain requirements and the lender has to review the consumer's borrowing history and provide certain notices.

LOAN TERMS

To qualify for the conditional exemption set forth in section 1041.6 of the rule, the loan cannot be secured by a vehicle, and it cannot be structured as an open-end loan. Auto title loans and open-end loans must, to the extent they are covered loans, be originated in compliance with the ability-to-repay requirements.

For a loan with multiple payments seeking to qualify for the principal-payoff option, the loan must amortize completely during its term, and the payment schedule must allocate a consumer's payments to the outstanding principal, interest and fees as they accrue only by applying a fixed periodic rate of interest to the outstanding balance of the unpaid loan principal during every repayment period for the term of the loan.

For a covered short-term loan made under the principal-payoff exemption, different principal amount limitations apply depending on whether the loan is the first, second or third loan in a loan sequence. A loan sequence is a series of consecutive or concurrent covered loans in which each of the loans (other than the first) is made during the period in which the consumer has a covered loan outstanding and for 30 days thereafter. The principal amount limitations apply regardless of whether any or all of the loans are made by the same lender, an affiliate or unaffiliated lenders.

Specifically, the loan must satisfy the following principal amount limitations:

- Loan 1: For the 1st loan in a sequence of covered short-term loans, ≤ $500.

- Loan 2: For the 2nd loan in a sequence of covered short-term loans, ≤ ⅔ of the principal amount of Loan 1.
- Loan 3: For the 3rd loan in a sequence of covered short-term loans, ≤ ⅓ of the principal amount of Loan 1.
- After this, the consumer may not receive another covered short-term loan or covered longer-term balloon loan until 30 days have elapsed since the repayment of Loan 3.

If a lender makes a covered short-term loan under the principal-payoff exemption, the lender or its affiliate must not subsequently make a non-covered loan to the consumer while the covered short-term loan is outstanding and for 30 days thereafter. The rule commentary provides an illustration:

> Assume that a lender makes both covered short-term loans under § 1041.6 and non-covered installment loans. Assume, further, that the lender makes on April 1 a covered short-term loan under § 1041.6 to a consumer who has not obtained a covered short-term loan under § 1041.6 in the previous 30 days. Assume that the consumer repays this loan on April 15 and that the consumer returns to the lender on April 30 to seek a non-covered installment loan. Because 30 days have not elapsed since the consumer repaid the loan made under § 1041.6, neither the lender nor its affiliate can make a non-covered installment loan to the consumer on April 30. May 16 is the earliest the lender or its affiliate could make a non-covered installment loan to the consumer.[8]

CONSUMER BORROWING HISTORY

In order to determine whether a loan can be made to a consumer under the principal-payoff exemption, the lender must first review and assess the consumer's borrowing history.

Before making the loan, the lender must determine that: (1) more than 30 days have elapsed since the consumer had an outstanding loan that was either a covered short-term loan made under section 1041.5 or a longer-term balloon payment loan made under section 1041.5 (i.e., subject to the ability-to-repay requirement); (2) the loan would not result in the consumer having a loan sequence of more than three covered short-term loans; and (3) the loan would not result in the consumer having, for any consecutive 12-month period, more than 6 covered short-term loans outstanding, or covered short-term loans outstanding for an aggregate period of more than 90 days. The Commentary offers a number of illustrations.

To make this determination, the lender must review the consumer's borrowing history in the lender's own records and the records of its affiliates, and a consumer report from a registered information system. If there are no such systems registered and available as of the time the lender is required to obtain the report, then the lender simply cannot make a covered short-term loan under the principal-payoff exemption.[9]

NOTICES

Lenders making loans subject to the principal-payoff exemption must provide certain notices to the borrower regarding the borrowing limits and restrictions on future loans. The rule provides model forms for this purpose.

Limiting Payment Withdrawal Attempts

As noted above, the second unfair and abusive practice defined by the Payday Lending Rule relates to creditors' payment processing conduct in connection with covered loans. In general, the rule will prohibit a creditor from processing a third or subsequent payment after two consecutive debit attempts failed due to insufficient funds, unless the creditor obtains a new payment authorization from the consumer. This restriction applies to all covered loans, not merely those short-term covered loans and longer-term covered loans with balloon payment features that are subject to the CFPB's new underwriting requirements.

The CFPB believes that processing multiple payments from a consumer's account when the creditor knew or had reason to know that the payments would fail could cause substantial harm to consumers, and that creditors making covered loans are more likely to attempt to process multiple payments.[10] The CFPB asserts that relying upon existing administrative authority under the Electronic Fund Transfer Act/Regulation E or enforcing general UDAAP principles through case-by-case enforcement will not be sufficient in mitigating consumer harm from the practice at issue, nor were existing industry standards, such as representment restrictions under NACHA rules.

Payment transfers subject to the restriction include most lender-initiated attempts to collect funds due on covered loans, regardless of payment channel or method. However, a transfer from a deposit account to a covered loan account at the same account-holding institution is not a "payment transfer" subject to the rule's limitations, as long as the transfer does not result in any consumer fees other than a late fee, and the institution does not close the consumer's deposit account in response to a negative balance that results from such a transfer.

Following two failed payment transfers, a creditor must obtain a new consumer authorization to process additional payments. If the creditor wants to reestablish authority to process recurring payments, it must obtain a consumer authorization in a form specified by the rule. Alternatively, the creditor may process any single (non-recurring) payment transfer within one business day after obtaining consumer authorization, as long as consent to process the single transfer is obtained after the creditor provides the "consumer rights" disclosure described below.

To support the payment transfer restrictions, the rule creates a series of required disclosures. The disclosures address the first payment made under a consumer authorization, any "unusual withdrawal" (a payment that varies from prior payments in amount, payment date or payment channel or that has been initiated as a second presentment of a returned transfer) and consumer rights following a second consecutive failed payment transfer. The rule provides model forms for use for each required disclosure.[11] Disclosures must be provided in writing or through electronic means. The rule establishes requirements for obtaining consumer consent for delivering disclosures via electronic means. The requirements are not as procedurally burdensome as those under the federal Electronic Signatures in Global and National Commerce (E-SIGN) Act, but a creditor delivering electronic disclosures must provide an email option to the consumer, and electronic short messages (through text or mobile applications) are required in certain circumstances.

ADDITIONAL OBLIGATIONS

Beyond defining two unfair and deceptive practices, the final Payday Lending Rule imposes certain compliance monitoring, compliance management and anti-evasion obligations.

Information Furnishing and Registered Information Systems

To facilitate compliance with the underwriting provisions of the Payday Lending Rule, the CFPB will require creditors to furnish certain information to newly established "registered information systems." The requirements add to the operational complexity of the rule, but potentially provide a new business opportunity to consumer reporting agencies willing to take on the burdens of handling consumer data for payday and payday alternative lenders.

Creditors will be required to furnish information to a registered system regarding covered short-term loans and covered longer-term loans with balloon features at the time of origination and satisfaction/termination.[12] At origination and at any point at which previously furnished origination information is no longer accurate, a creditor must furnish information

regarding certain loan terms and dates, which information will then be relevant to other creditors seeking to offer covered loans to the consumer. At satisfaction/termination (i.e., when a loan ceases to be an outstanding loan), a creditor must furnish information regarding the date the loan ceased to be outstanding and whether it was paid in full. In each case, information must be furnished to every information system that has been registered with the CFPB for 180 days or more.

The rule establishes substantive eligibility criteria and an application process for consumer reporting agencies to become registered information systems.

General eligibility criteria include: (i) the ability to receive furnished information and generate consumer reports; (ii) performance of consumer reporting activities in a manner that facilitates creditors' compliance with the underwriting requirements of the rule; (iii) implementation of a federal consumer financial compliance program, including written policies and procedures, comprehensive training and compliance monitoring, as well as an independent assessment of the compliance management program; (iv) implementation of an information security program and independent assessment of the program; and (v) acknowledgement of and/or consent to the CFPB's supervisory authority over the entity. Based on the eligibility criteria, the most likely candidates for serving as registered information systems seem to be the major credit bureaus or other consumer reporting agencies that are already subject to CFPB supervision as "larger participants"—to the extent each is able to satisfy independent assessment requirements for compliance management and information security. Consenting to CFPB supervision authority when no other grounds for supervision currently exist is a substantial burden for a new entrant to accept.

Entities seeking to become registered information systems will follow slightly different procedures depending on when they apply for registration. Between the effective date of the registration process, which is 60 days from the date the rule is published in the *Federal Register*, and the date 90 days thereafter (in total, 150 days from the date the rule is published in the *Federal Register*), entities may seek preliminary approval by submitting an application demonstrating that they are reasonably likely to satisfy the eligibility criteria within 120 days from the date preliminary approval is granted. The independent compliance management and information security assessments may be submitted after the initial request for preliminary approval, and the CFPB may request additional information necessary to process the application. In addition, following the effective date of the information furnishing rules (21 months from the date the rule is published in the *Federal Register*), an entity may seek provisional registration by submitting documentation sufficient for the CFPB to determine that the eligibility criteria are met—including the required independent assessments. A provisionally registered information system automatically progresses to full registration status 240 days after provisional registration unless the CFPB denies the application within that timeframe. All denials of registration status are subject to an administrative appeals process, as are determinations by the CFPB to suspend or revoke an entity's registration status.

The timelines for the registered information systems application process suggest that the first round of permanent approvals should be processed by late 2018 (assuming entities actually apply for preliminary approval). Once the deadline for preliminary approval applications has passed, it will not be possible to apply for provisional registration until mid-2019, likely delaying full approval until early 2020. As indicated above, this timing is critical, because lenders can only take advantage of the principal-payoff option once a registered information system is available.

Compliance Program

Creditors making loans covered by the Payday Lending Rule will be required to maintain a compliance program. Specifically, creditors making covered loans must develop and follow written policies and procedures reasonably designed to ensure compliance with the rule. Consistent with the CFPB's expectations in other areas of compliance management, policies and procedures for compliance with this rule must be tailored to the size, complexity, nature and scope of the activities of the creditor and its affiliates. In addition, the rule requires creditors to retain certain documentation—such as loan agreements, loan applications and consumer statements, underwriting verification documents and consumer payment authorizations—as well as electronic records relating to loan originations and payment processing attempts as evidence of compliance with the rule for a period of 36 months after any covered loan is no longer outstanding.

Anti-Evasion

The Payday Lending Rule prohibits creditors from taking any action with the intent of evading the rule. Anti-evasion provisions are included for the overall rule, as well as several of the substantive provisions of the rule, including the underwriting requirements and payment processing restrictions. The rule provides examples of evasive activities with the specific regulatory sections to which they relate.

When Does Compliance Become Mandatory?

The Payday Lending Rule is scheduled to become effective in mid-summer 2019, 21 months after it is published in the *Federal Register* (except that provisions facilitating registered information systems to which creditors will report information regarding loans subject to the new ability-to-repay requirements become effective 60 days after publication).

The timeline is six months longer than was indicated in the proposed rule. Extension of the effective date appears to have been driven by multiple factors, including an acknowledgement that it may take longer to get information systems established and registered and lessons learned from implementing the TILA-RESPA Integrated Disclosure (TRID) Rule for mortgage disclosures. Like the TRID Rule, the Payday Lending Rule involves multiple parties acting in concert to ensure compliance through development of new policies and procedures, as well as systems development and integration. In particular, this rule essentially requires creditors, disclosure vendors and consumer reporting agencies acting as registered information systems to align practices and systems to support compliance.

As mentioned above, political and legal developments could delay effectiveness of the rule. Current CFPB Director Richard Cordray's tenure is scheduled to end in mid-2018, and the future of the rule in his successor's hands is uncertain. In addition, since the rule is the CFPB's first attempt at engaging in UDAAP rulemaking under Section 1024 of the Dodd-Frank Act, it is possible that one or more interested parties may seek to challenge the sufficiency of the rulemaking process in court.

For more information section about the topics raised in this Legal Update, please contact any of the following lawyers.

Kristie D. Kully
+1 202 263 3288
kkully@mayerbrown.com

Stephanie C. Robinson
+1 202 263 3353
srobinson@mayerbrown.com

Eric T. Mitzenmacher
+1 202 263 3317
emitzenmacher@mayerbrown.com

Endnotes

[1] The Payday Lending Rule does not preempt state laws except where such laws are inconsistent with the rule. In essence, this means that the rule creates a floor for consumer protection requirements applicable to covered loans, but state laws may establish additional or more stringent requirements on loan origination or servicing. In particular, state laws prohibiting payday lending or establishing usury limits that make payday lending commercially unviable would not be affected by the rule. *See* "Payday, Vehicle Title, and Certain High-Cost Installment Loans," CFPB, https://www.consumerfinance.gov/policy-compliance/rulemaking/final-rules/payday-vehicle-title-and-certain-high-cost-installment-loans/ (Oct. 5, 2017) (hereinafter, "Payday Lending Rule").

[2] Payday Lending Rule at 199.

[3] The phrase "conditionally exempt" generally arises under the CFPB's statute, which authorizes the agency to issue rules and to "conditionally or unconditionally exempt" classes of persons, products or services. *See* 12 U.S.C. § 5512.

[4] Payday Lending Rule at 1619 (to be codified at 12 C.F.R. Part 1041, Supp. I, cmt. 5(c)(2)(ii)(A)-3).

[5] Payday Lending Rule at 777.

[6] Payday Lending Rule at 1625 (to be codified at 12 C.F.R. Part 1041, Supp. I, cmt. 5(c)(2)(iii)-1).

[7] Payday Lending Rule at 820.

[8] *See* Payday Lending Rule at 1641-42 (to be codified at 12 C.F.R. Part 1041, Supp. I, cmt. 6(d)-2). The commentary goes on to state: "The prohibition in § 1041.6(d) applies to covered short-term loans and covered longer-term balloon payment loans made under § 1041.5 but not to covered short-term loans made under § 1041.6. Section 1041.6(d) would, therefore, not prohibit the consumer from obtaining an additional covered short-term loan under § 1041.6 from the same lender or its affiliate on April 30, provided that such loan complies with the principal amount reduction and other requirements of § 1041.6. The prohibition in § 1041.6(d) on making subsequent noncovered loans applies only to a lender and its affiliates. Section 1041.6(d) would, therefore, not prohibit the consumer from obtaining on April 30 a non-covered installment loan from a lender not affiliated with the lender that made the covered short-term loan on April 1."

[9] *See* Payday Lending Rule at 1632-33 (to be codified at 12 C.F.R. Part 1041, Supp. I cmt. 6(a)-2).

[10] *See* Payday Lending Rule at 973, 978-80.

[11] *See* Payday Lending Rule at 1561-69 (to be codified at 12 C.F.R. Part 1041, App. A).

[12] The information furnishing requirement does not apply to longer-term covered loans without balloon payment features at this time. One would expect the CFPB to include additional information furnishing requirements in any final rule imposing underwriting requirements like those imposed by this rule on longer-term covered loans.

Mayer Brown is a global legal services organization advising clients across the Americas, Asia, Europe and the Middle East. Our presence in the world's leading markets enables us to offer clients access to local market knowledge combined with global reach.

We are noted for our commitment to client service and our ability to assist clients with their most complex and demanding legal and business challenges worldwide. We serve many of the world's largest companies, including a significant proportion of the Fortune 100, FTSE 100, CAC 40, DAX, Hang Seng and Nikkei index companies and more than half of the world's largest banks. We provide legal services in areas such as banking and finance; corporate and securities; litigation and dispute resolution; antitrust and competition; US Supreme Court and appellate matters; employment and benefits; environmental; financial services regulatory and enforcement; government and global trade; intellectual property; real estate; tax; restructuring, bankruptcy and insolvency; and wealth management.

Please visit www.mayerbrown.com for comprehensive contact information for all Mayer Brown offices.

Any tax advice expressed above by Mayer Brown LLP was not intended or written to be used, and cannot be used, by any taxpayer to avoid U.S. federal tax penalties. If such advice was written or used to support the promotion or marketing of the matter addressed above, then each offeree should seek advice from an independent tax advisor.

Mayer Brown comprises legal practices that are separate entities (the "Mayer Brown Practices"). The Mayer Brown Practices are: Mayer Brown LLP and Mayer Brown Europe-Brussels LLP, both limited liability partnerships established in Illinois USA; Mayer Brown International LLP, a limited liability partnership incorporated in England and Wales (authorized and regulated by the Solicitors Regulation Authority and registered in England and Wales number OC 303359); Mayer Brown, a SELAS established in France; Mayer Brown Mexico, S.C., a sociedad civil formed under the laws of the State of Durango, Mexico; Mayer Brown JSM, a Hong Kong partnership and its associated legal practices in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. Mayer Brown Consulting (Singapore) Pte. Ltd and its subsidiary, which are affiliated with Mayer Brown, provide customs and trade advisory and consultancy services, not legal services.

"Mayer Brown" and the Mayer Brown logo are the trademarks of the Mayer Brown Practices in their respective jurisdictions.

This publication provides information and comments on legal issues and developments of interest to our clients and friends. The foregoing is not a comprehensive treatment of the subject matter covered and is not intended to provide legal advice. Readers should seek legal advice before taking any action with respect to the matters discussed herein.

© 2017 The Mayer Brown Practices. All rights reserved.